RATING REPORT

Century Paper & Board Mills Limited

REPORT DATE:
November 23, 2018

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A+	A-1	A+	A-1
Rating Date	*November 23, 2018*		*December 11, 2017*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION	
Incorporated in 1984	External auditors: **BDO Ebrahim & Co., Chartered Accountants**
Public Limited Company	Chairman of the Board: **Mr. Iqbal Ali Lakhani**
Key Shareholders (with stake 5% or more):	Chief Executive Officer: **Mr. Aftab Ahmad**
Associated Companies –68.13%	
Modarabas and Mutual Funds – 7.32%	
General Public –11.32%	
Others – 6.89%	

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

Century Paper & Board Mills Limited

OVERVIEW OF THE INSTITUTION

Incorporated in 1984, Century Paper & Board Mills Limited (CPBM) is engaged in the manufacture of paper, paperboard and corrugated boxes. It is listed on Pakistan Stock Exchange. Financial Statements of the company for FY18 were audited by BDO Ebrahim & Co., Chartered Accountants.

Sponsor's Profile
Lakson Group was founded in 1954. The group has diversified operations in various sectors including paper & board, soap, detergents and toothpaste, printing & packaging, fast food and insurance. ***American franchises/affiliation*** *includes Colgate-Palmolive Company & McDonalds Corporation.*

Profile of Chairman
Mr. Iqbal Ali Lakhani has over 40 years of top management experience in group companies in finance, marketing, manufacturing industry and government relations. He also serves as a chairman of the corporate boards of 5 Lakson Group Companies. Mr. Lakhani received his ***B.A.*** *from the University of California – Berkeley and he is also a Charter Member of The Indus Entrepreneurs and Director of Pakistan Business Council.*

Financial Snapshot
Net Equity: June 2018: Rs. 5.5b, June 2017: Rs. 4.8b

Net Revenue: FY18: Rs. 18.9b, FY17: Rs. 15.4b

RATING RATIONALE

Century Paper & Board Mills Limited (CPBM) has around three decades of experience in paper and packaging industry and produces paperboard (Coated and Uncoated), paper (Machine Finished and Machine Glazed) and Corrugated boxes through its manufacturing facility located at N-5, District Kasur, Lahore-Multan Highway while registered office of the Company is based in Karachi. CPBM is a flagship Company of the Lakson Group of Companies with current installed capacity of 240,000 M.Tons (MT) per annum. During FY18, overall capacity utilization was reported at 95.6% (FY17: 89.4%). The Company's power requirement is being met by three Captive Power Plants, CoGen-1 (12.3 MW furnace oil & gas based power generation) and CoGen-2 (18 MW gas & diesel based power generation) and CoGen-3 (18 MW coal based power generation), with a 5MW LESCO connection as stand-by. CPBM uses various energy sources to arrive at the cheapest energy mix.

Product Portfolio

Paperboard Segment: Paperboard remains the flagship product category of the Company, accounting for around four-fifth of total sales. Over the last two years, capacity utilization of the segment has remained on the higher side at over 90%. The segment is further branched into Coated and Uncoated Paperboard. Both Coated and Uncoated Paperboard are used for packaging requirements of fast moving consumer goods (FMCG) segment. However, Uncoated Paperboard is primarily used in price conscious segments. Given the importance of quality of printing in the FMCG segment to attract customers, Uncoated board is increasingly being replaced by Coated board.

As per industry estimates, total local consumption of Coated Paperboard stands at approx. ~ 430,000 MT per annum; around two-third of the same comprises superior quality coated paper board which is primarily the segment catered to by CPBM. Around 70% of the demand for the quality paperboard segment is catered to by two local manufacturers - Bulleh Shah Packaging (Private) Limited (BSPPL) and CPBM, while the remaining demand is met through imports. Within the quality paperboard segment, CPBM remains the market leader and enjoys a market share of above 50%. Overall market share in the Coated Paperboard segment (including imports and lower quality segment production) stood over 35%.

