RATING REPORT

Askari Cement Limited

REPORT DATE:
January 13, 2020

RATING ANALYSTS:
Syed Fahim Haider Shah
fahim.haider@vis.com.pk

Maimoon Rasheed
maimoon@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A	A-1	A	A-1
Rating Action	Maintained		Initial	
Rating Outlook	Negative		Stable	
Rating Date	January 07, 2020		August 20, 2018	

COMPANY INFORMATION

Incorporated in 1990	External auditors: M/s KPMG Taseer Hadi & Co., Chartered Accountants.
Public Limited (Unlisted) Company	Chairman: Lt. Gen Syed Tariq Nadeem Gilani HI (M) (Retd) CEO: Maj Gen. Ghulam Mustafa Kausar (Retd)
Key Shareholders (with stake 5% or more):	
Fauji Foundation – 100%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (May 2019)
https://www.vis.com.pk/kc-meth.aspx

Askari Cement Limited

OVERVIEW OF THE INSTITUTION

Askari Cement Limited (ACL) was incorporated in 1990 as an 'unlisted' public limited company under the Companies Ordinance, 1984 (now Companies Act, 2017). ACL is a wholly owned subsidiary of Fauji Foundation. The company is primarily engaged in production and sale of ordinary Portland cement.

Financial Snapshot

Tier-1 Equity: end-1QFY20: Rs. 7.6b; end-FY19: Rs. 7.6b; end-FY18: Rs. 6.1b.

Assets: end-1QFY20: Rs. 35b; end-FY19: Rs. 35.7b; end-FY18: Rs. 32.3b.

Profit After Tax: 1QFY20: Rs. (98)m; FY19: Rs. 1.4b; FY18: Rs. 1.7b.

RATING RATIONALE

Askari Cement Limited (ACL) has two plants with cumulative nameplate cement production capacity of 2.68m tons per annum. The company has 7.3% market share in terms of installed capacity and 6.7% market share in terms of dispatches in the Northern Zone in FY19. The assigned ratings take into account strong sponsor profile as ACL is a wholly owned company of Fauji Foundation; one of the largest business conglomerates in Pakistan. The ratings also factor in largely stable capacity utilization, sustained sales in the face of challenging industry dynamics, and slightly improved leverage indicators. However, the downtrend in profitability is continuing due to weak retention prices amidst strong competition and slowdown in public private sector development spending as well as increasing cost pressure. The stability in liquidity position continue to emanate from short-term investments and cash flows generation. After considerable improvement during FY19, the debt service coverage ratio (DSCR) has declined significantly owing to lower FFO during 1QFY20. Going forward, the DSCR is expected to remain under pressure as grace period of syndicated term finance for Wah and Nizampur plants expired in September and November 2019, respectively. The ratings will remain sensitive to cash flows generation and ability to meet its financial obligations through operating cash flows.

Cement Industry

- Total capacity of Pakistan's cement industry has recently increased from 59.4m tons to 61.8m tons, with the completion of capacity enhancement by Power Cement Limited. Current expansion projects will add another 7.4m tons of cement capacities later this month and early next year.

- Overall cement industry dispatches increased to 20.46m tons during 5MFY20 (5MFY19: 19.25m tons) on account of slightly higher domestic dispatches of 16.85m tons (5MFY19: 16.28m tons) and exports of 3.61m tons (5MFY19: 2.08m tons). Local dispatches for Northern Zone players increased by 11.3% to 14.43m tons during the period, though exports declined by 2.9% to 1.21m tons. Lower than expected increase in demand coupled with oversupply and stressed exports kept the cement price under pressure. Local dispatches for Southern region players declined by 29% to 2.42m tons during 5MFY20, though exports increased by 39.2% to 2.39m tons. While cement price in Southern Zone is still Rs. 100 to Rs. 120 per bag higher than the Northern Zone, the price advantage is expected to erode with more capacities coming online. Total dispatches are expected to reach 49.11m tons by end-FY20 (FY19: 46.88m tons; FY18: 45.89m tons), however, significant excess capacity will remain a major challenge for the industry.

- Profit margins of the cement companies were under pressure during FY19, and this trend is expected to continue in FY20 on account of high interest rates, higher coal prices in rupee terms, and largely stagnant demand expected amid glut oversupply. Industry players plan to increasingly tap overseas markets in order to enhance capacity utilization levels, however, profit margins may not improve owing to cost pressure and strong competition.

