ICRA Lanka reaffirms the [SL]BBB+ issuer rating of E B Creasy & Company PLC

June 22, 2018

Instrument*	Current Rated Amount (LKR Mn)	Rating Action
Issuer Rating	N/A	[SL]BBB+ with Stable outlook reaffirmed

Rating action

ICRA Lanka Limited, Subsidiary of ICRA Limited, Group company of Moody's Investors Service has reaffirmed the Issuer rating of [SL] BBB+ (pronounced S L triple B plus[1]) with stable outlook assigned to E.B. Creasy & Company PLC ("EBCR"/ "the Company").

Rationale

ICRA Lanka has taken a standalone view on EBCR given the very low dependence of the Company on its subsidiaries (dividends/advances) and the absence of contractual obligations to support group entities which are currently reporting losses/recovering from past financial losses. The Group's strong corporate governance policy to maintain priority of the cash flows required for meeting EBCR's debt obligations and growth needs over that of its subsidiaries and to restrict intercompany borrowings, provides additional comfort. Moreover, ICRA Lanka takes the comfort from the recent Group shareholding restructuring exercise, which has resulted in a reduced direct investment in Lankem Ceylon PLC (Lankem). Lankem is now being treated as an associate company since Q4FY2018 (as against a subsidiary) and this has helped E B Creasy Group to improve its profitability indicators.

The reaffirmed rating primarily factors in the Company's strong brand name, leading market share in the highly stable consumer product segment, and the launch of new product categories for untapped markets. The company has a growing marketing & distribution segment - the main products being marketed and distributed under this segment include 3K batteries, generators, fork lifts and renewable energy products (such as net metering systems and solar water pumps). EBCR's financial profile is healthy, characterized by stable accruals, relatively comfortable capital structure and coverage metrics and adequate liquidity position supported by readily marketable securities, (where the market value is relatively higher than the cost of investments). ICRA Lanka also takes into account the experience of the promoters, the Company's strong track record and reputation in the industry which have helped the company to enjoy steady access to funding both from the capital markets as well as financial institutions that have supported its growth over the years. The Company's professional top management team coupled with strong corporate governance structure adds further comfort for the rating.

These rating strengths are moderately offset by the high competition prevalent in the consumer product segments from incumbents and as well as new entrants which moderates pricing flexibility and the high dependence on few major brands which exposes revenues to concentration risks (although, the company's business risk is diversified through Group subsidiaries to an extent).The company's revenues and profits are vulnerable to foreign exchange risks (given the large dependence on imports which are not hedged

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

fully) and the regulatory risks such as imposition of new taxes. The company's recent investments in Lanka Special Steels Limited, Candy Delights Ltd and the new investment in centrifuged medical latex products business would further diversify the business risks. However, as Group companies (including the newly setup operations) operate as independent entities, these investments are expected to be largely funded at standalone levels and hence, the company's financial commitments towards its group companies are limited to a larger extent.

While EBCR has a firm policy in place which greatly restricts intergroup transactions, ability of the Company to strictly enforce the same coupled with ability to diversify its own income streams would be key sensitivities to the rating. While the Company's financial profile is comfortable, EBCR is presently dependent on short term loans to fund its working capital position, as operating cash accruals have been invested for capital expenditure requirements. Ability of the Company to reduce reliance on short term debt and align cash flows in line with investment (fixed and working capital) requirements would be the other sensitivities to the rating.

Key rating drivers

Credit strengths

Experience of the promoters and the strength of the Group: Over the years, EBCR has grown by strategic acquisitions and now constitutes a diversified group with 40 subsidiaries which are in manufacturing of FMCG products, import/export of agricultural inputs/commodities, distribution and freight forwarding, trading of chemicals/auto components and power equipment (solar), managing hotels and plantations. The Colombo Fort Land & Building Company PLC (CFLB) is the parent company of E B Creasy & Company PLC (holding 52.98% stake), with EBCR accounting for approximately 97% of the revenue in FYE2017 and nearly 70% of the net profits of CFLB. Thus, EBCR is strategically important to the Group.

Lankem Ceylon PLC (LCEY) (including its subsidiaries) was EBCR's largest subsidiary contributing to 68% of the Group revenues in FYE2017. LCEY is engaged in the manufacturing and distribution of Agro Chemicals, Decorative Painting products, Industrial Chemical & Bitumen Products, and FMCG products. LCEY has been reporting financial losses over the past few years mainly due to negative performance of their Agro Chemical segment amidst the adverse weather conditions that prevailed in the country and the stringent regulatory environment in the agro chemical industry. However, during Q4FY2018, Lankem Ceylon PLC has concluded a rights issue and this was largely subscribed by CFLB (including the rights issue entitlements of EBCR). Therefore, post the rights issue, EBCR's direct investment stake in Lankem has declined to 32.4% from 45.5%. This has led the company to treat Lankem Ceylon PLC as an associate company rather than a subsidiary.

Strong brand name and dominant market share in a highly stable consumer product segment lends stability to the business profile: The Company is a market leader in several consumer product categories and enjoys healthy margins from most of the product categories. The BIC brand is a globally renowned brand and given the preference of disposable razors in Sri Lanka, BIC is also a leading product in Sri Lanka. The company's joss stick products, marketed under the brand name of Amritha, and Denta tooth brush are other key products of the company. Ninja mosquito coils is another leading product and under the Ninja Brand, the company has a leading market share in the mosquito coil market. The company intends to further strengthen the growing segments of mosquito repellent products such as mosquito liquid vaporizers, aerosol, and refills product segments, which have a higher demand in the urban areas.

