# RATING REPORT

# Agriauto Stamping Company (Pvt.) Limited

**REPORT DATE:**
April 1, 2024

**RATING ANALYSTS:**
Basel Ali Assad
*basel.ali@vis.com.pk*

| RATING DETAILS | | | | |
|---|---|---|---|---|
| Rating Category | Latest Rating | | Previous Rating | |
| | Long-term | Short-term | Long-term | Short-term |
| **Entity** | A- | A-2 | A- | A-2 |
| **Rating Outlook** | Stable | | Stable | |
| **Rating Action** | *Reaffirmed* | | *Initial* | |
| **Rating Date** | *April 1, 2024* | | *March 29, 2023* | |

| COMPANY INFORMATION | |
|---|---|
| **Incorporated in 2012** | **External Auditors:** A.F. Ferguson & Co. – Chartered Accountants |
| **Private Limited Company** | **Chairman:** Mr. Yutaka Arae<br>**Chief Executive Officer:** Mr. Fahim Kapadia |
| **Key Shareholders (with stake 5% or more):** | |
| Agriauto Industries Limited – 100% | |

## APPLICABLE METHODOLOGY

***Applicable Rating Criteria: Corporates***
***https://docs.vis.com.pk/docs/CorporateMethodology.pdf***

## APPLICABLE RATING SCALE

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

## OVERVIEW OF THE INSTITUTION

Agriauto Stamping Company (Pvt.) Limited (ASC) is a private limited company incorporated in 2012. ASC is the first stamping company in Pakistan having proper technology transfer in different areas of stamping including TPS, quality assurance, die maintenance & logistics.

**Profile of CEO**

Mr. Fahim Kapadia is the CEO of ASC and of the parent company AGIL. He has over 35 years of experience in the field of Finance, General Management and Business Development in Pakistan and abroad. He has been associated with the House of Habib (HoH) for the last 23 years. He is a Fellow Chartered Accountant (FCA) and Certified Public Accountant (CPA) from US. Also, he has a degree in Bachelor of Science (BSC) in Accounting.

## RATING RATIONALE

Agriauto Stamping Company (Pvt) Limited (ASC or 'the Company') is a wholly-owned subsidiary of Agriauto Industries Limited (AGIL) and is engaged in the manufacture and sale of sheet metal stamping parts, sub-assembly operations, dies/checking fixtures/jigs. ASC specializes in assembling and stamping of high tensile parts for automobiles, with technical collaboration with M/S. Ogihara (Thailand) Co. Ltd. The ratings factor in the strong sponsorship profile of the House of Habib (HoH), one of the country's largest business conglomerates which has diversified interests across several sectors including automobiles, building materials, packaging, plastics, property and financial services. ASC enhanced its manufacturing capacity with the addition of two new pressing lines and extension of storage facilities during the rating review period. However, the overall business risk profile of the Company was elevated over the rating review period on account of steep inflation, currency depreciation, policy rate hikes and import restrictions which have significantly impacted demand for automobiles as well as supply-side operations.

Resultantly, a significant decline in sales has been witnessed. This along with high production costs and financing charges have resulted in net losses during the ongoing year. Given deterioration in cash flows, coverages and debt service capacity have also been impacted. Meanwhile, capitalization indicators have remained sound despite some increase witnessed on account of higher debt levels. Going forward, the ratings will remain contingent on improvement in profitability and coverages whilst maintaining leverage indicators at manageable levels amidst the challenging business environment.

### Rating Drivers

**Business Risk**

The overall business risk of the auto-parts industry is considered to be in the high to medium category given appreciable cyclicality, historical volatility in gross margins, reliance on imported raw materials and notable exposure to exchange rate fluctuations. Over the rating review period, the Company's business risk has been elevated due to deterioration in the macroeconomic environment which has seen unprecedented levels of inflation and currency depreciation that have diminished disposable incomes of consumers as well as raised vehicle prices significantly. Additionally, the high policy rate environment coupled with restrictions on loan sizes and repayment durations by the State Bank of Pakistan (SBP) further discouraged car leasing activity. Consequently, demand for automobiles has dropped notably with total vehicle sales at end-Dec'23 amounting to 605,318 (FY23: 1,354,350, FY22: 2,162,521), forcing automobile manufacturers to shut down operations repeatedly. Moreover, on the supply-side front, import restrictions imposed by SBP to curb deterioration of the current account deficit hampered procurement of necessary raw materials thereby impacting production activity.