Completed installation of waste heat recovery plant and modernization of plants

ACL has two plants located in Wah and Nizampur, having clinker nameplate capacities of 1.05m tons per annum and 1.50m tons, respectively, during 1QFY20. Installed cement production capacity of Wah plant stood at 1.1m tons per annum and Nizampur plant stood at 1.58m tons per annum during 1QFY20. In order to enhance efficiencies, the company completed installation of 7.5MW Waste Heat Recovery (WHR) plant at Wah during 1QFY19. Moreover, the company also completed the balancing, modernization and replacement (BMR) of Nizampur plant during 1QFY19. The company is also in process of installing 10MW of WHR plant at Nizampur.

Power requirement of Wah plant is 18MW, while power requirement of Nizampur plant is 25MW. For company's power related needs, arrangement has been made through a dedicated line of 18MW electricity supply from Islamabad Electric Supply Company (IESCO) for Wah plant and two dedicated lines of 18MW and 12MW from Peshawar Electricity Supply Company (PESCO) for Nizampur plant.

ACL's cement production has remained largely stable over the past three years. Clinker and cement production was recorded at 0.44m tons (FY19: 2.28m tons) and 0.57m tons (FY19: 2.35m tons) respectively, during 1QFY20. Resultantly, capacity utilization of clinker and cement stood at 68.4% (FY19: 89.5%) and 84.6% (FY19: 87.8%), respectively, during 1QFY20. Efficiency of a cement plant is one of the key determinants for gross margins and profitability of cement players. The efficiency of Nizampur plant in terms of coal consumption (kCal/kg) and power consumption (kWh/ton) has improved considerably during FY19 and 1QFY20 due to BMR, whereas efficiency of Wah plant has remained largely stable.

Continued downtrend in profitability despite higher sales, followed by a net loss during 1QFY20

Net sales of the company increased to Rs. 16.1b during FY19 (FY18: Rs. 14.8b) as the impact of slightly lower dispatches was offset by higher retention price for both plants. In line with the industry trend, local dispatches of the company decreased slightly during FY19 owing to slowdown in public and private development projects, whereas exports dispatches increased marginally. Given the difference in retention prices between local and export market, proportion of local sales is projected to remain high.

Cost of sales amounted to Rs. 12.2b during FY19, mainly comprising energy cost, raw materials consumed, salaries & wages, and packing materials. Gross profit increased to Rs. 4b during FY19 on account of higher sales and slightly improved margin as the company was able to pass on the impact of increased coal and electricity prices. The company utilizes coal from Afghanistan and locally procured coal from Darra Adam Khel, Kohat. Operating costs were recorded higher on account of increase in administrative and distribution expenses as well as write-off charge related to plant & machinery of Nizampur plant. ACL earned other income of Rs. 286m, which mainly comprises profit on TDRs. Finance cost increased to Rs. 833m mainly on account of considerable increase in benchmark rate and higher average total debt. Despite higher gross profit, the company reported lower net profit of Rs. 1.4b during FY19 mainly due to higher finance cost.

ACL generated Rs. 3.4b in net sales during 1QFY20 with total dispatches of 0.57m tons. Local dispatches were impacted by slower off-take by dealers during 1QFY20 mainly due to supply side addition of new capacities and slowdown in infrastructure related spending by public and private sector. Amidst soft demand in the local market, the company is increasingly tapping exports in Afghanistan. Gross profit amounted to Rs. 319m as margin

decreased to 9.5% due to lower retention price. Going forward, gross margins of the company are expected to remain under pressure on account of sizeable new capacities coming online. Finance cost amounted to Rs. 353m, and resultantly, ACL reported net loss of Rs. 98m for 1QFY20.

Adequate liquidity in the presence of short-term investments, though debt service coverage is expected to come under pressure

Current ratio stood marginally higher at 1.05x at end-FY19 (FY18: 1.03x) as the impact of increase in trade and other payables and short-term borrowings was more than offset by increase in financial assets and stock in trade. In line with higher profits, the company's funds from operations (FFO) increased to Rs. 2.8b during FY19 (FY18: Rs. 1.6b). FFO to long-term debt improved to 0.39x (FY18: 0.20x) with the scheduled repayments, whereas FFO to total debt ratio stood slightly lower at 0.18x at end-FY19 (FY18: 0.21x) due to higher utilization of short-term borrowings. However, the debt service coverage ratio (DSCR) improved to 1.91x (FY18: 1.29x) owing to higher FFO and flat long-term repayments. Inventory plus trade receivables to short-term borrowings ratio stood lower at 0.66x (FY18: 0.69x) as the company is using surplus borrowings to invest in financial assets to earn a spread.

