Piramal Glass PLC [GLAS]: BUY [+25%]

Growth through the looking glass

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We initiate coverage on GLAS with a BUY rating. We believe the company is strongly positioned as the only glass bottle manufacturer in Sri Lanka, supplying mainly to the alcoholic beverages segment. The ongoing switch from the illicit segment and increasing export sales, point to an attractive growth story. The main drag on earnings is furnace oil, for which selling prices are regulated. The company is exploring various options to reduce this dependence. Moreover, the capacity increase in FY16 would give the company 25-30% higher sales capacity and should be a key growth catalyst. Our DCF based valuation implies an intrinsic value of LKR 6.60/share, including the FY16E DPS of LKR 0.25 we expect a 25% total return. BUY.

Demand is secured due to captive spirit market

GLAS is the sole glass bottle supplier in Sri Lanka, with ~95% market share in the glass bottle manufacturing market in Sri Lanka. Demand is driven by the alcoholic beverage segment, which accounts for ~63% of sales. The demand for the spirit segment is broadly inelastic, and hence GLAS is relatively insulated from the business cycle. The growth potential for the spirit industry is strong with more than 40% of sales estimated to be in the form of illicit liquor. We believe, even a modest conversion of this untapped segment has potential to increase GLAS's beverage segment sales by more than 25%.

Capacity expansion to free up headroom for growth

The main constraint on growth is GLAS's capacity. This will be addressed in FY16 with the relining of the furnace operated by the company, thereby increasing capacity by ~25-30%. While the investment of LKR 3bn will be funded with debt, the company has ample opportunity to leverage its balance sheet given its current net debt position. We believe this higher capacity would enable the company to grow its exports sales further and explore non-traditional markets niches in the food segment.

Energy costs a drag on earnings; GLAS exploring other options

Energy costs accounts for more than 40% of GLAS's production costs, due to the machine-intensive production process. Half of this expenditure is on furnace oil, for which the selling price is regulated by the government. The price of furnace oil in the local market of LKR 80/liter is much higher than the export price. GLAS has repeatedly approached the government to request for a pricing formula for furnace oil, with no avail. Hence we expect this to persist in the medium term. However, company is also exploring other options to reduce its dependence on furnace oil.

We rate GLAS a BUY based on our DCF-derived valuation

We valued GLAS based on the DCF method, and arrived at a share price of LKR 6.60, which implies an upside of 20.0%. Including a dividend yield of 4.5% we arrive at a total return of LKR 24.5%, We note that the successful completion of the furnace relining will be a key catalyst for growth. **BUY.**

Key statistics	
Bloomberg ticker	GLAS SL
CSE ticker	GLAS.N0000
GICS Subsector	Containers & Packaging
Price as at 16 Feb 16 (LKR)	5.50
52 week Hi/Lo (LKR)	7.10/5.40
Market cap (LKR mn)	5,226
Market cap (USD mn)	36
No. of shares (mn)	162
ADT (LKR mn) - 3M	1.0
ADT (USD k) - 3M	6.6
ADT (shares k) - 3M	162.7
Free float (%)	27.0

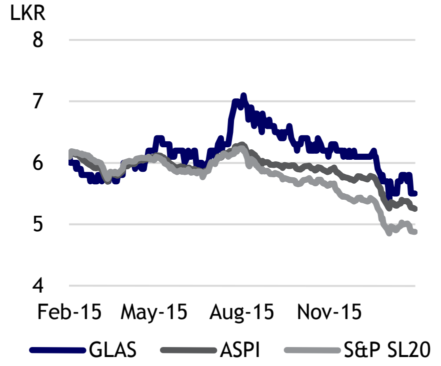
Company website | CSE website

Source: CSE, Bloomberg, Company data
Note: LKR converted at 144 LKR per USD

Valuation summary	
Price as at 16 Feb 16 (LKR)	5.50
Intrinsic value (LKR)	6.60
Upside (%)	**20.0**
FY16E DPS (LKR)	0.25
Total return (%)	**24.5**

Source: Asia Securities

Share price movement (indexed to GLAS)



Movement (%)	YTD	3M	12M
GLAS	(10)	(11)	(10)
ASPI	(9)	(10)	(14)
S&P SL20	(10)	(13)	(20)

Source: CSE, Bloomberg

Financial summary

In LKR mn	FY13	FY14	FY15	FY16E	FY17E	FY18E
Revenue	5,501	5,220	5,792	6,646	7,696	8,943
EBITDA	1,443	817	1,071	1,329	1,616	1,967
Recurring net profit	722	283	439	341	520	837
Diluted recurring EPS (LKR)	0.76	0.30	0.46	0.36	0.55	0.88
ROE (%)	21.0	7.9	12.2	9.3	13.5	20.0
P/E (x)	8.0	11.3	12.4	15.3	10.1	6.2
EV/EBITDA (x)	5.6	5.9	6.5	5.9	4.9	4.0
P/B (x)	1.6	0.9	1.5	1.4	1.3	1.2

Source: Company data, Asia Securities

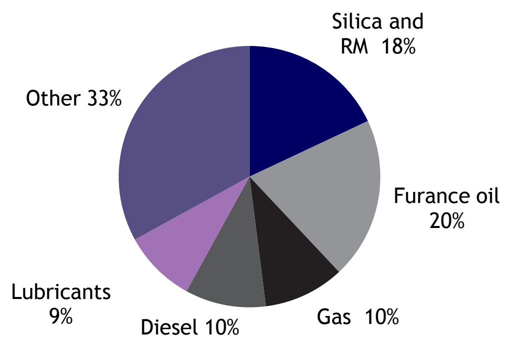
Company Investment Thesis

- Reliance on machinery has led to high energy costs
- Furnace oil prices limit margin growth but GLAS is exploring alternate fuel sources
- Strong market share in the beverage segment to drive growth
- The illicit liquor market of 40% presents a key growth opportunity
- Imported bottles are a threat but GLAS holds competitive edge
- Export market growth to become a major growth driver
- Key constraint for export sales is capacity; to be remedied through furnace relining which should increase capacity by 25-30%
- Valuation: DCF-derived valuation yields share price of LKR 6.60, which implies an upside of 20.0%. Including a dividend yield of 4.5% we arrive at a total return of LKR 24.5%,
- Key upside risks: 1) A reduction in the price of furnace oil by moving to a pricing mechanism, 2) Competition from imported bottles easing over time allowing GLAS more flexibility with its pricing.
- Key downside risks: 1) An unexpected drop in local alcoholic beverage sales, 2) Competition entering the market via the entry of a new player.
- Catalysts: 1) Successful completion of the capacity expansion, 2) The introduction of a pricing formula for furnace oil prices.

