RATING REPORT

Fatima Fertilizer Company Limited (FATIMA)

REPORT DATE:
October 15, 2020

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	AA-	A-1	AA-	A-1
Rating Outlook	*Stable*		*Stable*	
Rating Date	*October 15, '20*		*August 26, '19*	

COMPANY INFORMATION	
Incorporated in 2003	**External auditors:** Deloitte Yousuf Adil Saleem & Co. Chartered Accountants
Public Limited Company	**Chairman of the Board:** Mr. Arif Habib **Chief Executive Officer:** Mr. Fawad Ahmed Mukhtar
Key Shareholders (with stake 5% or more):	
Arif Habib Corporation Limited – 15.2%	
Mr. Muhammad Arif Habib – 8.6%	
Fatima Trade Company – 7.6%	
Fatima Management Company – 7.6%	
Mr. Faisal Ahmed Mukhtar – 6.3%	

APPLICABLE METHODOLOGY
VIS Entity Rating Criteria *Industrial Corporate (May 2019)* **http://www.vis.com.pk/kc-meth.aspx**

Fatima Fertilizer Company Limited (FATIMA)

OVERVIEW OF THE INSTITUTION

Fatima Fertilizer Company Limited (FATIMA) was established in 2003 as a public limited company. The company also acquired Dawood Hercules Plant and later named it FatimaFert. The plants are located at Sadiqabad and Sheikhupura road having production capacities of Urea 945,500 M.T, CAN 420,000 M.T and NP 360,000 M.T.

Profile of Chairman
Mr. Arif Habib is the chairman with a diversified experience. He is the CEO of Arif Habib Corporation Limited. He is the chairman of Pakarab Fertilizers Limited (Pakarab), Aisha Steel Mills Limited, Javedan Corporation Limited and director of Pakarab Energy Limited.

Profile of CEO
Mr. Fawad Ahmed Mukhtar is the CEO and director of the company. He has broad experience in manufacturing and industrial management. He is also the chairman of Reliance Weaving Mills Limited, Fatima Energy Limited, Reliance Commodities Private Limited, Fatima Sugar Mills Limited and CEO of Pakarab Fertilizers Limited and Fatima Cement Limited as well.

Financial Snapshot
Total Equity: end-1HCY20: Rs. 81b; end-CY19: Rs. 45b

Assets: end-1HCY20: Rs. 151.8b; end-CY19: Rs. 155b

Profit After Tax: end-1HCY20: Rs. 7.1b; end-CY19: Rs. 12b;

RATING RATIONALE

Fatima Fertilizer Company Limited (FATIMA) is principally engaged in the business of manufacturing, producing, buying, selling, importing and exporting fertilizers and chemicals. In Jan'19, Fatima's subsidiary, Fatimafert Limited, has been amalgamated in Fatima for financial reporting purpose. The company has 3 manufacturing facilities, which are listed as follows:

1. **Sadiqabad Plant:** Fully integrated production facility at Sadiqabad which mainly produces Calcium Ammonium Nitrate (CAN), Nitro Phosphate (NP) and intermediary products (Ammonia & Nitric Aicd). The Complex has a dedicated gas allocation of 110 MMCFD from Mari Gas Field and has 56 MW captive power plants in addition to off-sites and utilities.
2. **Sheikhupura:** The Sheikhupura plant is based on RLNG, and has a Urea manufacturing capability of 445,000 MTs annually.
3. **Pakarab Plant:** This plant has a nameplate capacity of 854,500 MTs (Urea: 100,000 MTs, NP: 304,500 MTs & CAN: 450,000 MTs). The plant has been acquired by FATIMA, effective September 1, 2020. Previously the plant has a history of remaining non-operational, as a result of non-availability of gas. However, the management has signed a Gas Supply Agreement (GSA) with Mari, valid for 7 years, in addition to building a separate gas supply infrastructure for the plant. Accordingly, the plant has been operational since January 16, 2020.

Subsequent to the latest acquisition, the company's annual nameplate capacity has increase to 2.57m MTs.

