RATING REPORT

Attock Cement Pakistan Limited (ACPL)

REPORT DATE:
November 07, 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 Outlook	Stable		Stable	
Rating Date	*October 24,2019*		*June 12, 2018*	

COMPANY INFORMATION	
Incorporated in 1981	**External auditors:** M/s A.F. Ferguson & Co., Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Laith G. Pharaon
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Babar Bashir Nawaz
Pharaon Investment Group Limited, Holding S.A.L Beirut, Lebanon – 84.06%	
Institutions – 2.39%	

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

Attock Cement Pakistan Limited

OVERVIEW OF THE INSTITUTION

Attock Cement Pakistan Limited (ACPL) is a subsidiary of Pharaon Investment Group Limited Holding S.A.L. (PIGL). PIGL has interest in diversified sectors. ACPL was incorporated in 1981 as a public limited company under the Companies Ordinance 1984. Main business of ACPL is manufacturing and sale of cement. The company is listed on Pakistan Stock Exchange Limited (formerly Karachi Stock Exchange Limited) with the head office located in Karachi while the factory is situated at Hub Chowki, Lasbella and Balochistan.

Profile of CEO:

Mr. Babar Bashir Nawaz is a seasoned professional with experience spanning over 30 years with Attock Group. Before his appointment as CEO in 2002, Mr. Babar held various positions in Finance, Personnel, Marketing and General Management. He holds a Master's degree in Business Administration from the Quaid-e-Azam University in Islamabad. Mr. Babar also serves as a Director on the Board of all the listed companies of the Group in Pakistan.

RATING RATIONALE

Attock Cement Pakistan Limited ('ACPL' or 'the Company') has the second largest cement facility in South Region, which has an aggregate of 6 cement producers.

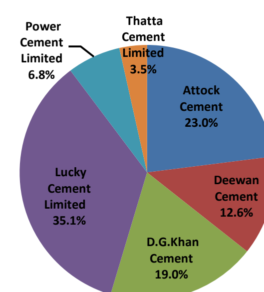

Figure 1: Market Share (South)

Local despatches to suffer amid curtailed fiscal space while exports pick up pace. Excess supply, rupee devaluation and additional taxation (FED) have kept margins under pressure.

The cement industry in Pakistan is going through an expansionary cycle whereby 10.7mn MTs have been added during the past 2 years and 16m MTs are in the pipeline to be installed over the next 2 years. However on the demand side, rupee devaluation and uptick in inflation has kept construction activity condensed resulting in a slowdown in industry despatches. Given the current economic scenario, VIS does not expect any major uptick in total local dispatches in the short to medium term, to absorb the incremental supply. This will likely impact profitability margins, as the cement producers partake in price competition.

So far, the South region has fared well on the back of sticky domestic sales prices – which have remained higher vis-à-vis prices in the North region, in addition to the added benefit of export sales. Export sales are not as prevalent in the North region, with their export market being limited to Afghanistan. Furthermore, in case of the South region, post-commencement of Power Cement's (PC) new plant, the expansionary phase has been concluded with no further capacity additions expected in the medium term.

Nevertheless, the addition of PCL's new capacity is still expected to cause a greater supply overhang, particularly in view of the macroeconomic forecasts. Risks to the South region remain, as additional capacity comes online in the North region, which is expected to translate in increasing influx of cement despatches from the North in the South region. Despite higher PSDP allocation budgeted for FY20, infrastructure driven local demand is expected to remain weak as fiscal constraints would not allow complete utilization of the budget. However, potential construction of mega-infrastructure projects i.e. dams, may revive overall demand for cement primarily for North players given their close proximity to dam sites, which may ease supply pressures in the South.