Demand for Coated Paperboard has grown at a Compound Annual Growth Rate (CAGR) of 9.2% over the past five fiscal years (FY13-18). Pakistan's high consumption to GDP ratio along with urbanization and projected growth of the FMCG segment is expected to bode well for demand growth. In order to cater to growing demand and capture market share of imported paperboard, CPBM is in the process of increasing its capacity of coated paper board by 130,000MT.

Paper Segment: CPBM currently manufactures two sub-categories of paper ~ machine finished (MF) writing and printing paper and machine glazed (MG) paper. MF covers the needs of publishing, exercise books and printing market segments while MG caters to lamination and wrapping needs. The segment contributes around one-tenth of the total revenues. CPBM faces strong competition in this segment from imports and organized/unorganized sector. Market share of CPBM in MF paper and MG paper production is estimated to be around 6% and 21% respectively. Capacity utilization of this segment stood at 86.2% in FY18.

Corrugated Boxes: Corrugated boxes constitute around 11.5% of total sales, catering to merely 4% of the industry demand. Around 70% of the local demand is fulfilled by unorganized sector. The largest corrugated boxes manufacturer is BSPPL which caters to around 14% of country's demand. The segment is characterized by fragmented market structure and high competition from already established local players.

Rating Divers

Strong sponsor profile and market position
CPBM is part of the Lakson Group, a reputable conglomerate with strong financial profile and presence in diversified sectors including paper & board, soap, detergents and toothpaste, printing & packaging, fast food, telecommunication and insurance. The Company has strong presence in coated paperboard segment. The clientele of the Company is largely major Printing Houses of the country catering packaging needs of reputed national and MNCs, producing and marketing FMCGs, Pharmaceuticals, Cigarettes and confectionery etc.

Positive demand outlook from packaging industry along with lower dumping from China supports business risk profile.
Imports on dumped prices from China have been tapered off (due to reduction in waste paper imports into China due to restriction by Chinese government on account of environmental concerns) which has improved the competitiveness of local players and consequently resulted in higher margins over past few years (FY16-Present). Moreover, National Tariff Commission (NTC) announced Anti-Dumping Duty (ADD) on both coated bleached board and coated duplex board – Grey back. Final ADD was imposed in July-2017 with duties ranging from 14.98% to 18.57% on Coated Duplex Board products being imported from China, Indonesia and South Korea. However, announced ADD practically is not applicable because of ongoing litigation as importers have filed review petitions.

In addition to duty protection in the form of ADD, convenience for local customers due to less lead time, limited exposure to currency rate risk, facility of procuring desired quantity (vis-à-vis importers who have to buy in bulk) and lower product off take risk provides further support to business risk profile. Presently, ability to pass on the increase in input prices is considered strong given that quantum of dumped imports remain low. Going forward, management expects no dumping given export enquiries being received by the management.

Healthy sales growth in FY18. With paperboard and paper segment operating at near full capacities, increase in sales will primarily be a function of higher average selling prices. Impact of higher finance cost & overheads to be offset by expected improvement in margins and increase in topline.
Net sales increased by 23% during FY18. Increase in sales was a function of higher average selling prices (17%) and quantity sold (5%). Growth momentum in sales continued during 1QFY19 and increased by 19% vis-à-vis corresponding period. With paperboard and paper segment operating at near full capacities, increase in sales will primarily be a function of higher average selling prices. Gross margins have increased during FY18 and are expected to improve further given improved market conditions and competitiveness. However, impact of improved topline and margins is expected to be offset by higher finance cost given increase in quantum of borrowings and sizeable jump in benchmark rates.

