RATING REPORT

Agha Steel Industries Limited

REPORT DATE:
July 7, 2023

RATING ANALYSTS:
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RATING DETAILS	
Rating Category	**Initial Rating**
Sukuk 3	**A+**
Rating Date (Sukuk 3)	July 7, 2023
Rating Outlook (Sukuk 3)	Stable
Rating Action (Sukuk 3)	Preliminary

COMPANY INFORMATION	
Incorporated in 2013	**External auditors:** Haroon Zakaria and Company Chartered Accountants
Public Listed Company	**Chairman of the Board:** Ms. Shazia Iqbal Agha
Key Shareholders:	**Chief Executive Officer:** Mr. Hussain Iqbal Agha
Mr. Hussain Iqbal Agha – 25.72%	
Mr. Raza Iqbal Agha - 24.34%	
Ms. Shazia Iqbal Agha – 3.12%	
Mr. Saad Iqbal Ali Muhammad- 8.71%	
Mr. Danish Iqbal Ali Muhammad- 8.67%	
Ms. Natasha Iqbal Ali Muhammad- 8.67%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates (May 2023):
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:
https://docs.vis.com.pk/docs/VISRatingScales.pdf

Agha Steel Industries Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Agha Steel Industries (ASIL) was incorporated in Pakistan on November 19, 2013 as a private limited company. On April 7, 2015 ASIL was converted into a public limited company. On November 02, 2020, the company had its IPO, which generated proceeds of Rs. 3.84 billion.

The Company is principally engaged in manufacturing and sale of steel bars, wire rods and billets, and its registered office and production plants are Port Qasim Authority, Karachi.

Profile of the CEO:
Since taking up this role, Mr. Hussain Iqbal Agha has remained actively involved in plant operations, business management, and strategic planning to ensure sustainable growth of the company. At present, he is leading the ongoing expansion plan that is expected to significantly increase capacity and improve overall efficiency.

The board comprises 7 members and is chaired by Ms. Shazia Iqbal Agha. Two Non-executive directors were added in the outgoing year including Mr. Muhammad Asif and Mr. Amer Hazim Haji.

Agha Steel Industries Limited (ASIL) stands amongst the top-tier players in the long steel sector, and is involved in the manufacturing and sale of billets and reinforcement bars (rebars). As part of the BMR and expansion project that started in 2018, the company was able to increase the capacity of re-bars and billets to 250,000 MT (per annum) and 450,000 MT (per annum), respectively. In Nov'20, ASIL raised Rs. 3.8b through an IPO. Funds generated from the same were to be utilized for the Phase II of the expansion plan, which involves further enhancing the production capacity of bars by 400,000 MT (per annum) through the installation of a state-of-the-art M.I.D.A. Rolling Mill and an air separation unit. Additionally, the new technology will result in higher yields as well as notable reduction in lead time and costs. Majority of the work pertaining to the project has been completed and COD is expected to by Dec'23. Moreover, in comparison to peers, ASIL offers technological competitive advantage stemming from the use of Electric Arc Furnace (EAF) for manufacturing of billets. Usage of the technology offers significant cost savings and flexibility in production.

Proposed New Sukuk

- ASIL plans to issue a Sukuk to the tune of Rs. 3.4b as a debt swap for the early repayment of current outstanding Sukuk issue.
- The tenor of the instrument shall be 4 years inclusive of a 1.5-year grace period.
- The principal will be paid in quarterly installments beginning from the end of the 21st month after issuance while profit payments will also be made in quarterly installments (in arrears) at a rate of 3M KIBOR + 0.8%.
- Moreover, the Sukuk will be secured by a first pari-passu hypothecation charge over all present and future fixed assets of the Company with a margin of 25% as well as a first pari-passu equitable mortgage charge over the Company's rights in immoveable property with a 25% margin.
- Additionally, ASIL is required to maintain a Debt-Service Reserve Account (DSRA) with a mutually agreed financial institution wherein a monthly deposit amounting to one-third of the upcoming coupon payment will be made.
- To provide further surety to investors of timely payments, a Sponsorship Support Agreement has been signed. As per the terms of the agreement, the sponsors of the Company are liable to inject cash equity into the DSRA account to meet any shortfall pertaining to an upcoming principal or profit payment.
- In case the sponsors are not able to pay any shortfall that is mandated under the agreement, the sponsors will be required to pay a penalty to the Investment Agent amounting to the aforementioned sum as well as 20% of

the shortfall for each day the amount remains unpaid. This penalty amount will be donated to charity by the Investment Agent as per their Shariah Supervisory Board.

Elevated Business and Financial Risk Profile

The business and financial risk of the steel sector has increased on a timeline basis emanating from import restrictions, limited raw material coverage, soaring raw material prices, exchange rate volatility, and higher interest rates, resulting in inflationary pressures and a decline in demand in the construction, engineering, automobiles and infrastructure development projects. The ongoing situation is expected to persist in the mid-term impacting the financial risk profile of companies across the sector.

