

CABLE SOLUTIONS LIMITED
Initial Public Offering
Report date: 16.07.2024

Size of the offer	LKR 605,899,500 <ul style="list-style-type: none"> - Offer for subscription LKR 109,999,500 - Offer for sale LKR 495,900,000
No. of shares to be issued	80,786,600 <ul style="list-style-type: none"> - Offer for subscription 14,666,600 - Offer for sale 66,120,000
Price per share	LKR 7.50
Stake on offer	17.16% on post-IPO shareholding
Objectives of the offer	<ul style="list-style-type: none"> - LKR 90Mn for investment in Singcheer's 600EXJ80/50 Extrusion Line which is a high-speed, semi-automated machine for automotive and solar cables, replacing the low-efficiency old model - LKR 20mn to be utilized for working capital purposes
Issue opening date	23 July 2024
Board to be listed	Diri Savi Board
Auditors to the offer	BDO Partners

Company Overview

Cable Solutions Limited (CSLK), established in 2008, is a major provider of comprehensive cable solutions. Its main production facility is located in Kadawatha, Sri Lanka. CSLK has opened a new production facility in Chennai, India to improve capacity and meet the expanding demand for cables. The company exports high-quality cables and harnesses to numerous countries, including the USA, Germany, India, Russia, Spain, Switzerland, Sweden, Maldives, and Australia, among others. Approximately 94% of their revenue is generated from exports.

As a leading exporter, CSLK benefits from the strategic backing of ACL Cables PLC (ACL). In 2019, the company became part of the ACL group following the purchase of a 75% stake by a consortium of investors led by ACL. Since then, CSLK has been a 52.64% held subsidiary of the ACL Group. The company has earned multiple international quality certifications, including ISO 9001:2015, ISO 14001:2015, and TUV Rheinland certification, demonstrating a commitment to quality, environmental standards, and sustainability.

Strengthening its global operations, the CSLK group was formed in January 2023 with the acquisition of a 99.9% stake in Cable Solutions Private Limited, India (CSIN). Specializing in designing, manufacturing, and distributing high-quality cables, CSLK offers a range of solutions, including standard cables, customized cables and cable systems, cable harnesses, and connectors. Their varied portfolio caters to the evolving needs of customers seeking reliable and efficient cable systems.

The products offered by CSLK include coaxial cables, power cables, communication cables, automotive cables, fire alarm cables, high-temperature cables, control and instrumentation cables, load-cell cables, and composite cables. They serve various target industries such as power, automotive, electrical, weighing and sensory, aerospace, and building management systems. A key differentiating aspect of the company is its strong R&D and engineering capabilities, enabling CSLK to customize cables to meet the diverse requirements and specifications of its international client base.

CABLE SOLUTIONS LIMITED**Initial Public Offering****Investment highlights****Export revenue is 94% of total revenue**

CSLK's revenue from exports is predominantly in USD, which provides a stable income stream less affected by local economic fluctuations. As per the management of CSLK, their export revenue distribution is 50% to the global market, 35% to Western Europe and 15% to India, reflecting a well-diversified market presence.

Local listed peers such as Kelani Cables PLC (~18% export revenue), ACL Cables PLC (~31% export revenue) and Sierra Cables PLC (~12% export revenue) predominantly focus on the domestic market, while CSLK derives ~94% of its revenue from exports. Consequently, the end markets targeted by local peers and CSLK differ significantly.

Direct exports account for ~45% of CSLK's export revenues, while deemed exports make up ~49%. Over the forecast period (FY25F to FY29F), direct export sales are projected to increase by a CAGR of 10.2% and deemed export sales by 8.5%. CSLK's management expects the revenue targets to be met without any need for additional expansion of their current factory capacity.

Focused on a diversified range of high-growth industries

While local peers are heavily invested in the construction and telecommunication sectors, CSLK serves a border range of industries requiring specialized cables minimizing their exposure to industry-specific risks. This includes high-growth industries such as power, automotive, electrical, weighing and sensory, aerospace, and building management systems.

