



## The Pakistan Credit Rating Agency Limited

### Rating Report

#### Cherat Cement Company Limited

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##### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2022	A+	A1	Stable	Maintain	-
28-Dec-2021	A+	A1	Stable	Upgrade	-
10-Apr-2021	A	A1	Positive	Maintain	-
10-Apr-2020	A	A1	Stable	Maintain	-
25-Oct-2019	A	A1	Positive	Maintain	-
26-Apr-2019	A	A1	Positive	Maintain	-
31-Dec-2018	A	A1	Positive	Maintain	-
30-Jun-2018	A	A1	Positive	Maintain	-
28-Dec-2017	A	A1	Stable	Maintain	-
06-Jun-2017	A	A1	Stable	Maintain	-

##### Rating Rationale and Key Rating Drivers

Cherat Cement's Ratings reflect its prominent presence in the cement sector emanating from its major market share (~7%) predominately in the north region. The latest period reported a reduction in cement production reflecting on economic downturn. Increase in prices of all the construction materials has impacted demand for cement as well. However, cement's demand is expected to come full circle once the macro level fundamentals improve. Though, industry wide volumetric decrease in sales has been reported but better selling prices have absorbed their impact. Consequently, company's revenues soared to PKR 9,050mln & PKR 32,085mln at the end of 1QFY23 & FY22 respectively (1QFY22: PKR 7.16bln, FY21: PKR 25.21bln). Company managed to improve margins in said period on back of efficient cost management enhanced through recently added captive solar power plant. The Company's leveraging is currently at an adequate level, especially with the repayments being made. Moreover, keeping in view the economic turndown the management has decided to delay the greenfield expansion project. The financial risk profile incorporates liquidity profile, evident from healthy cash flows and improved coverages. Further, the Ratings assigned to Cherat Cement also draw support from the strong financial profile of the Company's sponsor, Ghulam Faruque Group having a presence across multiple sectors mainly including Cement, Sugar, Packaging, Software Solutions, Air Conditioning and specialized engineering equipment.

The ratings remain dependent on upholding company's market position along with sustenance of business volumes, margins and achieving optimal utilization of production capacities. The company's good business performance as compared to other players in current stretched economic scenario - challenges on demand front - remains vital for ratings.

##### Disclosure

<b>Name of Rated Entity</b>	Cherat Cement Company Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Rating(Jun-22),Methodology   Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology   Rating Modifiers(Jun-22)
<b>Related Research</b>	Sector Study   Cement(Mar-22)
<b>Rating Analysts</b>	Anam Waqas Ghayour   anam.waqas@pacra.com   +92-42-35869504

## Profile

**Legal Structure** Cherat Cement Company Limited (Cherat Cement), a public limited company incorporated in 1981, commenced operations in 1985. The company is listed on Pakistan Stock Exchange (PSX).

**Background** Cherat Cement Company is one of leading companies of Ghulam Faruque Group. Over last decade, Ghulam Faruque Group has solidified its position by having interests in various sectors i.e cement, sugar, packaging, software solution, air conditioning, CNG installation, sales and servicing of engineering parts, etc.

**Operations** With an installed capacity of 4.5mln tons per annum, the company currently holds 7% share in country's operational cement capacity. The company's home markets include KPK, Azad Kashmir and Punjab.

## Ownership

**Ownership Structure** Ghulam Faruque Group (GFG) holds majority stake in the company through associated companies and family members; Financial Institutions and Mutual Funds also hold equity stake.

**Stability** Presently, third generation is heading the business of GFG companies. Hence, the ownership is expected to remain same in the foreseeable future.

**Business Acumen** The business acumen of sponsors is considered strong as sponsoring family has diversified interests. Over the years, GFG has strengthened its foothold in various business ventures.

**Financial Strength** Financial Strength of the group considered strong as the GFG group reported a revenue PKR 46bln and a profit of PKR 4.1bln during FY22.

## Governance

**Board Structure** The overall control of the company vests in eight-member board, including the CEO. The Board of Directors (BoD) comprises six non-executive directors, including three independent director out of which three are Ghulam Faruque family members, including the CEO.

**Members' Profile** Cherat Cement has a balanced and professional board with well-qualified members having diverse business experience.

**Board Effectiveness** During the year, six board meetings were held. Directors' attendance in the board meetings remained strong; meeting minutes are formally maintained. Two board committees, Audit and Human Resource & Remuneration, are in place to assist the board on relevant matters. Moreover, four Audit committee meetings and two HR & Remuneration meetings were held during the said period.

**Financial Transparency** M/s EY Ford Rhodes Chartered Accountants – 'A category' SBP panel member – is the external auditor of the company, has expressed unqualified opinion on Cherat Cement's financial statements for the year ended June 30, 2022.

## Management

**Organizational Structure** Cherat Cement has a well-tiered organization structure with the company's operations grouped under eight key functions. These include 1) Procurement, 2) Production, 3) Sales & Marketing, 4) Information Technology, 5) Finance, 6) Legal & Corporate Affairs, 7) Human Resource, and 8) Internal Audit. All departments are headed by Executive Directors/ General Managers (GMs), who, in turn, directly report to the CEO.