Table 1: Industry Despatches (in Mn MTs, unless stated otherwise)

	FY13	FY14	FY15	FY16	FY17	FY18	FY19
Industry Capacity	44.6	44.6	45.6	45.6	46.4	53.4	59.4
North Dispatches	26.4	27.1	27.9	30.9	32.3	37.1	35.0
South Dispatches	7.0	7.2	7.5	7.9	8.0	8.8	11.9
Total Dispatches	33.4	34.3	35.4	38.9	40.3	45.9	46.9

Operating Performance

Amidst a challenging macroeconomic environment, ACPL's despatches in the domestic market grew by 2%. Nevertheless, given capacity enhancement by other companies in the South region, ACPL's market share (cement) trended down sharply (Jun'19: 20.6%; Jun'18: 28.2%). In overview of the prevailing slowdown, the Company's strategy to develop export markets, over the years, has paid off

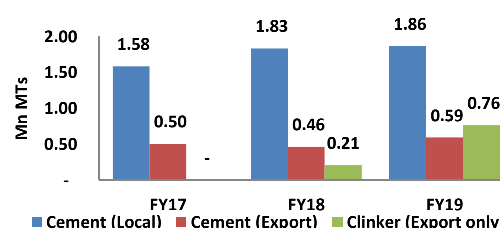

Figure 2: Cement & Clinker Despatches - ACPL

given healthy growth in cement despatches. Clinker exports, having been initiated in 2018, almost tripled in 2019.

Given addition of Line 3 in 2018, actual production increased from 2.5mn MTs to 3.2mn MTs. Capacity utilization for the year remained on the higher side (FY19: 110%; FY18: 109%). Given the recent addition of Line 3, which is technically advanced vis-à-vis Line 1 & 2, average power and heat consumption requirements have reduced translating in improved efficiency.

In FY19, ACPL reported topline revenue of Rs. 20.8bn, 26% higher than FY18 (Rs. 16.5bn). Gross sales in the domestic market depicted moderate growth of 5%, with majority (2/3rd) of the uptick arising from higher pricing. In the export market, the Company fared very well, with net sales revenue increasing by 121% (FY19: Rs. 7.1bn; FY18: 3.2bn). It is pertinent to mention that export sales are undertaken at significantly lower margins vis-à-vis domestic sales (roughly 5x lower). Going forward pressure on local sales for the company is expected in view of prevailing contraction in consumption and higher supply overhang while growth in quantum of export sales would be driven by clinker exports.

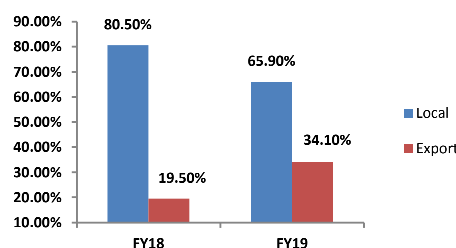

Figure 3: Net Sales Breakup - ACPL

Cost pressures coupled with increased competition have contracted gross margin, while higher financial charges has impacted net margins

In the last couple of years, the local currency (PKR) has significantly depreciated against the greenback (FY19: 32%; FY18: 16%). In the same period Federal Excise Duty (FED) has been increased by 67%. All of this has negatively impacted gross margins which have been dropping during this period. Furthermore, with the industry-wide enhancement in capacities and in view of the depressed demand outlook, the pricing power of industry participants has reduced.

In FY19, ACPL's operating profit was lower by 10%, mainly attributable to rising cost of production. The Company's gross margin reduced from 29.1% to 23.1%, despite being assisted by a 7% drop in international coal prices. With the management ensuring strong control on overheads – as evident from the 6% drop in overheads (incl. other expenses) – the impact on operating margin was relatively lower (FY19: 14.6%; FY18: 20.0%). Even though majority (50%) of the Company's debt – which entirely constitutes short-term financing– has been taken at subsidized rates (in line with export refinance scheme) the sizable increase in benchmark rates during the period, translated in increased interest cost burden[1] of 21.4% vis-à-vis 7.4% for FY18.

Following realization of major tax benefit in FY18, to the tune of Rs. 1.3bn, the Company incurred a tax charge of Rs. 330mn in FY19. Resultantly the bottom line was notably lower at Rs. 2.1bn (FY18: Rs. 4.4bn).

