

ICRA Lanka reaffirms the [SL] A+ long-term ratings of Access Engineering PLC

September 26, 2016

Instrument	Amount	Rating Action
Issuer Rating	N/A	[SL]A+ with Stable Outlook reaffirmed
Senior Unsecured Redeemable Debenture Programme	LKR 5,000 Mn	[SL]A+ with Stable Outlook reaffirmed

ICRA Lanka Limited, subsidiary of ICRA Ltd, a group company of Moody's Investors Service, has reaffirmed the Issuer rating of [SL]A+ (pronounced S L A plus¹) with stable outlook for Access Engineering PLC ("AEL" / "the Company"). ICRA Lanka has also reaffirmed the Issue Rating of [SL]A+ for the company's LKR 5,000 Mn Senior Unsecured Redeemable Debenture programme.

While reaffirming the rating, ICRA Lanka has taken a consolidated view on Access Engineering PLC and its subsidiaries as a whole, given the operational and financial linkages among them. The reaffirmation of the rating takes into consideration the longstanding track record and established position of the Access group as a leading Engineering, Procurement and Construction (EPC) contractor in Sri Lanka. AEL has sizable experience in the design and construction of Roads & Bridges, Medium-Rise Buildings, as well as foundations & sub-ground work for high-rise buildings. Further, AEL also has varied experience of undertaking EPC works in engineering segments such as water infrastructure, telecommunications, ports, airports, etc. The rating also takes into consideration the professional management team of the company, their healthy relationships with various stakeholders in the construction industry; and, the recently implemented MIS systems which aid in real-time project tracking and implementation. These apart, the rating also factors in AEL's healthy financial profile backed by its comfortable profitability, and the healthy capitalization with relatively lower gearing levels.

AEL (Consolidated) operates mainly in four sectors i.e. Civil Engineering, Construction Material, Commercial Real Estate, and Automobile dealership. For the FYE March 2016, Civil engineering segment contributed to approximately 67% of AEL's revenues, while the auto dealership segment contributed 23%, construction materials segment contributed to 9% and the remaining 1% was contributed by the commercial real estate operations of AEL. The company currently has a moderate order book of LKR 29 Bn. Some of the larger projects currently being handled by AEL include "Rehabilitation & Improvements to Colombo - Kandy Road section from Kadawatha to Nittambuwa" awarded by the Road Development Authority (RDA) and Towns East of Colombo District Water Supply Project awarded by National Water Supply & Drainage Board (NWSADB) and the "Construction of Housing for Relocation of under Served Settlements at Henamulla [Phase II]" awarded by the Urban Development Authority (UDA).

The construction sector in Sri Lanka experienced a slowdown during the previous year FY2014-15, amidst the uncertain macro environment in Sri Lanka; the government had placed some of the orders received by AEL under review and as such, these projects could not be executed. However, during this period, AEL's financial performance has not been negatively affected due to limited dependency on government projects that were funded through the central treasury. The Private Public Partnerships (PPPs) and Joint Ventures (JVs) that were undertaken by the company have supported the performance during the period under review. Currently, the projects that were suspended for reviews have been

¹ For complete rating scale and definitions please refer to ICRA Lanka's Website www.icralanka.com or other ICRA Rating Publications

reinstated. In addition, the government has introduced new mega development projects including megapolis development plan and elevated highways, etc. Thus, AEL being a leading construction company in Sri Lanka, is expected to benefit from these mega developments in the medium term. The currently ongoing order book of AEL has increased to LKR 29 Bn from LKR 24 Bn in the previous year. The ability of the company to manage its currently ongoing order book position and grow the business prospects along with the expected recovery of the construction sector, remains as a key rating sensitivity of the reaffirmed rating.

AEL records comfortable operating profit margins from its construction segment of around 20%, from its construction materials segment of around 25%, from its commercial real estate segment of around 95%, from its auto dealership 10-15%, and its Hotel/resorts construction segment of around ~7-10%. Both the auto-dealership as well as the construction of hotels & resorts are very competitive businesses in Sri Lanka and hence, the margins are moderated in these businesses.

