The Pakistan Credit Rating Agency Limited

Rating Report

Amreli Steels Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
10-May-2023	A-	A2	Stable	Maintain	-
05-Jul-2022	A-	A2	Stable	Maintain	-
05-Jul-2021	A-	A2	Stable	Maintain	-
02-Sep-2020	A-	A2	Stable	Maintain	-
24-Sep-2019	A-	A2	Stable	Downgrade	-
25-Mar-2019	A	A1	Stable	Maintain	-
18-Dec-2018	A	A1	Stable	Maintain	-
14-Jun-2018	A	A1	Stable	Maintain	-
29-Dec-2017	A	A1	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Amreli Steels has good business profile on account of the company’s market positioning in the industry. The Company produces two key products: i) steel billets, ii) rebars including a) Grade 60 Deformed Steel bars and b) Xtreme bars (G-500W). Melting capacity of company is 600,000 tons per annum while its rebar manufacturing capacity is 605,000 tons per annum. The company having significant presence in Rebars market, intends to sustain on its quality and a wide retail and distribution network spread across Pakistan. Exacerbating levels of inflation and political instability has slowed down overall economic growth in Pakistan. Operating in these dynamics, steel industry is grappling with grave challenges like contained demand and raw materials shortages due to imports restrictions. Margins improved in latest quarter due to improvement in price retention. The company reported a loss in 2QFY23, however as the prices picked up, bottom line turned green in 3QFY23. With significant contraction in volumetric sales, company's topline was reported at PKR 34.698 billion in Mar 23 (Mar 22: PKR 42.537 billion). Amreli's financial risk matrix is stretched owing to debt-to-equity ratio of ~60% due to significant reliance on short-term financing for day-to-day working capital requirements. Decision to further expand melting and rebar manufacturing facilities has been shelved due to struggling economic outlook. Management decided to diversify into non-ferrous operations and is establishing a new facility for production of Aluminium ingots. The project is, however stalled currently due to LCs related issues. Going forward, management aims to sustain the current volumetric levels and adopt cost efficiency model through measures like maintaining optimum inventory and receivable levels. Enhanced price retention shall further support company's performance.

The ratings draw comfort from the strong business acumen of Amreli Steels' sponsors - Akberali Family. The ratings are dependent on the management's ability to uphold in difficult times and improve its business vis-à-vis financial risk profile while operating in challenging economic conditions. Retention of its market share, timely repayments of long-term loans and sustained margins are vital. Moreover, prudent management of financial affairs is vital in the sustainability of the Company.

Disclosure

Name of Rated Entity	Amreli Steels Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Steel(Sep-22)
Rating Analysts	Uswa Sikandar | uswa.sikandar@pacra.com | +92-42-35869504

Profile

Legal Structure Amreli Steels Limited, a public limited company incorporated in 1984 under the Companies Ordinance and is traded under the section of Engineering.
Background Amreli Steel's two re-rolling plants situated at S.I.T.E. Karachi and Dhabeji are using one of the most modern hot re-rolling technologies in the industry with a nameplate capacity of 180,000 metric tons and 425,000 metric tons of rebars per annum respectively. The melt shop is situated in industrial zone at Dhabeji, Port Qasim, is constructed on 65 acres of land and has a nameplate capacity of 600,000 metric tons per annum .
Operations Amreli Steels produces two key products: i) steel billets, ii) rebars including a) Grade 60 Deformed Steel bars and b) Xtreme bars (G-500W). Amreli Steels has the largest billet manufacturing plant in Pakistan with a capacity of producing 600,000 tons. The Company's majority power need is being fulfilled by K-Electric.

Ownership

Ownership Structure Presently, the company is majority (75%) owned by Akberali family, followed by general public (~14.58%).
Stability Organogram of the company is such that key positions are filled by the individuals from sponsor family which bodes well for the stability in the structure. The majority stake rests with Akberali family.
Business Acumen The sponsors' _ Akberali family carries experience of more than six decades of successfully managing steel and allied business. The willingness towards the business is evident from the steadfast approach used by the management. Hence, sponsor's business acumen is considered strong.
Financial Strength The sponsors have demonstrated their commitment towards the company by injecting funds on as and when required basis. Given that Amreli is the flagship entity of sponsors, willingness to support the company in case the need arises is considered high; also supplemented by access to capital markets.

Governance

Board Structure The overall control of board vests in a seven-member board of directors, wherein four are from sponsoring family including the Chairman and CEO, while three are independent members.
Members' Profile Amreli arranges orientation courses for its directors on as and when required basis. The incoming directors are also provided with appropriate briefing and orientation material to equip them with first-hand knowledge of the company.
Board Effectiveness There are two board committees in place, these include: (i) Audit, and (ii) Human Resource & Remuneration. The audit committee comprises three independent members and one non-executive director. Attendance of board members in board meetings is considered good.
Financial Transparency M/s EY Ford Rhodes, Chartered Accountants, classified in category 'A' by SBP and having a QCR rating, are the external auditors of the company. They have expressed an unqualified opinion for the financial statements of the year ended 30th June, 2022 and 31st Dec, 2022.