Liquidity indicators have been impacted, albeit they still compare favorably to peers

Liquidity profile draws support from more than sufficient coverage of short term borrowings by way of inventory and receivables, favorable cash cycle and healthy cash flow generation. Given contraction of margins, the Company's FFO for FY19 was lower by 18% (FY19: Rs. 2.2bn; FY18: Rs. 2.6bn). The drop in FFO, along with a sizable repayment of long term debt (Rs. 1.25bn) in FY19, the debt service coverage for FY19 was notably lower at 1.5x (FY19: 7.5x).

Going forward, there are plans to set up a 7MW solar power plant, which is expected to cost up to USD 4.8mn (Rs. 720mn); capital expenditure, in this regard, is expected to be incurred in FY20, and is planned to be financed by debt at subsidized rates (at ~5% under the federal government scheme). Despite the notable drop in debt service coverage, the overall FFO to debt coverage at 0.32x is considered adequate and compares favorably to peer median.

[1] Interest Cost / Operating Income

Leverage indicators compares favourably to peer median while conservative dividend payout has kept equity base on the higher side

On the capitalization front, equity base has grown by 1.8x over the last 4 years while leverage indicators have remained on the lower side vis-à-vis peers (FY19: 0.7x; FY18: 0.8x). Dividend payout has trended downwards over the last 2 years (FY19: 26.5%; FY18: 20.8%; FY17: 51.0%). In view of a downward pressure on profitability, capital conservation is considered important from a rating perspective going forward. Total borrowings accumulated as at FY19 were Rs. 6.9b with (50%) composition of short term financing. Given future debt plans, assuming same level of profitability, we believe gearing level of the company would improve going forward.

Strong Sponsor Profile

Rating builds in strong and diversified business profile of the Pharaon Investment Group Limited Holding S.A.L. (PIGL) with investment in 10 different sectors across Middle East, Europe and Africa.

Adequate Corporate Governance

Ratings also incorporate adequate corporate governance infrastructure as evident from satisfactory board oversight, stable & professional management team and adequate IT and controls.

Attock Cement Pakistan Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions, unless stated otherwise)*			
BALANCE SHEET	**Jun 30, 2017**	**Jun 30, 2018**	**Jun 30, 2019**
Fixed Assets	16,660	17,963	17,686
Short Term Investments	-	-	-
Stock-in-Trade	1,930	3,649	3,396
Trade Debts	180	710	795
Cash & Bank Balances	122	325	303
Total Assets	20,709	26,406	27,317
Trade and Other Payables	3,816	4,984	3,577
Long Term Debt *(*incl. current maturity)*	1,604	4,702	3,448
Short Term Debt	1,981	1,363	3,419
Paid up Capital	1,145	1,145	1,374
Total Equity	11,948	14,873	16,099
INCOME STATEMENT	**Jun 30, 2017**	**Jun 30, 2018**	**Jun 30, 2019**
Net Sales	14,735	16,496	20,781
Gross Profit	5,892	4,798	4,803
Operating Profit	4,472	3,381	3,027
Finance Cost	28	251	648
Profit Before Tax	4,443	2,403	3,129
Profit After Tax	3,034	4,400	2,073
RATIO ANALYSIS	**Jun 30, 2017**	**Jun 30, 2018**	**Jun 30, 2019**
Gross Margin	40.0%	29.1%	23.1%
Net Margin	20.6%	26.7%	10.0%
Current Ratio	0.53x	0.87x	0.91x
(Inventory+Recievables)/ST Borrowings	1.07x	3.20x	1.23x
FFO to LT Debt	1.91x	0.56x	0.63x
FFO to Total Debt	0.86x	0.44x	0.32x
DSCR	-	7.52x	1.50x
Leverage	0.73x	0.78x	0.70x
Gearing	0.30x	0.41x	0.43x
ROAA	17.3%	18.7%	7.7%
ROAE	27.1%	32.8%	13.4%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

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	Attock Cement Pakistan Limited
Sector	Cement and Construction
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
Oct 24,'19	A+	A-1	Stable	Reaffirmed
June 12,'18	A+	A-1	Stable	Reaffirmed
Oct 31,'17	A+	A-1	Stable	Reaffirmed
April 13, '17	A+	A-1	Stable	Reaffirmed
Mar 31, '16	A+	A-1	Stable	Initial

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