Industry Update

- The fertilizer industry in Pakistan is dominated by the nitrogen-base Urea fertilizer; in volumetric terms, industry off take of Urea constituted 69% of the aggregate industry off take in 1HCY20, up from 60% in CY17. Over the years, the demand for Urea has depicted price inelasticity, as evident from average Urea off take of 5.9m MT in the last 10-year period. In view of the same, future demand is anticipated to remain intact.
- The second most used fertilizer is Diammonium Phosphate (DAP), albeit its volumetric offtake as a % of industry offtake has been declining on a timeline and stood at 15% during 1HCY20 (CY19: 20%; CY18: 24%; CY17: 24%). The negative trend in DAP off take is mainly attributable to increased pricing, triggered by rupee depreciation. With local prices of DAP being on the higher side, making it unaffordable for small farmers, DAP demand is likely to remain weak.
- The other 2 major products are Calcium Ammonium Nitrate (CAN) and Nitro Phosphate (NP), which represent 8% and 7% of the industry off take respectively. Off take of these products has depicted volatility, mainly on account of supply-side constraints.
- As illustrated in the table below, volumetric sales of Urea and DAP were lower in 1HCY20 by 7%, mainly as a result of the pandemic-induced slowdown. Domestic off take is expected to post recovery in 2HCY20, barring further continuation of the pandemic-induced slowdown.
- Urea prices were recently a cut by Rs. 400/bag, due to GIDC suspension on fuel and feedstock, which has reduced the cost of production. Resultantly, Urea prices were hovering at ~Rs. 1,630/bag as of Jul'20.DAP prices gradually started to drop since the start of CY20 on the back of international prices, down from Rs. 3,654/bag in Dec 2019 to Rs. 3,395/bag in Jul'20. The DAP prices in the upcoming months is anticipated to increase in tandem with international DAP prices.

Table 1: Fertilizer Industry Offtake (In k.T)

	CY17	CY18	CY19	1HCY19	1HCY20
Urea	5,861	5,812	6,228	2,888	2,672
DAP	2,378	2,237	1,879	646	598
CAN	731	609	472	262	292
NP	688	453	544	245	280

- In Aug'20, the Supreme Court of Pakistan ruled in favor of the Government of Pakistan, in the case pertaining to Gas Infrastructure Development Cess (GIDC). As per the ruling, GIDC charge of Rs. 700b, off which Rs. 295b has already been collected, is to be recovered from industrial consumers of natural gas. The amount of Rs. 405b is payable in a period of 24 months from Aug'20.
- At present, the industrial consumers have moved to the court to petition for an elongation of the time period for GIDC payment from 2 years to 10 years. So the cess payment has been put on hold. A longer time period would bode well for industry profitability & liquidity, as charge could be spread out to a longer time period.
- Key business risk factors for the industry include sensitivity to changes in international urea prices and adverse crop seasons.

FATIMA Market Positioning

Table 2: Market Share (Fatima)

	CY18	CY19	1HCY20
Urea	9.0%	5.0%	8.0%
DAP	1.5%	8.2%	5.3%
CAN	82.0%	99.0%	68.0%
NP	83.0%	87.0%	51.0%

- FATIMA is a relatively smaller-sized player in the Urea market, as evident from its market share.
- In case of DAP, FATIMA's off take is composed of DAP imported for reselling in the domestic market. In CY19, given attractive margins, the company imported more DAP thus increasing market share.
- The company is the sole producer CAN in Pakistan and enjoys a dominant market positioning in the NP market.

Production & Offtake

Table 3: Capacity Utilization

	CY18	CY19	1HCY20
Urea			
Capacity (MTs)	945,500	945,500	472,750
Production (MTs)	607,772	822,656	238,884
Capacity Utilization	64%	87%	51%
CAN			
Capacity (MTs)	420,000	420,000	210,000
Production (MTs)	474,968	403,444	243,922
Capacity Utilization	113%	96%	116%
NP			
Capacity (MTs)	360,000	360,000	180,000
Production (MTs)	429,250	407,511	289,987
Capacity **Utilization**	119%	113%	161%

- Urea capacity utilization increased to 87% in CY19 as the Sheikupura plant remained operational round the year, given RLNG availability. In 1HCY20, the production at Sheikhupura plant remained halted due to unavailability of gas.
- DAP off take increased to 106,702 MTs in CY19, as the company imported and sold healthy volume of DAP to increase its footprint in the market. The trend continued in 1HCY20, as international DAP prices were on the lower side in CY19, which helped to increase company's gross margin in 1HCY20.
- Subsequent to the Jun'20, gas supply to Sheikhupura Plant has been restored. Furthermore, GoP is in the process of completing framework to allow private parties to use unutilized and excess LNG regassification capacity of terminals. The Company has started completing regulatory requirements to use this new gas availability option for sustainable operations at its Sheikhupura Plant. These factors should allow the company to increase urea capacity utilization.
- Inclusive of additional capacity from Pakarab plant, which has recently been acquired, the Company's name plate capacity would increase to 2.57m MT/year, which should translate in an augmented topline for the company.

