

## ICRA Lanka reaffirms the issuer rating of [SL]A+ with Stable Outlook for JAT Holdings PLC

*September 13, 2021*

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

### Rating action

ICRA Lanka Limited has reaffirmed the Issuer rating of [SL]A+ (pronounced S L A plus) with Stable outlook for JAT Holdings PLC ("JAT"/"the Company").

### Rationale

The rating reaffirmation primarily factors the Company's dominant position in the Sri Lankan wood coating industry, strong brand equity, strong financial profile, and envisaged revenue diversification through the global expansion. The Company is the largest partner globally for the Sayerlack brand of Sherwin Williams. The Company has exclusive distribution rights for south Asian and African regions. JAT Holdings PLC has the highest market share in the Sri Lankan overall wood coating sector, despite competition from incumbent and new multi-national companies (MNC) due to the strong brand equity and higher-quality standards. Moreover, JAT has been operating in Bangladesh since 2001. This has enabled the Company to establish a significant market share and brand equity in Bangladesh. The Company's revenues declined by 14.9% in FY2021 because of the drop in revenue from furnishing solutions projects amidst the COVID-19 pandemic; however, strong performance in the local wood coating market together with new products that have been introduced has helped the Company sustain its profitability during FY2021 and Q1FY2022. The local wood coating market performed well due to the increased market share of the Company. The market share increased due to the expansion of the water base market and the Company penetrating the market of the financially weaker competitors during the pandemic. With the proposed state-of-the-art research center, the Company would expand the product range and improve the margins in the future. The Company raised LKR 1,507 Mn as fresh equity from the Initial Public Offering (IPO) in July 2021. The funds received from the IPO have strengthened the capital structure and the liquidity profile of the Company. The Company has already begun to expand its operations by investing in a manufacturing plant in Bangladesh in FY2022 and plans to set up a manufacturing plant in East Africa in FY2023. While the entire investment will be funded using the IPO proceeds, the Company has already used the foreign currency available through its retained earnings of its Export Company, namely JAT Exports DMCC, established in Dubai to transfer the required funds for the expansion in Bangladesh. The new manufacturing plant in Bangladesh will enable the Company to increase its market share in Bangladesh by offering a wider range of products at competitive prices, with a primary focus on its J Chem brand of wood coatings being sold in Bangladesh currently. The expansion will enable the Company to diversify its revenue base geographically.

The rating also factors in the weaker macro-economic conditions that prevail in the country, affecting the demand for housing and construction sectors. It also considers the Company's stretched working capital position due to the build-up of inventory to carry out operations without any disruptions during the current challenging times.

## Outlook: Stable

The Stable Outlook reflects ICRA Lanka's belief that company will continue to maintain its strong market position and healthy financial profile, despite the weaker macro-economic conditions.

## Key Rating Drivers

### Credit strengths

**Experience of the promoter/s and the management:** The experience of the promoter/s, the Company's strong track record and the reputation in the industry have enabled the Company to enjoy steady access to funding from financial institutions. The Company's professional management team coupled with relatively strong governance structure adds further comfort to the rating.

**Leading market share and strong brand equity:** JAT is synonymous with the water-based wood coating market in Sri Lanka due to strong brand equity as well as higher-quality standards of the Sayerlack products. Currently, JAT dominates the water-based premium wood coating market in Sri Lanka. In addition, JAT's other brands also enjoy strong brand equity with Harris dominating the brush market, and SEA Bauformat dominating the luxury kitchen units in the retail and mega projects markets in Sri Lanka. The core product segments of JAT, particularly Sayerlack wood coating products, enjoy relatively high gross margins, resulting in strong profitability for the Company. In FY2021, the local wood coating segment reported a gross profit margin of 46.3% compared to 43.8% in FY2020. The same moderated to 41.5% in Q1FY2022 due to increased raw material price due to exchange rate depreciation. Relatively high gross profit margins are attributable to strong brand equity that JAT commands, as most of the premium products sold by the Company are relatively less susceptible to the price competition in the industry. As a lateral diversification strategy, with the state-of-the-art Research and Development Center to be commissioned, which is an expansion of the existing Research and Development facility, the Company intends to introduce new wood coating product categories to penetrate into various wood coating segments. The Company has increased its market share of the wood coating segments during FY2021 as it benefitted from the cash flow constraints experienced by its financially weaker competitors. ICRA Lanka also draws comfort from growth opportunities in the wood coating market of Sri Lanka.

**The diversification Strategy:** The Global expansion into Asia and Africa will further diversify JAT's revenue base in the medium term. The proposed investment in manufacturing plant in Bangladesh and East Africa over the next two years will enable the Company to expand its presence in these regions. The rating also considers the Company's diversified product portfolio including ceiling products, Harris paint brushes, admixtures, and interior and living space products such as SEA, Herman Miller, Armstrong, etc. The Company has introduced "WHITE by JAT" to penetrate the decorative paint market through a unique online product offering. This will help the Company to scale up its non-core product segments. During FY2021, although some of the Company's non-core business segments and export markets have slowed down, the increased revenue contribution of the core products helped the Company to cushion this impact to a larger extent. The Company's key export market, Bangladesh, experienced a slowdown in H1FY2021 due to lockdowns imposed due to COVID-19 Pandemic. The Bangladesh market recovered strongly in H2FY2021 with the opening up of the country. Notwithstanding the Company's ongoing diversification initiatives, the Company's dependency on wood coating products of Sayerlack remains at a relatively high level. However, ICRA Lanka also notes that JAT is the largest exclusive partner for Sayerlack brand, for the South Asian region. Considering the established mutual relationship between JAT Holdings and Sherwin Williams, and the strategic nature of the tie-up with the supplier, ICRA Lanka views the risk of dependency on Sayerlack products by JAT as moderate.