Management

Organizational Structure Amreli has a multi-tier organizational structure. Including two senior positions i) COO-Strategy and ii) COO-Operations and Chief Financial Officer and six functions namely; Marketing, Govt. and Public Relations, Information Technology, Corporate Affairs & Liaison, New Businesses, and CSR and communication reports to COO-Strategy.
Management Team Mr. Shayan Akberali, the elder son of Mr. Abbas Akberali, is CEO - an engineer by profession and has been associated with the company for the last two decades. Mr. Hadi Akberali, the younger son, has been working as COO – Strategy, Mr. Fazal Ahmed, has been working as 'COO – Operations" and while Mr. Taha Umer has been appointed as CFO in the current period.
Effectiveness Amreli has five management committees in place. These committees review key performance areas of the company, inter-alia, daily production analysis, yield analysis, mechanical or production breakdown and downtime analysis.
MIS The company has implemented SAP as an ERP solution with the following operational modules, i) Production planning, ii) Material Management, iii) Sales and Distribution, iv) Finance, v) Controlling, and vi) Human Capital Management including success factor module. Reports generated on daily basis.
Control Environment Amreli has obtained ISO-9001 certification from Lloyd's Register Quality Assurance, which shows that the company's manufacturing processes and procedures are in conformity with international standards.

Business Risk

Industry Dynamics Domestic steel industry has landed into crisis in recent quarters due to steep increase in interest rates in FY 2023 by the SBP, rupee depreciation, significant increase in costs of inputs, geo-political unrest and import restrictions imposed for dollars conservation. All these unfavorable circumstances have forced the informal competitors to exit the market to the benefit of listed players as the market share has transitioned from ungraded to graded manufacturers.
Relative Position Amreli Steels is one of the leading players specifically in south region. It is the only steel company in Pakistan with sales offices in Sukkur, Hyderabad, Multan, Lahore, Islamabad and Karachi and has warehouses in Karachi, Lahore and Islamabad and plans to make a big warehouse in Northern bypass of Karachi to feed Baluchistan and bypass city traffic. It has a network of 186 retailers currently.
Revenues During 3QFY23, topline declined to stand at PKR 34.698bln (3QFY22: PKR 42.537bln; FY22: PKR 58.184bln;) mainly driven by reduced demand due to market uncertainty as significant drop in volumetric sales was observed resulting in reduced capacity utilization levels of the plant. Moreover, finance cost almost doubled and increased to PKR 2,951mln (3QFY22: PKR 1,504mln) owing to significant increase in borrowings as well as substantial increase in policy rate. Resultantly, company booked net profit of PKR 291mln only in 3QFY23, as opposed to PKR 1,834mln reported in same period last year.
Margins Amreli Steel's margins witnessed improvement (Gross: 3QFY23: ~13.1% FY22: ~11.2%, FY21: ~11.6%, Operating: 3QFY23: ~9.4% FY22: ~7.8%, FY21: ~7.8%) due to increase in Steel Rebar prices in the market starting from January 2023 and cut in operational expenses, however net margins dropped due to significant increase in financial charges owing to increase in policy rate as well as increased utilization of WC lines due to unprecedented inflation levels(Net: 3QFY23: ~0.8%, FY22: ~2.3%, FY21: ~3.5%).
Sustainability Amreli Steels is diversifying into Aluminium business i-e- recycling of Aluminium scrap into refined Aluminium ingots. Financial close for this has already been achieved however, the project has been delayed due to LC related issues . Company's strategies to sustain in the overall shrinking economy include holding any fixed assets capital expenditure, hiring freeze, maintaining optimum inventory and receivables levels and moving breakeven quantity of sales at least.

Financial Risk

Working Capital During 3QFY23, Amreli Steel's working capital requirements represented by net cash cycle increased to 121days (end- Jun22: 89days) driven by increase in receivable days (3QFY23: 41days; FY22: 38days) and inventory days (3QFY23: 83days; FY22: 53days). The company manages its working capital requirements through mix of internally generated cash and short-term borrowings. However, on account of increased WC requirements due to rising scrap prices and rupee devaluation and lesser support from FCFO's, company's reliance on short-term borrowings increased (3QFY23: PKR 16.6bln; FY22: PKR 12.573bln).
Coverages During 3QFY23, slight dip in EBITDA and FCFO's was observed as EBITDA was recorded at PKR 4,012mln (end-Jun22: PKR 4,799mln; end-Mar22: PKR 4,149mln) & FCFO were recorded at PKR 3,357mln; (end-Jun22: PKR 4,088mln; end-Mar22: PKR 3,606mln). Steep increase in finance costs & slight decrease in FCFOs resulted in lower coverages (coverage: end-Mar23: ~1.4x; end-Jun22: ~2.1x; end-Jun21: ~2.2x).
Capitalization During 3QFY23, leveraging stood at ~60% (end-Jun22: 60.6%, end-Jun21: ~57.8%). Out of total debt, ~71% pertains to short-term borrowings (end-Jun22: ~53.6%) which were recorded at PKR ~16.6 billion to finance increase in international scrap prices, and massive rupee devaluations over the period. The company's equity base has improved slightly due profits reported and was recorded at PKR ~15.546bln (FY22: PKR 15.25bln; FY21: PKR 13.9bln).

