RATING REPORT

Century Paper & Board Mills Limited

REPORT DATE:
November 10, 2021

RATING ANALYST:

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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	AA-	A-1	A+	A-1
Rating Date	*November 10, 2021*		*December 1, 2020*	
Rating Outlook	Stable		Positive	
Rating Action	Upgrade		Maintained	

COMPANY INFORMATION	
Incorporated in 1984	External auditors: **BDO Ebrahim & Co., Chartered Accountants**
Public Listed Company	Chairman of the Board: **Mr. Iqbal Ali Lakhani**
Key Shareholders (with stake 5% or more):	Chief Executive Officer: **Mr. Aftab Ahmad**
Associated Companies *–68.67%*	
Modarabas and Mutual Funds *– 7.38%*	
General Public *–13.22%*	
Others *– 5.10%*	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria ***Industrial Corporates (August 2021)***
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

OVERVIEW OF THE INSTITUTION

Century Paper & Board Mills Limited (CPBM) was incorporated in 1984 as part of Lakson Group of Companies. The sponsor has diversified interest in paper & packaging, soap, detergents and toothpaste, fast food and insurance sectors. American franchises/affiliation includes Colgate-Palmolive Company & McDonalds Corporation.

Profile of Chairman

Mr. Iqbal Ali Lakhani has over 43 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 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.

RATING RATIONALE

Century Paper & Board Mills Limited (CPBM) with an extensive experience of more than three decades enjoys established market position in paper and packaging industry, particularly in coated board segment. The company has its production facility (mill) in District Kasur, Lahore-Multan Highway with total installed capacity of 265,000 MT (FY20: 240,000 MY) per annum at end-FY21 while overall capacity utilization level has remained above 95% over the past three years. As per management, the capacity has been increased by 10% in FY21 on account of modifications in existing plant & machinery along with quality & efficiency enhancement initiatives. Capacity enhancement is primarily in the coated board segment.

Category	Capacity (MT)	Actual Production (MT)	Capacity Utilization (%)
FY21			
Coated Board	183,500	181,500	99%
Uncoated board	20,000	13,500	68%
Paper	21,500	16,700	78%
Line/Fluting for Box plant	40,000	40,300	101%
Total	**265,000**	**252,000**	**95%**
Box plant (Conversion)	35,000	35,000	100%

The company has planned capital expenditure for BMR, total outlay of which is estimated at Rs. 3.9b, 65%, 27% and 8% of which comprises capacity enhancement of paper and board machines, power and utilities, and upgradation/replacement, respectively. 72% of the cost is projected to be financed through TERF facility while the remaining shall be funded through internal cash generation. Around Rs. 1.1b worth of investment has been incurred at end-June'21. By end-Mar'22, management envisages installed capacity to report at 285,000MT.

In addition, CPBM owns three captive power plants which fulfill its entire power requirements while a combination of coal, gas and furnace oil powered sources is employed to arrive at the cheapest and most efficient fuel mix. The company has recently installed solar grid panels for in-house energy consumption in factory. Total installed capacity of the solar panels is 3.6MW at end-FY21.

Product Portfolio

- **Coated Paperboard –** CPBM's flagship product category and accounts for around three-fourth of total revenue of the company. Given growth in overall paper & paperboard industry, coated board market size (high & low quality segments) grew by 10% in 2021 and stood at 473k MT (FY20: 430k MT) due to shift in consumer sentiments towards online shopping amidst COVID-19. Of this, around 70% comprises high quality segment wherein CPBM has more than 70% market share while the same stands at 40% in terms of overall coated board market size. Given the higher demand for improved quality printing, the quality coated board segment has grown at a faster pace vis-à-vis overall coated board market. The same is evident from increasing productivity levels and consequently reporting higher capacity utilization at 99% (FY20: 95%) in FY21. This has facilitated CPBM to enhance the customer base in the segment.

- **Paper –** CPBM currently manufactures two sub-categories of paper ~ machine finished (MF) writing and printing paper and machine glazed (MG) paper which is mainly used for food packaging. This segment contributes around 8% of total sales in FY21. Overall paper segment contracted in FY21 given closure of schools amidst COVID-19. Certain high margin value added products were added in paper segment during last couple of years. Going forward, sales from the paper segment are expected to improve to best utilize the available capacity, as per management.