The ratings take into consideration ASC's position as the sole producer of sheet metal stamping parts and catalytic converters in the local auto parts industry. The Company also benefits from synergies through its association with AGIL which has more than four decades of experience in the auto industry as the only producer of car shock absorbers and struts in the domestic market. Moreover, ASC's competitive advantage also stems from its technical partnership with M/s. Ogihara (Thailand) Co. Ltd. which is a leading die making & stamping part supplier to Toyota, Honda & Mitsubishi in Thailand. Ogihara Thailand is a subsidiary of Ogihara Corporation, Japan which has overseas operations in USA, UK, China and India.

**Capacity and Operations**

ASC's manufacturing facilities are located in Port Qasim, Karachi. Details of the same are

outlined below:

| *Facility* | **Details** |
|---|---|
| **Tandem Press Line** | Tandem Press Line 1= 800-500-500-500 Tons<br>Tandem Press Line 2= 800-500-500-1000 Tons |
| **Welding Gantry** | Portable Spot Welder= 70<br>Stationary Spot Welder= 3<br>Portable Strut Welder= 1 |
| **Catalytic Converter** | Complete Catalytic Converter & Sub Muffler Manufacturing Plant |

The Company has also invested in couple of projects including the installation of two new tandem press lines of 1000 and 800 tons (which recently began commercial operations) and the extension of the welding assembly line to accommodate production of a new car model. Additionally, the storage area for finished goods and dies was also expanded. The total capital expenditure on these projects amounted to around Rs. 1.03b out of which about 25% was financed through long-term borrowings while the remainder was met through internal capital sources. Going forward, the management does not plan to incur further capital expenditure as the current manufacturing facilities are at excess capacity relative to expected demand levels in the foreseeable future.

**Declining trend in sales in FY23 and HY24**

The Company's topline witnessed a declining trend in the last 1.5 years amounting to Rs. 984m (FY23: Rs. 3b; FY22: Rs. 6.5b; FY21: Rs. 3.6b) in 1HFY24. This was largely on account of lower volumetric offtake in line with notable drop in demand for automobiles amidst the challenging macroeconomic environment. The overall business mix depicted a shift largely to stamping products, the main revenue driver, as demand for catalytic converters was particularly impacted. Breakdown of the business mix is tabulated below:

| | **FY22** | | **FY23** | | **1HFY24** | |
|---|---|---|---|---|---|---|
| Catalytic Converter | 2,840.2 | 43.4% | 1,228.7 | 38.1% | 323.8 | 28.6% |
| Stamping | 3,339.9 | 51.1% | 1,904.4 | 59.1% | 742.7 | 65.7% |
| Other | 360.1 | 5.5% | 91.0 | 2.8% | 64.6 | 5.7% |
| **Total** | **6,540.2** | **100.0%** | **3,224.0** | **100.0%** | **1,131.1** | **100.0%** |

Moreover, the Company's client concentration risk is notably high consisting largely of institutional customers, in line with dynamics of the auto parts industry, with almost the entire topline emanating from the top ten clients. However, the associated risk is moderated on account of the long-term nature of contracts with clients. Additionally, the majority of revenue is concentrated with Indus Motor Company (IMC) which is an associated company that is part of the House of Habib (HoH) Group. ASC is also the sole supplier of catalytic converters and sheet metal stamping for IMC in Pakistan, further reducing selling risk. Breakdown of sales of top ten clients is tabulated below:

| | **FY23** | | **1HFY24** | |
|---|---|---|---|---|
| | **(Rs. mln)** | **%** | **(Rs. mln)** | **%** |
| Indus Motor Company | 2,759.6 | 85.6% | 931.3 | 82.3% |
| Qureshi Brothers | 34.4 | 1.1% | 82.7 | 7.3% |
| Honda Atlas | 107.2 | 3.3% | 53.7 | 4.7% |
| Metaline Industries | 83.3 | 2.6% | 20.2 | 1.8% |
| Pak Suzuki Motor Company | 48.3 | 1.5% | 15.4 | 1.4% |
| Thal Boshoku Pakistan | 22.1 | 0.7% | 12.9 | 1.1% |
| Agriauto Industries | 15.7 | 0.5% | 4.7 | 0.4% |

| Yamaha Motor | 5.3 | 0.2% | 3.9 | 0.3% |
|---|---|---|---|---|
| M.A Wood Products | 80.4 | 2.5% | 3.7 | 0.3% |
| Noorani Trading Company | 4.6 | 0.1% | 2.6 | 0.2% |
| Loads | 1.6 | 0.0% | 0.1 | 0.0% |
| New Madina Processing | 42.7 | 1.3% | - | 0.0% |
| Qureshi Traders | 18.9 | 0.6% | - | 0.0% |
| **Total** | **3,224.0** | **100.0%** | **1,131.1** | **100.0%** |