Growth in cash flows has translated into improvement in liquidity profile. Sizeable capex planned over the rating horizon may weaken cash flow coverages of outstanding debt till inflows from enhanced capacity materializes
In absolute terms, Funds from Operations (FFO) amounted to Rs. 2.3b (FY17: Rs. 1.7b) depicting a 35% increase on account of higher overall profitability. Debt Service Coverage Ratio (DSCR) and FFO/Long-Term Debt remain adequate at 1.8x (FY17: 1.6x) and 0.5x (FY17: 0.3x) during FY18, respectively. The company's working capital cycle necessitates utilization of short term debt with extended time to collect receivables and fund inventory level. On a timeline basis, increase in raw material prices (including coal) and higher quantity produced has led to growth in short term borrowings. Stock in trade and trade debts represented around 154% of outstanding short-term borrowings while current ratio of CPBM was reported at 1.14(x) at end-FY18. Ageing profile of trade debts remains adequate. Going forward, sizeable debt funded capex planned over the rating horizon will translate in a weakening in cash flow coverage of outstanding debt till projected inflows from enhanced capacity materialize.

Gearing levels to remain elevated over the rating horizon
On account of higher profit retention, net equity of CPBM was reported at Rs. 5.5b (FY17: Rs. 4.8b) at end-FY18. Dividend payout ratio was reported at 36% (FY17: nil) during FY18. Higher utilization level of short term financing has led to gearing and leverage indicators remaining at elevated levels. Gearing (inclusive of preference shares) and leverage (including preference shares) stood at 1.63x (FY18: 1.48x; FY17: 1.62x) and 2.34x (FY18: 2.12x; FY17: 2.21x) at end-1QFY19. During 1QFY19 CPBM has approved redemption of outstanding preference share capital of Rs. 901.21 million along with proportionate dividends which would be financed through borrowings. Going forward, quantum of equity injection for planned expansion will determine trend in leverage indicators. JCR-VIS expects leverage indicators to remain elevated over the rating horizon.

Century Paper & Board Mills Limited **Appendix I**

FINANCIAL SUMMARY			*(amounts in PKR millions)*
BALANCE SHEET	**FY18**	**FY17**	**FY16**
Fixed Assets	9,613.4	9,733.2	10,092.9
Stock-in-Trade	2,897.3	1,963.1	1,731.9
Trade Debts	2,366.3	1,585.4	1,265.4
Cash & Bank Balances	415.5	226.5	217.5
Total Assets	17,304.2	15,437.5	14,980.7
Trade and Other Payables	2,215.8	1,841.4	1,580.9
Long Term Debt ***(*incl. current maturity + preference shares)***	4,769.8	4,970.5	5,725.4
Preference shares	901.2	901.2	901.2
Short Term Debt	3,426.7	2,840.2	1,988.4
Total Equity ***(*excluding preference shares)***	5,541.7	4,811.8	4,949.4
INCOME STATEMENT			
Net Sales	18,964.6	15,401.2	13,389.1
Gross Profit	2,505.8	1,791.5	1,267.3
Operating Profit	1,891.6	1,310.7	792.1
Profit After Tax	991.9	602.2	322.4
RATIO ANALYSIS			
Gross Margin (%)	13.2%	11.6%	9.5%
FFO to Total Debt (x)	0.29	0.22	0.15
FFO to LT Debt (x)	0.49	0.35	0.21
Gearing (x)	1.48	1.62	1.56
Leverage (x)	2.12	2.21	2.03
DSCR (x)	1.82	1.58	1.58
ROAA (%)	6.06%	3.96%	2.22%
ROAE (%)	16.32%	10.42%	5.67%

ISSUE/ISSUER RATING SCALE & DEFINITION — Appendix II

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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	Century Paper & Board Limited				
Sector	Paper & Board				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	23-Nov-18	A+	A-1	Stable	Reaffirmed
	11-Dec-17	A+	A-1	Stable	Reaffirmed
	23-May-16	A+	A-1	Stable	Reaffirmed
	15-Dec-14	A+	A-1	Stable	Reaffirmed
	20-Nov-13	A+	A-1	Stable	Upgrade
Instrument Structure	N/A				
Statement by the Rating Team	JCR-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	JCR-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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