RATING REPORT

Arif Habib Equity Private Limited

REPORT DATE:
January 07, 2020

RATING ANALYSTS:
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RATING DETAILS		
Rating Category	**Entity Rating**	
	Long-term	**Short-term**
Entity	AA-	A-1
Rating Outlook	Stable	
Rating Date	December 28, 2019	

COMPANY INFORMATION	
Incorporated in 2004	**External auditors:** Naveed Zafar Ashfaq Jaffery &Co.
Private Limited Company	**Chairman of the Group:** Arif Habib
Key Shareholders (with stake 5% or more): Mr. Arif Habib – 99.9%	**Chief Executive Officer:** Samad A. Habib

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (May, 2019) https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Arif Habib Equity Private Limited (AHEPL)

OVERVIEW OF THE INSTITUTION

Arif Habib Equity Private Limited was incorporated in Pakistan on 18th May 2004 under companies' ordinance, 1984. Registered office of the company is located in Karachi, Pakistan

Profile of Chairman

Mr. Arif Habib is a veteran businessman and is CEO of Arif Habib Corporation Limited, director of Pakarab Energy Limited and Chairman of PFL, Aisha Steel Mills Limited and Javedan Corporation Limited.

RATING RATIONALE

Arif Habib Equity Private Limited (AHEPL) was incorporated as a private limited company in 2004. It was formed as an investment holding company by way of acquiring interest in group and non-group companies with the aim of increasing shareholder value by a stream of dividends and realizing capital gains. Mr. Arif Habib is the majority shareholder of the company holding 99.99% stake.

Balance Sheet Snapshot

Total asset base of the Company stood at Rs. 13.7b (FY18: Rs. 12.0b). Investments carried on balance sheet represent around 74.4% of total assets at end-FY19 and are in listed companies. Around 69% of the investments are long-term in nature with the remaining comprising short-term investments in a related party fertilizer sector company. Other major assets held on balance sheet include loan to related parties which are short and long term in nature. Asset base has primarily been funded through equity. As at end-June 2019, total contingent liabilities stood at over Rs. 21.6b.

Profitability

Profit before tax grew by 79.8% in FY19 (FY19: Rs. 1.7b; FY18: Rs. 0.9b). The increase in PBT in comparison to preceding year can be mainly associated with gain on sale of investment property during the outgoing year. Topline of the company comprises recurring dividend income and mark-up on loan given to associates. Recurring dividend income and mark-up loan amounted to Rs. 95.2m (FY8: Rs. 122.4m) and Rs. 33.4m (FY18: Rs.163.5m) respectively. Expense base of the company is very low (primarily comprises salaries of senior management personnel) with resource sharing arrangement in place with group companies.

Investment Portfolio

Investment portfolio of the company (at market value) amounted to Rs. 8.2b (FY18: Rs. 10.5b). Decline in investment portfolio is attributable to lower market values in line with dip in the benchmark index. During FY19, the Company has invested in National Resources (Private) Limited which has been formed for exploring Mineral Mining opportunities in Baluchistan. AHEPL has also invested in the commercial project to be launched by Javedan Corporation Limited while additional investment in this project is also planned. Investment portfolio as at end-FY19 comprises the following investments

Company Name	Fair Value (Rs. in m)	Holding (%)
Aisha Steel Mills Limited - Ordinary Shares	2,407	33.29
Aisha Steel Mills Limited - Preference Shares	133	
Javedan Corporation Limited	2,649	28.68
Power Cement Limited	1,336	19.54
National Resources (Private) Limited	50	25.0
Fatima Fertilizers Company Limited	1,624	2.59
Total	**8,199**	

Performance of Investments

Aisha Steel Mills Limited

Aisha Steel Mills Limited (ASML) is a listed entity and manufactures Cold Rolled and Hot Dipped Galvanized coils.. The current production capacity of ASML is 700,000 MT; around 450,000 is CRC capacity while around 250,000 is HDGC capacity. Profitability witnessed pressure in FY19 due to decline in margins and sizeable finance cost. Achieving projected volumetric sales and enhancement in margins is important (amidst significant increase expected in finance cost) for improving profitability profile. ASML has been assigned a credit rating of A-/A-2 (Single A Minus/A-Two).

Rs. in m	FY18	FY19	1QFY19
Net Sales	18,904	20,231	6,160
Gross Margin	17.5%	8.3%	9.0%
PBT	1,916	(412)	(240)
Net Margin	6.8%	1.3%	-3.9%
FFO*	2,028	708	(389.6)
FFO/Total Debt	19%	3%	-1.8%
Gearing	1.51	3.02	3.1
Dividend Payout %	0%	0%	0%
Total Equity	6,933	7,235	7,043

**Annualized*

Javedan Corporation Limited

Javedan Corporation Limited (JCL) is in the process of development of "Naya Nazimabad" (NN) project. NN is a housing scheme targeting the progressive middle class segment of the society which is spread over 1,366 acres of land. The project includes bungalows, open plots, flat and commercial sites, apartments, malls, shopping centers etc. The first phase of NN was launched in the year 2011 spread over 513 acres of land and subsequently launched 78 acres in 2015. Major portion of inventory of Phase-1 has been sold while the management plans to launch the Commercial Area of approx. 60 acres soon. Financial risk profile is adequate as evident from low leveraged capital structure, reserves on balance sheet and adequate cash flow profile. Cash flow requirements are expected to remain elevated for funding of development and construction expenditure of commercial area of the project is planned to be met through booking receipts. JCL has been assigned an entity rating of 'A+/A-1' (Single A Plus/A-One).