Reliance on machinery has led to high energy costs
The production process is heavily reliant on machinery rather than human labour. The relatively low human intervention, and raw material costs also means that factory running costs are the major contributor to production costs. As such, the single largest cost in the production process is energy to run the production plants, which accounts for ~40% of production costs and is split between furnace oil, gas and diesel.

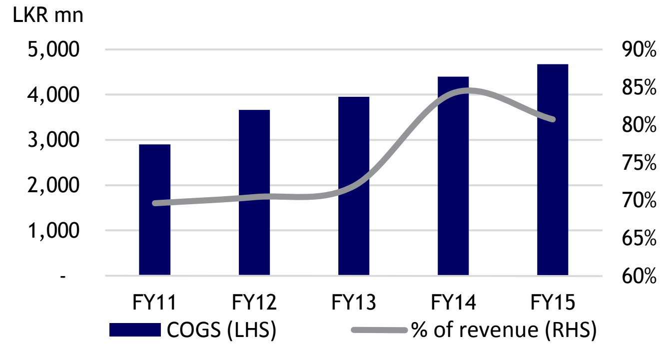
GLAS's COGS have increased at a five year CAGR of 12.3% during 2011-15, along with the expansion in the manufacturing operation. Since GLAS is an established operator in a mature market, with stable revenue growth, we are of the view that, the key in sustaining margins is controlling costs along the production process.

Furnace oil is the single highest contributor to production cost



Source: Company data, Asia Securities

COGS has increased in the last few years

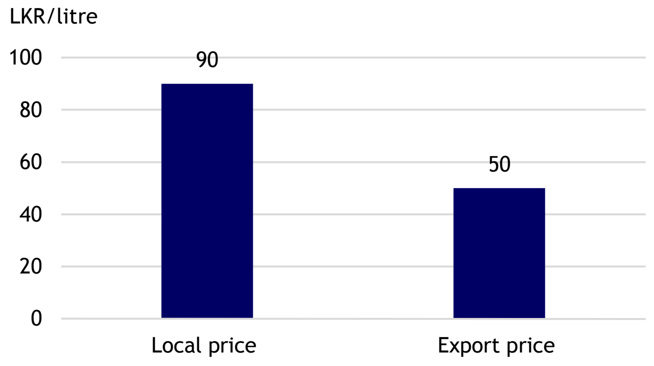


Source: Company data, Asia Securities

Price controls on furnace oil limits margin growth
Furnace oil prices are the single biggest contributor to GLAS's production costs at ~20%. This is a regulated commodity in Sri Lanka, as only 10% is sold locally while the rest are exported. No importation of furnace oil is permitted by the government. The Ceylon Petroleum Corporation maintains a high unit price of LKR 90/litre on local sales, which is 60% more than the export price of ~LKR 50/litre.

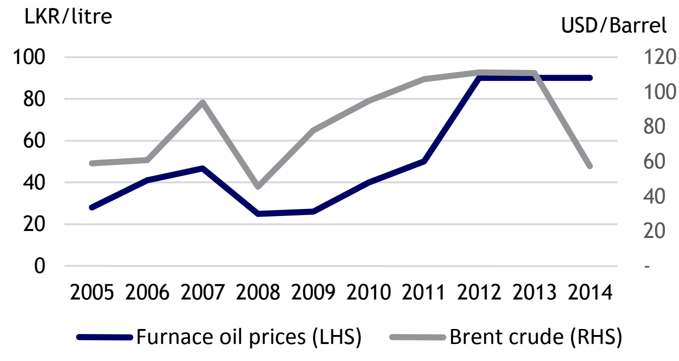
With oil prices declining to USD30 per barrel, GLAS has continually requested the government to introduce a pricing formula for furnace oil, similar to the one for Petrol and Diesel (currently not being applied), which is more reflective of global oil prices. If such, a formula is introduced GLAS will be one of the main benefactors, since it is one of the four largest buyers of furnace oil in the country. As such, we estimate a reduction in the price of furnace oil to improve GLAS's gross margins substantially. However, to-date GLAS's requests from the government have not yielded any results.

Furnace oil is sold at a much higher price locally



Source: Central Bank of Sri Lanka, Company data, Asia Securities

Furnace oil prices have remained at LKR 90 for three years



Source: Central Bank of Sri Lanka, Asia Securities

Alternate fuels can reduce reliance on furnace oil
GLAS is currently in the process of exploring other fuel sources which would enable it to reduce the dependence on furnace oil. One of the drawbacks faced by GLAS is that the other fuel sources available also are comparable in cost to furnace oil. Hence a move to other fuel sources will be more with the intention of reducing the company's reliance on furnace oil as a fuel source, rather than reducing the costs.

Silica is the key raw material in the production process
Key raw material used in the production process is Silica. Altogether, silica and other raw materials (adhesives, processing materials) account for ~18% of production costs. The relatively low contribution of raw materials is mainly due to production relying on processed Silica, rather than its raw form. The processing happens at the company's own plant, which is heavily automated.

GLAS sources silica from Sri Lanka due to cost and quality
Sri Lanka remains a cheaper source market for Silica and other minerals required in the production process since it is c. 10-15% cheaper than India. While raw silica prices are cheaper in India, the net selling prices are higher given the cost incurred in transporting silica over longer distances. Sri Lanka's smaller land mass makes transportation costs much cheaper, leading to the lower prices.

In addition, GLAS also views Sri Lankan silica as being of higher quality than imports. For these reasons, GLAS currently sources its silicon requirement exclusively from Sri Lanka. However, in the event that there are supply shortages, GLAS is able to import silica from India as well, given the strong standing and supply chain of the parent company in India.

Once the raw material is acquired, this is processed at GLAS's own mining and processing plant, thereby giving it a strong hold over the early stage of value addition in the supply chain. The processing plant can supply GLAS's full capacity at present. An in-house facility manufactures the necessary polythene for shrink wrapping as well.

