# RATING REPORT

## Crescent Steel & Allied Products Limited

**REPORT DATE:**
October 11, 2022

**RATING ANALYSTS:**

M. Amin Hamdani
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| RATING DETAILS | | | | |
|---|---|---|---|---|
| **Rating Category** | **Latest Rating** | | **Previous Rating** | |
| | **Long-term** | **Short-term** | **Long-term** | **Short-term** |
| **Entity** | A- | A-2 | A- | A-2 |
| ***Rating Date (Entity)*** | *Oct 11, 2022* | | *June25, 2021* | |
| **Rating Outlook** | Stable | | Stable | |
| **Rating Action** | Reaffirm | | Reaffirm | |

| COMPANY INFORMATION | |
|---|---|
| **Incorporated in 1983** | **External auditors:** A.F Ferguson & Co Chartered Accountants |
| **Public Limited Company** | **Chairman of the Board:** Mr. Ahmad Waqar |
| **Key Shareholders:** | **Chief Executive Officer:** Mr. Ahsan M. Saleem |
| - The Crescent Textile Mills Limited – 11.00% | |
| - Pak Qatar Family Takaful Limited – 10.45% | |
| - Islamic Development Bank – 6.11% | |
| - Trustees Crescent Steel and Allied Products Provident Fund – 5.19% | |
| - General Public – 39.58% | |

| APPLICABLE METHODOLOGY(IES) |
|---|
| ***Applicable Rating Criteria: Corporates (August 2021)*** |
| **https://docs.vis.com.pk/docs/SCB202106-1.pdf** |

# Crescent Steel & Allied Products Limited (CSAPL)

## OVERVIEW OF THE INSTITUTION

*CSAPL was incorporated on August 1, 1983 as a public limited company listed on the Pakistan Stock Exchange (PSX). It is a conglomerate with predominantly operations in Steel manufacturing.*

***Profile of Chairman***

*Mr. Ahmad Waqar is the Chairman of CSAPL. He is also currently serving as the member Policy Board, Dept. of Auditor General Pakistan. Mr. Waqar has diversified experience across entities in both the Public and Private Sector.*

***Profile of CEO***

*The management team is spearheaded by Mr. Ahsan M. Saleem. Mr. Saleem has been the Chief Executive Officer and Managing Director of Crescent Steel & Allied Products Limited since its inception. He has over 35 years of extensive industry experience in managing multiple business operations across variety of sectors such as steel, sugar, power, textile and engineering.*

## RATING RATIONALE

**Sponsor Profile**

Crescent Steel and Allied Products Limited (CSAP) is a public listed entity with the operations segregated into five divisions, namely Steel Division, Crescent Hadeed (Billet) Division, Crescent Cotton Products, Investment and Infrastructure Development and Energy Division (IID). CSAPL also has two wholly owned subsidiaries, namely CS Capital (Pvt.) Ltd, and Solution de Energy (Pvt.) Ltd and associated companies Altern Energy Limited and Shakarganj Limited. The Company's long term investments represent 28.4% of the total asset base.

**Proposed Sukuk Structure**

CSAPL is in process of issuing secured, privately placed Sukuk to the tune of Rs. 800 Mn. The proceeds of the issue will be utilized to meet working capital requirement. The proposed pricing of the issue will be six month KIBOR plus yet to be finalized spread. The tenor of the instrument will be three years. Principal will be redeemed in six equal installments starting from the 6th month of drawdown. Security features of the Sukuk entail ranking charge on Fixed Assets/constructive mortgage charge

**Ratings incorporate CSAPL's diversified revenue stream including exposure to steel, textile, billet, capital markets and power sector.**

**Steel Division**

This segment operates two spiral pipe (SP) production lines (ranging from 8 to 120 inches) & a coating line primarily manufacturing large diameter pipe used in fluid and oil & gas transmission. This division also has an engineering unit engaged in fabrication and erection of machinery located at Dalowal, District Faisalabad, Punjab. Since sales are majorly dependent on public sector and pipeline augmentation projects of gas utility companies, it exposes the business to volatility in demand. The revenue from the steel division was reported lower at Rs. 1.39b (FY21: Rs. 2.7b; 9MFY21: Rs. 2.6b) during FY22. The decline was due to fewer projects materializing during FY22.

