

RATING REPORT

International Steels Limited

REPORT DATE:

October 29, 2024

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A+	A1	A+	A1
Outlook/Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Maintained	
Rating Date	October 29, 2024		November 24, 2023	

COMPANY INFORMATION

Incorporated in 2007	External auditors: M/s A.F. Ferguson & Co.
Public Listed Company	Chairman of the Board: Mr. Kamal A. Chinoy
	Chief Executive Officer: Mr. Samir M. Chinoy
Key Stakeholders (with stake 5% or more):	
<i>International Industries Limited – 56.34%</i>	
<i>Sumitomo Corporation – 9.08%</i>	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates

<https://docs.vis.com.pk/docs/CorporateMethodology.pdf>

RATING SCALE(S)

VIS Issue/Issuer Rating Scale:

<https://docs.vis.com.pk/docs/VISRatingScales.pdf>

International Steels Limited

OVERVIEW
OF THE
INSTITUTION

RATING RATIONALE

International Steels Limited (ISL) was incorporated in 2007 and is currently Pakistan's premium producer of flat steel products with an annual production capacity of 1,000,000MT. The primary activity of the Company is manufacturing cold rolled steel coils (CRC), hot dipped galvanized coils (HDGC), and color coated coils.

Major shareholders of the Company are International Industries Ltd. (IIL) and Sumitomo Corporation with a shareholding of 56.33% and 9.07% in ISL respectively. The remaining shareholders include directors, financial institutions, mutual funds, foreign companies, and general public

Brief Profile of CEO:

Mr. Samir M. Chinoy joined ISL in 2009 and was appointed as COO in 2019

In this role, he has led several key functions and overseen its tremendous success in driving sales volumes and profitability domestically and internationally, winning the prestigious FPCCI Top Exporter award consecutively. He has also led the Company's digital transformation initiative and has successfully transformed the companies end to end supply chain infrastructure into a signal source of truth.

This initiative is one of the first in Pakistan using advance analytics to help the Company be the best-in-class partner to both internal and external customers.

Corporate Profile

International Steels Limited ('ISL' or 'the Company') was incorporated as a public unlisted company limited by shares in Sindh, Pakistan, on September 3, 2007. The Company became publicly listed on the Pakistan Stock Exchange Limited on June 1, 2011. The Company is a subsidiary of International Industries Limited ('IIL' or 'the Parent'), holding 56.34% of its shares as of June 30, 2024. ISL acquired the Steel Project Undertaking of International Industries Limited in August 2010, issuing 417,716,700 fully paid-up ordinary shares in exchange. ISL is primarily engaged in manufacturing cold-rolled, galvanized, and color-coated steel coils and sheets. The Company's registered office is located in Karachi, with manufacturing facilities in the Landhi Industrial Area, Karachi. ISL also has sales offices in Lahore, Islamabad, and Multan. On October 1, 2024 Mr. Samir M. Chinoy has taken over ISL as the new CEO.

Group Profile:

The Amir S. Chinoy Group ('ASC Group' or 'the Group') has maintained a presence in Pakistan's industrial sector for over seven decades. The Group's operations encompass diverse industries, including heavy chemicals through Pak Chemicals Ltd (established 1951), steel and galvanized pipes through International Industries Limited ('IIL') (established 1948), and electrical wires and cables through Pakistan Cables Limited ('PCAL') (established 1953). The Group's activities have also extended into areas such as trading, electrical contracting, and representation of major international companies in South Asia. In 2007, the Group expanded its portfolio by investing in a greenfield project focused on the production of Cold Rolled, Galvanized, and Color Coated steel coils and sheets through International Steels Limited.

Industry Overview:

The flat steel sector experienced a challenging operating environment in FY23-24, impacted by macroeconomic instability, energy crises, and policy measures. Rising gas and electricity prices significantly increased costs for manufacturers, putting pressure on profit margins. High inflation eroded consumer purchasing power, reducing demand for manufactured goods. Sales tax exemptions provided to the FATA/PATA regions led to an uneven competitive landscape, disadvantaging domestic manufacturers. The economic slowdown further dampened domestic demand, affecting production and capacity utilization. Government efforts to stabilize the economy, including monetary tightening and fiscal consolidation, had mixed outcomes. While addressing macroeconomic imbalances, these measures increased borrowing costs and reduced liquidity within the sector.

Operational Highlights:

During FY24, capacity utilization levels remained subdued, primarily due to the constrained economic environment characterized by inflationary pressures and restrictive monetary and fiscal policies. However, an improvement was observed in the utilization levels of Cold Rolled Coil and Color Coated segments, which benefited from an increase in agricultural output during the year. Going forward, demand is expected to be supported by a downward

movement in the local policy rates noted in recent months, with further revisions anticipated in the near-term.

