The Pakistan Credit Rating Agency Limited

Rating Report

Fatima Fertilizer Company Limited | Sukuk

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
01-Nov-2018	AA-	-	Stable	Maintain	-
08-Aug-2017	AA-	-	Stable	Maintain	-
26-Jan-2017	AA-	-	Stable	Initial	-
11-Nov-2016	AA-	-	Stable	Preliminary	-

Rating Rationale and Key Rating Drivers

The ratings reflect strong business profile of the company on the back of diversified product mix. Secure supply of gas from Mari field together with lower feed stock price (under fertilizer policy -2001 up till 2021), represents inherent strengths of the company compared to its peers. Overall capacity utilization continued to exceed 100% (previously: 90% - 98%) based on ammonia debottlenecking. In line with the industry, company revived from the supply surplus situation due to oversupply in the domestic market. Plus, the latest domestic supply/demand scenario is favourable, increased urea prices, provided additional cushion to the business in enhancing its margins. Eyeing for a prolific business model, Fatima Fertilizer has proposed merger with its wholly owned subsidiary - Fatimafert along with the acquisition of all five fertilizer plants of its associate - Pakarab Fertilizer Limited including Ammonia, Urea, Nitric Acid, NP, CAN and clean development mechanism. Regulatory approvals are being sought. Post-acquisition, Fatima Fertilizer tends to become a prominent supplier of CAN & NP with the overall nameplate capacity of 2,572,400 Metric tonnes/year. Fatima Group has also ventured an undertaking to secure gas supply to Pakarab by laying gas pipeline. The leveraging is expected to move up yet would remain aligned with the risk profile of the entity. Given strong cashflows, financial risk remain comfortable.

The ratings are dependent upon the company’s ability to absorb debt profile of the proposed acquisitions. Revival of the Pakarab's plants, acquired by Fatima Fertilizer is crucial.

Disclosure

Name of Rated Entity	Fatima Fertilizer Company Limited | Sukuk
Type of Relationship	Solicited
Purpose of the Rating	Debt Instrument Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Debt Instrument(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	
Rating Analysts	Raniya Tanawar | raniya.tanawar@pacra.com | +92-42-35869504

Profile

Legal Structure Fatima Fertilizer Company Limited (FFCL), was incorporated in Dec 2003 and is listed on Pakistan Stock Exchange since (PSX) 2010

Background FFCL was formed by way of a joint venture between two major business groups in Pakistan namely, Fatima Group and Arif Habib Group. Based in Lahore, with a fertilizer complex located at Mukhtar Garh, Sadiqabad, Rahim Yar Khan which began it commercial production in July 2011

Operations FFCL core business involves supply of fertilizers (Urea, CAN and NP) to 61 districts, 3000 dealers, spanning over 10 regions across Pakistan. FFCL , along with its associate - Pakarab Fertilizer Limited is the largest fertilizer company in Pakistan to produce CAN. It is the largest producer of Nitrogen Phosphate (NP), with an allocated 110MMCFD of gas from the dedicated Mari Gas Fields.

Ownership

Ownership Structure Fatima Group (FG), the key sponsors, holds 45%, while Arif Habib Group holds 34% and the remaining is held by Fazal Group (11%).

Stability Ownership structure is represented by strong conglomerates, having a stable in share in the company since inception.

Business Acumen Company's establishment as one of the key players in the fertilizer sector, over considerable timeline basis, is a representation of strong business acumen.

Financial Strength Fatima Fertilizer has the back of strong partnership of Fatima Group and Arif Habib Group; two renowned names of Pakistan's corporate industry. Arif Habib Group ranks amongst the prominent financial services group in Pakistan, having diversified investments.

Governance

Board Structure FFCL business control rested in the hands of eight member board of directors, including the CEO, Mr. Fawad Ahmed Mukhtar. Strong governance is the hallmark of the company.

Members' Profile The chairman of Arif Habib Group, Mr. Arif Habib, with more than four decades of experience and a well-known business professional of the country will chair the company's board in a non-executive role.

Board Effectiveness Formally, seven meetings have been convened throughout the period under review. The board has two committees namely Human Resource and Remuneration Committee and Board Audit Committee, witnessing strong participation by the board members

Financial Transparency The external auditors of the company is Deloitte Yousaf Adil, Chartered Accountants are rated 'A' on the SBP panel. they have expressed an unqualified opinion on the financial statements for the year Ended Dec, 2017.

Management

Organizational Structure The organizational structure of the company is divided into various functional departments, namely: (i) Operations, (ii) Finance, (iii) Administration, (iv) Procurement (v) Human Resource (vi) IT (vii) Marketing, and (viii) Internal Audit. The management is a balanced blend of professional people from the industry

Management Team FFCL has filled its management palette with experienced professionals with strong leadership reign. Mr. Fawad, CEO of Fatima Fertilizer is also on the board of group companies while Mr. Asad Murad, a finance professional, has been aptly deploying his services as Chief Finance Officer (CFO) and Director Finance, with more than two decades of experience in the relevant industry.

Effectiveness FFCL doesn't have formal management committees as the directors themselves are involved in the day to day operations of the business.

MIS Company's operating system is an upgraded Oracle based ERP system, marking in timely MIS reporting framework. Business maintains a regimen of updated IT systems from time to time.

Control Environment Company has smooth trail of integrated business processes from initiation to customers' feedback and disaster management.