For the next year, project pipeline looks healthier. The Company is currently negotiating contract worth Rs. 3.8b with China Harbour Engineering Company for manufacturing and coating of pipes for the K-4 project (Greater Karachi Bulk Water Supply Scheme). Subject to the execution, the manufacturing is expected to begin in 2QFY23 for a period of 6-10 months. Business risk in the execution of this project is largely mitigated as raw material (HRC) is to be provided by the buyer and therefore the company is not exposed to any commodity price of exchange risk. In addition, projected pipeline tenders from gas utility companies is strong. Nevertheless, the political uncertainty will continue to weigh in on the outcome and timelines of the projects.

The company is also negotiating contract from China Harbour Engineering Company solely for coating of pipe for K-4 project (Greater Karachi Bulk Water Supply Scheme). The contract for coating is worth approximately PKR 3.27b.

CSAP witnessed attrition in margins during FY22 owing to massive hike in raw material prices. This is due to bids being made based on current or expected HRC prices at the time of the contract while contract award and procurement of HRC is done with a time lag. However, exchange risk is mitigated as per contract terms. Quantum of gross loss amounted to Rs. (134.4m) in FY22.

| Steel segment (Rs.mn) | FY20 | FY21 | FY22 |
|---|---|---|---|
| **Sales - net** | 1,291.2 | 2,740.1 | 1,391.6 |
| **Cost of sales** | 1,257.5 | 2,319.9 | 1,526.1 |
| **Gross profit / (loss)** | **33.7** | **420.2** | **(134.4)** |
| **Gross margin** | 2.6% | 15.3% | -9.6% |
| **Profit / (loss) before tax** | **(392.2)** | **85.1** | **(549.9)** |

Company is projecting strong growth in FY23 in the steel division on account of two major projects of SSGC and SNGPL. In addition, with the downward trend observed in HRC prices, gross margins of the Company are likely to recover.

**Hadeed Billet Division**

Hadeed (Billet) Division commenced operations in 2016. Located in Bhone, Punjab the plant has an annual production capacity of 85,000 MT of steel billets. This division manufacturers steel long products (billets) which are used as a raw material by re-rolling mills to manufacture other steel products for use in the construction and engineering sector. This division posted net loss before tax of Rs. 171.6m during FY21 and the trend continued in FY22 with net loss before tax of Rs. 235.2m mainly due to power constraint resulting in lesser absorption of fixed cost.. The power supply for this division is currently being met through in-house bagasse fired power plant, which is only operational during sugar season. We expect this division's contribution in the bottom line to remain constrained, partly due to energy issues and partly due to anticipated slowdown in construction sector.

| Hadeed (Billet) Rs. Mn | FY20 | FY21 | FY22 |
|---|---|---|---|
| **Sales - net** | 971.7 | 2,065.1 | 2,465.5 |
| **Cost of sales** | 960.7 | 2,203.7 | 2,629.4 |
| **Gross profit / (loss)** | **11.1** | **(138.6)** | **(163.9)** |
| **Gross margin** | 1.1% | -6.7% | -6.6% |
| **Profit / (loss) before tax** | **(35.4)** | **(171.6)** | **(235.2)** |

**Cotton Division**

This unit has 19,680 spindles installed and situated at Jaranwala near Faisalabad. The company produces a variety of yarn, with a count range from 7s to 40s, for greige and towels. The sales revenue from this unit increased to Rs. 2.6b (FY21: Rs. 2.0b) in FY22, owing to higher yarn prices and upbeat textile demand. Going forward, textile sector's demand is expected to witness slowdown given fragile macro-economic environment and a tougher global markets indirectly hampering overall local and global textile demand. Hence, in view of current situation, the Company has shelved off installation of additional 7,920 spindles. Going forward, the Company is expected to earn a modest income from this division.

| Cotton Segment (Rs. Mn) | FY20 | FY21 | FY22 |
|---|---|---|---|
| **Sales - net** | 1,346.0 | 2,000.1 | 2,695.3 |
| **Cost of sales** | 1,320.2 | 1,788.6 | 2,419.7 |
| **Gross profit / (loss)** | **25.8** | **211.5** | **275.5** |
| **Gross margin** | 1.9% | 10.6% | 10.2% |
| **Profit / (loss) before taxation** | **(26.7)** | **171.1** | **199.3** |

**Investment and Infrastructure Development Division (IID)**

This division acts as a liquidity buffer for the company providing liquidity in times of cash flow constraints and earns income through dividends and capital gains emanating from investing in multiple asset categories. During the period under review, the division recorded hefty one-off dividend income of Rs. 1.1b, majorly due to partial settlement of circular debt of its associated company, Altern Energy, which provided healthy uptick to profitability despite lackluster performance in other segments.

