RATING REPORT

Fauji Fertilizer Bin Qasim Limited

REPORT DATE:
August 30, 2019

RATING ANALYSTS:
Talha Iqbal
talha.iqbal@vis.com.pk

Muhammad Ibad Deshmukh
ibad.deshmukh@vis.com.pk

RATING DETAILS		
Rating Category	Initial Rating	
	Long-term	Short-term
Entity	A+	A-1
Rating Date	*Aug 27, 2019*	
Rating Outlook	Stable	
Outlook Date	*Aug 27, 2019*	

COMPANY INFORMATION	
Commenced Operations in January 2000	**External auditors:** EY Ford Rhodes
Listed Public Limited Company	**Chairman of the Board:** Lt Gen Syed Tariq Nadeem Gilani, HI(M), (Retd.)
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Lt Gen Javed Iqbal, HI(M), (Retd.)
Fauji Fertilizer Company Limited – 49.88%	
Fauji Foundation – 18.29%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria *Industrial Corporates (May 2016)* ***http://www.vis.com.pk/docs/Corporate-Methodology-201605.pdf***

Fauji Fertilizer Bin Qasim Limited (FFBL)

OVERVIEW OF THE INSTITUTION

Headquartered in Islamabad, Pakistan, Fauji Fertilizer Bin Qasim Limited (FFBL) is the pioneering, sole domestic producer of Di-Ammonium Phosphate (DAP) fertilizer.

RATING RATIONALE

Corporate Profile

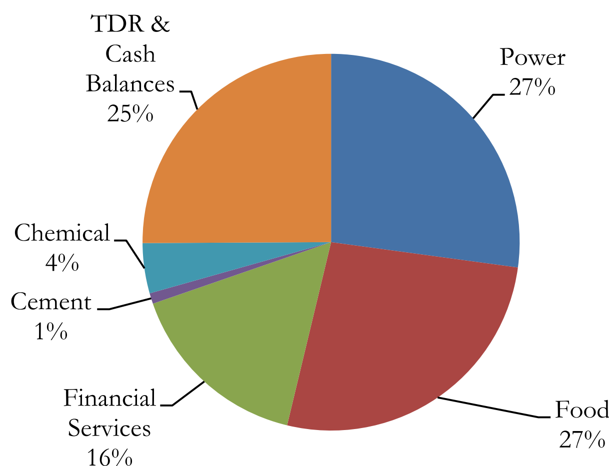
Headquartered in Islamabad, Pakistan, Fauji Fertilizer Bin Qasim Limited (FFBL) is the pioneering, sole domestic producer of Di-Ammonium Phosphate (DAP) fertilizer. It is also the only producer and marketer of granular form UREA (in contrast to widely marketed 'prilled' variant). FFBL enjoys leadership in DAP fertilizers with market share of 30.7% and is Pakistan's 4th largest producer of UREA. Fauji Foundation (FF) and its subsidiary Fauji Fertilizer Company Limited (FFC) hold majority shareholding in FFBL.

Both FFC and FFBL market their products under one umbrella brand 'Sona', which has wide recognition among the farmers' community. The company has an installed annual capacity equaling 650.0m tonnes of DAP and 551.1m tonnes of UREA. During 2018, actual capacity utilization for DAP and UREA remained close to full capacities at 112.3% and 101.9% respectively.

As part of company's strategic vision to offer sustainable returns to shareholders, FFBL carries a sizeable book of diversified investments. Investment portfolio (including TDRs) amounted to Rs. 32.8b (2018: Rs. 39.2b; 2017: Rs. 40.8b) and represented 38.6% of total asset base at end-1Q19. Of this, 75% of investments pertain to strategic investments in related parties including joint ventures, subsidiaries and associates.

As depicted in Figure 1, the investment portfolio is diversified. The portfolio features a mix of investment in defensive and growth industries. Projected dividend income from equity investment in subsidiary and associates along with income from debt exposure can provide support to earnings in prevalent interest rate and economic scenario.