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Financial Summary
PKR mln

Amreli Steels Ltd Infrastructure | Steels	Mar-23 9M	Jun-22 12M	Jun-21 12M	Jun-20 12M
A BALANCE SHEET				
1 Non-Current Assets	22,560	21,870	20,418	17,883
2 Investments	14	14	15	15
3 Related Party Exposure	-	-	-	-
4 Current Assets	20,374	21,666	15,934	17,345
a Inventories	*9,973*	*11,018*	*5,992*	*7,814*
b Trade Receivables	*4,777*	*5,680*	*6,320*	*4,900*
5 Total Assets	42,948	43,550	36,366	35,243
6 Current Liabilities	3,222	3,684	2,614	3,373
a Trade Payables	*297*	*365*	*408*	*414*
7 Borrowings	23,034	23,105	18,781	22,049
8 Related Party Exposure	316	341	341	341
9 Non-Current Liabilities	830	1,166	689	435
10 Net Assets	15,546	15,254	13,941	9,046
11 Shareholders' Equity	15,546	15,255	13,941	10,951
B INCOME STATEMENT				
1 Sales	34,698	58,184	39,218	26,532
a Cost of Good Sold	*(30,148)*	*(51,693)*	*(34,676)*	*(24,719)*
2 Gross Profit	4,550	6,491	4,542	1,813
a Operating Expenses	(1,272)	(1,940)	(1,500)	(1,185)
3 Operating Profit	3,278	4,552	3,042	628
a Non Operating Income or (Expense)	*(198)*	*(167)*	*(8)*	*(271)*
4 Profit or (Loss) before Interest and Tax	3,080	4,385	3,033	356
a Total Finance Cost	*(2,951)*	*(2,307)*	*(1,649)*	*(2,299)*
b Taxation	*162*	*(753)*	*(16)*	*701*
6 Net Income Or (Loss)	291	1,326	1,368	(1,242)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*3,357*	*4,088*	*3,101*	*1,043*
b Net Cash from Operating Activities before Working Capital Changes	*727*	*2,045*	*1,153*	*(1,025)*
c Changes in Working Capital	*709*	*(4,244)*	*1,287*	*(2,978)*
1 Net Cash provided by Operating Activities	1,435	(2,199)	2,440	(4,003)
2 Net Cash (Used in) or Available From Investing Activities	(1,243)	(2,138)	(1,146)	(1,361)
3 Net Cash (Used in) or Available From Financing Activities	(1,836)	4,523	(1,996)	5,825
4 Net Cash generated or (Used) during the period	(1,644)	185	(701)	462
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-20.5%	48.4%	47.8%	-7.2%
b Gross Profit Margin	13.1%	11.2%	11.6%	6.8%
c Net Profit Margin	0.8%	2.3%	3.5%	-4.7%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	11.7%	-0.3%	11.2%	-7.3%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	2.5%	9.1%	11.0%	-10.7%
2 Working Capital Management				
a Gross Working Capital (Average Days)	124	91	116	156
b Net Working Capital (Average Days)	121	89	113	152
c Current Ratio (Current Assets / Current Liabilities)	6.3	5.9	6.1	5.1
3 Coverages				
a EBITDA / Finance Cost	1.6	2.5	2.6	0.7
b FCFO / Finance Cost+CMLTB+Excess STB	0.9	1.2	1.2	0.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	5.5	3.1	3.8	-8.3
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	60.0%	60.6%	57.8%	67.2%
b Interest or Markup Payable (Days)	93.0	100.0	69.6	101.4
c Entity Average Borrowing Rate	13.2%	8.6%	7.1%	14.0%

Credit Rating

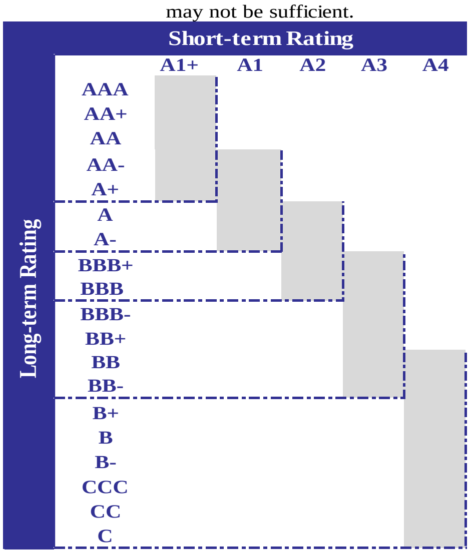
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** 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.
A+ A A-	**High credit quality.** 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.
BBB+ BBB BBB-	**Good credit quality.** 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.
BB+ BB BB-	**Moderate risk.** 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.
B+ B B-	**High credit risk.** 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.
CCC CC C	**Very high credit risk.** 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.
D	Obligations are currently in default.

Short-term Rating

Scale	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
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 surveill 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

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

Rating Team Statements
(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

Restrictions
(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(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)

Conduct of Business
(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)

Independence & Conflict of interest
(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)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst’s area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(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)
Proprietary Information