

## RATINGS (OCTOBER 2009)

### HAZARA PHOSPHATE FERTILIZERS (PVT.) LIMITED (HPFL)

Entity	New
Long Term	A+
Short Term	A1

## FINANCIAL DATA

PKR (mln)

	Jun-09	Jun-08
Total Assets	3,485	1,002
Equity	2,303	282
Net Income	547	126
EBITDA	529	151
ROA (%)	15.7	17.3
ROE (%)	47.5	57.5
EBITDA / Interest (x)	10.8	12.8
Net Debt / Equity (%)	-0.54*	52.1

\* Negative due to net cash

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## RATING RATIONALE AND KEY RATING DRIVERS

- The ratings reflect HPFL's low business risk profile emanating from robust, indeed growing, demand of its product in the domestic market. Subsequent to privatization, the new management has initiated different efficiency measures, enabling the company to achieve higher production, while controlling the related cost. Meanwhile, HPFL has a predominantly equity based capital structure, which provides cushion for further expansion.
- These ratings are dependent on the company's ability to sustain its competitiveness through intense, though occasional, price volatility in the key inputs (sulphur and phosphorus). Meanwhile, any significant erosion in gross margins, and/or rise in gearing level thereby impacting HPFL's profitability and coverages would have negative implications.

## ASSESSMENT

- Pak American Fertilizer Limited (PAFL), a urea production facility with 7% market share, acquired 100% stake in HPFL, during Nov 08, through the privatisation process. PAFL, to augment overall performance of the subsidiary, has brought certain changes to HPFL including scheduling of maintenance, extended use of low cost local raw material and setting up of a gas fired power production engine (~2MW). As HPFL had no independent sales/marketing function, this is managed by expansion in the group marketing team. Other group synergy includes finance, internal audit and other similar functions being managed at the group level. HPFL's product is branded as "Tara", the brand for all fertilizers of the group. HPFL's core production – Granulated Single Super Phosphate (GSSP) – primarily serving the phosphatic fertilizer market, has an estimated offtake of above 1mln ton per annum, of which HPFL enjoys ~3% share.
- During FY09, HPFL experienced significant growth in its turnover. This was mainly an outcome of rising price trend in the international phosphatic market, followed domestically as well. The GoP responded to the situation by providing subsidy to insure affordability for the farmers. The company also witnessed substantial upturn in gross margins, attributed to inventory gains. However, this is subject to grant of subsidy (PKR 495mln) to the company for the period from Jan-09 till mid Apr-09. HPFL's operating expenses increased as a result of addition in marketing expenditure, previously borne by a public sector entity. Meanwhile, the company made a provision of ~PKR 60mln for a pending dispute, as agreed in the privatisation agreement. Moreover, its finance cost increased in line with rising interest rates in the country. Nonetheless, the company posted robust bottomline during the year.
- Going forward, HPFL intends to gradually increase its production capacity to tap the growth potential in the phosphatic market. In the first phase, the capacity would be enhanced to 500MT per day at a cost of US\$ 1mln through (i) operational de-bottlenecking (ii) replacement of the grinding unit (iii) addition of mines and (iv) better utilization of steam. In the next phase, this capacity would be doubled by adding a new plant at an estimated cost of US\$ 15mln. Meanwhile, the management does not see significant pressure on the gross margins, as GSSP's prices are directly linked with DAP prices in the international market. The company has plans to switch from its current manual accounting system to Oracle based information system, which is in the process of implementation at PAFL.
- HPFL's working capital requirements are mainly a function of its raw material procurement. The company, for this, uses PAFL's platform in order to avail short term credit facilities of which the cost is currently being borne by the parent.
- HPFL has predominantly an equity based capital structure, which has been strengthened after privatisation through recognition of a sizeable revaluation surplus on fixed assets. The company has strong cashflows, emanating from mostly cash nature of its sales. Moreover, with robust profits, coverages of the company remain well within the comfortable range.

## PROFILE

- Hazara Phosphate Fertilizers (Pvt.) Limited (HPFL), incorporated in 1985, commenced commercial production of GSSP in 1989. HPFL's plant, with a designed capacity of 300MT per day of GSSP (current utilization: 120%), is located in Haripur, 75km from Islamabad. HPFL's parent – Pak American Fertilizer Limited (PAFL) – is a wholly owned subsidiary of Azgard Nine Limited (ANL). PAFL has undertaken a major plant revamp, which is expected to result in substantial capacity improvement. Meanwhile, the group is in the process of enlisting PAFL on the stock exchange. ANL, listed on the Karachi Stock Exchange, started commercial production in 1997 and is a leading exporter of denim fabric and garments. *Shaikh* family has a majority stake (40%) in ANL, followed by JS Group (36%).
- The BoD of HPFL comprises five members including the Chief Executive Officer (CEO). All the directors hold executive positions in the group companies. The CEO, Mr. Hamid Iqbal, a chemical engineer from UET, has over 30 years of experience in the fertilizer industry. He is assisted by a team of professionals, most of whom have been working with the sponsoring group for long.