However, silica should see upward pressure due to construction demand
We believe silica prices will continue to escalate given the limited supply available in Sri Lanka, and increasing demand from the construction sector. In the next two years, we expect constructions to be a major driver of economic growth in Sri Lanka, with the Western Province Megapolis Development Plan scheduled to get underway from 1H2016.

However, we note that GLAS does not see silica as a major factor in its cost structure, given its low contribution to the overall cost base. As discussed the production process relies on processed silica, than its raw form, which only accounts for around 12% of production costs. The processing is done at GLAS's own plant in Nattandiya. Hence escalation of Silica prices is not seen as a major threat.

Dominant market position enables GLAS to pass on raw material cost increases to buyers
Given the mature state of operations costs are key focus for possible margin expansion. As a result raw material prices and costs of the manufacturing process are thoroughly scrutinized by the company. However, since GLAS is Sri Lanka's only manufacturer of glass bottles on a large scale, the company has almost absolute dominance over the market. As a result, if required

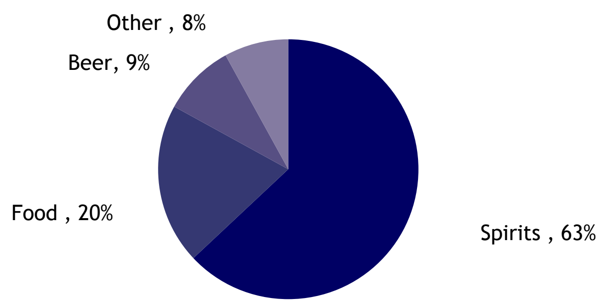
GLAS has the ability to pass on cost increases to its key buyers in the short term. Given the high dependence of the buyers on GLAS and the importance of the products supplied, we do not forsee an immediate move away from its buyers in the event prices are increased. As such, we believe the demand for GLAS's products is price inelastic at least in the short to medium term. This is a key positive for the company as it is insulated from margin pressure arising as a result of cost-push factors.

In the medium to long term however, buyers would be able to negotiate supply contracts with importers, who are GLAS's main competitors in the absence of any Sri Lankan competition.

Strong market share in the beverage segment to drive growth
GLAS is the main supplier of glass bottles to all four leading spirit manufacturers – Distilleries Company of Sri Lanka, IDL, Rockland and Mendis. Collectively they accounted for a 92% share of the spirit market according to excise department data for 2014. Sales to the spirit segment are GLAS's main sales driver, contributing 58% of the topline as at FY15. The demand for spirits is broadly inelastic, and as such, does not vary significantly with the swings in the business cycle. Therefore, we believe this positions GLAS as a defensive play, which is a key positive.

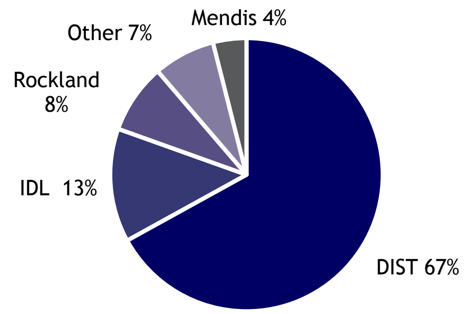
Sales to grow despite re-usage
While re-using bottles even upto 6-10x is the norm in the spirits industry, GLAS has still seen its sales to the sector rising by c. 20% YoY. This is mainly because, 1) some bottles going out of circulation due to breakage, and, 2) liquor bottles being used for other domestic purposes in rural households instead of being returned to retailers. As such, we expect sales to the industry to beverages to grow at an average rate of ~15-20% in the medium term.

Spirits contribute the major's share of GLAS's revenue



Source: Company data, Asia Securities

The spirit market is dominated by four players

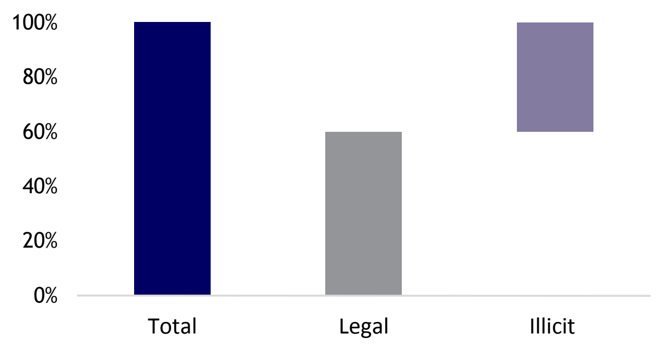


Source: Excise Department, Asia Securities

Demand for spirits is a part of consumption demand and less cyclical
Spirits are predominantly sold to households and end-consumers, through various delivery channels such as exclusive dealerships, retail outlets and supermarkets. As such, the demand for spirits forms a part of a household's consumption, which we believe is less cyclical than investment demand in Sri Lanka. We expect consumption to continue to grow in the next couple of years as well, especially with the increasing affluence of the Sri Lankan population with per capita GDP trending towards USD 4,000. A detailed study of the interplay between economic growth and the demand for spirits is included in our Alcoholic Beverages sector report – *Balancing act of duties and profits*.

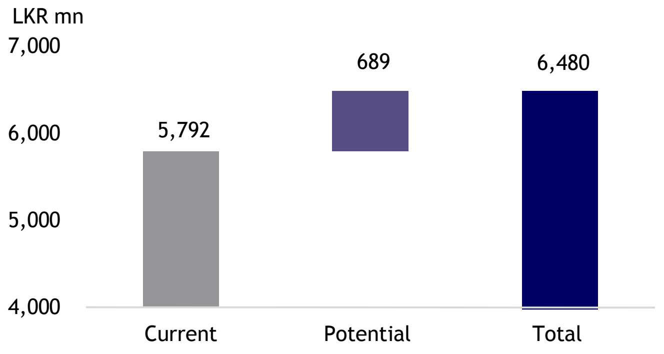
The illicit liquor market of 40% presents a key growth opportunity
The illicit market is estimated to amount to more than 40% of the spirit market according to our discussions with market participants. This market remains out of reach for key suppliers to the industry, like GLAS. Hence any conversion from the illicit category to legal sales is likely to substantially increase volumes for GLAS. Going by today's sales levels, we estimate a 40% conversion of the illicit market to yield a LKR 634mn (+26.7% from FY15 beverage segment sales) increase in sales for GLAS assuming its current market share of 95% in the spirit segment.