Figure 1: Diversified investment portfolio



FFBL's largest power sector investment (FPCL) paid its first cash dividend in 2018 amounting to Rs. 1.1b. Going forward, quantum of future dividend receipts from FPCL is expected to double over the rating horizon. This along with dividend income from other investments is projected to contribute 27-54% to pre-tax profits of the company over 2019-22. However, majority of dividend income will continue to emanate from power projects over the rating horizon. Excluding return on non-earning investments, overall return on strategic investment portfolio is considered healthy.

JOINT VENTURES

Pakistan Maroc Phosphore S.A

In 2005, Fauji Group started a joint venture with Office Cherifien des Phosphates Group (OCP) and formed a new entity named Pakistan Maroc Phosphore S.A (PMP). FFBL has 25% equity holding in PMP. PMP has facilitated in ensuring continuous supply of phosphoric acid (a raw material for DAP production) to FFBL.

SUBSIDIARIES

FFBL Power Company Limited

FFBL Power Company Limited's (FPCL) 118 Megawatt (MW) (Net Capacity: 103 MW) coal based power plant is amongst the first coal based projects to be operational in Pakistan and is located within the FFBL complex at Port Qasim. FPCL was incorporated to support the energy requirements of FFBL as a substitute of natural gas fuel based system. Moreover, the company contributes a sizeable portion of its generating capacity to national grid via K-Electric (KE). FPCL has been awarded tariff on 'take and pay basis' (dispatch would depend on economic merit order with no guaranteed payment). However, demand Risk has been assessed to be manageable due to relatively high position in KE's merit order along with dispatch guarantees from KE and firm commitment for off-take from FFBL. The plant was constructed on a non-EPC basis; it commenced commercial operations on May 19, 2017. The company posted a profit of Rs. 3.1b (2017: Rs. 1.7b) in 2018 while Fund Flow from Operations (FFO) increased to Rs. 4.46b (2017: Rs. 1.3b). Given the jump in FFO, higher payout from FPCL is expected in 2019.

Figure 2: Key financial indicators

Rs. In m	2017	2018
Gross Margin (%)	38%	34%
Net Margin	22%	19%
FFO	1,305*	4,315
Equity	10,213	11,765
Total Debt	21,769	21,020
FFO to Total Debt (%)	6%	21%
FFO to Long Term Debt (%)	7%	25%
Current Ratio (x)	1.2	1.4
Debt Servicing Coverage Ratio (x)	1.07	1.75
Leverage (x)	2.39	1.91
Gearing (x)	2.13	1.79
ROAA (%)	5.5%	8.9%
ROAE (%)	20.0%	27.8%

**(7 months of operations)*

Fauji Foods Limited

Fauji Foods Limited (FFL) is principally engaged in processing and sale of toned milk, milk powder, fruit juices, allied dairy and food products. The company was founded in 2015 after acquisition of Noon Pakistan Limited, a company with an over 50-year dairy legacy in Pakistan. FFL's brand 'Nurpur' is one of the oldest and highly recognizable brands in Pakistan. In 2017, FFL ventured into the Juices & Nectars segment.

In 2018, FFL incurred a net loss of Rs. 2.8b (2017: Rs. 2.3b). Net loss incurred increased further to Rs. 2.34b (1HCY18: Rs. 1.47b) during 1HCY19. The increase in net losses is attributed to higher cost incurred in relation to input costs of raw materials owing to fluctuations in foreign currency exchange rates, and finance costs owing to increase in policy rate. Moreover, inability of industry and company to increase prices of certain products despite increase in processing cost, including impact of change in input costs and additional regulatory duty and high availability of low priced loose milk through informal sector also contributed to losses. Management has undertaken various initiatives to enhance production and procurement efficiency which along with improved industry pricing power, product diversification

(Cheese), projected increase in volumes (butter and tea whitener) and realignment of distribution network is projected to result in break even for the Company being achieved earlier than previously anticipated.