Product specification

CSLK specializes in customized products tailored to the specific requirements of a global customer base, necessitating significant investments in R&D and operational expertise. This distinguishes CSLK from local peers, who focus on generalized products for the domestic market.

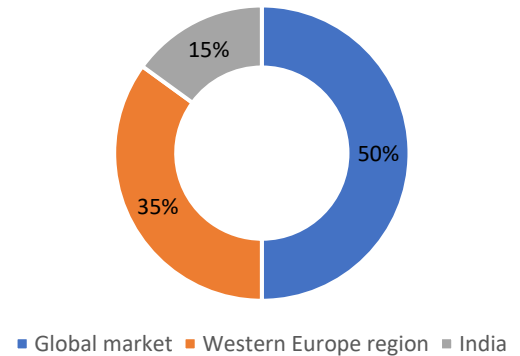
Exclusive export advantages through BOI registration

CSLK pays tax at a concessionary rate of 15% due to the special status under the Board of Investment (BOI) Act. Specifically, the company pays a 15% tax rate on export and deemed export income, and a 30% tax rate on local income. In contrast, CSIN is subject to a 10% tax rate. The basis of tax is on the taxable profit allocated as percentages of sales categories.

Key customers, who are long-standing and established

CSLK competes effectively in the global customized cable market, boasting a proven track record with over 30 long-standing customers. Approximately 76% of the company's total revenue comes from 10 key customers. The high cost of switching suppliers ensures customer retention and long-term business relationships. It's important to note that company orders are facilitated through extensive business-to-business (B2B) channels, which CSLK has developed and maintained over a significant period. The high switching costs for clients arise because CSLK's products have been approved by their customers for inclusion in their final products.

Export revenue distribution



Sources: KPMG independent valuation

CABLE SOLUTIONS LIMITED**Initial Public Offering****Strategic Synergy with ACL Cables**

The partnership with ACL Cables PLC has allowed CSLK to capitalize on ACL's established customer base, enabling further growth in the export market. Also, this partnership facilitates joint procurement of raw materials, streamlining costs in product sourcing, with ACL focusing on raw material acquisition and general cable products, while CSLK concentrates on R&D and tailored cable solutions.

Financial strengths

Company's Return on Equity (ROE) was reported at 29%-32% in FY22-FY23 and dropped to ~13% in FY24. This drop was primarily due to the recessionary environment in Europe, which accounted for ~35% of the company's revenue. CSLK's management expects a positive uptick from this region in the current financial year, expecting ROE to stabilize around 20% from FY25F to FY29F.

CSLK's net profit margin was at 13%-17% in FY22-FY23 but fell to ~9% in FY24 for the same reasons. A recovery in Europe is expected to help the margin stabilize around 13% from FY25F to FY29F.

CSLK's debt-to-equity ratio averaged 27% over the past three years and is expected to remain between 5%-12% during the forecast period from FY25F to FY29F.

Inventory days are projected to stabilize at 120 due to easing supply constraints and better economic conditions in Sri Lanka. The working capital balance is expected to average USD 4.20Mn from FY25F to FY29F, reflecting improved liquidity and operational efficiency.

Investment risk**Dependence on imported raw materials**

Copper is the key raw material for CSLK, representing 55% of total expenses and making up a significant portion of the cost of sales, which constitutes 70% of total expenses. Company's operations are heavily influenced by fluctuations in the global prices of copper, as well as the stability of supply chains from international markets.



Sources: www.investing.com

CABLE SOLUTIONS LIMITED**Initial Public Offering****Global bulk shipping rates are heavily volatile due to geopolitical incidences**

Global bulk shipping rates are highly volatile due to geopolitical incidents, which can impact CSLK's costs and profitability margins. The shipping costs are heavily volatile at present, reflecting the ongoing crisis. In late 2023 and early 2024, shipping costs have surged notably, especially for journeys to North America, Europe, and the Mediterranean, due to the persistent Houthi assaults on ships in the Red Sea and the drought's influence on the Panama Canal.