However, going forward, investment income from IID is expected to be rationalized with subdued market activity and weak macro-economic situation.

| In Rs.mn | FY19 | FY20 | FY21 | FY22 |
|---|---|---|---|---|
| **Dividend income** | 208.9 | 353.4 | 19.3 | 1,155.8 |
| **G\L on sale of FVTPL investments** | (16.1) | (4.3) | 6.6 | (2.4) |
| **Unrealized gain/(loss) on FVTPL investments** | (3.9) | 37.7 | 200.7 | (186.6) |
| **Rental income-investment properties** | 2.6 | 2.6 | 5.9 | 3.2 |
| **Investment Income** | **191.6** | **389.3** | **232.6** | **970.0** |

**Uptick in core business likely to support future profitability, although business remains susceptible to changes in commodity and exchange rate volatility.**

| Rs mn | FY20 | FY21 | FY22 |
|---|---|---|---|
| **Net Sales** | 3,822.2 | 7,259.2 | 7,089.9 |
| **Gross Profit** | 50.9 | 496.7 | (65.2) |
| **Gross Margin** | **1.3%** | **6.8%** | **-0.9%** |
| **Net Profit/Loss** | **(17.1)** | **351.9** | **366.6** |
| **Net Margin** | **-0.4%** | **4.8%** | **5.2%** |

We expect FY23 projected profitability to be supported by uptick in core business. The steel division is projecting a healthy growth in pipeline orders on account of which revenues will remain upbeat. Margins are also trending positive, however, they remain vulnerable to exchange rate volatility and commodity price fluctuations. Ratings remain underpinned on achievement of budgeted financial metrics.

**Adequate liquidity profile**

Fund From Operations (FFO) has varied in line with the profitability of the Company. In line with higher profits during FY21, FFO turned positive to Rs. 311.5 (FY20: Rs. -17.6m) and jumped to Rs.861m during FY22 majorly driven by dividend income received from its associate company. While investment income has continued to provide support to bottom line, the windfall dividend income received in FY22 is expected to streamline going forward. Sensitizing FFO for this dividend income debt service coverage remains satisfactory. Going forward, based on projected profitability levels provide an adequate debt servicing capability. Liquidity profile remains adequate with current ratio of 1.37x and stock in Trade and Trade Debts providing adequate coverage for short-term borrowings at 168%. In addition, with declining raw material price trend and mitigation of input price risk in a major contract, working capital cycle is expected to improve, although inflationary pressure may continue to exert pressure on working capital requirements

**Conservative financial management provides comfort.**

Ratings derive comfort from conservative financial management of the Company, whereby gearing and leverage indicators have been maintained at reasonable levels. With the dividend income coming in, quantum of short-term borrowing declined. Consequently, gearing (FY22: 0.18x; FY21: 0.32x) and leverage (FY22: 0.38x; FY21: 0.46x) ratios inched lower. With the proposed Sukuk, gearing is expected to increase, albeit remaining within manageable levels.