Healthy financial profile marked by stable accruals, relatively comfortable capital structure and coverage metrics: The Company has maintained a healthy revenue growth in excess of around 10% or more overall for the last several years. This has been on the back of sustained brand building efforts which have enabled the Company to garner a large share of the product segments it is present in. During FY2017, the company's operating income has increased noticeably by YOY 16.2% to LKR 4,286 Mn. This is largely attributable to the growth in key product categories such as Amritha, BIC, Denta, Ninja and others. However, during 9MFY2018, the revenue contribution from some of the key product categories such as Amritha, BIC and Denta have slowed down due to growing competition under these product categories in Sri Lanka as well as the impact from the increased VAT. During FY2017 and 9MFY2018, the company has recorded a profit after tax of LKR 383 Mn and LKR 104 Mn respectively.

The company's gearing levels has been at ~0.9-1.1(x) over the past few years. Moreover, the Company's coverage and key debt metrics are also relatively comfortable given the debt levels on the books as compared to the profits generated. Going forward, the overall capital structure and credit profile is expected to remain healthy given the relatively stable industry outlook, healthy market share which would help sustain revenues/profits and the Company's conservative policy in terms of leverage and group support. During 9MFY2018, the company's working capital intensity has further improved as the company's inventory holding has reduced noticeably notwithstanding the increased intercompany trade receivables from Darley Butler & Company Limited, after the company has changed its repayment policy with Darley Butler & Company since Sep CY2014.

Credit challenges

High competition from incumbent as well as new entrants hinders pricing flexibility to a large extent and undercuts the stable market segments: Although, the BIC brand is the market leader in disposable razor market in Sri Lanka, BIC has faced increased competition from Gillette which is the largest disposable razor producer in the world. Similarly, other key products such as Denta, Amritha and Ninja have faced increased competition from the established local/international players in Sri Lanka.

Despite the strong market share across product segments, the competitive pressures from incumbents and new entrants severely restrict pricing flexibility. However, with the lower price ticket size of key product categories, the company could pass on the cost increases to consumers over the short to medium term and the same is not expected to adversely affect the company's market share given the strong brand equity of the key consumer product categories.

High dependence on few major brands (albeit leading brands) exposes revenues to concentration risks: Despite the company's leading product categories and healthy profitability, the Company's revenues are largely concentrated on few major brands/products such as BIC, Ninja, Denta and Amritha with those four products accounting for over 85% of the company's revenues. In order to mitigate the revenue concentration risk, the company has started expanding the scope of these products, and focuses more on indigenous/private label products to diversify its revenue streams. The company's ability to achieve this, would be key towards improving the business risk profile over the medium term. The same would also enable the company to enter into higher margin segments, where competitive pressures would be lesser and hence, mitigate the risk of dependency on few products/brands.

Company's exposure to foreign currency and other macroeconomic volatilities; The macro economic conditions such as increasing interest rate, depreciation of Sri Lankan rupee and other policy directives of the consumer markets, would likely have an impact on the overall performance of the company. Given the lower price ticket size of key product categories, the company would be in a position to pass on the price increases to the consumers over a short/medium term period, and therefore, the profitability margins would be affected to an extent during such periods.

Underperformance of Group companies: During 9MFY2018, the financial performances of some group companies were negatively affected. The Group has invested ~LKR 210 Mn (funded by debts at the subsidiary level) for their confectionary operation under Candy Delights Ltd to further upgrade the technology in the manufacture of new confectionaries. Due to the above investment, the financial performance of Candy Delights was affected negatively during FYE2018. Similarly, during this period, the financial performance of Laxapana Batteries PLC was affected to an extent due to changes in its product strategies. During this period, Lankem Ceylon PLC, the new associate company of the group, has sustained further losses owing to several reasons including adverse weather conditions and regulatory related issues with the agro chemical segment. However, Lanka Special Steel Pvt Ltd has performed well during 9MFY2018 due to increased order book position. Therefore, going forward, ICRA Lanka will continue to monitor the financial performance of the group companies.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria: *www.icralanka.com/images/pdf/Corporate%20Rating%20Methology.pdf*

About the company:

Established in 1878, E B Creasy & Company PLC ("EBCR"/"the Company"), was converted to a limited liability Company and listed on the Colombo Stock Exchange in 1968. It is one of the oldest companies in Sri Lanka. The company is among the pioneers of the Ceylon Chamber of Commerce having joined it in 1890. Over the years, EBCR has expanded by organic growth as well as by strategic acquisitions and now constitutes a diversified group. The Company on a standalone basis manufactures, markets and distributes a range of homecare, personal care and household products. The range offered include imported and manufactured disposable razors, toothbrushes, mosquito coils, mosquito liquid vaporizers, coconut shell powder, wood powder and torch/automotive batteries. Besides, own operations, the Company also acts as the key holding company for the Group.

Group Financial Profile:

On a consolidated basis, for the FYE 2017, EBCR reported a net loss of LKR 463 Mn on a total income of LKR 26,346 Mn compared to a net profit of LKR 242 Mn reported on a total income of LKR 24,924 Mn in FYE2016. During 9M ending FYE2018, EBCR has reported a net loss of LKR 519 Mn on total income of LKR 18,918 Mn compared to a net loss of LKR 361 Mn on total income of LKR 19,028 Mn in the same period of FYE17.

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