**Management Team** The CEO, Mr. Azam Faruque, is a grandson of Mr. Ghulam Faruque and is associated with the company since 1992. Mr. Faruque is a foreign qualified professional with diversified exposure including Oil and Gas, packaging, cement, power, sugar, and financial sectors.

**Effectiveness** The management is supported by five committees (i) Management, (ii) Production, (iii) Sales & Marketing, (iv) IT Steering and (v) Human Resource. The necessary information is captured in minutes.

**MIS** Cherat Cement is one of the cement companies that deploys SAP based ERP solution in Pakistan. The software enables the management to generate various regular and customized reports of different frequency (daily, weekly, monthly and yearly) pertaining to production, sales, cement prices and other important financial figures.

**Control Environment** CCCL operates with three lines; one is European and others are Chinese Technology. Accredited with ISO9001: 2015 and ISO14001: 2015 certifications. Power needs are managed through gas and dual fuel generators, also from alternate sources including solar energy, WHR, RDF and TDF. Post line III installation, power requirement stands at 50-53.5 MW. Captive power capacity has been increased to 70 MW. CCCL has national grid connection of 63 MW.

## Business Risk

**Industry Dynamics** In FY21, overall sector gross revenues rebounded by ~35% and were recorded at PKR~542bln coming off a low base, as in FY20 due to COVID-19 related restrictions the industry size receded by ~8.7% to PKR~402bln. However, during the current turmoil of Russia-Ukraine conflict and pressure of global recession caused the downturn in cement demand by ~25% in 1QFY23. Going forward, there is a possibility of increase in local demand as government starts to repair the infrastructure damaged by floods and work on rehabilitation starts. Cement Sector is composed of 17 companies of which 16 companies are operational. The Sector is divided into two regions; North and South, with North covering areas of Punjab, KPK and AJK and South including areas of Sindh and Baluchistan. Cement sector's production capacity is recorded around ~69mln MT in FY21 (~64mln MT in FY20), an increase of ~8.8% YoY.

**Relative Position** The company's market positioning strengthened with 7% installed cement capacity in the country.

**Revenues** Cherat Cement has achieved continuous growth and have a considerable market share of ~7%. Sales volume analysis revealed that total dispatches of the company decreased by 25% as compared to the corresponding period due to the slowdown in economic activities in the country and also a considerable decrease in exports to Afghanistan. The sales mix remained tilted towards local sales (1QFY23: 85.11%, FY22: 91.75%, FY21: 87.06%). During 1QFY23 and FY22, the company's topline stood at PKR 9,050mln & 32,085mln respectively (FY21: PKR 25,206mln), up 26% YoY. This growth is attributed to upward adjustment in cement prices on account of higher input costs.

**Margins** During the year, the company's margins showed upward movement on back of sale prices (GP; 1QFY23: 32%, FY22: 27.9%, FY21: 26.7%). Similarly, operating margins and EBITDA margins also remained intact and stands at (OM; 1QFY23: 29.4%, FY22: 25.2%, FY21: 22.8%. EBITDA; 1QFY23: 33%, FY22: 30%, FY21: 30%).

**Sustainability** Work on BMR for Cement Line1 and installation of a new Crusher at the quarry face were affected due to manufacturing disruptions and international shipment delays. The company expects them to be completed by Jan-23. Furthermore, The Board of Directors of the Company has decided to install a greenfield cement plant at D.I. Khan, Khyber Pakhtunkhwa Province. The plant will have an installed production capacity of 11,000 tons per day of clinker.

## Financial Risk

**Working Capital** During 1QFY23, Cherat Cement's working capital requirements, represented by net cash cycle (net working capital days) – a function of inventory, receivables and payables – Increased to 30 days (FY22: 22 days). However, showing a declining trend on yearly basis (FY22: 22, FY21: 27). The quantum of STBs stood at PKR 2,700mln (FY22: PKR 3,136mln) on account of enhanced working capital needs.

**Coverages** During 1QFY23, Cherat Cement's EBITDA improved to PKR 3,005mln as compared to annual of PKR 9,701mln (FY21: PKR 7501mln) while finance costs also witnessed significant uptick of 61% as compared to the corresponding period. However, company managed to restrict the total impact of the cost through prudent management and debt service coverage inclined to 6.1x at the end of 1QFY22 (FY22: 6.9x, FY21: 4.8x). Going forward, vigilant management of cashflows remains vital.

**Capitalization** During 1QFY23, the company's total debt stands at PKR 16,362mln (FY22: PKR 17,082mln, FY21: PKR 17,153mln). CMLTD marginally increased to PKR 3,073mln (FY22: PKR 3,068mln). Company is regularly paying the installments. Thus, leveraging is continuously declining and stands at 46.6% at end Sep-22 (FY22: 49.7%, FY21: 55.8%).