Illicit market is estimated to be 40% of spirit consumption



Source: Company data, Asia Securities

Illicit segment presents a key growth opportunity



Source: Excise Department, Asia Securities

Government's aim of boosting excise collections to drive conversion from illicit segment
Our channel checks indicated that almost 70% of the retail price of a spirit bottle is excise duty. As such, we estimate that this is key source of government revenue leakage which will very soon be scrutinized more thoroughly given the government's drive to increase its revenues from the current 12% of GDP. We are of the view this this would accelerate the process of the illicit market converting to legal sales.

However, excise duties will temporarily dampen conversion from illicit
However, we believe the anticipated conversion from the illicit segment to legal spirits will be delayed following the government's increase in excise duties according to the budget for 2016 which made this switch more expensive. Nevertheless, with increasing health awareness on the dangers of illicit liquor, and rising per capita incomes, we expect the long term trend of switching from illicit liquor to legal liquor to stay on track, albeit at a slower pace.

We also note that the budget also increased excise duties on beer. This was a policy reversal, after many years of keeping duties lower on beer to encourage consumers to switch from spirits to beer. Sales to the beer segment only amounted to less than 5% according to GLAS, and are accounted for as a part of the beverage segment. Nevertheless, this was a growing segment given the switch to soft liquors especially, from the younger demographic. Beer and soft liquors are not as profitable as the spirit segment for GLAS, since can usage is prevalent, and because bottles are re-used ~12-15x, much higher than the spirit segment. Hence the switch back from beer to spirits, reversing the earlier trend, should prevent any drop in sales in the beverage segment over time.

Imported bottles are a threat but GLAS holds competitive edge
Our channel checks indicated that imported spirit bottles are on par with GLAS's prices. However, despite this the liquor manufacturers prefer GLAS over them due to several non-price factors:

Chinese and Indian mass producers of glass bottles often have quality issues, and do not conform to the high standards required by the liquor manufacturers.

GLAS has a return policy which allows the beverage companies to ask for new batches in the event quality standards are not met. Given the relatively smaller size of the Sri Lankan businesses, and the mass production techniques used by Chinese and Indian bottle manufacturers, it is unlikely that buyers will be able to follow this practice with them.

In addition, glass bottle supplies are often delivered just in time (JIT), since carrying stocks of bottles ties up working capital of the liquor manufacturers. Given GLAS's long association with the local liquor players, their supply chain is fully integrated to cater to this JIT requirement, which frees up working capital financing for GLAS's buyers. Furthermore, with GLAS being the only bottle manufacturer in Sri Lanka, and given the co-dependent nature of the relationship between liquor manufacturers and GLAS, the liquor firms hold significant bargaining power. In recognition of this GLAS also prioritizes the local market over export orders, since maintaining its leading supplier status in the Sri Lankan market is a key factor for its continued dominance.

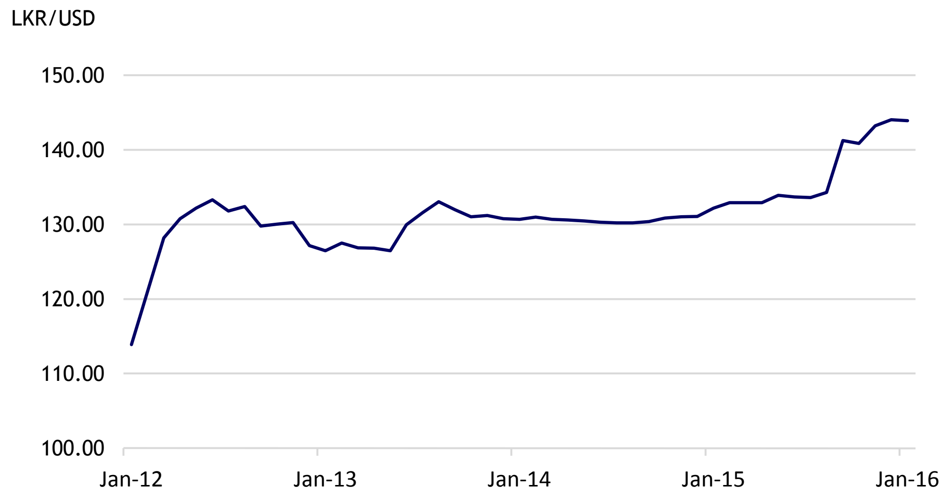
Majority of GLAS's demand stems from annual fixed contracts
Moreover, ~70% of GLAS's demand is fixed annual order quantities which are renewed annually. These are orders done for the most established buyers, who have formed very close relationships with GLAS over a number of years. GLAS allows these buyers the flexibility to change the timing of the orders within the year, based on their demand fluctuations. This flexibility will not be given by importers, given their longer delivery cycles.

As such, we do not see an immediate competitive threat from cheaper Indian and Chinese competitors who are vying for market share from GLAS's buyers, mainly spirit manufacturers.

Competition from importers forms a price cap for GLAS
As we mentioned earlier, pricing between GLAS and the importers have now reached parity, despite a 15% duty on imported glass vessels. This is because labour and manufacturing costs in Sri Lanka are generally more expensive than the South Asian region, and India and China in particular.

While the competitive pressure from imports does not pose a threat for GLAS's market share in the short term, it significantly diminishes the pricing flexibility of GLAS. In effect the current prices act as a price cap, since moving above this would make importers cheaper than GLAS. The depreciation of the LKR against the USD by 10% last year should help GLAS in this regard since imported products have become more expensive. As such, the scope for pricing increases is limited for GLAS. Hence margin increases will have to come from either cost reductions or product differentiation.