Figure 3: Key financial indicators

Rs. In m	2017	2018
FFO	(2,658)	(2,962)
LT Debt	4,489	4,595
Total Debt	5,938	9,586
Total Equity	3,486	718
Gross Margin	2.8%	4.7%
Net Margin	-32.7%	-35.2%
Net Working Capital	1,652	(2,875)
FFO/Long term Debt	-59%	-64%
FFO/Total Debt	-44.8%	-30.9%
Gearing	1.70	13.35
Leverage	2.00	15.89
ROAA	-23.4%	-22.4%
ROAE	-86.6%	-135.5%
DSCR	(5.56)	(4.08)
Dividend Payout %	0%	0%
Trade Debt % Net Sales	1.9%	1.5%

Fauji Meat Limited

Fauji Meat Limited (FML) was incorporated in 2013 as a subsidiary of FFBL. FML has established Halal meat processing facility near Port Qasim, Karachi with a daily production capacity of 100 tons of meat including 85 tons of beef and 15 tons of Mutton. In 5 years, FML expanded its international ecosystem to around 22 countries. This includes all key GCC markets, Malaysia and Iran while management is also in the process of obtaining approvals for China. Resultantly, capacity utilization is expected to improve on a timeline basis. FML recently entered the domestic arena by launching a one stop meat shop, under the brand name of 'Zabeeha'. 'Zabeeha' stores are now present in major cities across the country. However, majority sales are expected to be driven by exports. Higher capacity utilization along with realization of export orders will be key drivers for achieving break even as per projected timeline in 2021.

Figure 4: Key financial indicators

	2017	2018
Gross Margin (%)	-43%	-32%
Net Margin	-109%	-118%
Net Working Capital	(3,398)	(1,967)
Trade debts/Sales	24%	32%
FFO	(210)	(667)
Equity	848	1,031
Total Debt	6,971	4,012
FFO to Total Debt (%)	-3%	-17%
FFO to Long Term Debt (%)	-9%	-73%
Current Ratio (x)	0.3	0.4
Debt Servicing Coverage Ratio (x)		(0.19)
Leverage (x)	8.49	6.47
Gearing (x)	8.22	3.89
ROAA (%)	-16.8%	-16.7%
ROAE (%)	-159.8%	-140.3%

Associates

Foundation Wind Energy-I (Private) Limited

Foundation Wind Energy-I (Private) Limited (FWEL-I) operates and maintains a wind power plant having a name plate capacity of 50 MW. The company achieved commercial operations date (COD) of its plant on April 11, 2015. Recurring revenues of the company are expected to largely sustain owing to fixed tariff and wind risk and evacuation compensation borne by the power purchaser. Gearing and leverage of the company has improved on a timeline basis to 1.1x (FY18: 1.1x; FY17: 1.4x) and 1.2x (FY18: 1.2x: FY17: 1.5x), respectively, on account of periodic repayment of borrowings and enhanced equity base. With decline in borrowings and largely stable cash flows, coverages are expected to remain sound, going forward.

Figure 5: Key financial indicators

Rs. In m	FY17	FY18	9MFY19
Gross Margin (%)	70.0%	63.1%	56.4%
Net Margin	44.4%	37.5%	27.4%
FFO	1,560	1,437	1,079
Equity	5,069	6,008	6,318
Total Debt	7,179	6,802	6,971.5
FFO to Total Debt (%)	22%	21%	15%
FFO to Long Term Debt (%)	22%	21%	15%
Current Ratio (x)	1.11	1.43	1.44
Debt Servicing Coverage Ratio (x)	1.44	1.26	1.61
Leverage (x)	1.48	1.21	1.18
Gearing (x)	1.42	1.13	1.1
ROAA (%)	8.69%	7.26%	4.55%
ROAE (%)	25.54%	16.94%	9.96%

