RATING REPORT

Fauji Fertilizer Bin Qasim Limited

REPORT DATE:
March 16, 2021

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Initial Rating		Initial Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA-	A1	A+	A1
Rating Date	*Mar 16, 2021*		*Aug 27, 2019*	
Rating Outlook	Stable		Stable	
Outlook Date	*Mar 16, 2021*		*Aug 27, 2019*	

COMPANY INFORMATION

Commenced Operations in January 2000	**External auditors:** EY Ford Rhodes
Listed Public Limited Company	**Chairman of the Board:** Mr. Waqar Malik
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Sarfaraz Ahmed Rehman
Fauji Fertilizer Company Limited – 49.88%	
Fauji Foundation – 18.29%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: *Industrial Corporates (April 2019)*
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.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 of granular form Urea (in contrast to widely marketed 'prilled' variant). FFBL enjoys leadership in the DAP fertilizers segment, with market share estimated at 41% for 2020 (2019: 34%), and is Pakistan's 4th largest producer of Urea. The plant is located at Port Qasim, Karachi. 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'. The company has an installed annual capacity of 650.0m tonnes of DAP and 551.1m tonnes of Urea.

Business Update

Urea capacity utilization remained intact, while sales offtake has posted notable increase

Capacity Utilization	2018	2019	2020
Urea	102%	92%	101%
DAP	112%	128%	114%
Production (K.Tons)	**2018**	**2019**	**2020**
Urea	562	508	559
DAP	730	831	740
Offtake (K.Tons)	**2018**	**2019**	**2020**
Urea	562	508	559
DAP	687	688	926
Offtake as % of Production	**2018**	**2019**	**2020**
Urea	100%	100%	100%
DAP	94%	83%	125%

- In 2020, the company's capacity utilization of Urea improved to 101%, while DAP capacity utilization was relatively lower at 114%; this was mainly attributable to diversion of gas towards Urea production, given carryover of excessive inventory of DAP from previous year.
- Sales offtake, for both Urea and DAP, depicted strong growth pf 10% and 35% respectively. FFBL's market share in Urea increased from 8% in 2019 to 9% in 2020, while market share for DAP increased from 34% in 2019 to 41% in 2020.
- Offtake of DAP was notably higher than production, as the management successfully offloaded all outstanding inventory by end-2020.

Gross margin for 2020 was notably higher

PKR (Mn)	2018	2019	2020
Sales	61,511	66,839	83,234
Cost of Sales	53,327	60,955	70,655
Gross Profit	8,183	5,885	12,579
Gross Margin	***13.3%***	***8.8%***	***15.1%***
Selling & Distribution	(4,525)	(5,344)	(5,518)
Administrative	(1,549)	(1,422)	(1,255)
Other Expenses	(112)	(3)	(312)
Exchange Loss	(1,147)	(635)	
Core Earnings	**850**	**(1,520)**	**5,494**
Other Income	3,182	4,370	5,184
Impairment on Investment	-	(1,520)	(4,082)
GIDC Reversal			2,741
Investment Income	**3,182**	**2,850**	**3,843**
Aggregate Income	**4,032**	**1,330**	**9,337**
Finance Cost	(2,223)	(5,199)	(4,444)
Profit Before Tax	**1,810**	**(3,869)**	**4,893**
Profit After Tax	**1,437**	**(5,921)**	**2,192**
Net Margin	***2.3%***	***-8.9%***	***2.6%***

- FFBL's profitability came under pressure in 2019 on account of lower gross margins. This was mainly a result of higher cost of phosphate imported from Pakistan Maroc Phosphore S.A, Morocco (Joint Venture).
- However, profitability metrics have depicted notable improvement in 2020, on account of significantly better sales performance and disposal of older inventory, allowing the company to record inventory gains.
- Nevertheless, given sizable provisioning undertaken on subsidiaries, the improvement in bottom line was restricted.

Treatment of GIDC liability

- For GIDC liability, the Supreme Court of Pakistan has issued its judgement, as per which the company is required to make payment of outstanding GIDC in 48 equal monthly installments. The company has currently obtained stay from Sindh High Court against the payment until the GIDC liability is correctly ascertained.

- The GIDC liability has been dissected in 2 parts, which are as follows:
  - Rs. 7.4b has been recognized as current payable.
  - Rs. 12.1b has been recognized as deferred liabilities (non-current)
  - The remaining (Rs. 2.7b) has been recorded as notional income by recognizing the present value of GIDC in accordance with IFRS 9 and IFRS 13. This income will we reversed going forward, in the form of notional expense.