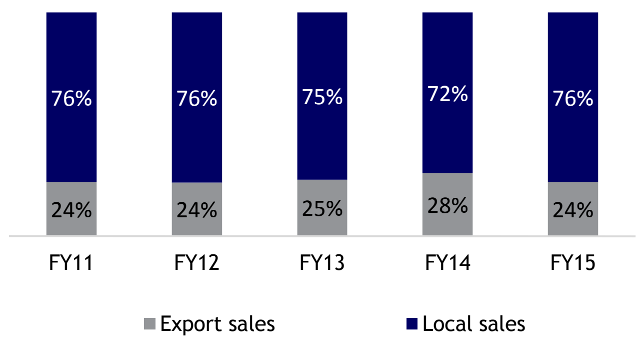
LKR has depreciated against the USD in the last three years



Source: Central Bank of Sri Lanka, Asia Securities

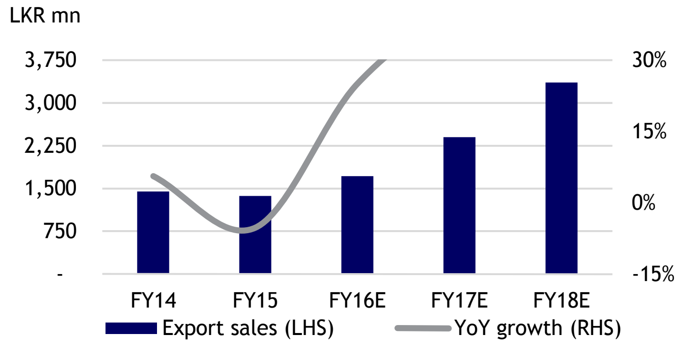
Export market growth to become a key driver in the next few years
GLAS has been systematically developing its export base in the last few years, by leveraging on its presence in India and the region. One of the main drivers in FY16 so far have been exports to USA, which the company expects to grow significantly in the next few years. The overall strategy in the export product offering has been to concentrate on niche areas rather than serving vanilla products since GLAS is not keen on expanding sales at the expense of margins. We forecast export sales to grow at a CAGR of 25% YoY in the next three years, following the company's strategy.

Export contribution to topline has remained at 24-25%



Source: Company data, Asia Securities

We expect exports to grow at a CAGR of 25% in the next 3 years



Source: Company data, Asia Securities

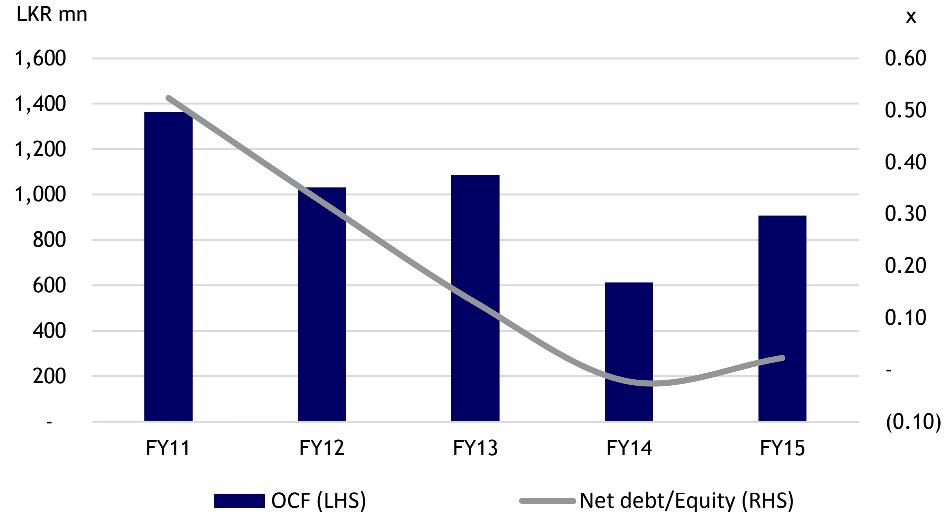
Key constraint for export sales is capacity
Currently GLAs is operating at 100% capacity and prioritizes the local market. However, export sales have been growing the last few years, and thus we believe GLAS would be better served by diversifying its markets over time. The major constraint is capacity, since GLAS only operates one furnace locally. As such, we believe the relining of the furnace, planned for FY16, will go a long way towards addressing the capacity issue for the time being.

Furnace relining to increase capacity by 25-30%
This is a major capex expenditure estimated at ~LKR 3Bn and will increase capacity by 25-30% from the current levels. Given the strong sales pipeline for GLAS, and with the interest stemming from the export markets, we believe the higher capacity should translate into additional sales.

Short term operational disruption expected, but GLAS has sufficient cover
Company expects its operation to be disrupted for around 2-3 months due to the relining. However, GLAS is already making plans by building up buffer stocks and making arrangements with its parent in India to take up some of the volume during this period. Since, most of the moulds used by the company are already maintained in India, we do not see the relining causing a major disruption in the company's supply. The local operation has only one furnace while Piramal Group has nine furnaces operating in India, hence we believe the Indian operation has more than enough capacity to take on the extra load.

Strong balance sheet and low net debt to leaves headroom for leverage
Company is also sufficiently covered on the balance sheet front to take on debt for the LKR 3Bn expenditure since its net debt/equity was negligible as at FY15. On average the company has generated operating cash flow (OCF) of around LKR 1.9bn annually in the last five years. Hence we do not see the company having any problems with the repayment of the debt either. Any sales growth arising out of the capacity expansion, should enable the company to make higher profits, which would in turn increase the cash generating profile.

OCF profile has generally been healthy while net debt to equity has come down



Source: Company data, Asia Securities

Food segment should also increase with rising health consciousness

Another key driver that the company is looking to penetrate is the food segment, specifically virgin coconut oil. With the rise of health consciousness in the world virgin coconut oil has been highlighted as a nutritious product to be added to household cooking. With Sri Lanka being one of the leading producers of coconut in the world (4.9% market share in 2014 according to the Food and Agriculture Association) virgin coconut oil has potential both as a domestic and an export product. In order to preserve the health benefits, the oil needs to be stored in high quality jars, the demand for which can be captured by GLAS. With the awareness of the health benefits of virgin coconut oil, exporters are particularly interested in developing advanced markets such as Japan and USA. GLAS is confident that this will prove to be another sales driver for the company in the next few years, which will also have profit potential.