Risk of delay in procuring the new machinery

The machinery specified under the IPO objective needs to be imported from China. There is a potential risk of new import restrictions being imposed due to fluctuations in foreign currency within the country. However, considering the recent economic recovery and Sri Lanka's alignment with the IMF program, CSLK's management does not anticipate any significant change in the existing policies.

Risk of LKR depreciation against foreign currencies

Since the expenses for purchasing the machinery will primarily be in USD, any depreciation of the LKR between the raising of the IPO proceeds and the utilization of the proceeds as per the timeline will decrease the USD funds available. This will increase the estimated cost of the machinery, impacting the viability and profitability of using the asset.

Industry overview

The specialized cable manufacturing industry is poised for growth due to increased urbanization, industrialization, adoption of renewable energy and technological improvements contribute to an increased need for specialized cables.

Recent economic indicators suggest a rebound in the global economy, with GDP expected to reach levels of 2.5% to 3.5% and inflation rates of 3% to 5% during the forecasted period from FY25F to FY29F. Similarly, the Western European region is projected to recover to pre-pandemic levels, with GDP expected to range from 1% to 2% and inflation rates from 1.5% to 2.5% over the same period. These trends could potentially benefit CSLK by stimulating increased demand for their products.

Compared to the pre-pandemic year (2019), there has been robust growth in household consumption, with global consumption increasing by 11%, Western Europe by 5%, and India by 20%. According to the KPMG analysis, there is a positive correlation between the revenues of the largest listed cable operators and global GDP (+0.75) as well as household consumption (+0.55). Therefore, the expected rebound in household consumption patterns, particularly in emerging economies, India and developed economies in Western Europe, may significantly contribute to the increased demand for CSLK's product offerings in the coming years.

According to the KPMG valuation report, in the near term, the copper supply gap is expected to decrease, which may prevent significant price increases. Looking ahead, the London Metal Exchange (LME) forecasts a slight increase in the supply-demand gap for copper by FY27, driven by recovering industrial activities. This trend could exert upward pressure on prices over the longer term.

According to KPMG's analysis, global bulk shipping rates are nearing pre-pandemic levels (Baltic Dry Index (BDI) in the range of USD 1200-2200) and are expected to continue with slight increments. This could be

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identified as a positive indicator suggesting that CSLK's logistics costs may decrease to pre-pandemic levels, potentially improving profit margins.

Valuation
Valuation summary

Valuation summary of three methodologies	Value per share (LKR)	Offer price (LKR)	Discount/(Premium)
Discounted cash flow approach	10.30	7.50	27.30%
Multiples approach - comparable companies	15.30	7.50	50.90%
Net asset value approach	3.70	7.50	-102.5%

Based on reported financials	EPS (LKR)	NAVPS (LKR)	PE	PBV
31st March 2023 (audited)	1.18	3.76	6.37	1.99
31st March 2024 (unaudited)	0.46*	3.61	16.22	2.08

*The decline in PAT is attributable to the recession in the Europe region.

DCF Valuation

All figures in USD'000, unless otherwise stated

Financial period ended	FY24F (3MF)	FY25F (12MF)	FY26F (12MF)	FY27F (12MF)	FY28F (12MF)	FY29F (12MF)	Terminal period
EBIT (1- t)	177.85	1,281.38	1,389.79	1,627.02	1,862.88	2,150.94	2,150.94
Add: depreciation and amortization	123.02	428.51	438.53	417.14	406.71	240.17	240.17
Add: non-cash expenses	10.05	10.97	11.84	12.52	12.83	13.34	13.34
Less: estimated CAPEX	(94.75)	(150.00)	(150.00)	(150.00)	(150.00)	(150.00)	(120.09)
Less: change in working capital	178.53	(470.62)	(327.87)	(367.39)	(194.68)	(232.67)	(232.67)
Free cash flow to the firm	394.70	1,100.24	1,362.29	1,539.29	1,937.73	2,021.77	2,051.69
WACC	17.10%	15.80%	15.20%	14.90%	14.60%	14.60%	14.60%
Terminal growth rate							4.60%
Discount period	0.25	1.25	2.25	3.25	4.25	5.25	
Discount factor	0.96	0.83	0.73	0.64	0.56	0.49	0.49
Discounted FCFF	379.45	915.45	990.21	979.41	1,085.05	987.72	10,490.27
Enterprise value	15,448.10						
Less: net debt	(798.57)						
Less: Employee benefit obligation	(97.57)						
Plus: surplus assets	-						
Equity value	14,551.96						
Exchange rate used, 323.5 LKR = 1 USD (as of 31 Dec 2023)	323.50						
Equity value (translated to LKR'000)	4,707,560.35						
No. of shares pre-IPO (in '000)	456,000						
Value per share (LKR)	10.30						