Capacities and Utilization	FY23	FY24
Cold Rolled Annealed Capacity (MT)	454,000	454,000
Cold Rolled Annealed Actual Production (MT)	135,270	95,477
Utilization (%)	29.79%	21.03%
Galvanized Steel Capacity (MT)	462,000	462,000
Galvanized Steel Actual Production (MT)	154,006	172,200
Utilization (%)	33.33%	37.27%
Color Coated Capacity (MT)	84,000	84,000
Color Coated Actual Production (MT)	14,268	6,185
Utilization (%)	16.98%	7.36%
Total Capacity	1,000,000	1,000,000
Total Production	303,544	273,862
Utilization (%)	30.35%	27.39%

Key Rating Drivers

The business risk profile of the steel industry is characterized by sensitivity to economic cyclicality, high competitiveness, exposure to exchange rate and transfer risks.

The demand for steel, primarily driven by cyclical industries such as construction, automotive, engineering, and home appliances, is closely linked to macroeconomic conditions. This cyclicality increases the flat steel industry's susceptibility to shifts in fiscal and monetary policies, thereby heightening its exposure to economic downturns. Furthermore, the energy-intensive nature of steel production renders the sector sensitive to energy price volatility, with relatively high domestic energy costs placing local producers at a disadvantage in export markets.

The industry is characterized by limited pricing power due to the commodity-like nature of steel, which offers minimal value addition. Susceptibility to import substitution constrains manufacturers' ability to pass through production cost increases, resulting in sustained pressure on profit margins. Ratings incorporate the Company's reliance on imported Hot Rolled Coils (HRC) as the primary raw material, where price and quality fluctuations directly influence production costs. HRC prices are subject to global supply and demand dynamics, impacted by economic conditions and inventory levels of international producers. The Company's dependence on imports also subjects it to exchange rate risk due to PKR depreciation against USD and transfer risk associated with State Bank of Pakistan (SBP) policies on letters of credit and forex controls.

Topline decline cushioned by growth in export sales

During FY24, the topline decreased by 9.71% to PKR 69,299.63 mln (FY23: PKR 76,753.34 mln), primarily driven by a decline in domestic sales., although export sales recorded an increase of 33.87% to PKR 16,674 mln (FY23: PKR 12,455 mln), supported by higher export volumes. Domestic sales fell to PKR 52,626 mln (FY23: PKR 64,299 mln) due to fluctuation in international prices, along with lower volumes of 196,000 MT (FY23: 253,000 MT). The increase in export sales additionally supports the business in providing ease in accessing FX for imports.

Despite a notable rise in energy costs, the decline in margins remained contained. Net margins improved despite reduced operating margins.

In FY24, the Company's conversion costs increased as a result of 163% increase in the gas tariff rising to PKR 3,250/mmbtu from PKR 1,250/mmbtu in the prior year. While this impacted the margins negatively, the Company was able to limit the impact to 8.02% (FY23: 9.71%) in operating margins in FY24, primarily through optimizing on other operational efficiencies. Nevertheless, net margins improved to 5.27% (FY23: 4.58%) due to lower finance cost, benefitting from the deleveraging of the balance sheet by the management in the previous year. Moreover, the Company commenced installation of a 6.4 MW solar power plant expected to be completed in November 2024, which is projected to reduce power costs.

Sound liquidity profile

The Company maintains a healthy liquidity profile reflected by a 5-year average current ratio of 1.21x. In FY24 the current ratio of the Company was reported at 1.29x (FY23: 1.25x). Furthermore, improvement in Cash Conversion Cycle (CCC) of the Company also bodes well for the liquidity profile of the Company.

Deleveraged balance sheet supports the capitalization profile of the Company.

The Company has carried out deleveraging of the balance sheet in the last two years. Therefore, the gearing ratio has decreased from 1.13x in FY22 to 0.23x (FY23: 0.24x) in FY24, while the leverage ratio has reduced to 1.02x (FY23: 1.06x) in FY24 from 1.79x in FY22. This has been largely due to efficient working capital management. The Company's debt profile largely consists of concessionary long-term financing, which has resulted in margin improvement for the Company.

Strong debt coverage.

Debt coverage of ISL remained strong relative to the industry. Strong FFO generation provided FFO to Long term debt at 3.37x (FY23: 3.33x) at the end of FY24. In addition, the debt service coverage ratio (DSCR) increased to 3.87x (FY23: 1.90x). The coverage profile in FY24 benefitted from the deleveraging of the balance sheet in FY23 as finance costs paid during the year dropped to PKR 897.96 mln (FY23: PKR 2,296.54 mln). Moreover, the current portion of debt has also reduced as the Company has retired most of the long-term debt. Resultantly, the debt service coverage ratio of the Company improved to 3.87x (FY23: 1.90x).