- **Corrugated Boxes –** Represent around 14% of total sales, catering to 5% of industry demand. The segment is characterized by fragmented market structure and high competition from unorganized sector which caters to around 75% of local demand. The company is focusing and serving the quality conscious and organized sector users as per business strategy.

- **Uncoated Board-** Represents around 4% of total sales. As per management, this segment is declining on a timeline basis due to overall demand reduction, consequently capacity utilization of the same is reported lower at 68% in FY21. However, with recent modifications company has planned to use this capacity for some value added and growing market segment, which is coated packaging boards segment.

<u>Key Rating Divers:</u>

Strong sponsor profile

The parent entity 'Lakson Group' is a reputable conglomerate with strong financial profile and diversified presence in paper & packaging, soap, detergents, toothpaste, printing & packaging, fast food, telecommunication and insurance sectors.

Overall business risk profile is supported by end clients mostly belonging to FMCG segment and favorable demand supply dynamics. Going forward, the growth rate of the sector is expected to exceed GDP growth rate of the economy.

After contracting by 6% in FY20, the market size of paper & paperboard industry increased by 3.5% in FY21 on account of gradual improvement in demand. Gradual contraction of imports of coated board along with other benefits (such as availability and lower lead time to customers) provides support to local industry players. End clients mostly belonging to FMCG segment reduces the demand risk where the demand is relatively stable. In addition, COVID-19 crisis has affected consumers' consumption patterns and health consciousness which has favorably impacted the packaging industry over medium to long term.

Revenue of CPBML has depicted a double-digit year on year growth during the last three years being a function of increased aggregate demand and higher average selling prices. Gross Margins have been improving on a timeline basis owing to operational efficiencies, inventory gains and lower fuel cost. Going forward, management envisages consistent financial performance on the backdrop of higher projected industry demand and cost-efficiencies post expansion.

Sales revenue of the company has grown at a CAGR of 15% over the past three years (FY18-FY21)

During FY21, net sales registered a year-on-year (YoY) growth rate of ~18%. The growth has been a function of both volumetric growth of 8% and a 9% increase in average selling prices. Given that the Company has been operating at nearly full capacities in the ongoing year, sufficient orders in hand in lieu of stable demand topline is projected to depict growth going forward.

Raw material cost forms the major portion of cost of sales. Around 58% of the raw material is imported while the remaining is procured locally. Rapid increase in wood pulp prices, waste paper and energy costs was witnessed in the second half of the outgoing year and selling prices were adjusted as per market conditions to pass on impact of cost escalations. Consequently, gross margins of the company improved to 19.9% in FY21 vis-à-vis 16.2% in FY20 due to operational efficiencies, inventory gains and lower fuel cost. Finance costs were reported significantly lower at Rs. 406.0m (FY20: Rs. 987.0m) in FY21 on the back of lower policy rate, cheaper borrowing schemes introduced by the State Bank of Pakistan along with reduced quantum of short term borrowings at end-FY21. Despite increase in taxation (FY21: Rs. 1.3b; FY20: Rs.0.6b), bottom line was reported higher at Rs. 3.0b (FY20: Rs. 1.5b) in FY21. Going forward, management envisages consistent financial performance on the backdrop of higher projected industry demand and cost-efficiencies post expansion.

Healthy cash flow generation has resulted in strong liquidity profile. Decrease in working capital cycle has resulted in lower utilization of short-term borrowings. Going forward, liquidity profile is expected to remain strong in view of higher projected profitability.

In absolute terms, Funds from Operations (FFO) amounted to Rs. 4.7b (FY20: Rs. 2.7b; FY19: Rs. 1.8b) depicting a 74% increase on account of higher overall profitability and noticeable decrease in finance costs. This has translated into improved liquidity indicators with Debt Service Coverage Ratio (DSCR) being reported at 4.28x (FY20: 2.20x; FY19: 1.44x) in FY21. Similarly, FFO in relation to long-term debt improved considerably to 141.9% (FY20: 93.1%; FY19: 43.5%) in FY21. CPBM's working capital cycle necessitates utilization of short-term debt with extended time to collect receivables. Stock in trade and trade debts represented around 388% of outstanding short-term borrowings. Going forward, liquidity profile is expected to remain strong in view of consistent financial performance.