In order to address the declining trend in sales, the management plans to initiate the sale of dies to IMC which were previously imported and also intends to export dies to Toyota South Africa; both these projects are expected to contribute modestly towards sales in the initial years. ASC also aims to diversify its product base by exploring production of fenders for the after-market sale as well as water dispensers in collaboration with two local companies, namely, Haier and Dawlance. Both these projects are under consideration. As per management, the bottom-line losses are expected to reduce to around Rs. 35.7m for FY24 vis-à-vis a loss of Rs. 84m for HY24 given orders from IMC in the pipeline. Going forward, while the diversification efforts are viewed positively, uplifting the Company's core revenue generation streams amidst the challenging business environment will be considered important for the assigned ratings, moving forward.

**Decline in margins and profitability**

The Company's gross margins depicted a notable decrease on a timeline basis to 1.7% during 1HFY24 (FY23: 10.7%, FY22: 14%) on account of rising production costs due to sharp currency depreciation and inflationary pressure coupled with lag in price adjustments. Additionally, the impact of depreciation following capitalization of plant and machinery had a further drag on gross margin. This decline is also reflected in the net margin which turned negative (FY23: 3.3%, FY22: 6.6%); the same also encountered pressure due to higher finance costs on account of policy rate hike and higher debt levels. In order to address the stress on profitability margins, the management aims to partially localize its raw material procurement, which was being completely imported previously, through an agreement with International Steels Limited which will meet about 30% of ASC's raw material needs from June'24 onwards; the same will help moderate direct exposure to currency rate fluctuations and risks associated with uncertain import policies. However, going forward, the profitability metrics are expected to remain stressed given suppressed demand amidst the challenging short to medium-term macroeconomic outlook. The ratings will continue to be sensitive to improvement in profit margin levels.

**Cash flows and coverages were adversely impacted**

Funds from Operations (FFO) turned negative (FY23: Rs. 232.4m, FY22: Rs. 553.4m) due to loss incurred in 1HFY24. Consequently, cash flow coverages were adversely impacted during the ongoing year. Debt service capacity witnessed notable pressure as DSCR levels decreased to 0.50x (FY23: 3.59x, FY22: 10.66x) in 1HFY24.

In conjunction with drop in sales, both inventory levels and trade debts declined over the rating review period to Rs. 903m and Rs. 226.1m, respectively, at end-FY23 (FY22: Rs. 1.6b, Rs. 440.6m). However, inventory levels increased to Rs. 1.2b by end-1HFY24. Meanwhile, the aging of receivables is considered adequate with about 86.6% of trade debts due within 30 days while the remainder are due between 1-3 months during the ongoing year. On the other hand, trade payables and short-term borrowings increased to Rs. 667.7m and Rs. 421.7m, respectively, (FY22: Rs. 595.4m, Rs. 194.9m; Rs. 559.1m, Rs. 363.6m) on account of higher working capital requirements due to inflationary pressure. Consequently, the current ratio and short-term borrowing coverage levels depicted a downtrend on a timeline basis, and stood at 1.54x and 3.39x, respectively (FY23: 1.87x, 5.79x; FY22: 2.45x, 5.51x); nonetheless, the aforementioned liquidity indicators remained largely in line with the assigned rating. Going forward,

improvement in the overall liquidity profile, and debt service coverages, will remain important rating factors.

**Equity erosion was witnessed though leverage indicators remained manageable**
The Company's equity base decreased to Rs. 2.8b during the outgoing year (FY22: Rs. 2.9b) on account of cash dividend payout of Rs. 228.8m, higher than the net profit of Rs. 99m for FY23. The downtrend in equity erosion continued during the ongoing year as net loss was registered, depleting the equity base to Rs. 2.7b by end-Dec'23. In terms of borrowings, the Company's short-term debt increased to Rs. 421.7m by end-1HFY24 (FY23: Rs. 194.9m, FY22: Rs. 363.6m) due to higher working capital requirements. Additionally, long-term borrowings increased over the rating review period to Rs. 299.8m (FY23: Rs. 299.7m, FY22: Rs. 45.1m) to partially fund the aforementioned capital expenditure; about 15.2% of the same pertained to the SBP renewable energy refinance scheme obtained at concessionary rates for the solar energy project. Consequently, leverage and gearing levels depicted an increase to 0.53x and 0.26x, respectively, at end-Dec'23 (FY23: 0.43x, FY22: 0.17x; FY22: 0.39x, 0.14x); nonetheless, capitalization levels remained satisfactory relative to assigned benchmarks. Going forward, the management plans to focus on the sale of current inventory stockpiles thereby reducing short-term borrowings on the balance sheet by end-FY24. Consequently, given that further capital expenditure is not envisaged in the foreseeable future, debt leverage and gearing levels are expected to depict improvement. Going forward, the ratings will remain sensitive to the Company's ability to maintain capitalization levels through internal profit generation.