Financial Outlook

GLAS reported FY15 revenue of LKR 5,792mn (+11.0% YoY), driven by the alcoholic beverage segment, which consists of sales to the spirit and beer industries. Gross margin expanded by 3.5pp to 19.3%. although this stemmed from a lower base in FY14, where gross margin stood at 15.8%. We note that the five-year average gross margin is 24.6%, although this is unlikely in the short term due to furnace oil prices being held at LKR80-90 despite international oil prices dropping below USD30/barrel. EBITDA margin also expanded to 18.5% from 15.6% in FY14. At net level GLAS made a net profit of LKR 439mn, which was a 55.1% improvement YoY.

Looking ahead, we believe the alcoholic beverage segment will continue to drive revenue and forecast the segment to grow at 10% in FY16 and at 15% thereafter, with the higher capacity of the company kicking in post-2016. We also believe there will be a gradual shift away from illicit liquor which would translate to sales growth for GLAS.

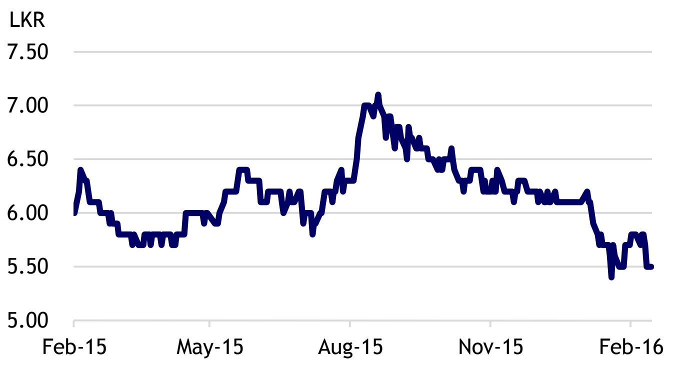
Export sales declined 5.2% YoY to LKR1,371mn in FY15, due to GLAS prioritizing the domestic segment, given capacity constraints. As a result, export contribution reduced to 24.0% from 28.1% in FY14. We expect this situation to be remedied with the capacity expansion, and for exports to be a major growth focus in the next few years increasing by 20% YoY.

Overall we forecast revenues in FY16E to be up 14.4% YoY and EBIT margin to stand at 10.5% slightly down from FY15 levels, due to the higher depreciation expense. Hence we believe that FY16E full year net profit of LKR 503mn (+13.0% YoY). We expect HHL to declare a full year dividend of LKR 0.30/share, resulting in a payout of ~30.0%.

Valuation

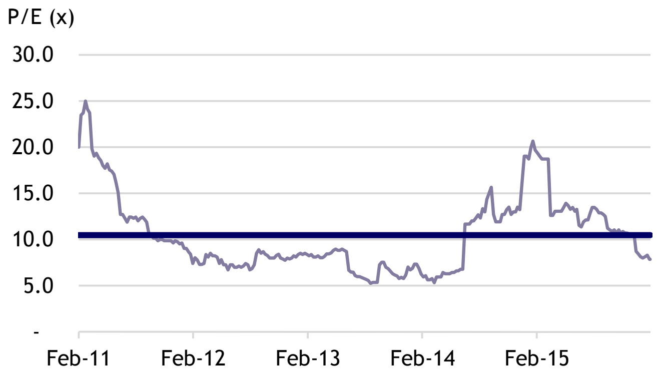
The stock is down 10.0% YTD and up 8.3% YoY and is currently trading 10.7% below its five-year trading average. The share price picked up mid last year, however, it has slid along with the market since then. The recent drop in the GLAS share share price, since beginning of 2016, was more a reflection of tepid market sentiment than reflection of the share's intrinsic value and fundamentals.

Export contribution to topline has remained at 24-25%



Source: Bloomberg, Asia Securities

We expect exports to grow at a CAGR of 15% in the next 3 years



Source: Bloomberg, Asia Securities

Since GLAS is the only local manufacturer in its sector, we have valued it through its internal cashflows using a three stage discounted cashflow (DCF) method. Our valuation yields a share price of LKR 6.60 which implies an upside of 20.0%.

Key WACC assumptions

Beta	1.20	
Equity risk premium	7.5%	
Risk free rate	8.0%	
Cost of debt	6.5%	USD borrowing rates with headroom for a pickup in LIBOR
Capital structure	30.0%	Factoring in the higher debt incurred in capacity increase
Terminal growth	2.5%	Factoring growth from beverages, export sales and food segments

Source: Asia Securities

We note that our valuation is conservative especially since we have assumed that the company will be funding its LKR 3bn capex expenditure on the religning of the furnace completely through debt. As we have noted in the report, given GLAS's negligible net debt position, and debt to equity of ~5% we believe it has enough balance sheet head room to take on the debt. Furthermore, we have modeled debt to equity to be at 30%, slightly higher than the historical average for the last five years, despite the company having very low appetite debt in the last few years.

Key upside risks: 1) A reduction in the price of furnace oil by moving to a pricing mechanism, 2) Competition from imported bottles easing over time allowing GLAS more flexibility with its pricing, 3) GLAS getting higher manufacturing capacity via acquisitions or expansion, and, 4) Company moving into higher value added niches leading to margin growth.

Key downside risks: 1) An unexpected drop in alcoholic beverage sales locally, 2) Competition entering the market via the entry of a new player, 3) Cost of furnace oil increasing due to a pick-up in oil prices,4) Export growth not taking off at expected levels leading to idle capacity following the furnace relining.

Catalysts: 1) Successful completion of the capacity expansion, 2) The introduction of a pricing formula for furnace oil prices, 3) The entry of a foreign glass bottle manufacturer who can supply to the alcoholic beverage market.