**Comfortable Financial Profile:** JAT's Operating Profit Margin (OPM) improved marginally to 14.1% in FY2021 from 13.8% in FY2020 due to higher share of revenues from the local wood coating segment, which commands higher margin. In Q1FY2021, OPM improved further to 14.9% due to reduced overheads. JAT has recorded a PAT of LKR 161.6 Mn in Q1FY2022 compared to the 12 months performance of LKR 600.4 Mn in FY2021 Mn and LKR 707.1 Mn in FY2020. The Company's capital structure is comfortable on account of healthy internal generation and relatively low debt level. The Company also raised LKR 1,507 Mn through an IPO in Jul-20. This will enable the Company to fund Capex using equity and maintain a comfortable capital structure in the medium term. The debt profile of the Company is skewed towards short-term loans for working capital requirements. The Company is free of term debt at the standalone level, and the consolidated entity has less than 5% term debts. The Company's debt indicators remain healthy amidst the lower debt levels and comfortable operating profit margins.

## Credit challenges

**Cyclical nature of the construction industry and relatively high working capital intensity:** Since the demand for the Company's core product categories is driven by the growth in the local construction industry, the macro-economic conditions such as the depreciation of Sri Lankan rupee and import restrictions that have been imposed, would likely have an impact on the overall performance. The furnishing solutions and projects segment reported a drop in revenue in FY2021 due to delays in mega real estate projects because of the labour force and supply-chain disruptions experienced due to the pandemic. However, most of the mega real estate projects have resumed in the past few months. Since most of the order book in furnishing solutions and projects segment consists of projects approved by the Board of Investment, Sri Lanka (BoI), the impact of import restrictions on the Company's revenue would be minimal. Due to exchange rate depreciation and import restrictions, the Company is building inventory to carry out operations without disruption during this challenging period. As a result, the Company's working capital position remains overextended. ICRA Lanka expects this to moderate in the medium term.

**Competition:** The painting industry is generally characterized by intense competition from a larger number of competitors in Sri Lanka. Moreover, during the past three years, new players have also entered the local painting industry. The competition has moderated post the pandemic due to cash flow issues faced by some of the weak competitors. However, Sayerlack products have strong brand equity compared to that of the competitors. Moreover, established distribution network and manufacturing setup gives JAT an edge over its competitors.

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

**Links to applicable criteria:** <https://www.icralanka.com/corporate-rating-methodology>

## About the Company:

The Company was Incorporated in 1993 and was listed on the Colombo Stock Exchange on August 12, 2021. JAT Holdings PLC is a dominant player in the Sri Lankan wood coating, decorative painting, and interior living spaces market segments. The Company has a commanding market position in the Sri Lankan wood coating industry, mainly due to its brand equity. While wood coating products are its core business segment, the Company has successfully ventured into adjacent market segments, such as decorative paints, paintbrushes, furniture accessories, and interior products. JAT has the competitive advantage of being the sole distributor and marketer for Sayerlack premium wood coating products for selected countries in the Asian and Africa regions. The exclusive distribution rights have enabled JAT to rapidly grow its export sales in much larger markets such as Bangladesh and India. In addition to its core wood coating and

decorative products, JAT envisages to position itself as the leading player in the broader interior and living spaces market. The Company has taken some strategic initiatives, including introducing SEA luxury kitchen units, Herman Miller premium furniture, and Armstrong architectural products to the Sri Lankan market.

### Key financial indicators (audited)

<i>Revenue and profitability indicators</i>					
<i>Figs are in LKR Mn</i>	FY18	FY19	FY20	FY21	*Q1FY22
Operating Income	5,446.7	6,547.2	6,295.5	5,359.5	1,395.7
OPBDITA	751.0	1,136.9	885.0	770.0	207.7
PAT	634.8	881.0	707.1	600.4	161.6
NWC / OI (%)	55.8%	60.6%	59.0%	63.1%	71.7%
Total Debt	977.5	1,407.1	879.3	502.1	949.1
Networth	3,830.9	4,568.7	4,968.1	5,344.9	5,401.7
Gearing (x)	0.26	0.31	0.18	0.09	0.18
OPBDITA/Interest & Finance Charges (x)	6.35	8.80	6.65	9.28	9.62
Total Debt/OPBDITA (x)	1.30	1.24	0.99	0.65	1.14

Note; Gearing-(Total Debts/ Networth),\*-Unaudited

### Rating history for last three years

Instrument	Current rating (FY22)		Chronology of Rating History for the past three years			
	Type	Amount Rated (LKR MN)	Date & Rating in Sep-21	Date & Rating in Sep-20	Date & Rating in Sep-19	Date & Rating in Sep-18
Issuer rating	N/A	N/A	[SL]A+ (Stable)	[SL]A+ (Stable)	[SL]A+ (Stable)	[SL]A+ (Stable)



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