Key Rating Rationale

Diversified Sales Mix

- The business risk profile of FATIMA is underpinned by well-diversified product portfolio, as illustrated from the topline breakup in table 4.
- FATIMA's topline increased by 46% in CY19 on account of higher volumetric sales in Urea, DAP and NP. DAP sales volume posted a highest growth of 3x in CY19 when compared to CY18.
- In 1HCY20, topline posted a drop of 27% Y/Y because of volumetric decline in CAN, NP and DAP while lower pricing also played a part.
- FATIMA's gross margin has depicted volatility, albeit still comparing favorably to peers; this is mainly attributable to provision of concessionary gas, under GSA from Mari, as allowed under Fertilizer Policy 2001. In CY19, the gross margin of the company had declined to 37% mainly because of running Sheikhupura plant at higher cost RLNG.
- In 1HCY20 gross margin clocked in at 61%, partly because of the augmented DAP offtake and partly due to subsidy released by GoP to SNGPL against subsidized gas supply to Sheikhupura plant and suspension of GIDC.
- Going forward, as the concessionary gas supply agreement, under Fertilizer Policy 2001, will expire in 2021, the company's margins are projected to normalize in line with the industry.

Table 4: Sales & Margins

	CY18	CY19	1HCY20
Sales (In PKR' Millions)	51,310	74,964	24,833
Product-wise Breakup			
- Urea	38%	36%	32%
- CAN	23%	20%	23%
- NP	34%	34%	28%
- DAP	3%	10%	16%
- Others	1%	1%	1%
Gross Margin	50.0%	37.2%	61.2%
Operating Margin	36.3%	28.0%	49.3%
Net Margin	23.2%	16.1%	28.8%

Table 5: Volumetric Off take (In MTs)

	CY18	CY19	1HCY20
Urea	662,034	777,526	244,804
CAN	499,608	471,828	197,781
NP	377,726	477,992	142,657
DAP	26,371	106,702	62,475
Others	13,820	14,377	7,142
	1,579,559	1,848,425	654,859

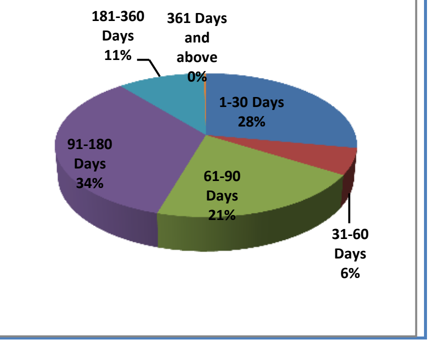
Cash flow Coverage Indicators Remain Intact

- Liquidity position of the company is underpinned by healthy cash flow generation.
- The company has a negative cash conversion cycle. The inventory days as of Jun'20 were notably higher, mainly on account of 1.7x increase in finished goods inventory. The most notable increase was witnessed in the inventory of NP, which increased from Rs. 0.3b to Rs. 3b. As per management, this is in anticipation of increased NP demand in 2HCY20.
- FATIMA's payable days continue to inflate, mainly as a result notably lower sales offtake in 1HCY20. In absolute terms, outstanding payables stood at Rs. 23b as of Jun'20 (Dec'19: 26b). This includes GIDC payable of Rs. 5.8b (Dec'19).
- The company's receivable days have remained on the lower side. As of Jun'20, the company had outstanding receivable balance of Rs. 2.3b. Aging of trae debts is provided in figure 1.
- FATIMA's FFO was lower by 22% in CY19, mainly on account of higher finance cost and taxes paid in the period.

Table 6: Liquidity Indicators (All figures in PKR' Millions, unless stated otherwise)

	CY18	CY19	1HCY20
Cash Conversion Cycle (Days)	(152)	(81)	(176)
- Receivable Days (Days)	18	35	17
- Inventory Days (Days)	87	89	243
- Payable Days (Days)	257	205	436
FFO	17,364	13,587	8,019
FFO – Debt	81%	46%	71%
FFO – Long Term Debt	108%	102%	139%
DSCR (x)	2.1	1.6	1.8

Figure 1: Aging of Trade Debts (Jun'20)



- Further, DSCR of the company clocked in at 1.8x in 1HCY20, which remains commensurate with the assigned rating band.
- Going forward, given relatively lower off take projections for the ongoing year and projected drop in gross margin, subsequent to end of the concessionary gas agreement in Jun'21, FFO is projected to be impacted.
- Nevertheless, conservatively speaking, the company's FFO-Long Term Debt is projected to remain above 1x while DSCR above 1.5x throughout our rating horizon.