Rs. in m	FY18	FY19	1QFY20
Net Sales	2,479	1,899	436
Gross Margin	56%	59%	86%
PBT	1,100	696	262
Net Margin	28.4%	30.5%	42.6%
FFO*	912	141	847
FFO/Total Debt	25%	2.6%	16.2%
Gearing	0.45	0.62	0.59
Dividend Payout %	27%	-	-
Total Equity	8,033	8,609	8,829

**Annualized*

Power Cement Limited

Power Cement Limited (PCL) has completed the installation of 7,700 TPD clinker production plant and 8,500 TPD cement production plant. The plant has been procured from FLSmidth & Co. (Danish global engineering company). Market position is expected to improve significantly with commencement of new line. Business risk profile incorporates cyclical nature of the cement industry. The cement sector has now entered a competitive phase with slowing demand growth and increasing capacities exerting pressure on selling prices which has been compounded by rising cost of inputs. Given the sizeable expected contraction in the large scale manufacturing sector in FY20 along with continuity of high fiscal deficit, cement dispatches are expected to remain under pressure in FY20. Over the medium term, pick-up in demand growth along with enhanced capacity is expected to position the company to capture a higher stake in cement consumption growth expected to emanate from construction of dams and housing units. PCL has been assigned a credit rating of A-/A-2 (Single A Minus/A-Two).

Rs. in m	FY18	FY19	1QFY20
Net Sales	4,343	3,858	583
Gross Margin	16%	4%	-17%
PBT	349	(412)	(290)
Net Margin	7.4%	15.09%	1.36%
FFO*	89	(108)	(249)
FFO/Total Debt	1%	-0.47%	-1%
Gearing	0.94	1.9	2.0
Dividend Payout %	-	-	
Total Equity	11,299	12,222	12,143

**Annualized*

Fatima Fertilizer Company Limited

Fatima Fertilizer Company Limited (FATIMA) was established as public limited company in 2003 to undertake manufacturing and selling of fertilizers. The business risk profile of FATIMA is underpinned by well-diversified product portfolio. The company is involved in manufacturing and supply of Urea, Nitrogen Phosphate (NP), and Calcium Ammonium Nitrate (CAN) fertilizers through a dealer network of 4,863 retailers in 61 districts of Pakistan. FATIMA's financial profile draws support from positive earnings trajectory, improving cash flows generation, and decline in leverage indicators on a timeline basis. Moreover, comfort is drawn from access to concessionary gas, which provides a cushion against the increasing gas prices. Fatima has been assigned a credit rating of AA-/A-1 (Double A Minus/A-One).

Rs. in m	CY17	CY18	9MCY19
Net Sales	37,611	45,963	39,380
Gross Margin	54.1%	57.6%	57.9%
PBT	12,736	18,510	5,347
Net Margin	28.1%	28.9%	28.8%
FFO*	12,346	16,887	19,345
FFO/Total Debt	68%	95%	119%
Gearing	0.34	0.28	0.28
Dividend Payout %	44.7%	27.7%	-
Total Equity	53,741	62,261	58,455

**Annualized*

Rating Drivers

Strong sponsor profile
The assigned rating to AHEPL is underpinned by financial profile and demonstrated track record of support of the Company's major sponsor. The support is reflected in funding support provided by sponsor. VIS anticipates support from sponsors for AHEPL, if needed.

Diversified investment portfolio with long-term time horizon
Investment portfolio of AHEPL is diversified with investments in cement, steel, real-estate and fertilizer sector. Cyclicality in cement and steel sectors is expected to be off-set by stable business risk profile of fertilizer and real-estate investment. Investments have been undertaken from a long-term perspective given the country's low per capita cement and steel consumption, deficit of affordable housing units and significant infrastructure investments (dams etc.) projected over the long term.

Dividend stream expected to witness limited growth from current levels during FY20. Recurring dividend inflows reflect limited debt repayment capacity in case of debt drawdown
Barring 2015, Fatima has historically maintained a consistent dividend payout history and given the projected growth in profitability dividend income from the same is expected to remain strong. ASML, PCL and JCL are currently in growth phase and have already completed (PCL and ASML) or expected to commence expansion JCL). Resultantly, overall dividend inflow from investments is expected to remain constrained in FY20. Comfort is drawn from funding line made available by the sponsor which can be drawn upon in case of need.

Low leverage capital structure is a positive rating driver
During the outgoing year, AHEPL has obtained external debt to fund PCL's line 3 expansion. The principal and mark up payment on the loan is to be made by PCL and management does not expect to incur any cash outflow on account of the same.

FINANCIAL SUMMARY			*(amounts in PKR millions)*
	FY17	**FY18**	**FY19**
Operating Revenue	1,644	286	129
Dividend Income	109	122	95
Profit Before Tax	1,637	941	1,692
Profit After Tax	1,400	810	1,611
Long Term Investments	6,283	8,124	8,545
Investment Properties	1,250	-	-
Total Assets	10,230	11,998	13,675
Loans From Sponsor	945	1,078	-
Total Liabilities	965	2,010	2,084
Paid Up Capital	267	267	267
Total Equity	9,264	9,988	11,591
CFO	(346)	203	(427)
Current Ratio (x)	2.78	1.37	45.77
Gearing (x)	0.10	0.11	0.16

ISSUE/ISSUER RATING SCALE & DEFINITION — Appendix II

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 II
Name of Rated Entity	Arif Habib Equity Private Limited
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	
Instrument Structure	N/A
Statement by the Rating Team	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
29/12/2019	AA-	A-1	Stable	Reaffirmed
12/26/2018	AA-	A-1	Stable	Initial