ICRA Lanka also notes, notwithstanding the company's healthy gearing and coverage indicators in the past, the working capital requirements are sizable and could expose AEL to liquidity risk in case of increasing commitments towards larger projects and increasing scale of operations. AEL's working capital intensity has been moderately high albeit a noticeable reduction in FYE March 2016. The working capital position has been largely driven by elongated receivables position, typically around 100-130 days. The company maintains raw material inventory of around 30-45 days generally. In addition, claims and variations are recorded as work-in-progress until they are accepted by the employer.

Backed by relatively stable working capital intensity and comfortable profitability margins in the past, and coupled with the sizable proceeds from the debenture program of LKR 5 Bn in FYE March 2016, AEL has been able to maintain strong capitalization matrix with relatively low gearing level at the standalone level. Further, it had sizable cash & liquid investments of ~ LKR 5.8 Bn as on June 30, 2016 (at the consolidated level) which could be utilized towards additional working capital requirements or future business acquisitions. AEL's subsidiaries – Access Realities, Sathosa Motors and Access Projects together had total borrowings to the extent of LKR 641.3 Mn. Access Realities and Sathosa motors have well established operations with positive cash flows and adequate debt servicing ability and hence no financial support is anticipated towards these businesses.

In addition to the company's earlier investments in the Horizon Holdings Pvt Ltd, AEL, has recently, invested LKR 800 Mn in Blue Star Constructions (Pvt) Ltd, a real estate company to penetrate into the condominium real-estate segment. ICRA Lanka expects that the company's financial support & commitments for these newly started operations in the short to medium term is likely to be high amidst its limited experience in such business operations. Therefore, the ability of the company to turnaround these investments in the medium term, whilst driving positive synergistic benefits from the company's strong construction segment, remains to be seen.

Company Profile

Access Engineering PLC (AEL) started its operations in 2001 as the Engineering, Procurement & Construction arm of the Access Group. Promoted by Mr. Sumal Perera, Mr. Christopher Joshua, and Mr. Ranjan Gomez, the Access group also has presence in telecom, healthcare, power & renewable energy, and information technology in addition to the aforesaid businesses under AEL and its subsidiaries. Over the last 15 years, AEL has become one of the leading players in the Civil Engineering and Construction industry of Sri Lanka. The Company was listed on the Colombo Stock Exchange in March 2012 following an initial public offering. Since then, AEL has grown sizably with acquisitions of businesses, and through expanding its presence in construction, real estate and other segments. In February 2012, Access Engineering acquired Sathosa Motors PLC (Sathosa), which holds the franchise for Isuzu commercial vehicles. Also, Sathosa's subsidiary - SML Frontier Automotive (Pvt.) Ltd. – is the

sole agent for Land Rover in Sri Lanka. This apart, Access Realties (Private) Limited, which owns a commercial office property - 'Access Towers' - and its subsidiary, Access Realties 2 (Private) Limited, which is developing another commercial property - "Access Tower II", are fully-owned subsidiaries. In FYE March 2016, the Company has invested in Horizon Holdings Ventures Pvt Ltd, Horizon Knowledge City Limited and Horizon Holdings (Pvt) Ltd- These companies together own 21 acres of property in the Malabe Information Technology Zone, which is expected to be developed on a staggered basis. The company has recently invested LKR 800 Mn in Blue Star Constructions (Pvt) Ltd, to penetrate into the condominium real-estate segment.

For the FYE Mar-2016, on a consolidated basis, AEL reported a net profit of LKR 2,550.8 Mn on a revenue of LKR 17,624.6 Mn, as compared to a net profit of LKR 2,423.9 Mn reported on a revenue of LKR 16,514.1 Mn in FYE Mar-2015. For the 3M ending FYE Mar-2017, on a consolidated basis, AEL reported a net profit of LKR 531.6Mn on a revenue of LKR 4,648.6 Mn.

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