Changes in Asset Mix

PKR (Mn.)	Dec'19		Dec'20	
Non-Current Assets				
Property Plant & Equipment	10,428	11.4%	10,193	11.2%
Long Term Investments	26,180	28.7%	24,546	27.0%
Long Term Loans	3,130	3.4%	6,990	7.7%
Advances & Deposits	97	0.1%	82	0.1%
Current Assets				
Stores & Spares	2,989	3.3%	2,894	3.2%
Stock in Trade	14,756	16.2%	2,862	3.1%
Trade Debts	8,607	9.4%	1,656	1.8%
Advances	923	1.0%	773	0.8%
Other Receivables	6,005	6.6%	5,170	5.7%
Sales Tax Refundable	8,717	9.6%	8,435	9.3%
Cash & Cash Equivalents	5,294	5.8%	25,048	27.5%
Short Term Investments	1,009	1.1%	-	-
Others	3,032	3.3%	2,318	2.5%
Total Assets	91,167		90,968	

- Given the strong sales performance in Q4'2020, the company's stock in trade has declined notably on a YoY basis. The year-end inventory almost entirely comprised raw material and work in progress, with finished goods comprising less than 8% of the aggregate.
- Resultantly the company's liquid assets (cash & cash equivalents) have increased notably, comprising 27.5% of the asset base.
- Credit risk on the books has declined with current receivables position comprising 18.7% of the asset base, vis-à-vis 28.5% as of Dec'19.
  - The trade debts have declined significantly, having a positive impact on cash conversion cycle.
  - The other receivables remained almost at similar level. These broadly constituted subsidy receivable from Government of Pakistan (61%) and due from FFC (35%).
  - The sales tax and income tax refundable has slightly reduced, albeit remains a sizable (11%) part of the company's asset base. Implied credit risk is low, as the amount is due from Government of Pakistan.

PKR (Mn.)	Dec'19	Dec'20
Trade Debts	8,607	1,656
Other Receivables	6,005	5,170
Sales Tax Refundable	8,717	8,435
Income Tax Refundable	2,651	1,745
	25,980	17,007

- The company has increased its investment in strategic holdings.

PKR (Mn.)	Dec'19	Dec'20
Long Term Investments	**26,180**	**24,546**
- Associate Companies		
o Fauji Cement Company Limited	300	-
o Askari Bank Limited	5,231	5,231
o FWE I & II	2,461	2,461
- JV		
o PMP	1,411	1,411
- Subsidiary Companies		
o Fauji Meat Limited (net of impairment of Rs. 4.8b (Dec'19: Rs. 1.1b)	5,785	2,103
o FFBL Foods Limited	299	299
o FFBL Power Company Limited	6,441	6,441
o Fauji Foods Limited (net of impairment of Rs. 820mn (Dec'19: Rs. 420mn)	4,253	6,602

Long Term Loans	3,130	6,990
- Fauji Meat Limited	500	1,065
- Fauji Foods Limited	2,630	5,925
Total	29,310	31,537

- The company has increased its investment in Fauji Foods Limited (FFL) by Rs. 2.7b (equity stake) and Rs. 3.3b (by way of loan provided)
- In addition the investment in Fauji Meat Limited (FML) has increased by Rs. 565m, by way of loan provided.
- Both of the above investments, by way of loan provided, are towards subsidiaries that are still in losses, and the company continues to book yearly impairment on the same. The outstanding loans provided to FFL and FML are equity convertible.

Key Rating Drivers

Rating incorporates sponsor profile & a diversified revenue base

- The assigned rating incorporates strength of sponsor, Fauji Foundation, which is a diversified conglomerate with strategic stakes in a wide variety of sector including fertilizer, cement, food, power generation, gas exploration, LPG marketing and distribution, financial services, and security services.
- Furthermore the rating also incorporates FFBL's revenue base diversification. Over the past 3-year period, other revenues from subsidiaries/associates, recorded as 'other income', comprised an average of a third of the revenue base (gross profit + other income).

Cash flow coverage indicators have improved in 2020 and net debt stands lower on a timeline.

- The higher turnover in 2020, and the resultant increase in FFO, translates in notably better FFO to (net) Debt ratio.
- Going forward, given our expectation on gross margin, and projected income from subsidiaries/associates, we expect FFO to (net) debt ratio to sustain.

PKR (Mn.)	2018	2019	2020
Days Inventory (Days)	26	61	46
Days Receivable (Days)	20	39	23
Days Payable (Days)	142	194	146
Cash Conversion Cycle (Days)	(96)	(94)	(78)
FFO	2,843	(779)	5,956
Debt	35,122	46,585	38,064
Net Debt (Debt – Cash)	31,432	41,291	13,015
FFO to Net Debt	9.0%	(1.9%)	45.8%
DSCR (x)	0.93	0.40	1.15
Current Ratio (x)	0.88	0. 74	1.04
Acid-test Ratio (x)	0.71	0.49	0.92

Capitalization buffer has been reinforced subsequent to the recent equity infusion

