RATING REPORT

Automobile Corporation of Pakistan

REPORT DATE:

April 22, 2021

RATING ANALYST:

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RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	BBB	A-2	BBB	A-2
Rating Outlook	Stable		Rating Watch-Negative	
Rating Date	22 April, 2021		21 May, 2020	

COMPANY INFORMATION	
Incorporated in 1968	**External auditors:** Ibrahim Shaikh and Co. Chartered Accountants
Private Limited Company	**Chairman and CEO:** Mr. Khayam Husain
Key Shareholders (with stake 5% or more):	
Mr. Khayam Husain- 75% Mrs. Nighat Husain- 7% Mrs. Aamana Husain- 9% Mr. Omar Khayam- 9%	

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

Automobile Corporation of Pakistan

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Automobile Corporation of Pakistan was incorporated in 1968 as a Private Limited Company under the Companies Ordinance, 1984. Principal activities of the company include fabrication, designing, repairing and servicing of trailers, tankers and other heavy vehicles.

Financial Statements of the company for FY20 were audited by Ibrahim Shaikh and Co. Chartered Accountants. Auditors belong to category 'C' on the approved list of auditors published by the State Bank of Pakistan (SBP).

Automobile Corporation of Pakistan (AUTOCOM) is a family owned business with around three fourth of the shareholding vested with Mr. Khayam Hussain, while the remaining ownership is divided among three other family members. Principal activities of the company include fabrication, designing, repairing and servicing of trailers, tankers and other heavy vehicles through two facilities at West Wharf and Port Qasim. The company commenced operations in 1970s with the import of Cometto trailers as CBUs and catered largely to Government and Military segment. After developing necessary expertise, the company then started manufacturing UNADR compliant petroleum tanks for Shell Pakistan in 1998. Currently, the product line of the company comprises petroleum tanks, trailers and other specialized vehicles (refuelers, garbage compactors, and municipal vehicles).

In comparison to the other formal competitors, AUTOCOM has the largest automated assembly line for oil tankers at Port Qasim comprising 80 units per month. Consolidated capacity of other players is estimated at 40-50 units per month. Moreover, a new assembly for trailers is also being established currently. AUTOCOM manufactures oil tankers as per OGRA standards. Competitive advantage stems from long term association with foreign technology partner- Industrie Cometto of Italy, ISO 9001 certification, strength of a multi-disciplinary engineering team, a 24/7 after sales service and strict in-house engineering quality control. AUTOCOM also holds long term investment in Lucky Cement Limited and Ibrahim Fibres Limited to the tune of Rs. 7.5m and Rs. 0.3m at end-1HFY21.

Key Rating Drivers:

Business risk profile is characterized by high competition due to presence of large number of informal players; the company has strong market presence and competitive edge against both formal and informal players

The trucking industry comprises large number of informal and un-organized players yielding high competition. These informal players dominate the overall trailer and tanker market. To formalize the industry, the Government of Pakistan introduced Trucking Policy in 2008 which laid incentives for trailer manufacturers in order to encourage the use of modern prime movers/multi-axle, Euro standard trucks. Under the policy, the GoP rationalized tariff structure on heavy vehicles. Moreover, to encourage the local trailer manufacturing, sales tax exemption was allowed to bring them at par with the Trucks and Prime movers. Demand for trailer and tanker manufacturers has increased over time in the light of these incentives. However, the transportation industry continues to remain cyclical in nature. With imposition of lockdown on account of COVID-19 and reduction in oil prices, demand for tankers and trailers remained subdued during FY20. Subsequently, ease in lockdown measures and recovery in economic activity have translated to improvement in demand during FY21. Demand risk for the company is considered manageable given the Government's increased focus on shift towards standardized tankers and trailers; the company's focus is on acquiring government contracts to cater to the replacement demand and mitigate demand risk. Business risk profile of the company is considered moderate given strong market presence and competitive edge against other formal and informal players.

Reduction in employee related expenses and effective raw material procurement strategy have contributed to improvement in profitability; enhanced business from government and growth in trailer business is expected to support profitability profile going forward

Due to COVID-19, the company witnessed slowdown in demand as the customers decreased during FY20. However, the management revised its business strategy by targeting corporate clients and government contracts to secure confirmed business. Acquisition of orders from corporate clients enabled the company to sustain its topline at Rs. 1.3b (FY19: Rs. 1.3b) during FY20. Since corporate client orders mostly pertained to trailers, sales mix (in terms of volumes) also witnessed change with trailers forming the largest proportion of sales (FY20: 42%; FY19: 5%), followed by tankers (FY20: 37%; FY19: 73%) and specialized vehicles (FY20: 20%; FY19: 22%). Sales of the company are directed towards the local market with major customers comprising Logistic companies (J Holding, Rasch Private Limited, and Asif Jadoon) and OMCs (Hascol, Shell, Total Parco, PSO, and Puma). The company follows a Made to Order business model with around three month orders in hand at all times. With increase in the cost of raw materials, gross margins of the company decreased to 16.7% (FY19: 17.2%) in FY20. Nevertheless, net margin and net profit were reported higher at 4.0% (FY19: 2.6%) and Rs. 51.4m (FY19: 33.2m) due to significant reduction in employee related expenses.