While the current ratio stood stable at 1.05x, FFO generation stood lower at Rs. 17m during 1QFY20 as the company reported before tax loss. Resultantly, the debt service coverage ratio of the company decreased to 0.38x at end-1QFY20. Going forward, the DSCR is expected to remain under pressure as the recent expiry of grace period of syndicated term finance for Wah and Nizampur plants.

Leverage indicators continue to improve with the scheduled repayments and augmentation of equity

Paid-up capital of the company remained unchanged at Rs. 1.6b at end-FY19 while tier-1 equity accumulated to Rs. 7.6b (FY18: Rs. 6.1b; FY17: Rs. 4.6b) with retention of profits. The increase in total liabilities to Rs. 18.3b (FY18: Rs. 16.1b; FY17: Rs. 13.8b) was mainly due to higher trade and other payables and short-term borrowing. Trade and other payables stood higher at Rs. 2.2b at end-FY19 (FY18: Rs. 1.3b; FY17: Rs. 1.4b) mainly with the increase in creditors to Rs. 1.3b (FY18: Rs. 574m) due to BMR at Nizampur plant. Despite increase in total borrowings to Rs. 11.4b (FY18: Rs. 10.9b; FY17: Rs. 8.2b), gearing and debt leverage ratios of the company improved to 1.49x (FY18: 1.79x; FY17: 1.80x) and 2.40x (FY18: 2.66x; FY17: 3.03x) respectively, owing to enhanced equity base.

Tier-1 equity remained at Rs. 7.6b at end-1QFY20 as the company incurred net loss of Rs. 98m during the quarter. Gearing ratio remained unchanged at 1.48x while debt leverage decreased slightly to 2.32x due lower trade and other payables at end-1QFY20. Given the declining profitability and procurement of further borrowings, increase in leverage indicators is expected by end-FY20.

Askari Cement Limited Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**1QFY20**
Non-Current Assets	19,602	25,582	25,878	25,783
Stores, Spares. And Loose Tools	1,699	2,098	2,164	1,886
Stock-in-Trade	959	1,134	1,827	1,592
Trade Debt	580	831	890	705
Other Financial Assets	1,745	1,270	3,542	3,512
Cash and Bank Balance	463	403	407	368
Total Assets	**25,493**	**32,263**	**35,746**	**34,991**
Trade and Other Payables	2,502	1,252	2,163	1,529
Short-Term Borrowings	3,088	2,855	4,125	3,961
Long-Term Borrowings *(Inc. current matur)*	5,097	8,007	7,262	7,305
Deferred Liabilities	2,972	2,733	3,314	3,303
Total Liabilities	**13,833**	**16,110**	**18,305**	**17,648**
Tier-1 Equity	**4,559**	**6,058**	**7,636**	**7,601**
Total Equity	11,660	16,153	17,441	17,343
Paid-up Capital	1,601	1,601	1,601	1,601
INCOME STATEMENT	**FY17**	**FY18**	**FY19**	**1QFY20**
Net Sales	15,953	14,752	16,124	3,356
Gross Profit	5,118	3,513	3,969	319
Operating Profit	4,461	2,659	2,753	284
Profit/(Loss) Before Tax	3,955	2,144	1,921	(69)
Profit After Tax	2,694	1,720	1,437	(98)
FFO	3,444	1,629	2,817	17
RATIO ANALYSIS	**FY17**	**FY18**	**FY19**	**1QFY20**
Gross Margin (%)	32.1	23.8	24.6	9.5
Net Margin (%)	16.9	11.7	8.9	(2.9)
FFO to Long-Term Debt	0.68	0.20	0.39	0.01*
FFO to Total Debt	0.17	0.21	0.18	0.01*
Debt Servicing Coverage Ratio (x)	2.39	1.29	1.91	0.38
Gearing (x)	1.80	1.79	1.49	1.48
Debt Leverage (x)	3.03	2.66	2.40	2.32
Current Ratio	0.85	1.03	1.05	1.05
Inventory Plus Receivables/Short-term Borrowings (x)	0.50	0.69	0.66	0.58

** Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Annexure 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 — Annexure III

Name of Rated Entity	Askari Cement Limited
Sector	Cement and Construction
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
08-01-2020	A	A-1	Negative	Maintained
20-08-2018	A	A-1	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.
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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, 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. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2020 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.