RATING REPORT

Ittehad Chemicals Limited (ICL)

REPORT DATE:
January 25, 2018

RATING ANALYSTS:

Maimoon Rasheed
maimoon@jcrvis.com.pk

Hamza Rizwan
hamza.rizwan@jcrvis.com.pk

RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2	A-	A-2
Rating Date	*25 Jan'18*		*20 Dec'16*	
Rating Outlook	Stable		Stable	
Rating Date	*25 Jan'18*		*20 Dec'16*	

COMPANY INFORMATION

Incorporated in 1991	**External auditors:** M/s BDO Ebrahim & Co. Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Mohammad Siddique Khatri
Key Shareholders:	**Chief Executive Officer:** Mr. Abdul Sattar Khatri
Sponsoring Family – 27.7% Chemtix Industries Ltd. – 5.5%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: *Industrial Corporate (May 2016)*
http://www.jcrvis.com.pk/home2.aspx

Ittehad Chemicals Limited

OVERVIEW OF THE INSTITUTION

ICL was incorporated as a public limited company in 1991 under the Companies Ordinance, 1984. Privatization of the company took place in 1995. The company is listed on Pakistan Stock Exchange. ICL is engaged in the business of manufacturing and selling caustic soda and other allied chemicals.

Profile of Chairman

Mr. Mohammaed Siddique Khatri has about 30 years of experience in the field of Chemical, Textile Industries, Finance and Corporate Affairs of International and local Companies. He is also working as Partner of M/s Ittehad Developers.

Profile of CEO

Mr. Abdul Sattar Khatri carries experience of above 22 years across Chemical Manufacturing, Business Development and Textile Processing Industries. He is also on the Board of Ittehad Developers and Chemi Dyestuffs Industries (Pvt) Limited.

Core Equity: 1QFY18: Rs. 2.4b; FY17: Rs. 2.4b; FY16: Rs. 2.0b

Assets: 1QFY18: Rs. 6.6b; FY17: Rs. 6.6b; FY16: Rs. 6.2b

Profit After Tax: 1QFY18: Rs. 23.3m; FY17: Rs. 233.3m; FY16: 167.4m

RATING RATIONALE

Ratings assigned to Ittehad Chemicals Limited (ICL) take into account the company's prominent position in the chlor-alkali sector. Ratings also incorporate conservative risk appetite of sponsors that has resulted in adequate financial profile of the company. Ratings also recognize management's continuing efforts of technology advancement in order to minimize operating costs. However, volatile product prices have kept margins under pressure recently.

- **Industry:** The chlor-alkali sector is oligopolistic in nature with three players operating in the country. Demand of caustic soda is linked to overall industrial production; there has been an oversupply situation in the industry. Overall capacity utilization has remained moderate owing to imbalance in the demand and supply of product. The export channel has also been utilized; however, the extent of the same has remained limited. Going forward, the industry foresees relative stability in local prices along with better availability of gas.

- **Production Technology**: ICL has maintained its focus on technological advancement to improve operational efficiencies. The company is in the process of replacing IEM-I plant with more efficient IEM-III, which is likely to be commercially operational by 4QFY18. Subsequently, the management intends to utilize IEM-I plant only on a need basis. Meanwhile, the obsolete DSA plant has been scrapped in FY17.

- **Operating Performance:** Caustic soda remained the primary contributor representing 70% (FY16: 71%) of overall sales during FY17; other major contribution emanated from the sale of hydrochloric acid and sodium hypochlorite. While revenue increased on the back of higher volumetric sales, the positive impact was partly diluted on account of decline in margins. Gross margins declined owing to lower average prices of caustic soda and some other auxiliary products. Although pretax profit remained largely stagnant, bottom line stood higher mainly on the back of tax credit availed on the acquisition of plant and machinery. During 1QFY18, margins have remained under pressure. However, recent increase in the product price and commencement of timely commercial operations of IEM-III are expected to help in improving margins. Being prudent, the company continues to recognize provision related to industrial as well as captive power consumption under Gas Infrastructure Development Cess that amounted to Rs. 497.6m (FY16: Rs. 346m) by end-FY17.

- **Funding and Cash flows:** Long term borrowing (including current portion) comprises 35.1% (FY16: 40.6%) of total liabilities at end-FY17. The company has issued right shares worth Rs. 300m each during the last two consecutive years. This along with reduction in borrowings have resulted in decline in gearing to 0.86x (FY16: 1.19) by end-FY17. With higher funds from operations, FFO to total debt improved to 0.25x (FY16: 0.16x) while debt service coverage ratio also stood comfortable at 1.35x.

- **Future Projects:** The company has embarked upon exploring various avenues in order to diversify its business risk. While the company intends to finance capex through commercial borrowings, gearing and coverages are projected to remain sound, going forward.

Ittehad Chemicals Limited — Appendix I

FINANCIAL SUMMARY

(amounts in PKR millions)

BALANCE SHEET	Sept-30-17	Jun-30-17	Jun-30-16	Jun-30-15
Fixed Assets	4,534	4,531	4,235	3,914
Stock-in-Trade	483	392	477	171
Trade Debts	472	551	501	462
Cash & Bank Balances	139	108	126	119
Total Assets	6,640	6,596	6,249	5,351
Trade and Other Payables	1,087	1,006	821	802
Long Term Debt *(*incl. current maturity)*	1,062	1,188	1,409	1,084
Short Term Debt	952	890	949	863
Total Equity	3,240	3,216	2,779	2,373

INCOME STATEMENT	Sept-30-17	30-Jun-17	Jun-30-16	Jun-30-15
Net Sales	1,266	4,990	4,557	4,046
Gross Profit	189	820	791	423
Operating Profit	75	384	372	31
Profit After Tax	23	233	167	84

RATIO ANALYSIS	Sept-30-17	30-Jun-17	Jun-30-16	Jun-30-15
Gross Margin (%)	14.9	16.4	17.4	10.5
Net Working Capital	-462	-370	-86	-608
Gearing	0.83	0.86	1.19	1.23
FFO to Total Debt (x)	0.18	0.25	0.16	0.001
FFO to Long Term Debt (x)	0.36	0.43	0.28	0.002
Debt Servicing Coverage Ratio (x)	0.81	1.35	1.33	0.69
ROAA (%)	1.4	3.6	2.9	1.7
ROAE (%)	3.8	10.6	9.4	5.4

ISSUE/ISSUER RATING SCALE & DEFINITIONS

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	Ittehad Chemicals Limited
Sector	Chlor-alkali (Chemical Sector Sub-set)
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	(see table below)
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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, JCR-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. JCR-VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2018 JCR-VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to JCR-VIS.

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
		RATING TYPE: ENTITY		
01/25/2018	A-	A-2	Stable	Reaffirmed
12/20/2016	A-	A-2	Stable	Reaffirmed
12/22/2015	A-	A-2	Stable	Reaffirmed
12/22/2014	A-	A-2	Stable	Reaffirmed
03/18/2013	A-	A-2	Stable	Reaffirmed