Net sales of the company were reported at Rs. 864.1m in 1HYFY21. The company had managed to secure one sizeable contract pertaining to tankers from a government client in FY20. However, due to delay in execution timeline on account of COVID-19, the order was partly executed in 1HFY21, while the remaining will be executed in 2HFY21. Hence topline of the company will be supported through realization of revenues from this project going forward. Moreover, the management is also negotiating other government contracts and aims to grow the trailer vehicle business post installation of the trailer line assembly. Based on orders in hand, the management is projecting double digit growth in sales in FY21 vis-à-vis FY20. Gross margin of the company witnessed improvement to 17.6% in 1HFY21 due to reduction in raw material costs on account of effective procurement strategy. The management opted to import steel at cheaper rates rather than relying on local vendors. Going forward, future profitability is contingent upon the projected growth in volumetric sales. The risk of currency devaluation impacting profitability over the long term remains given the increasing reliance of the company on imports and strong competitive environment.

Capitalization indicators are expected to remain sound over the rating horizon given low debt drawdown to finance capital expenditure

Equity base of the company has grown to Rs. 539.5m (FY20: Rs. 486.0m; FY19: Rs. 436.7m) on account of profit retention. Long term debt was reported higher at Rs. 66.6m (FY20: Rs. 48.1m; FY19: Rs. 54.0m) at end-1HFY21 on account of utilization of low cost refinance scheme offered by SBP for payment of wages and salaries of employees. Going forward, management plans to acquire additional long term debt in the range of 40 – 45m to finance capital expenditure pertaining to trailer assembly. The company has acquired approval for Temporary Economic Refinance Facility (TERF) offered by SBP in this regard. The company is expanding its capacity at port Qasim with the addition of two new production sheds. Fresh investment on plant and equipment is also being made to improve the cycle time of production. However, this investment will be undertaken through internally generated funds. The company has signed an MOU with NED university to bridge academia and industry. AUTOCOM will have access to RND of NED university while the student will benefit from work experience during their academic break. Short term borrowings have been mobilized for working capital requirements and stood at Rs. 76.5m at end-December 2020. At end-1HFY21, gearing and leverage ratios stood at 0.27(x) (FY20: 0.27(x); FY19: 0.17(x)) and 1.47(x) (FY20: 2.09(x); FY19: 2.24(x)), respectively. Given low debt drawdown and projected profitability, leverage indicators are expected to remain sound over the rating horizon.

Liquidity profile is satisfactory

Funds flow from Operations (FFO) has varied in line with the profitability of the company. FFO was reported at 26.1m (FY19: 19.9m) in FY20. Debt Service Coverage Ratio (DSCR) and FFO/Total Debt remained adequate at 1.1(x) (FY19: 1.0(x)) and 20.1% (FY19: 26.5%), respectively during FY20. Current ratio remains well above 1x on a timeline basis. Stock in trade and trade debts at 10.9(x) at end-June'20 are well in excess of short term borrowings. Working capital cycle is also manageable.

Automobile Corporation of Pakistan Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**HYFY21**
Fixed Assets	300	422	407	429
Long term Investments	8	6	7	7
Stock-in-Trade	650	799	815	520
Trade Debts	64	54	78	70
Cash & Bank Balances	12	6	25	10
Total Assets	1,267	1,543	1,629	1,459
Trade and Other Payables	569	844	827	591
Long Term Debt	74	54	48	67
Short Term Debt	115	21	82	76
Total Debt	190	75	130	143
Paid Up Capital	107	107	107	107
Total Equity	404	437	486	539
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**HYFY21**
Net Sales	1,491	1,293	1,291	864
Gross Profit	282	222	216	152
Profit Before Tax	120	69	74	75
Profit After Tax	88	33	51	53
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**	**HYFY21**
Gross Margin (%)	18.9%	17.2%	16.7%	17.6%
Net Margin	5.9%	2.6%	4.0%	6.2%
Trade debts/Sales	4%	4%	6%	8%
Current Ratio	1.3	1.2	1.3	1.5
Net Working Capital	214.5	204.2	261.3	319.4
FFO	62	20	26	N/A
FFO to Total Debt (%)	33%	27%	20%	N/A
FFO to Long Term Debt (%)	84%	37%	54%	N/A
(Stock + Trade Debts)/ Short term borrowing	619%	4046%	1093%	770%
Debt Servicing Coverage Ratio (x)	3.8	1.0	1.1	N/A
Gearing (x)	0.47	0.17	0.27	0.27
Leverage (x)	2.02	2.24	2.09	1.47
Dividend Payout Ratio (%)	0%	0%	0%	0%
ROAA (%)	8%	2%	3%	7%
ROAE (%)	24%	8%	11%	21%

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix 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						Appendix III
Name of Rated Entity	Automobile Corporation of Pakistan					
Sector	Automobile					
Type of Relationship	Solicited					
Purpose of Rating	Entity Rating					
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**	
	RATING TYPE: ENTITY					
	4/22/2021	BBB	A-2	Stable	Maintained	
	5/21/2020	BBB	A-2	Rating Watch-Negative	Maintained	
	7/25/2019	BBB	A-2	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.					
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Due Diligence Meetings Conducted	**S.No**	**Names**	**Designation**	**Date**		
	1	Mr. Noor Sheikh	Chief Audit Executive/ Chief Financial Controller	April 12, 2021		