Sizable Capital Buffers

- On the back of strong profitability and profit retention, the company has been able to build up sizable capital buffers.
- The company's long term debt has been on a declining trend.
- Both gearing and leverage dropped in 1HCY20, as illustrated in table 7. The company's capital structure is 21:79 (Debt: Equity) as at Jun'20.
- As of Jun'20, the capitalization ratios remained in line with the threshold for the assigned rating.
- Assuming routine capital expenditure projections, the capitalization ratios are expected to remain within the threshold throughout the rating horizon.

Table 7: Capitalization (All figures in PKR' Millions, unless stated otherwise)

	CY18	CY19	1HCY20
Net Equity	**69,595**	**78,008**	**80,971**
- **Paid-up Capital**	21,000	21,000	21,000
- **Reserves**	48,595	57,008	59,971
Debt	**21,502**	**29,594**	**22,683**
- **Long Term**	16,008	13,329	11,500
- **Short Term**	5,495	16,265	11,182
Gearing (x)	0.31	0.38	0.28
Leverage (x)	0.84	0.99	0.87
Dividend Payout Ratio	31%	35%	NA

Fatima Fertilizer Company Limited (FATIMA) Annexure I

Financial Statement (*Amount in Million)*

BALANCE SHEET	CY17	CY18	CY19	1HCY20
Property, Plant & Equipment	86,705	91,719	100,721	101,348
Long-term Investments	86	146	175	190
Long-term Loan to Associated Company	2,999	1,999	2,999	2,999
Stock in Trade	4,208	6,100	11,518	12,820
Trade Debts	1,931	2,565	7,207	2,301
Short-term Loan to Associated Company	1,242	3,242	3,242	3,242
Cash & Bank Balances	832	717	515	1,259
Other Assets	19,659	21,721	28,740	27,568
Total Assets	**117,661**	**128,208**	**155,116**	**151,727**
Trade and Other Payables	13,864	18,069	26,484	23,050
Short Term Borrowings	2,117	5,495	16,265	11,182
Long-Term Borrowings *(Inc. current matur)*	20,892	16,008	13,329	11,500
Deferred Liabilities	14,826	18,609	19,943	20,075
Other Liabilities	316.6	432	1,088	4,948
Total Liabilities	52,016	58,613	77,108	70,756
Issued, Subs, and Paid Up Capital	21,000	21,000	21,000	21,000
Tier-1 & Total Equity	65,645	69,595	78,008	80,971
INCOME STATEMENT	CY17	CY18	CY19	1HCY20
Net Sales	45,371	51,310	74,964	24,833
Gross Profit	18,686	25,671	27,899	15,185
Operating Profit	12,828	18,613	20,954	12,242
Profit Before Tax	10,120	16,790	17,193	10,057
Profit After Tax	9,268	11,914	12,070	7,161
FFO	9,974	17,364	13,587	8,019
RATIO ANALYSIS	CY17	CY18	CY19	1HCY20
Gross Margin (%)	41.2	50.0	37.2	61.2
Net Margin (%)	20.4	23.2	16.1	28.8
FFO to Long-Term Debt	0.5	1.1	1.1	1.5*
FFO to Total Debt	0.4	0.8	0.5	0.7*
Debt Servicing Coverage Ratio (x)	1.5	2.1	1.5	2.1
ROAA (%)	7.4	9.7	8.5	9.3*
ROAE (%)	14.7	17.6	15.5	17.7*
Gearing (x)	0.35	0.31	0.37	0.27
Debt Leverage (x)	0.79	0.84	0.99	0.87
Current Ratio	0.9	0.9	0.9	0.9
Inventory + Receivables/Short-term Borrowings	2.90	1.58	1.15	1.35

ISSUE/ISSUER RATING SCALE & DEFINITIONS A

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	Annexure IV
Name of Rated Entity	**Fatima Fertilizer Company Limited**
Sector	Fertilizer
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
10/15/2020	AA-	A-1	Stable	Reaffirmed
08/26/2019	AA-	A-1	Stable	Reaffirmed
12/22/2017	AA-	A-1	Stable	Reaffirmed
12/21/2016	AA-	A-1	Stable	Reaffirmed
1/7/2016	AA-	A-1	Stable	Reaffirmed
4/16/2014	AA-	A-1	Stable	Initial

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 Conducted	

Name	Designation	Date
Mr. Kashif Mustafa	Financial Controller	October 9, 2020