RATING REPORT

Century Paper & Board Mills Limited

REPORT DATE:
November 21, 2019

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 21, 2019*		*November 23, 2018*	
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 – 8.04%	
General Public –11.16%	
Others – 6.38%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria *Industrial Corporates (May 2016)*
http://www.vis.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 42 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 also served as Director of Pakistan Business Council.

Financial Snapshot

Net Equity: June 2019: Rs. 6.2b, June 2018: Rs. 5.5b

Net Revenue: FY19: Rs. 22.2b, FY18: Rs. 18.9b

RATING RATIONALE

Century Paper & Board Mills Limited (CPBM) has been engaged in paper and packaging business for around three decades and operates as a flagship Company of Lakson Group of Companies. CPBM production capacity stood at 240,000 tons per annum (TPA). Manufacturing facility is located at District Kasur, Lahore-Multan Highway while registered office of the company is based in Karachi. Capacity utilization has remained on the higher side and was reported at 95% during FY19.

CPBM's power requirement is being met by three Captive Power Plants; 1) CoGen-1 (12.3 MW furnace oil based power generation) 2) CoGen-2 (18 MW gas & diesel based power generation) 3) CoGen-3 (18 MW coal based power generation), with a 5MW LESCO connection as stand-by arrangement. The company utilizes various energy sources to arrive at the cheapest and most efficient energy mix.

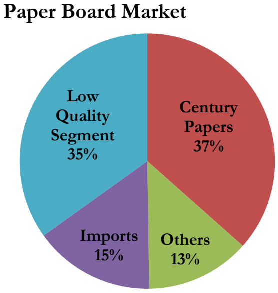
<u>Product Portfolio</u>

Paperboard (Coated and Uncoated)

Paperboard continues to remain the flagship product category, accounting for around four-fifth of total revenue. The segment is further branched into coated and uncoated paperboard with both being used for packaging requirements of fast moving consumer goods (FMCG). Capacity utilization in this segment remains on higher side at above 90%. Given consistently high capacity utilization and in order to capture market share of higher priced imports, management is reassessing capacity expansion project feasibility based on revised rupee dollar parity and change in demand supply dynamics. Amid expansion plans, the management is diversifying its footprint in international market through exports (at reasonable margins) to few countries in the region.

Exhibit 1

Coated Paper Board Market



Coated paper board market size was estimated at 424,000 tons in 2019. Of this, two-third comprises premium quality product wherein 56% market share (Premium Segment) is held by CPBM. Remaining overall demand is met by Bulleh Shah Packaging Private Limited (BPPL) and imports. CPBM, despite slight contraction of paper & paperboard industry demand, managed to maintain its market share in coated paperboard (including imports and lower quality segment) at ~37%.

Paper (Machine Finished and Machine Glazed)

CPBM currently manufactures two sub-categories of paper ~ machine finished (MF) writing and printing paper and machine glazed (MG) paper. The segment contributes around one-tenth of the total revenues. Capacity utilization of this segment stood at 95% in FY19.

Corrugated Boxes

Corrugated boxes also constitute around one-tenth of total sales, catering to 4% of industry demand. The segment is characterized by fragmented market structure and high competition from unorganized sector which caters to around 70% of local demand.

<u>Key Rating Divers</u>

Established track record of sponsors and strong market reputation

The parent entity 'Lakson Group' is 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. CPBM has a stronghold (market leader) in coated paperboard industry along with reputed client base which is a key rating driver.

Challenging economic environment impacted the paper & paperboard industry demand. Slowdown in imports due to rupee devaluation and lower dumping from China supported sales of local players. Demand growth in expected to rebound in the ongoing year.

Paper & paperboard industry has witnessed a slight contraction by ~3% in overall market size during outgoing fiscal year 2019. The decline is attributable to overall economic slowdown in the country. Nonetheless, CPBM withstood the challenging operating environment and maintained its market share whereas reduction was observed in imports of coated paperboard. Significant rupee devaluation resulted in higher landed cost of imports vis-à-vis local products. Moreover, Imports on dumped prices from China have 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.

Anti-Dumping Duties on coated paperboard provide additional support to local industry players. While gap remains in effective implementation of these duties, risk of liability on importers (in terms of duty payment) acts as a constraint for imports.

In FY19, sales growth was primarily a function of higher selling prices. However, profitability declined due to sizeable jump in finance cost. Going forward, stable sales volume and declining international raw material prices are expected to support earning profile despite significant increase expected in power cost.