Foundation Wind Energy-II (Private) Limited

Foundation Wind Energy-II (Private) Limited (FWEL-II) operates and maintains a wind power plant having a name plate capacity of 50 MW. The plant is built at Ghora, District Thatta, Province of Sindh, Pakistan. FWEL-II signed an Energy Purchase Agreement (EPA) with National Transmission & Dispatch Company Limited (NTDCL) through Central Power Purchasing Agency (Guarantee) Limited (CPPA) on December 20, 2012 for a period of 20 years. As per the implementation agreement, payment obligations of the power purchaser are guaranteed by Government of Pakistan. With largely sustainable revenue and decline in borrowings, profitability is likely to remain sound, going forward. The company has not been utilizing short-term borrowings since the last two years. Therefore, as a result of gradual repayment of long-term obligations coupled with increase in equity base, gearing and leverage decreased to 1.09x (FY18: 1.07; FY17: 1.30x ;) and 1.15x (FY18: 1.13x; FY17: 1.36x) respectively on a timeline basis, by end-9MFY19. FFO is projected to remain stable on an annual basis while the same is expected to remain sufficient for timely debt repayment.

Figure 6: Key financial indicators

Rs. In m	FY17	FY18	9MFY19
Gross Margin (%)	64.8%	62.2%	56.1%
Net Margin	37.5%	38.1%	28.2%
FFO	1,278	1,356	1,075
Equity	5,227	6,169	6,290
Total Debt	6,793	6,631	6,826
FFO to Total Debt (%)	19%	20%	21%
FFO to Long Term Debt (%)	19%	20%	21%
Current Ratio (x)	1.34	1.78	1.51
Debt Servicing Coverage Ratio (x)	1	1.39	1.37
Leverage (x)	1.36	1.13	1.15
Gearing (x)	1.3	1.07	1.09
ROAA (%)	6.4%	7.4%	4.7%
ROAE (%)	17.3%	16.5%	10.1%

Askari Bank Limited

AKBL was incorporated in 1991. The parent entity of the Bank is Fauji Foundation which collectively owns 71.91% shares in the Bank. At end-2018, the Bank has 516 branches including 91 Islamic banking branches and a wholesale bank branch in Kingdom of Bahrain. Deposit base of the bank exhibited a growth of around 9% during FY18. The CASA deposits represented almost 84% (FY17: 85%) of the deposit base; the bank largely maintained its market share in system deposits. The bank posted profit after tax of Rs. 4.4b in 2018.

Figure 7: Key financial indicators

(Amounts in Rs. m)	*2016*	*2017*	*2018*
Gross Advances	262,123	284,340	369,259
Gross Infection	10.9%	9.4%	7.2%
Net Infection	0.9%	0.7%	0.4%
Deposits	472,811	525,808	573,636
CA	*26.5%*	*27.3%*	*28.4%*
CASA	79.4%	*82.9%*	*83.5%*
Net NPLs to Tier 1 capital	8.9%	6.9%	4.3%
Tier-1 CAR	9.1%	9.3%	10.9%
CAR	12.5%	12.1%	12.5%
Net Interest Income	14,911	16,195	18,610
Efficiency	77.0%	74.6%	69.0%
Overheads	4.5%	2.3%	2.4%
ROAA	0.9%	0.8%	0.6%
ROAE	22.1%	20.1%	15.0%
Operating Profit / (Loss)	8,477	8,492	6,879
Profit/ (loss) after Tax	5,221	5,268	4,431

Key Rating Drivers

Strong sponsor with diversified operations, revenue streams and financial strength.

The assigned ratings incorporate FFBL's association with primary shareholder, Fauji Foundation Group (FF). FF is a charitable trust incorporated under the Charitable Endowments Act 1890. Founded in 1954, FF is a diversified conglomerate with strong financial muscle and exposures in more than 18 industries. In line with its mandate, more than 80% of the institution's income goes towards welfare activities every year.

Dominant market position in DAP; market share in UREA has been sustained.
FFBL's business profile is underpinned by the significant scale of its operations, its leading position in the domestic DAP market (market share of 31%) with the Company being the sole local manufacturer in the country. The Company is the 4th largest player in the UREA space and is also the sole manufacturer of granular form UREA in the country with a market share of around 10% in 2018 offtake.