New business initiatives to support future growth of the Company.

In FY24, ISL invested in Chinoy Engineering and Construction (Pvt.) Ltd. ('CECL'), which is a partnership between ISL, IIL and PCAL all associate concerns within the ASC Group. CECL has successfully entered into a contract with Reko Diq Mining Company for the design and construction of a Permanent Accommodation Camp at Reko Diq Copper Gold Mines, Baluchistan. This collaboration is anticipated to support ISL's demand and contribute to incremental revenue streams over the medium-long term.

International Steels Ltd
Appendix I

Financial Summary				
Balance Sheet (PKR Millions)	FY21A	FY22A	FY23A	FY24A
Property, plant and equipment	19,180	20,750	20,305	20,016
Stock-in-trade	17,081	30,197	17,262	18,259
Trade debts	940	1,034	1,149	1,423
Cash & Bank Balances	293	896	1,765	2,708
Other Assets	4,226	3,028	1,911	2,284
Total Assets	41,720	55,905	42,392	44,690
Creditors	1,905	435	4,238	5,671
Long-term Debt (incl. current portion)	5,216	4,263	1,433	1,220
Short-Term Borrowings	6,796	17,360	3,334	3,560
Total Debt	12,012	21,623	4,767	4,780
Other Liabilities	8,914	12,252	11,703	11,042
Total Liabilities	22,832	34,309	20,708	21,492
Paid up Capital	4,350	4,350	4,350	4,350
Equity (excl. Revaluation Surplus)	17,667	19,185	19,496	21,085
Income Statement (PKR Millions)	FY21A	FY22A	FY23A	FY24A
Net Sales	69,796	91,424	76,753	69,300
Gross Profit	13,492	12,381	10,608	8,573
Operating Profit	11,107	9,323	7,456	5,554
Finance Costs	811	1,323	2,264	856
Profit Before Tax	10,295	8,001	5,191	4,698
Profit After Tax	7,466	5,412	3,519	3,655
Ratio Analysis	FY21A	FY22A	FY23A	FY24A
Gross Margin (%)	19.33%	13.54%	13.82%	12.37%
Operating Margin (%)	15.91%	10.20%	9.71%	8.02%
Net Margin (%)	10.70%	5.92%	4.58%	5.27%
Funds from Operation (FFO) (PKR Millions)	10,871	7,784	4,778	4,113
FFO to Total Debt* (%)	90.50%	36.00%	100.24%	86.05%
FFO to Long Term Debt* (%)	208.41%	182.59%	333.51%	337.27%
Gearing (x)	0.68	1.13	0.24	0.23
Leverage (x)	1.29	1.79	1.06	1.02
Debt Servicing Coverage Ratio* (x)	4.84	3.44	1.90	3.87
Current Ratio (x)	1.38	1.20	1.25	1.29
(Stock in trade + trade debts) / STD (x)	2.75	1.85	5.82	5.78
Return on Average Assets* (%)	17.65%	11.09%	7.16%	8.39%
Return on Average Equity* (%)	51.25%	29.37%	18.19%	18.01%
Cash Conversion Cycle (days)	90.91	111.35	128.50	89.47

*Annualized, if required

A - Actual Accounts

P - Projected Accounts

M - Management Accounts

REGULATORY DISCLOSURES					Appendix II
Name of Rated Entity	International Steels Limited				
Sector	Steel Industry				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	<u>RATING TYPE: ENTITY</u>				
	29-Oct-24	A+	A1	Stable	Reaffirmed
	24-Nov-23	A+	A1	Stable	Maintained
	10-April-23	A+	A1	Rating Watch - Developing	Maintained
	23-May-22	A+	A1	Stable	Reaffirmed
	12-Mar-21	A+	A1	Stable	Maintained
	20-Oct-20	A+	A1	Rating Watch-Negative	Maintained
	21-Jun-19	A+	A1	Stable	Reaffirmed
	04-Apr-18	A+	A1	Stable	Reaffirmed
13-Jan-17	A+	A1	Stable	Initial	
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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Due Diligence Meetings Conducted	S.No.	Name	Designation	Date	
	1	Yousuf H. Mirza	Outgoing CEO	25/09/2024	
	2	Samir M. Chinoy	Incoming CEO	25/09/2024	
	3	Mujtaba Hussain	CFO	25/09/2024	