During the ongoing year, the Company's financial risk profile depicted pressure, particularly in debt servicing capacity. Topline was reported at Rs. 15.5b in 9MFY23 (FY22: Rs. 25.6b, Rs. 19.9b), representing a decline of 19.7% on an annualized basis, as lack of raw material availability affected volumetric output. While gross margins witnessed improvement to 23.4% (FY22: 21.4%, FY21: 22.7%) in 9MFY23 due to transfer of higher costs to customers, net margins compressed to 4.6% on account of uptick in finance costs in line with policy rate hikes and greater selling and distribution expenses. Decline in profitability as well as rise in financing payments not only adversely impacted cash flow coverages but also resulted in significant stress in debt service coverage ratio which reduced to 0.71x on a timeline basis (FY22: 1.14x, FY21: 1.99x) in 9MFY23. However, leverage and gearing indicators improved to 1.45x and 1.29x, respectively (FY22: 1.65x, 1.47x; FY21: 1.56x, 1.4x) owing to decrease in debt quantum as lower business activity reduced the need for short-term borrowings to meet working capital requirements. Given the weak economic outlook meeting projected profitability and liquidity indicators at levels that commensurate with the assigned ratings is considered important.

Agha Steel Industries **Appendix I**

FINANCIAL SUMMARY (Rs. in m)					
BALANCE SHEET	**FY19**	**FY20**	**FY21**	**FY22**	**9MFY23**
Fixed Assets	10,374	13,826	17,066	19,149	20,237
Stock-in-Trade	7,757	8,627	9,505	12,300	8,805
Trade Debts	3,366	3,840	4,047	5,272	5,660
Cash & Bank Balances	243	68	833	215	232
Total Assets	24,507	29,958	35,411	41,477	40,092
Trade and Other Payables	530	1,339	1,011	1,129	922
Long Term Debt	5,837	7,512	9,469	8,908	8,941
Short Term Debt	10,171	11,950	9,829	14,046	12,144
Total Debt	16,008	19,462	19,298	22,954	21,085
Current maturity of LTD	181	713	2,728	3,394	1,965
LTD/TD	36.5%	38.6%	49.1%	38.8%	42.4%
STD/TD	63.5%	61.4%	50.9%	61.2%	57.6%
Paid Up Capital	3,614	4,561	5,761	6,049	6,049
Total Equity	6,182	8,160	13,811	15,666	16,371
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**FY22**	**9MFY23**
Net Sales	10,482	13,427	19,858	25,648	15,452
Gross Profit	2,031	3,397	4,503	5,490	3,620
Finance Cost	(1,135)	(1,703)	(1,409)	(2,136)	(2,263)
Profit Before Tax	607	1,517	2,553	2,288	969
Profit After Tax	769	1,363	2,036	1,855	705
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**FY22**	**9MFY23**
Gross Margin (%)	19.4%	25.3%	22.7%	21.4%	23.4%
Net Margin	7.3%	10.2%	10.3%	7.2%	4.6%
Net Working Capital	2,245	1,211	3,893	2,561	3,831
Trade debts/Sales	32%	29%	20%	21%	18%
FFO	1,085	1,529	2,795.4	3,341.9	1,111
FFO to Total Debt (%)	7%	8%	14.5%	14.6%	7%
FFO to Long Term Debt (%)	19%	20%	29.5%	37.5%	17%
Current Ratio (x)	1.20	1.08	1.28	1.13	1.25
Debt Servicing Coverage Ratio (x)	1.33	1.72	1.99	1.14	0.71
Gearing (x)	2.59	2.39	1.40	1.47	1.29
Leverage (x)	2.96	2.67	1.56	1.65	1.45
Stock+Trade Debts/STB	1.09	1.04	1.38	1.25	1.19
ROAA (%)	3%	5%	6%	5%	2%
ROAE (%)	13%	19%	19%	13%	6%
CCC (days)	367	362	260	244	317

REGULATORY DISCLOSURES				Appendix II
Name of Rated Entity	Agha Steel Industries Limited			
Sector	Steel Industry			
Type of Relationship	Solicited			
Purpose of Rating	Sukuk 3 Rating			
Rating History	**Rating Date**	**Medium to Long Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: SUKUK 3			
	7-July-2023	A+	Stable	Preliminary
Instrument Structure	ASIL's newly proposed Sukuk is of Rs. 3.4b with a tenor of 4 years, inclusive of a 1.5-year grace period. The principal will be paid in quarterly installments beginning from the end of the 21st month after issuance while profit payments will also be made in quarterly installments (in arrears) at a rate of 3M KIBOR + 0.8%.			
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	**Name**	**Designation**	**Date**	
	Kamran Ahmed	CFO	July 03, 2023	