Sector Dynamics

Industry DAP offtake declined by 11% during FY19 while inventory level continue to remain on the higher side. With expected decline in imports, gradual improvement in demand supply dynamics expected over the next 1 year.
As at end-June'2018, inventory of DAP stood at 406 Kt (Dec'2018: 494Kt; Dec'2017: 171Kt; Dec'2016: 82Kt). Imports during the period were 1,511 Kt while domestic production of DAP was 783 Kt (FY18: 753 Kt). DAP offtake decreased to 2,200 Kt (FY18: 2,471 Kt) on account of rise in local prices per bag. Importers accounted for 1,520 Kt of DAP offtake or ~69% of the total offtake. FFC, FFBL and EFERT recorded a decline in DAP offtake while Pak Arab and Fatima Fert reported an increase in DAP offtake. Given the sizeable increase in quantum of imports along with decline in DAP offtake, closing inventory of DAP has depicted a noticeable jump to 504 Kt as at end-June'2019 and remains on the higher side. Given the sizeable inventory carried by major players, quantum of imports is expected to reduce in the ongoing year resulting in a gradual improvement in demand supply dynamics. Over the past three years, market share of the only domestic DAP producer, FFBL has decreased while share of imports has increased.

With majority of DAP being imported, domestic DAP prices move in tandem with international DAP prices. International DAP prices have depicted a declining trend since September'2018 due to restricted demand from India and increased export availability in China although prices have shown some recovery in June'2019. Phosphoric acid is the key raw material of DAP. Decline in prices of phosphoric acid (in dollar terms) since December'2018 along with increase in prices of DAP due to rupee devaluation and import parity pricing mechanism followed bodes well for future margins of the Company.

Favorable demand-supply and pricing dynamics and low ending inventories bodes well for profitability of UREA manufacturers.
As at end-June'2018, inventory of UREA stood at 167 Kt (June'2017: 1,084 Kt). Imports during the period were 105 Kt while total production of UREA increased by 11% to 5.9m tons (FY18: 5.4m tons). The increase was due to functioning of two UREA manufacturing plants (Fatimefert Limited and Agritech Limited), as supply of LNG was available on subsidized rates. During FY19, UREA offtake increased slightly by 1% to 5.94m tons (FY18: 5.89m tons). Barring Fatima Fertilizer, most large players witnessed 4-14% dip in UREA offtake. At end-FY19, closing inventory was reported at 178 Kt (FY18: 167 Kt), around prior year levels.

International UREA prices increased from US$ 224/MT at end-June 2018 to US$ 305/MT at end-November 2018 before declining to US$ 256/MT at end-June 2019. On the other hand, domestic UREA prices have increased from Rs. 1,583/bag at end-June 2018 to Rs. 1,869/bag at end-June 2019. Meanwhile, significant rupee devaluation, by making imported UREA more expensive, provided support to local UREA pricing. Given the low ending inventories and favorable demand supply and pricing (local UREA prices are at a discount to international prices) dynamics, profitability for UREA manufacturers is expected to remain healthy.

Proposed Gas Infrastructure Development Cess (GIDC) settlement to be broadly positive for the fertilizer sector, particularly FFBL.
GIDC since its inception in 2012 has faced various litigations and court stay orders, thus depriving government of the full GIDC collection. To resolve this, GoP has proposed GIDC Amendment Act 2019 which may include the following provisions:

- 50% waiver of arrear amounts in GIDC which are held up due to protracted litigations.
- 50% reduction in prospective GIDC fuelstock and feedstock rates.

- No GIDC on concessionary gas going forward.

Given the decline in cost of production due to 50% reduction in in prospective GIDC fuelstock and feedstock rates, future profitability (in a scenario where no price reduction is undertaken) will be positively impacted for all players with the impact being more profound for FFC and FFBL. In a scenario where benefit of proposed reduction in GIDC is passed on to consumers, FFBL will be the biggest beneficiary given that cost of production will reduce while prices of DAP (which constitutes around three-fourth of revenues) will remain unchanged. While earning implications will be negative for players operating on concessionary gas in the short to medium term, profitability will be positively impacted given that gas at concessionary rates will not be available post 2021.