Offer price is at a discount of 27.30% to the estimated DCF value.

CABLE SOLUTIONS LIMITED**Initial Public Offering****Multiples approach**

All figures in USD'000, unless otherwise stated

As at 31-Dec-23	EV/EBITDA		EV/EBIT		PER	
	Low	High	Low	High	Low	High
Peer multiples	14.68x	16.23x	17.96x	19.85x	34.01x	37.58x
Discount for comparability	10.00%	10.00%	10.00%	10.00%	10.00%	10.00%
Selected multiples	13.22x	14.61x	16.16x	17.86x	30.60x	33.83x
Financial data						
EBITDA	1,551.86	1,551.86	-	-	-	-
EBIT	-	-	1,098.79	1,098.79	-	-
Earnings	-	-	-	-	805.25	805.25
Enterprise value	20,508.56	22,667.36	17,755.83	19,624.87	-	-
Less: net debt	(798.57)	(798.57)	(798.57)	(798.57)	-	-
Plus: surplus assets	-	-	-	-	-	-
Equity value	19,709.99	21,868.79	16,957.26	18,826.30	24,644.42	27,238.57
Average equity value	21,540.89					
High equity value	22,644.55					
Low equity value	20,437.23					
Exchange rate used, 323.5 LKR = 1 USD (as at 31 Dec 2023)	323.50					
Equity value (translated to LKR'000)	6,968,477.59					
No. of shares pre-IPO (in '000)	456,000					
Value per share (LKR)	15.30					

Offer price is at a discount of 50.90% to the peers.

NAV approach

Equity value (USD)	5,221,428
Exchange rate used (as of 31 Dec 2023)	323.50 LKR = 1 USD
Equity value (translated to LKR)	1,689,131,958
No. of shares pre-IPO	456,000,000
Value per share (LKR)	3.70

Offer price is at a premium of 102.50% to the NAV.

Company	TTM EPS (LKR)	NAVPS (LKR)	Price per share (LKR)	PE	PBV
Cable Solution*	0.46	3.61	7.50	16.22x	2.08x
Peers					
Kelani Cables PLC	75.88	502.73	295.50	3.89x	0.59x
ACL Cables PLC	12.13	111.85	83.40	6.87x	0.75x
Sierra Cables PLC	1.42	9.36	10.80	7.59x	1.15x

*TTM EPS and NAVPS are calculated based on 31.03.2024 unaudited figures.

CABLE SOLUTIONS LIMITED**Initial Public Offering****Financial Summary**

Ratios	FY21	FY22	FY23	FY24*	FY25F	FY26F	FY27F	FY28F	FY29F
Gross profit margin	29.78%	29.34%	32.62%	29.42%	30.50%	31.05%	31.87%	32.14%	33.35%
Net profit margin	1.94%	13.87%	16.33%	8.38%	11.76%	11.24%	12.09%	12.97%	14.34%
Debt to equity	62.18%	26.70%	26.81%	25.90%	11.51%	9.23%	7.50%	6.18%	5.15%
ROE	3.59%	31.38%	29.20%	12.32%	19.25%	18.69%	19.48%	19.77%	20.16%
ROA	1.82%	17.94%	20.29%	8.73%	15.83%	15.70%	16.68%	17.21%	17.80%