## Crescent Steel and Allied Products (CSAPL) Appendix I

| FINANCIAL SUMMARY *(amounts in PKR millions)* | | | | |
|---|---|---|---|---|
| **BALANCE SHEET** | **FY19** | **FY20** | **FY21** | **FY22** |
| **Fixed Assets** | 2,493.7 | 2,274.3 | 2,058.9 | 2,216.8 |
| **LT Investments** | 2,264.8 | 2,303.8 | 2,468.9 | 2,362.6 |
| **Stock-in-Trade** | 821.4 | 2,130.7 | 1,236.5 | 1,190.0 |
| **Trade Debts** | 96.4 | 225.8 | 137.1 | 175.2 |
| **Cash & Bank Balances** | 27.8 | 23.4 | 4.0 | 6.7 |
| **Total Assets** | 8,287.0 | 9,660.8 | 8,705.7 | 8,445.1 |
| **Trade and Other Payables** | 691.9 | 1,068.5 | 755.2 | 1,136.9 |
| **Long Term Debt (including current maturity)** | 455.2 | 364.2 | 410.9 | 260.9 |
| **Short Term Debt** | 1,577.2 | 2,675.4 | 1,514.9 | 812.6 |
| **Total Debt** | 2,032.4 | 3,039.6 | 1,925.8 | 1,073.5 |
| **Total Liability** | 2,893.0 | 4,212.5 | 2,734.7 | 2,346.7 |
| **Paid up Capital** | 776.3 | 776.3 | 776.3 | 776.3 |
| **Total Equity (Without revaluation surplus)** | 5,394.1 | 5,448.3 | 5,970.8 | 6,098.4 |
| | | | | |
| **INCOME STATEMENT** | **FY19** | **FY20** | **FY21** | **FY22** |
| **Net Sales** | 4,066.5 | 3,822.2 | 7,259.3 | 7,090.9 |
| **Gross Profit** | 220.4 | 50.9 | 496.7 | (65.3) |
| **Profit/Loss Before Tax** | 24.9 | -117.8 | 426.5 | 315.1 |
| **Profit/Loss After Tax** | 143.5 | -17.1 | 351.9 | 366.7 |
| | | | | |
| **RATIO ANALYSIS** | **FY19** | **FY20** | **FY21** | **FY22** |
| **Gross Margin (%)** | 5.4% | 1.3% | 6.8% | -0.9% |
| **Net Margin** | 3.5% | -0.4% | 4.8% | 5.2% |
| **Adjusted FFO** | -289.3 | -17.6 | 311.5 | 861.6 |
| **Current Ratio (x)** | 1.19 | 1.11 | 1.45 | 1.37 |
| **(Stock+ Trade Debts)/ Short-term Debt** | 0.58 | 0.88 | 0.91 | 1.68 |
| **Debt Servicing Coverage Ratio (x)** | (0.25) | 0.59 | 1.67 | 2.62 |
| **Gearing (x)** | 0.38 | 0.56 | 0.32 | 0.18 |
| **Leverage (x)** | 0.54 | 0.77 | 0.46 | 0.38 |
| **ROAA (%)** | 1.6% | -0.2% | 3.8% | 4.3% |
| **ROAE (%)** | 2.4% | -0.3% | 6.2% | 6.1% |

## ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

### RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

**Medium to Long-Term**

**AAA**
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

**AA+, AA, AA-**
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

**A+, A, A-**
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

**BBB+, BBB, BBB-**
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

**BB+, BB, BB-**
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

**B+, B, B-**
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

**CCC**
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

**CC**
A high default risk

**C**
A very high default risk

**D**
Defaulted obligations

**Short-Term**

**A-1+**
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

**A-1**
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

**A-2**
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

**A-3**
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

**B**
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

**C**
Capacity for timely payment of obligations is doubtful.

**Rating Watch:** VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

**Rating Outlooks:** The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

**(SO) Rating:** A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

**(blr) Rating:** A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

**'p' Rating:** A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

**'SD' Rating:** An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

## REGULATORY DISCLOSURES — Appendix III

| | |
|---|---|
| **Name of Rated Entity** | Crescent Steel & Allied Products Limited |
| **Sector** | Steel Industry |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Entity Rating |

**Rating History**

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| | | **SUKUK RATING** | | |
| **Dec 08, 2021** | A- | | Stable | Preliminary |
| | | **ENTITY RATING** | | |
| **Oct 11, 2022** | A- | A-2 | Stable | Reaffirmed |
| **Jun 25, 2021** | A- | A-2 | Stable | Reaffirmed |
| **Apr 8, 2020** | A- | A-2 | Stable | Downgrade |
| **Dec 26, 2018** | A | A-2 | Stable | Downgrade |
| **May 29, 2018** | A+ | A-2 | Negative | Maintained |
| **July 03, 2017** | A+ | A-2 | Stable | Initial |

| | |
|---|---|
| **Instrument Structure** | CSAPL intends to issue a secured Privately Placed Sukuk of Rs. 1,000m; inclusive of green shoe option of Rs. 200m. . The funds will be used to meet working capital requirements. Proposed pricing of the issue is six month KIBOR plus yet to be finalized spread. The tenor of the instrument is three years. Principals will be redeemed in six equally installments starting from the 6th month of drawdown. Security features of the Sukuk entail ranking charge on Fixed assets/constructive mortgage charge |
| **Statement by the Rating Team** | VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities. |
| **Probability of Default** | VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default. |
| **Disclaimer** | Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.  |

**Due Diligence Meetings Conducted**

| | Name | Designation | Meeting Date |
|---|---|---|---|
| 1 | Mr. Azeem Sarwar, FCA | Senior Manager Finance & Control | July 04th, 2022 |
| 2 | Mr. M. Haseeb Iqbal | Manager Treasury | |
| 3. | Mr. Saad Thaniana | Chief Financial Officer | |