	Dec'18	Dec'19	Dec'20
Gearing (x)	2.5	6.8	2.7
Leverage (x)	4.8	12.3	5.5

- On account of the sizable losses incurred in 2019, FFBL had experienced significant equity erosion and as a result the company's capitalization metrics posted an adverse movement.
- However, the Board of Director, in their meeting held in October 2020, deliberated to issue right shares to the tune of Rs. 5b. The equity issuance proceeds were almost entirely received by January 2021, and the transaction is expected to be closed in Q1'2021. The new equity, is included in the Dec'20 financials as advance against share issuance and hence been incorporated in our gearing & leverage ratios.
- Gearing & leverage ratios stand lower on a timeline. Calculated on the basis of net debt, the company's gearing came in at 0.93x as of Dec'20. With further debt reduction in 2021 and projected internal capital generation through earnings, capitalization metrics are expected to improve over the rating horizon.

Corporate Governance Framework

- Board of Directors at FFBL comprises 12 members including Chairman and CEO & Managing Director. Board includes 4 independent directors and 6 non-executive directors. In order to ensure effective oversight, there are three sub-committees of the board, Board Audit Committee, Board HR & Remuneration Committee and Board Investment Committee.
- Board performance is ensured through the annual performance evaluation and ongoing board development activities.
- 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.
- Changes in senior management recruitment policy have been noted in the company, as a result of which certain senior management appointments have been revised. These revisions are viewed positively and in line with best practices.

Fauji Fertilizer Bin Qasim Limited (FFBL) Appendix I

FINANCIAL SUMMARY				*(amounts In PKR millions)*
BALANCE SHEET	**31-Dec-17**	**31-Dec-18**	**31-Dec-19**	**31-Dec-20**
Property, Plant & Equipment	10,405	9,748	10,428	10,193
Long Term Investments	23,065	24,565	26,180	24,546
Long Term Loans to Subsidiaries	-	2,400	3,130	6,990
Stock-in-Trade	1,854	5,655	14,756	2,862
Trade Debts	1,005	5,719	8,607	1,656
Advances	1,143	1,458	923	773
Short Term Investments	14,194	10,936	1,009	-
Cash & Bank Balances	3,547	3,690	5,294	25,048
Total Assets	**65,652**	**80,364**	**91,167**	**90,968**
Trade and Other Payables	23,198	29,825	34,993	21,638
Short Term Borrowings	9,934	13,913	28,227	15,822
Long Term Borrowings inc. Current Maturity	18,542	21,208	18,358	22,242
Total Interest Bearing Debt	28,476	35,122	46,585	38,064
Total Liabilities	**52,501**	**66,467**	**84,333**	**77,009**
Paid-up Capital	**9,341**	**9,341**	**9,341**	**9,341**
Total Equity	**13,151**	**13,897**	**6,834**	**13,959**
INCOME STATEMENT	**2017**	**2018**	**2019**	**2020**
Net Sales	52,733	61,511	66,839	83,234
Cost of Sales	46,705	53,327	60,955	70,655
Gross Profit	**6,028**	**8,183**	**5,885**	**12,579**
Selling & Distribution Expenses	4,872	4,525	5,345	5,518
Administrative Expenses	1,727	1,549	1,421	1,255
Other Income	4,377	3,182	4,370	7,925
Other Expense	423	1,259	2,158	4,394
Finance Cost	1,941	2,223	5,199	4,444
Profit / (Loss) before Tax	**1,441**	**1,810**	**(3,869)**	**4,893**
Taxation	(437)	(373)	(2,052)	(2,700)
Profit / (Loss) After Tax	**1,004**	**1,437**	**(5,921)**	**2,192**
RATIO ANALYSIS	**2017**	**2018**	**2019**	**2020**
Gross Margin (%)	11.4%	13.3%	8.8%	15.11%
Net Margin (%)	1.9%	2.3%	-8.9%	2.63%
Current Ratio (x)	0.84	0.88	0.74	1.04
Net Working Capital	(5,884)	(5,963)	(17,630)	2,103
Gearing (x)	2.17	2.53	6.82	2.73
Leverage (x)	3.99	4.78	12.34	5.52
FFO	808	2,843	(779)	5,956
FFO to Long Term Debt (%)	4.4%	13.4%	-4.2%	26.8%
FFO to Total Debt (%)	2.8%	8.1%	-1.7%	15.6%
Debt Servicing Coverage Ratio (x)	0.60	0.93	0.40	1.15
ROAA (%)	1.6%	2.0%	-6.9%	2.40%
ROAE (%)	7.8%	10.6%	-57.1%	21.10%

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.
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Due Diligence Meetings Conducted	see table below

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
16-3-2021	AA-	A-1	Stable	Upgrade
27-8-2019	A+	A-1	Stable	Initial

Due Diligence Meetings Conducted

Name	Designation	Date
Aamir Qureshi	Section Manager (Treasury)	October 22, 2020