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

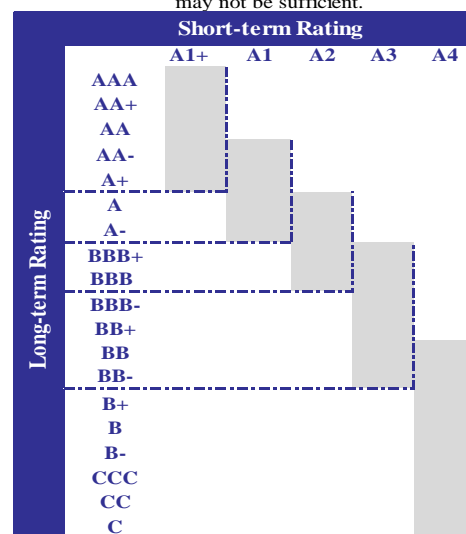
Cherat Cement Company Limited Cement	Sep-22 3M	Jun-22 12M	Jun-21 12M	Jun-20 12M
<b>A BALANCE SHEET</b>				
1 Non-Current Assets	27,637	27,658	25,687	25,847
2 Investments	-	-	-	-
3 Related Party Exposure	457	482	661	391
4 Current Assets	12,110	10,465	7,846	6,685
a Inventories	1,753	926	1,006	962
b Trade Receivables	732	534	408	301
5 Total Assets	40,203	38,605	34,194	32,923
6 Current Liabilities	4,256	3,643	2,850	2,776
a Trade Payables	127	119	149	171
7 Borrowings	16,362	17,082	17,153	20,064
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	812	563	602	28
10 Net Assets	18,774	17,316	13,590	10,055
11 Shareholders' Equity	18,774	17,316	13,590	10,054
<b>B INCOME STATEMENT</b>				
1 Sales	9,050	32,085	25,207	17,090
a Cost of Good Sold	(6,155)	(23,135)	(18,479)	(16,704)
2 Gross Profit	2,895	8,951	6,728	386
a Operating Expenses	(236)	(878)	(972)	(653)
3 Operating Profit	2,659	8,072	5,757	(266)
a Non Operating Income or (Expense)	(48)	115	105	71
4 Profit or (Loss) before Interest and Tax	2,611	8,188	5,861	(196)
a Total Finance Cost	(480)	(1,359)	(1,524)	(2,527)
b Taxation	(648)	(2,373)	(1,132)	830
6 Net Income Or (Loss)	1,483	4,456	3,205	(1,893)
<b>C CASH FLOW STATEMENT</b>				
a Free Cash Flows from Operations (FCFO)	2,907	9,020	7,178	1,314
b Net Cash from Operating Activities before Working Capital Changes	2,641	7,725	5,406	(1,162)
c Changes in Working Capital	(1,569)	(2,913)	(287)	2,208
1 Net Cash provided by Operating Activities	1,072	4,811	5,120	1,046
2 Net Cash (Used in) or Available From Investing Activities	(352)	(4,502)	(1,877)	(294)
3 Net Cash (Used in) or Available From Financing Activities	(285)	(1,713)	(2,218)	(745)
4 Net Cash generated or (Used) during the period	435	(1,403)	1,024	7
<b>D RATIO ANALYSIS</b>				
1 Performance				
a Sales Growth (for the period)	12.8%	27.3%	47.5%	7.7%
b Gross Profit Margin	32.0%	27.9%	26.7%	2.3%
c Net Profit Margin	16.4%	13.9%	12.7%	-11.1%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	14.8%	19.0%	27.3%	20.6%
e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/Sh	32.2%	27.3%	24.0%	-18.2%
2 Working Capital Management				
a Gross Working Capital (Average Days)	32	23	29	49
b Net Working Capital (Average Days)	30	22	27	44
c Current Ratio (Current Assets / Current Liabilities)	2.8	2.9	2.8	2.4
3 Coverages				
a EBITDA / Finance Cost	6.3	7.4	5.0	0.6
b FCFO / Finance Cost+CMLTB+Excess STB	2.3	2.1	1.7	0.4
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.4	1.8	2.7	-14.6
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	46.6%	49.7%	55.8%	66.6%
b Interest or Markup Payable (Days)	130.3	120.9	74.6	78.2
c Entity Average Borrowing Rate	11.7%	7.9%	8.1%	12.6%

### Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
AA-	
A+	
A	<b>High credit quality.</b> Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
A-	
BBB+	
BBB	<b>Good credit quality.</b> Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BBB-	
BB+	
BB	<b>Moderate risk.</b> Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
BB-	
B+	
B	<b>High credit risk.</b> A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
B-	
CCC	
CC	<b>Very high credit risk.</b> Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*\*The correlation shown is indicative and, in certain cases, may not hold.*

**Outlook (Stable, Positive, Negative, Developing)** Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

**Rating Watch** Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

**Suspension** It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

**Withdrawn** A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

**Harmonization** A change in rating due to revision in applicable methodology or underlying scale.

**Surveillance.** Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

**Note.** This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

### **2) Conflict of Interest**

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

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- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

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- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA’s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers’ associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
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- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

### **Probability of Default**

- (22) PACRA’s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA’s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA’s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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