Business risk profile of UREA industry is characterized by reasonable to sizeable capital intensity while availability of gas is a risk. Owing to farmers' dependence on the monsoon, the industry is exposed to seasonality in end-user demand. Players with strong raw material linkages (natural gas), low energy consumption levels, competitive cost structure and economies of scale are expected to fare better over the long term. Business risk profile draws support from economic importance of fertilizer industry and implied government support, as share of fertilizer in cost of production of Pakistan's major crops is ~10-15%.

Financial risk.
Despite lower volumetric sales, topline has continued to increase on the back of higher selling prices. DAP segments constitutes bulk of revenues.
Net sales of FFBL increased to Rs. 61.5b (2017: Rs. 52.7b) in 2018. On average, around three-fourth of sales are accounted by DAP while remaining revenues are contributed by UREA.

Figure 8: Sales in terms of volume and value

	2016			2017			2018			1H19		
	Qty	Amt		Qty	Amt		Qty	Amt		Qty	Amt	
	000 MT	Rs. m	%	000 MT	Rs. m	%	000 MT	Rs. m	%	000 MT	Rs. m	%
UREA	443	11,600	26%	546	13,331	25%	562	16,654	27%	214	7,533	35%
DAP	791	33,412	74%	831	39,402	75%	687	44,857	73%	202	13,964	65%
Total	**1,233**	**45,012**	**100%**	**1,377**	**52,733**	**100%**	**1,249**	**61,511**	**100%**	**416**	**21,497**	**100%**

DAP
After increasing by 5% in 2017 to 831 Kt (2016: 791 Kt), volumes decreased by 17% in 2018 to 687 Kt. Decline in sales is attributed to high imports, which created an oversupply situation in the market, leading to severe competition. Upward price trend encouraged dealers to invest in phosphate products. However, water shortage and higher DAP prices affected consumption at farmer level. As a result, market share of FFBL in DAP segment witnessed decline. Despite overall decline in DAP volumes on a timeline basis, revenues increased on account of rising trend in average prices charged. Given the sizeable inventory carried by major players, quantum of imports is expected to reduce in the ongoing year resulting in a gradual improvement in demand supply dynamics.

UREA
Volumes increased 23% in 2017 to 546 Kt (2016: 443 Kt). However, in 2018, sales growth was reported at 3% with volumes increasing to 562 Kt. In 2017, growth in UREA revenues was driven by volumes. In 2018, increase in UREA revenues was primarily supported by higher average prices. Market share in UREA has gradually increased over past three years to 9.7% in 2018.

Despite increase in dividend income, weak DAP market dynamics and increasing finance cost has impacted profitability, particularly in ongoing year. Gradual improvement in DAP demand supply dynamics and GIDC settlement are expected to improve earnings profile over the rating horizon.

Although favorable demand trends in UREA offtake and increasing DAP prices have supported growth in FFBL's topline, the company's profitability has depicted volatility due to market imbalances in the DAP segment which affected offtake and pricing power, fluctuation in raw material costs and bouts of rupee devaluation resulting in exchange losses. However, growing dividend income (2018: Rs. 1.98b; 2017: Rs. 803.6m) from investments provides support to the bottom line. Nevertheless, high debt levels remain a burden on the bottom line.

Gross margins of FFBL increased to 13.3% (2017: 11.4%; 2016: 2.7%) in 2018. This increase is primarily due to replacement of subsidy with reduction in GST to the tune of Rs 100 per bag w.e.f. July 1, 2018, which is now classified as sales instead of other income. Selling & distribution expenses remained a function of sales. Lower administrative expenses were incurred on account of decrease in salary expenses. In line with higher borrowings and increase in benchmark rates, finance cost increased to Rs. 2.2b (2017: Rs. 1.9b) during 2018. Moreover, the company reported sizeable exchange loss of Rs. 1.1b (2017: Rs. 176.1m) due to rupee devaluation. Increase in dividend income (augmented by FPCL's first payout) and higher gross profit, compensated higher operating expenses and lower subsidy from GoP (Rs. 314.6m vs. Rs. 2.8b), resulting in profit after tax of Rs. 1.4b (2017: Rs. 1.0b).