Scenarios

Qualitative	Bear	Base	Bull
Growth in the alcohol beverage segment	Growth slows down unexpectedly	Growth of 10% in FY16E, followed by 12% growth due to capacity increase	Capacity increase converts to sales; 20% sales growth
Furnace oil prices are revised	Furnace oil prices rise as a result of a rise in oil prices	Prices kept at current level in FY16E	Furnace oil prices are reduced by 25%
Export sales growth	Export sales remain stagnant at current levels	Export sales increase by 25% annually following capacity increase	Export sales increase at a rapid rate of 40% annually
Fundamentals	**Bear**	**Base**	**Bull**
Revenue CAGR (FY16E-18E)	6.4	15.6	21.4
EPS CAGR (FY16E-18E)	4.0	24.0	35.5
EBIT Margin (%)			
FY16E	6.9	7.5	7.7
FY18E	10.0	12.3	13.6
Valuation	**Bear**	**Base**	**Bull**
Target price (LKR)	5.50	6.60	7.50
DPS (LKR)	0.25	0.25	0.25
Total return (%)	4.5	24.5	40.9
Current price (LKR)	5.50	5.50	5.50

Source: Asia Securities

Company profile

Piramal Glass is the only large-scale, local glass manufacturing company which manufactures glass bottles and jars. They cater mainly to the alcoholic beverage segment. In addition to supplying the local market, they export their products to many countries. The headquarters are located in Colombo, Sri Lanka. The company was established in 1956. It was acquired by Piramal Group, a large Indian conglomerate, in 1999. Their market capitalization was USD 36mn as at 16th February 2016. They have a glass manufacturing factory in Horana, Sri Lanka and a Sand & Polythene manufacturing factory in Nattandiya, Sri Lanka.

Top 10 shareholders as at 3QFY16

Voting	% Held
Piramal Glass Limited	56.5
Employee Provident Fund	9.5
CITI Bank NY S/A Norges Bank Account 2	2.5
City Bank NY S/A Forward International Dividend Fund	1.9
Mr Dangampola and Mrs N P Dangampola	1.1
Mr S D R Arudpragasam	1.0
Mr N Perera	0.8
AIA Insuarnce Lanka PLC A/C No 7	0.8
DFCC Bank PLC A/C 1	0.8

Source: Company data

Board of Directors

Vipul Shah – Chairman and Independent Director
Vipul Shah was appointed to the board in year 1999 and he took over as the Chairman since 2002. He joined Piramal Glass in 1988. He holds a Bachelor's Degree in Commerce, and is a Rank Holder and member of The Institute of Chartered Accountants of India (1981). He has also completed a Management Education Program from IIM Ahmedabad in 1987and the Advance Management Program (AMP) from the Harvard Business School, Boston, USA in 1997.

Sanjay Tiwari – CEO and Executive Director
Sanjay Tiwari was appointed to the board in December 2005 as CEO and Executive Director. Since 1st June 2013 he has been designated as Chief Operating Officer. He is an alumni of London Business School, holds a Bachelor's Degree in Commerce from India and is Fellow member of the Institute of Chartered Accountants of India. He has completed Advanced Financial Management & General Management form the Indian Institute of Management, Ahmedabad, India, and is qualified in Executive Management from the University of Michigan, USA and Senior Executive Management from London Business School, UK.

C. T. S. B. Perera – Non-Executive, Independent Director
C.T.S.B. Perera was appointed to the board in year 2003 and served as the Managing Director from July 1995 to March 2002. He holds a PhD-CNAA-North Staffordshire UK, BSc(Hons) CNAA-North Staffordshire UK, BSc University of Ceylon and Fellow of the Institute of Metal, Materials & Mining (UK).

R. M. S. Fernando – Non-Executive, Independent Director
R.M.S. Fernando was appointed to the board on October 2007. He is a fellow of the Chartered Institute of Bankers, UK, Companion of the Chartered Institute of Management in UK and a fellow of the Chartered Institute of Management Accountants in UK. He holds an honours degree in Law from the University of Colombo and is an Attorney-at-Law. He is also the Chairman of the Urban Development Authority, Sri Lanka.

Samit Datta – Non-Executive, Non-Independent Director
Samit Datta was appointed to the board on April 2015. He holds a BE (Honours) in Mechanical Engineering for NIT, Durgapur, India and a MBA in Manufacturing Management from SP Jain Institute of Management & Research, Mum

Income statement

In LKR mn	FY2013	FY2014	FY2015	FY2016E	FY2017E	FY2018E
Revenue	**5,501**	**5,220**	**5,792**	**6,646**	**7,696**	**8,943**
Operating expenses	(4,058)	(4,404)	(4,721)	(5,317)	(6,080)	(6,975)
EBITDA	**1,443**	**817**	**1,071**	**1,329**	**1,616**	**1,967**
Depreciation and amortization	(420)	(427)	(436)	(828)	(845)	(865)
EBIT	**1,023**	**390**	**635**	**501**	**771**	**1,102**
Interest income	1	0	0	3	9	9
Interest expense	(257)	(202)	(127)	(102)	(169)	(127)
Associate/JV income	-	-	-	-	-	-
FX gain/loss	-	-	-	-	-	-
Other non-operating income/expenses	1	101	1	1	1	1
Profit before tax	**767**	**289**	**509**	**402**	**611**	**985**
Income tax expenses	(46)	(6)	(69)	(60)	(92)	(148)
Profit for the year	**722**	**283**	**439**	**341**	**520**	**837**
Minority interest	-	-	-	-	-	-
Preferred dividends	-	-	-	-	-	-
Recurring net profit	**722**	**283**	**439**	**341**	**520**	**837**

Source: Company data, Asia Securities

Key ratios

	FY2013	FY2014	FY2015	FY2016E	FY2017E	FY2018E
Revenue growth (%)	5.8	-5.1	11.0	14.7	15.8	16.2
EBITDA margin (%)	26.2	15.6	18.5	20.0	21.0	22.0
Net margin (%)	13.1	5.4	7.6	5.1	6.8	9.4
Recurring diluted EPS (LKR)	0.76	0.30	0.46	0.36	0.55	0.88
DPS (LKR)	-	-	-	0.25	0.30	0.40
Tan. BVPS (LKR)	3.82	3.74	3.82	3.93	4.17	4.65
ROA (%)	13.8	7.0	8.4	5.4	7.1	10.2
ROE (%)	21.0	7.9	12.2	9.3	13.5	20.0
OCF (LKR mn)	1,085	613	908	1,459	1,272	1,440
Unlevered FCF (LKR mn)	860	301	589	(1,864)	1,060	1,194
Levered FCF (LKR mn)	147	(209)	351	534	291	467
P/E (x)	8.0	11.3	12.4	15.3	10.1	6.2
EV/EBITDA (x)	5.6	5.9	6.5	5.9	4.9	4.0
P/B (x)	1.6	0.9	1.5	1.4	1.3	1.2