Leverage indicators have trended downwards on a timeline basis with gearing reporting below 1.0x at end-FY21. Despite projected increase in debt levels to finance BMR, gearing and leverage levels are expected to remain within manageable levels on the back of projected increase in equity through profit generation.

Equity base of the company grew by 36% in FY21 and was reported at Rs. 10.3b (FY20: Rs. 7.6b) on the back of higher profit retention. Debt profile of the company comprises a mix of short and long term debt with total interest bearing liabilities amounting to Rs. 5.5b (FY20: Rs. 6.5b) as at end-FY21; long term debt constituted 60% of total debt. Going forward, the company has plans to drawdown long-term debt to fund BMR project. Gearing and leverage indicators remain on the lower side at 0.53x (FY20: 0.86x) and 1.07x (FY20: 1.45x) respectively at year-end FY21. Despite projected increase in debt levels, gearing and leverage levels are expected to remain within manageable levels on the back of projected increase in equity through profit generation.

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

Century Paper & Board Mills Limited (Financial Summary) (PKR Mlns)				
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**FY21**
Fixed Assets	9,589.72	9,372.85	9,290.19	9,946.26
Stock-in-Trade	2,897.29	3,484.17	3,727.78	5,188.54
Trade Debts	2,366.32	3,046.32	2,907.93	3,259.02
Cash & Bank Balances	415.51	351.70	237.17	492.50
Total Assets	17,304.20	18,453.72	18,597.00	21,407.56
Trade and Other Payables	2,215.77	2,528.06	2,893.27	4,022.72
Long Term Debt	4,769.78	4,182.89	2,905.76	3,310.95
Short Term Debt	3,426.69	4,247.27	3,616.77	2,178.24
Total Debt	8,196.47	8,430.15	6,522.54	5,489.19
Total Liabilities	11,762.56	12,264.81	11,014.72	11,085.64
Total Equity	5,541.66	6,188.93	7,582.27	10,321.92
Paid Up Capital	1,470.18	1,470.18	1,470.18	1,764.22
INCOME STATEMENT				
Net Sales	18,964.57	22,240.62	24,344.96	28,659.91
Gross Profit	2,505.77	2,662.30	3,936.37	5,695.36
Operating Profit	1,891.57	2,001.14	3,142.77	4,652.27
Profit Before Tax	1,431.22	1,238.98	2,155.74	4,246.29
Profit After Tax	991.86	884.15	1,521.77	2,959.66
RATIO ANALYSIS				
Gross Margin (%)	13.2%	12.0%	16.2%	19.9%
Net Margin	5.2%	4.0%	6.3%	10.3%
Net Working Capital	960.89	1,603.78	1,939.18	4,290.86
Trade debts/Sales	12.5%	13.7%	11.9%	11.4%
FFO	2,340.82	1,820.49	2,705.87	4,698.15
FFO to Total Debt (%)	28.6%	21.6%	41.5%	85.6%
FFO to Long Term Debt (%)	49.1%	43.5%	93.1%	141.9%
Current Ratio (x)	1.14	1.21	1.26	1.60
Debt Servicing Coverage Ratio (x)	1.86	1.44	2.20	4.28
Gearing (x)	1.48	1.36	0.86	0.53
Leverage (x)	2.12	1.98	1.45	1.07
(Stock in Trade+Trade Debts)/STD	154%	154%	183%	388%
ROAA (%)	6%	5%	8%	15%
ROAE (%)	16%	15%	22%	33%

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	see table below

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
10-Nov-21	AA-	A-1	Stable	Upgrade
1-Dec-20	A+	A-1	Positive	Maintained
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.
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	see table below

Name	Designation	Date
Mr. Rashid Dastagir	CFO	15- Sept-2021
Mr. Tanveer Ahmed	General and Marketing Manager	15- Sept-2021