**Unaudited*

LKR Mn	FY21	FY22	FY23	FY24*	FY25F	FY26F	FY27F	FY28F	FY29F
Revenue	1,074.97	1,903.12	3,324.90	2,538.56	3,366.33	3,849.94	4,223.97	4,533.71	4,755.82
Gross profit	320.17	548.03	1,084.43	745.81	1,026.72	1,195.52	1,346.28	1,457.22	1,586.16
Profit before tax	27.40	281.32	651.76	247.99	465.57	508.96	600.84	691.80	802.33
Profit for the year	21.44	233.27	543.08	210.79	395.74	432.61	510.71	588.03	681.98
Total non-current assets	500.89	529.32	811.71	737.50	675.27	581.93	495.51	412.46	383.29
Total current assets	705.78	1,099.34	1,652.04	1,584.89	1,824.31	2,173.89	2,566.43	3,005.07	3,448.26
Total assets	1,206.66	1,628.66	2,463.75	2,322.39	2,499.57	2,755.81	3,061.93	3,417.53	3,831.56
Equity attributable to owners of the company	612.58	721.33	1,722.39	1,646.67	2,055.38	2,314.94	2,621.37	2,974.19	3,383.37
Total non-current liabilities	154.84	155.21	125.09	120.18	308.14	293.07	284.12	279.63	278.67
Total current liabilities	439.24	752.13	616.27	555.53	136.06	147.81	156.45	163.72	169.51
Total liabilities	594.08	907.33	741.36	675.71	444.20	440.87	440.56	443.35	448.18

UnauditedThe exchange rate used is as of December 31, 2023: 323.50 LKR = 1 USD.**Sources: CSLK's financial statements, independent valuation conducted by KPMG*

USD '000	FY21	FY22	FY23	FY24*	FY25F	FY26F	FY27F	FY28F	FY29F
Revenue	5,693.40	9,163.96	9,351.94	8,016.15	10,405.98	11,900.89	13,057.10	14,014.55	14,701.15
Gross profit	1,695.71	2,688.64	3,050.17	2,358.09	3,173.78	3,695.58	4,161.60	4,504.54	4,903.13
Profit before tax	142.23	1,442.18	1,833.21	790.28	1,439.18	1,573.28	1,857.30	2,138.47	2,480.15
Profit for the year	110.64	1,270.68	1,527.53	671.74	1,223.30	1,337.29	1,578.71	1,817.70	2,108.12
Total non-current assets	2,516.65	2,577.86	2,480.18	2,413.95	2,087.38	1,798.85	1,531.71	1,275.00	1,184.83
Total current assets	3,546.08	4,506.72	5,047.78	5,283.06	5,639.28	6,719.90	7,933.31	9,289.25	10,659.24
Total assets	6,062.74	7,084.57	7,527.96	7,697.00	7,726.66	8,518.75	9,465.02	10,564.25	11,844.07
Equity attributable to owners of the company	3,077.82	4,048.92	5,232.06	5,451.83	6,353.56	7,155.93	8,103.15	9,193.77	10,458.65
Total non-current liabilities	778.01	519.09	382.21	394.52	952.52	905.92	878.26	864.39	861.42
Total current liabilities	2,206.91	2,516.57	1,913.69	1,850.65	420.59	456.90	483.61	506.08	524.00
Total liabilities	2,984.92	3,035.66	2,295.90	2,245.17	1,373.10	1,362.82	1,361.87	1,370.47	1,385.42

UnauditedSources: CSLK's financial statements, independent valuation conducted by KPMG*

CABLE SOLUTIONS LIMITED**Initial Public Offering****Note:**

- *Financial statements of the company were prepared for the period ended 31st December. However, the reporting period was changed to 31st March from 31st March 2022.*
- *In FY24, PAT declined by ~56% reaching USD 0.67Mn. This was primarily due to a ~14% decline in revenue, which fell to USD 8.02Mn, leading to a ~23% drop in gross profit, which reached USD 2.36Mn. This downturn was attributable to the economic recession in Europe, which accounts for about 35% of CSLK's revenue. Further, administration expenses increased by ~59%YoY reaching USD 1.25Mn*

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