Source: Company data, Asia Securities

Balance sheet

In LKR mn	FY2013	FY2014	FY2015	FY2016E	FY2017E	FY2018E
Assets						
Non-current assets						
Property, plant and equipment	3,734	3,678	3,561	6,056	5,422	4,803
Intangible assets	28	31	26	26	26	26
Goodwill	-	-	-	-	-	-
Equity method investments	-	-	-	-	-	-
Interest earnings investments	-	-	-	-	-	-
Other investments	5	5	7	7	7	7
Other non-current assets	337	1	-	-	-	-
Total non-current assets	**4,104**	**3,715**	**3,595**	**6,090**	**5,456**	**4,837**
Current assets						
Accounts receivable	1,045	1,117	1,260	1,292	1,497	1,709
Inventories	1,564	1,589	1,433	1,613	1,844	2,175
Prepaid expenses	-	-	-	-	-	-
Other WCA	-	-	-	-	-	-
Cash and cash equivalent	60	135	128	427	442	538
Restricted cash	-	-	-	-	-	-
Short term interest earning investments	-	-	-	-	-	-
Other short term investments	-	-	-	-	-	-
Other current assets	339	38	49	49	49	49
Total current assets	**3,007**	**2,879**	**2,871**	**3,381**	**3,832**	**4,471**
Total assets	**7,111**	**6,594**	**6,466**	**9,471**	**9,288**	**9,307**
Liabilities						
Non-current liabilities						
Long term borrowings	506	30	176	2,676	2,076	1,476
Employee benefits	112	115	130	130	130	130
Other non-current liabilities	19	48	112	112	112	112
Total non-current liabilities	**637**	**193**	**418**	**2,918**	**2,318**	**1,718**
Current liabilities						
Accounts payable	1,083	1,043	870	1,271	1,454	1,616
Accrued expenses	-	-	-	-	-	-
Other WCL	-	-	-	-	-	-
Short term borrowings	24	23	32	32	32	32
Other current liabilities	1,738	1,785	1,520	1,520	1,520	1,520
Total current liabilities	**2,845**	**2,852**	**2,422**	**2,823**	**3,006**	**3,168**
Total liabilities	**3,482**	**3,045**	**2,840**	**5,741**	**5,324**	**4,886**
Equity						
Common equity	1,526	1,526	1,526	1,526	1,526	1,526
Preferred equity	-	-	-	-	-	-
Retained earnings	2,103	2,023	2,100	2,204	2,438	2,896
Other reserves	-	-	-	-	-	-
Minority interest	-	-	-	-	-	-
Total equity	**3,629**	**3,549**	**3,626**	**3,730**	**3,965**	**4,422**
Total equity and liabilities	**7,111**	**6,594**	**6,466**	**9,471**	**9,288**	**9,307**

Source: Company data, Asia Securities

Cash flow statement

In LKR mn	FY2013	FY2014	FY2015	FY2016E	FY2017E	FY2018E
Cash flows from operating activities						
EBITDA	**1,443**	**817**	**1,071**	**1,329**	**1,616**	**1,967**
Other non-cash items	-	-	-			
Change in working capital	(356)	(218)	(178)	189	(253)	(381)
Tax paid	-	-	-	(60)	(92)	(148)
Other	(2)	15	15	1	1	1
Cash generated from operating activities	**1,085**	**613**	**908**	**1,459**	**1,272**	**1,440**
Cash flows from investing activities						
Capex on PPE & intangibles	(228)	(312)	(322)	(3,323)	(212)	(246)
Proceeds from disposals	2	0	3	-	-	-
Net (acquisition)/disposal of subsidiaries	-	-	-			
Net (acquisition)/disposal of EMIs	-	-	-	-	-	-
Dividends received	0	0	0	-	-	-
Interest received	-	-	-	3	9	9
Other	12	781	10	-	-	-
Cash used in investing activities	**(213)**	**469**	**(309)**	**(3,320)**	**(203)**	**(237)**
Cash flows from financing activities						
Issuance/(repurchase) of common shares	-	-	-	-	-	-
Issuance/(redemption) of preference shares	-	-	-	-	-	-
Drawdown/(repayment) of debt	(456)	(308)	(111)	2,500	(600)	(600)
Dividends paid to common shareholders	(334)	(353)	(352)	(238)	(285)	(380)
Dividends paid to preferred shareholders	-	-	-	-	-	-
Interest paid	(257)	(202)	(127)	(102)	(169)	(127)
Dividends paid to minority interest	-	-	-	-	-	-
Other	1	1	1	-	-	-
Cash from financing activities	**(1,045)**	**(861)**	**(589)**	**2,160**	**(1,054)**	**(1,107)**
Net increase/(decrease) in cash	(173)	221	9	299	15	96
Cash and cash equivalent at BOP	48	(123)	98	107	406	421
Effect of exchange movements	2	1	(0)			
Cash and cash equivalent at EOP	**(123)**	**98**	**107**	**406**	**421**	**517**

Source: Company data, Asia Securities | EMI stands for equity method investments

Analyst Certification

I, Hasantha Uswatta, certify that the views expressed in this report accurately reflect my personal views about the company. I also certify that no part of my compensation was, is, or will be, indirectly or directly, related to the specific view or recommendation expressed in this report.

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Shiyam Subaulla	(94-11) 7722 011	0773-502 016	shiyam@asiasecurities.lk
Gagani Jayawardhana	(94-11) 7722 014	0714-084 953	gagani@asiasecurities.lk
Niroshan Rathnam	(94-11) 7722 006	0773-717 515	ratnam@asiasecurities.lk
Miflal Farook	(94-11) 7722 010	0772-253 730	miflal@asiasecurities.lk
Charith Perera	(94-11) 7722 015	0773-598 937	charith@asiasecurities.lk

Foreign Sales

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CSE Floor	CSE,01-04, World Trade Centre, Colombo - 1	Thushara Adhikari	(011)-5735 122	0773-688 202	adhikari@asiasecurities.lk
		Nuwan Eranga	(011)-5735 122	0777-368 0.12	eranga@asiasecurities.lk
Negombo	72/A,2/1 Old Chilow Road, Negombo	Uthpala Karunatilake	(031)-5676 881	0773-691 685	uthpala@asiasecurities.lk
		Gayan Perera	(031)-5676 881	0777-567 941	gayand@asiasecurities.lk
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