



Media Release

RAM Ratings Lanka reaffirms Tokyo Cement Company (Lanka) PLC at A/P2

RAM Ratings Lanka has reaffirmed Tokyo Cement Company (Lanka) PLC's ("Tokyo" or "the Group") long- and short-term corporate credit ratings of A and P2 respectively. The long term rating carries a stable outlook. The ratings are supported by its sizable market share, its healthy balance sheet, and the healthy debt coverage levels. The above positives are, however, moderated by the inability to immediately pass on cost increases to the end-customer, funding mismatch and the exposure to the cyclical nature of the construction industry. The Group is primarily involved in the manufacture and sale of Portland and ready mix cement both to retail customers and large projects.

Tokyo is one of the only 2 cement suppliers in Sri Lanka that operate local manufacturing plants; Together they supply around half of the cement in Sri Lanka. The rest of the market is populated by importers. The Group performed well both in the retail and project-based segments during FYE 31 March 2011 ("FY March 2011"), securing approximately the largest share of the domestic cement market during the same period.

Tokyo has been utilising its strong cashflow generation to pare down its debts. As such, the Group's debt burden reduced from LKR 4.27 billion as at end-March 2010 to LKR 3.56 billion as at end-March 2011. Concurrently, its gearing ratio eased from 0.75 times to 0.62 times. This further reduced to 0.57 times in end-June 2011. As the proposed bio mass plant is anticipated to be funded largely via internally generated funds, with only the remainder via debt the gearing levels are expected to remain at current levels.

Further, the Group's funds from operations ("FFO") strengthened to LKR 2.21 billion in FY Mar 2011, from LKR 2.08 billion a year ago, supported by sales which grew 11.92% year-on-year while gross margins also improved to 17.62% in FY Mar 2011 from 15.58% last year. This together with the reduced debt burden translated into an improved FFO debt coverage of 0.62 times (end-March 2010: 0.49 times), which is strong compared to similar-rated peers.

On the other hand, cement suppliers are required to adhere to the retail price ceiling set by the Consumer Affairs Authority of Sri Lanka ("CAASL"). Therefore, performance may be affected during periods of rising raw material costs as they may not be able to pass on cost increases to the customer in a timely manner. The ceiling price however does not apply to project sales. While the Group is also

exposed to exchange rate fluctuations as its raw materials are imported, the Sri Lankan rupee exchange rate is managed within a band by the Central Bank of Sri Lanka ("CBSL").

In addition Tokyo relied heavily on short-term borrowings to finance its capital expenditure. As a result, its short-term funds to total borrowings stood at 73.13% as at end-March 2011 compared to 66.25% last year. This together with the Group's low cash holdings translated into a low short-term funds to cash and cash equivalents ("CCE") ratio of 0.08 times. Nevertheless, RAM Ratings Lanka derives some comfort from the Group's short operating cashflow cycle which has remained below 1 month and its healthy annual FFO generation of around LKR 2 billion.

Inherently, the Group is exposed to the cyclical nature of the construction industry, which is the largest cement consumer. For example, the downturn in the construction industry in fiscal 2009 and 2010 resulted in the Group's Operating Profit before Depreciation Interest and Tax ("OPBDIT") levels dropping to LKR 1.63 billion in FY Mar 2010 from 2.30 billion a year earlier. Nevertheless, with the recovery of the sector which improved with economic growth in FY Mar 2011, it increased to LKR 2.06 billion. Given the construction industry's positive outlook, we anticipate this momentum to continue in the short to medium term. The Group's revenue and the output of the country's construction sector recorded a positive correlation of 0.85 for the past 6 years.

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