Gross margins were reported at 6% (1HCY18: 7.5%) during 1HCY19 and have declined due to inability to completely pass increase in raw material prices (due to significant rupee devaluation) given sizeable DAP ending inventories. This along with higher finance cost (1HCY19: Rs. 2.12b; 1HCY18: Rs. 917.1m) and other operating expenses (1HCY19: Rs. 1b; 1HCY18: Rs. 455.4m) has translated into a higher loss before tax of Rs. 2.43b (1HCY18: Rs. 1.26b) in 1HCY19.

Going forward, possible reduction in prospective GIDC rates and gradual improvement in sector dynamics for DAP are likely to bode well for FFBL's profitability over the rating horizon while proposed reduction in GIDC payable is expected to result in one-time gain during 2019. Nevertheless, increase in gas prices and elevated finance cost are expected to keep profitability growth in check.

Elevated leverage indicators are a rating constraint. Improvement in financial performance of subsidiaries and GIDC settlement will be critical for reduction in leverage indicators.

Figure 9: Financial indicators

Rs. In m	2016A	2017A	2018A	1Q19A
Total Equity	12,757	13,151	13,897	11,096
Dividend Payout %	34.90	79.06	64.89	
Current Maturity	2,833	3,208	5,125	4,708
LT Debt	20,023	18,542	21,208	20,916
ST Debt	15,724	9,934	13,913	18,399
Total Debt	35,747	28,476	35,122	39,315
Adjusted Total Debt(exc. STI+Cash)	19,975	10,734	20,497	31,093
Short Term Investment	9,949	14,194	10,936	3,209
Cash	5,823	3,547	3,690	5,012
Adjusted Gearing	1.57	0.82	1.47	2.80
Adjusted Leverage	2.76	2.64	3.73	5.91

Given the group's philosophy of maintaining a high dividend payout ratio, equity base has grown at a modest 3-year CAGR of 4% (2015-18). Equity base declined to Rs. 11b (2018: Rs. 13.9b) at end-1HCY19 on account of losses incurred and dividend paid. Capital structure of FFBL illustrates that the company is significantly leveraged. Total debt of the company equaled Rs. 35.1b (2017: Rs. 28.5b) at end-2018 and increased further to Rs. 39.3b on account of higher short term borrowings. Around half of debt is represented by long-term borrowings. Long-term debt was primarily obtained to fund the company's long-term investment portfolio. Given the nature of investments and timeline of expected return from the same, maturity profile of long-term debt is on the lower side. Short term borrowing is

utilized for working capital requirements and has varied in line with inventory levels and quantum of sales. Adjusted gearing and leverage were reported at 2.80x (2018: 1.47x; 2017: 0.82x) and 5.91x (2018: 3.73x; 2017: 2.64x) respectively at end-1Q19. Funding requirements for subsidiary companies will primarily be through commercial bank borrowings. At end-1HCY19, the company has provided long-term loan of Rs. 3.5b to FML while support to the tune of Rs. 3b will also be made available to FFL, if needed.

Cash flow coverage is currently low but is expected to improve over the rating horizon.
With an increase in profitability, Funds flow from operations (FFO) (including recurring dividend income) increased to Rs. 2.4b (2017: Rs. 0.5b) in 2018. FFO was recorded negative during 1HCY19 on account of losses incurred during the period. Given the sizeable debt outstanding, cash flow coverage of outstanding debt is currently on the lower side while DSCR has remained below 1(x). This is partly attributable to long-term debt profiling of the Company not being in alignment with dividend income from investments. With projected improvement in cash flows, DSCR and cash flow coverage is projected to improve. Till such time cash flows improve, re-profiling of debt arrangement with lenders is planned to be pursued. As at end-Dec'2018, cash and short-term investments were in excess of short-term borrowings. However, level of coverage may vary during the year given seasonality in sales. Trade debts and stock in trade have depicted a noticeable jump at end-1HCY19 but are expected to reduce by the end of the year.