| Financial Summary (PKR in mln) | | | | |
|---|---|---|---|---|
| **Balance Sheet** | **FY21** | **FY22** | **FY23** | **1HFY24** |
| Operating fixed assets | 1,318 | 1,600 | 2,418 | 2,407 |
| Stock in trade | 669 | 1,563 | 903.0 | 1,186 |
| Trade debts | 382 | 441 | 226.1 | 242 |
| Short-term investments | 144 | 39 | 37 | 37 |
| Cash and bank balances | 60 | 103 | 73 | 3 |
| Other assets | 389 | 361 | 386 | 318 |
| Total assets | 2,963 | 4,106 | 4,043 | 4,193 |
| Long-term borrowing (inc current portion) | - | 45 | 300 | 300 |
| Short-term borrowing | - | 364 | 195 | 422 |
| Total borrowings | - | 409 | 495 | 721 |
| Trade payables | 259 | 559 | 595 | 668 |
| Other liabilities | 179 | 180 | 124 | 60 |
| Total liabilities | 438 | 1,148 | 1,214 | 1,449 |
| Paid up capital | 1,144 | 1,144 | 1,144 | 1,144 |
| Total equity | 2,525 | 2,958 | 2,828 | 2,744 |
| | | | | |
| **Income Statement** | **FY21** | **FY22** | **FY23** | **1HFY24** |
| Net sales | 3,600 | 6,528 | 3,019 | 984 |
| Gross profit | 676 | 913 | 323 | 16 |
| Operating profit | 615 | 816 | 209 | (55) |
| Financial cost | 1 | 48 | 45 | 43 |
| Profit before tax | 598 | 646 | 135 | (97) |
| Profit after tax | 407 | 433 | 99 | (84) |
| | | | | |
| **Ratio Analysis** | **FY21** | **FY22** | **FY23** | **1HFY24** |
| Gross margin (%) | 18.8 | 14.0 | 10.7 | 1.7 |
| Net margin (%) | 11.3 | 6.6 | 3.3 | NM** |
| Trade debts/net sales (%)* | 10.6 | 6.7 | 7.5 | 12.3 |
| ROAA (%)* | 14.4 | 12.2 | 2.4 | NM** |
| ROAE (%)* | 16.7 | 15.8 | 3.4 | NM** |
| Current ratio (x) | 4.7 | 2.5 | 1.9 | 1.5 |
| Stock in trade + Trade debts/Short-term borrowings (x) | - | 5.5 | 5.8 | 3.4 |
| FFO* | 792 | 553.4 | 232.4 | (11.9) |
| FFO to long-term debt (%)* | - | 12.3 | 0.8 | NM** |
| FFO to total debt (%)* | - | 1.4 | 0.5 | NM** |
| DSCR (x)* | 796.5 | 10.7 | 3.6 | 0.5 |
| Cash conversion cycle (days)* | 90 | 90 | 69 | 71 |
| Gearing (x) | - | 0.1 | 0.2 | 0.3 |
| Leverage (x) | 0.2 | 0.4 | 0.4 | 0.5 |

**Annualized*
***Not Meaningful*

| REGULATORY DISCLOSURES | Appendix II |
|---|---|
| **Name of Rated Entity** | Agriauto Stamping Company (Pvt.) Limited |
| **Sector** | Auto Parts |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Entity Ratings |
| **Rating History** | (see table below) |
| **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** | (see table below) |

**Rating History**

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| | | **RATING TYPE: ENTITY** | | |
| **01-April-24** | **A-** | **A-2** | **Stable** | **Reaffirmed** |
| 29-Mar-23 | A- | A-2 | Stable | Initial |

**Due Diligence Meetings Conducted**

| Name | Designation | Date |
|---|---|---|
| Mr. Fahim Kapadia | CEO | February 22, 2024 |
| Mr. Tariq Iqbal | CFO | |