

## MAPLE LEAF CEMENT FACTORY LIMITED (MLCFL)

### RATINGS (Sep 2007)

#### MAPLE LEAF CEMENT FACTORY LIMITED

Entity	New
Long Term	A
Short Term	A1
Sukuk secured PKR 8,000mln	A+

### FINANCIAL DATA

	PKR (mln)	
	30-Jun-07	30-Jun-06
Total Assets	23,437	19,144.9
Equity	8,993	7,555.7
Turnover	3,711.1	5,709.8
Net Income	42.1	1,059.2
Gross Margin (%)	8.4	37.6
ROE (%)	0.5	15.6
Net Debt / Equity (%)	136.3	124.2

### ANALYSTS

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### SUKUK ISSUE

MLCFL intends to issue a secured Sukuk of PKR 8,000mln – including a Green Shoe option of PKR 4,000mln – to re-profile its existing long-term borrowings. The Sukuk issue is for a tenor of 6 years (with two years grace period), carrying profit at the rate of 6-months KIBOR plus 170bps, payable semi-annually in arrears. The Musharaka investments will be repurchased in eight installments commencing from the 30<sup>th</sup> month after the date of first contribution. Each of first four installments will be of 10% of original principal amount, while each of the remaining four installments will be of 15% of the original issue amount. The instrument would be secured by way of a ranking charge to be upgraded to first pari passu charge within 150 days after the date of first contribution over all present and future fixed assets of the company with 25% margin.

### ASSESSMENT

- The ratings reflect the expected improvement in the overall performance of the company based on better business prospects and likely increase in efficiency as new production lines commence full operations. The ratings also take into account MLCFL's strong equity base and its association with a reputed business group. However, at the same time, the ratings recognize the cyclical nature of the cement industry and the emerging significant capacity overhang in the sector engendering high business risk.
- In the recent period, the cement industry, with additional capacities increasing the supply surplus, has experienced weakening of the tacit understanding amongst producers in terms of capacity utilization and pricing. This has put pressure on the selling price of cement, resulting in dampening profitability for most companies during FY07. While domestic cement demand is showing consistent growth, to achieve higher capacity utilization, the industry is putting greater emphasis on tapping export markets. In this regard, the recent development regarding prospects of exports to India is likely to reduce the cement industry's business risk to some extent in the near-term and is expected to have a positive impact on the local market in the shape of price stability.
- MLCFL is one of the leading cement manufacturers in the country with the third largest market share. The company has a diversified product portfolio. At the same time, multiple production lines provide the company with flexibility for undertaking production of specialized and value-added products. With its new capacity coming online, the company is expected to further strengthen its market position. MLCFL posted strong results in FY06 and FY05 (PAT FY06: PKR 1,059mln FY05: PKR 728mln) on the back of robust demand and high cement prices. However, the sanguine pattern did not continue in FY07 and MLCFL's performance, in line with the industry, was subdued. Lower selling price, as a consequence of a long price war in the North region (MLCFL's primary market), high cost carry over inventory and breakdown of dry production line resulted in lower profit margins and depressed performance of the company.
- The company is poised to commence its export operations to India soon. MLCFL, due to its close proximity to Northern India and connection to railway network, enjoys advantage over its peers in terms of logistic arrangements. The management intends to export around 15%-20% of its grey cement production. Due to supply deficit in India, which is expected to continue in the near-term, the company is expected to achieve its export targets at good margins. Going forward, the management intends to fully utilize its new production lines that are more cost efficient. The company is planning to launch new products – Oil well cement and colour variants of white cement – to further diversify its portfolio and effectively utilize its wet process lines. The management is taking initiatives to improve overall performance by rationalizing the workforce, finding cheaper alternative energy sources and restructuring its debt profile. These steps augur well for the overall profitability of the company.
- The company's capital structure, despite substantial borrowings to finance its capacity expansion, remained strong due to further equity injection and full profit retention policy in the recent years. Moreover, the preference shares, with pre-dominantly equity like features, support the capital structure. However, the cashflow generation ability of the company was adversely impacted due to lower turnover and subdued performance in FY07, distorting the coverage ratios as well. MLCFL enjoys favourable credit terms with its suppliers as reflected by its net cash cycle surplus. This helps the company in managing its working capital requirements. Cashflows and coverage ratios are expected to improve with better performance prospects, going forward. At the same time, the management is working on the re-profiling of its expansion related borrowings. The restructuring, while lowering the financial cost, is expected to synchronize the debt repayment with the emerging cashflow pattern.

### Key Rating Drivers

- The ratings are dependent on successful execution of the management's export strategy and its ability to effectively utilize new capacity to improve turnover, margins and cashflows. The sustainability of the export operations, especially in the medium-term, also remains critical. Meanwhile, any prolonged price war in the domestic market, dampening the margins, or a major slump in cement demand would have negative implications for the ratings.

### Profile

- Maple Leaf Cement Factory Limited, established in 1956 as joint collaboration between West Pakistan Industrial Development Corporation and Government of Canada, was taken over by the Kohinoor Maple Leaf Group, subsequent to its privatisation in 1992.
- The group – mainly through Kohinoor Textile Mills Limited (KTML) – owns the majority stake (50%) in the company, while various financial institutions, corporate entities and individuals own the rest. The group also has presence in the textile sector (KTML) and in trading of agriculture machinery industry. Saigol family, renowned and established industrialists of Pakistan, effectively controls group companies including MLCFL with strong presence on the board of directors and key management positions.
- Mr. Sayeed Saigol, the CEO, joined the company in 2005. The COO of the company is a prominent professional of the cement industry with over 25 years of experience. The top management is supported by a team of professionals with extensive experience in project development and cement sector.