Figure 10: Cash flow indicators

Rs. M	2016A	2017A	2018A	1Q19A
FFO	(83)	527	2,381	(1,946)
FFO to Adjusted Total Debt	0%	5%	12%	-6%
DSCR	0.80	0.60	0.93	

Strong Corporate Governance Framework

Board of Directors at FFBL comprises 12 members including Chairman and CEO & Managing Director. Board includes 3 independent directors, 1 executive director and 8 non-executive directors. During 2018, 5 Board meetings were convened with good participation of members. In order to ensure effective oversight, there are three sub-committees of the board, Board Audit Committee, Board HR & Remuneration Committee and Board System and Technical Committee.

Board performance is ensured through the annual performance evaluation and ongoing board development activities. The board awarded performance evaluation for the year 2018 to one of the leading external consultants.

FFBL's management team comprises experienced professionals having long association with the company. The organizational structure of the company comprises well segregated functional departments. The company follows the best practices to ensure effectiveness, throughout the course of operations.

FFBL has a well-established, state-of-the-art and efficient IT infrastructure that augments Company`s operations at all levels. SAP enterprise resource planning solution has been installed. The company has maintained a comprehensive management system provides an end to end solution for financial, logistics, distribution, inventories, plant maintenance, human capital management, material management etc.

Fauji Fertilizer Bin Qasim Limited (FFBL) **Appendix I**

FINANCIAL SUMMARY

(amounts In PKR millions)

BALANCE SHEET	31-Dec-17	31-Dec-18	30-Jun-19
Property, Plant & Equipment	10,405	9,748	9,801
Long Term Investments	23,065	24,565	24,565
Long Term Loans to Subsidiaries	-	2,400	3,500
Stock-in-Trade	1,854	5,655	19,989
Trade Debts	1,005	5,719	7,272
Advances	1,143	1,458	1,450
Short Term Investments	14,194	10,936	1,359
Cash & Bank Balances	3,547	3,690	6,586
Total Assets	**65,652**	**80,364**	**95,424**
Trade and Other Payables	23,198	29,825	34,484
Short Term Borrowings	9,934	13,913	25,447
Long Term Borrowings inc. Current Maturity	18,542	21,208	22,775
Total Interest Bearing Debt	28,476	35,122	48,222
Total Liabilities	**52,501**	**66,467**	**84,412**
Total Equity	**13,151**	**13,897**	**11,012**
INCOME STATEMENT	**31-Dec-17**	**31-Dec-18**	**30-Jun-19**
Net Sales	52,733	61,511	21,497
Cost of Sales	46,705	53,327	20,203
Gross Profit	**6,028**	**8,183**	**1,294**
Distribution Expenses	4,872	4,525	1,890
Administrative Expenses	1,727	1,549	623
Other Income	4,377	3,182	1,931
Other Expense	423	1,259	1,021
Finance Cost	1,941	2,223	2,125
Profit before Tax	**1,441**	**1,809**	**(2,434)**
Taxation	(437)	(373)	483
Profit After Tax	**1,004**	**1,437**	**(1,951)**
RATIO ANALYSIS	**31-Dec-17**	**31-Dec-18**	**30-Jun-19**
Gross Margin (%)	11.4%	13.3%	6.0%
Net Margin (%)	1.9%	2.3%	-9.1%
Current Ratio (x)	0.84	0.88	0.84
Net Working Capital	(5,884)	(5,963)	(10,667)
Adjusted Gearing (x)	0.82x	1.47x	3.66x
Adjusted Leverage (x)	2.64x	3.73x	6.94x
FFO	808	2,843	n/a
FFO to Long Term Debt (%)	4.4%	13.4%	n/a
FFO to Total Debt (%)	2.8%	8.1%	n/a
Debt Servicing Coverage Ratio (x)	0.60	0.93	n/a
ROAA (%)	1.6%	2.0%	-4.4%
ROAE (%)	7.8%	10.6%	-31.3%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix III

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 IV

Name of Rated Entity	Fauji Fertilizer Bin Qasim Limited (FFBL)
Sector	Fertilizer
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see table below
Instrument Structure	N/A
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. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2019 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
27-8-2019	A+	A-1	Stable	Initial