Topline of the company amounted to Rs. 22.2b (FY18: Rs. 18.9b) in FY19, registering a growth of ~17%. Growth in sales was primarily a function of increase in average selling prices (16%) whereas sales volume grew moderately by ~1%. Higher raw material costs (largely due to rupee devaluation) and increased fuel/power expenses (higher RLNG prices) translated into significantly higher cost of sales. Resultantly, gross margins declined and were reported at 12% (FY18: 13.2%) during FY19. This along with significant increase in finance cost effected profitability. Profit after tax was reported at Rs. 884.2m (FY18: Rs. 991.9m) in FY19. Going forward, stable sales volume and declining international raw material prices are expected to support earning profile despite significant increase expected in power cost.

Adequate liquidity profile and comfortable debt coverage indicators.

In line with lower profitability, Funds flow from Operations (FFO) decreased to Rs. 1.82b (FY18: Rs. 2.34b) in FY19. As a result, FFO in relation to long term and total debt were reported lower at 43.5% (FY18: 49.1%) and 21.6% (FY18: 28.6%), respectively. Debt Service Coverage Ratio (DSCR) also stood lower at 1.44x (FY18: 1.82x) in FY19. However, cash flow coverage of outstanding debt obligation is considered adequate. Stock in trade and trade debts represented around 154% of outstanding short-term borrowings while current ratio of CPBM was reported at 1.21(x) at end-FY19. 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, short term borrowings have grown on account of higher working capital requirements amidst rupee devaluation.

Leverage indicators witnessed improvement on the back of higher equity base. Gradual reduction in leverage indicators is expected till debt for expansion is undertaken.

At end-FY19, net equity was reported at Rs. 6.2b (FY18: Rs. 5.5b (without preference share)) on account of higher profit retention. Dividend payout ratio (to ordinary & preference) was reported at 20% (FY18: 40%) during FY19. Debt profile of the company comprises a mix of short term and long term debt with total interest bearing liabilities amounting to Rs. 8.4b (FY18: Rs. 8.2b) as at end-FY19; long term debt constituted around one-half of total debt. During outgoing year, CPBM redeemed its outstanding preference share in full amounting to Rs. 901.2m along with proportionate cumulative dividends. Gearing and leverage stood lower at 1.36x (FY18: 1.48x; FY17: 1.62x) and 1.98x (FY18: 2.12x; FY17: 2.21x) at end-FY19. Going forward, gradual reduction in leverage indicators is expected due to higher internal capital generation till debt for expansion is undertaken.

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

FINANCIAL SUMMARY			*(amounts in PKR millions)*
BALANCE SHEET	**FY19**	**FY18**	**FY17**
Fixed Assets	9,395.3	9,613.4	9,733.2
Stock-in-Trade	3,484.2	2,897.3	1,963.1
Trade Debts	3,046.3	2,366.3	1,585.4
Cash & Bank Balances	351.7	415.5	226.5
Total Assets	18,543.7	17,304.2	15,437.5
Trade and Other Payables	2,528.1	2,215.8	1,841.4
Long Term Debt ***(*incl. current maturity + preference shares for FY18 & FY17)***	4,182.9	4,769.8	4,970.5
Preference shares	-	901.2	901.2
Short Term Debt (STD)	4,247.3	3,426.7	2,840.2
Paid Up Capital	1,470.2	1,470.2	1,470.2
Total Equity ***(*excluding preference shares for FY18 & FY17)***	6,188.9	5,541.7	4,811.8
INCOME STATEMENT			
Net Sales	22,240.6	18,964.6	15,401.2
Gross Profit	2,662.3	2,505.8	1,791.5
Operating Profit	2,001.1	1,891.6	1,310.7
Profit Before Tax	1,239.0	1,431.2	903.8
Profit After Tax	884.2	991.9	602.2
RATIO ANALYSIS			
Gross Margin (%)	12.0%	13.2%	11.6%
Net Margin (%)	3.9%	5.2%	3.9%
Trade Debt/Sales (%)	13.7%	12.5%	10.3%
FFO to Total Debt (x)	0.22	0.29	0.22
FFO to LT Debt (x)	0.44	0.49	0.35
Current Ratio	1.21	1.14	0.98
Stock+ Trade Debts/STD (%)	154%	154%	125%
Gearing (x)	1.36	1.48	1.62
Leverage (x)	1.98	2.12	2.21
DSCR (x)	1.58	1.86	1.60
ROAA (%)	4.9%	6.1%	3.9%
ROAE (%)	14.0%	16.3%	10.4%

ISSUE/ISSUER RATING SCALE & DEFINITION 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	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				
21-Nov-19	A+	A-1	Stable	Reaffirmed
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	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.
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