Business Risk

Industry Dynamics The fertilizer industry is prevalent for Agriculture & allied sector of the country. The industry revived from the supply surplus situation but came down to supply shortage of Urea, as some of the major urea plants remained closed. Removal of subsidy by the GoP resulted in increased Urea prices which provided additional cushion to industry players to enhance their margins.

Relative Position Sustainable growth despite gas curtailment and water shortage issues, FFCL is relatively placed prominent in the industry. After the closure of some major fertilizer plants currently, FFCL holds highest share in CAN market. As part of strategic expansion plan, sponsors of the company have decided to amalgamate Fatimafert (its wholly owned subsidiary) with Fatima fertilizer and acquire major plants of its associated company Pakarab Fertilizer Limited.

Revenues Continued growth in Fatima's topline, which stood at PKR ~23bln in 1HCY18, 31% higher than the corresponding period (PKR ~17.6bln). Company's market share recorded at 85% for CAN and 9% for Urea. Exports surged to PKR ~1.5bln as compared to merely 0.3bln in the same period last year

Margins Effective resource utilization and operational efficacy resulted in persistent gross and operating margins for the period 1HCY18; 60%:41% respectively, almost stable from the previous years. Net profit clocked in at PKR ~6bln for the period 1HCY18 (CY17: PKR ~11bln)

Sustainability With an aim to form a prolific business model, Fatima Fertilizer has proposed merger with its wholly owned subsidiary - Fatimafert along with the acquisition of major fertilizer plants of its associate - Pakarab Fertilizer Limited including Ammonia (316,800 MTPA), Urea(100,000 MTPA), Nitric Acid(455,400 MTPA), NP(304,500 MTPA), CAN(450,000 MTPA) and clean development mechanism. Resultantly, FFCL will become the sole supplier of CAN & NP with an overall nameplate capacity of 2,572,400 Metric tonnes/year. Fatima Group has ventured an undertaking to secure gas supply to Pakarab by laying gas pipeline. However, realization of the planned group level acquisitions is critical for the Company.

Financial Risk

Working Capital In line with the industry dynamics, working capital cycle remained in comfortable zone during 1HCY18. Receivable days continue to be on a lower side since past two years (CY17: 17days, CY16: 23days). Net cash cycle was recorded at 61 days for 1HCY18 (CY17: 120 days). A downward trend witnessed in company's short term borrowings from CY15 onwards (CY17: PKR ~1bln, CY16: PKR ~8bln, CY15: PKR ~10bln) due to strong internal cash generation. The figure slightly rose in 1HCY18 standing at PKR 2.9bln to finance its working capital needs.

Coverages FCFO of Fatima amounted to PKR 9.6bln, which is sufficient to fulfill its debt financing appetite for 1HCY18 (CMLTD: 5.6bln and interest: 0.6bln). Debt coverage resorts in better position largely due to reduced S.T borrowings 2.8x in 1HCY18 (CY17: 1.9x). Proposed strategic alliance will result in reasonable outflows a) gas pipeline cost b) consideration price of Pakarab's plants; PKR~9bln, consequently placing a pressure on company's cashflows. Although, mode of consideration payment to Pakarab has to be unfold. Present company's overall coverages stands adequately however, post-acquisition, leveraging is expected to rise, yet would remain aligned with the risk profile of company. Given steady cashflows of the company, financial risk remain comfortable.

Capitalization FFCL, currently has low leverage capital structure. Long term borrowing (LT), amounting PKR~8bln and short term borrowings PKR ~2.9bln, represented 47%; 17% of the total debt (1HCY18: PKR ~17bln) respectively. Debt to Equity was locked 23% in 1HCY18. Company financial position is adequate enough to absorb the accompanied debt with Fatimafert merger; PKR ~8bln, out of which PKR~4bln already belongs to FFCL. Company has a listed, rated and secured Sukuk of PKR 10.5bln, which has a tenor of 5 years, ending by Nov '21. Redemption of the Sukuk is left with 7 semi-annual installments with a coupon payments @6MK+1.10%.

Fatima Fertilizer Limited

BALANCE SHEET	30-Jun-18	31-Dec-17	31-Dec-16
	1HCY18	CY17	CY16
Non-Current Assets	**74,435**	**73,142**	**73,089**
Investments (Incl. associates)	**11,651**	**9,204**	**7,686**
Equity	2,240	2,238	2,238
Debt	9,411	6,966	5,448
Current Assets	**18,180**	**16,990**	**29,822**
Inventory	3,719	3,814	6,243
Trade Receivables	2,243	1,796	2,116
Others	12,218	11,380	21,463
Total Assets	**104,267**	**99,336**	**110,597**
Debt	**8,522**	**7,378**	**13,529**
Short-term	2,935	1,726	8,011
Long-term (Inlc. Current Maturity of long-term debt)	5,587	5,652	5,518
Other shortterm liabilities	16,117	11,627	17,658
Other Longterm Liabilities	24,275	26,589	32,035
Shareholder's Equity	**55,353**	**53,742**	**47,374**
Total Liabilities & Equity	**104,268**	**99,336**	**110,597**
INCOME STATEMENT			
Turnover	**23,101**	**37,612**	**33,765**
Gross Profit	13,759	20,337	17,985
Other Income	354	517	420
Financial Charges	(640)	(2,198)	(2,739)
Net Income	**6,337**	**10,576**	**9,782**
Cashflow Statement			
Free Cashflow from Operations (FCFO)	9,649	15,152	15,976
Net Cash changes in Working Capital	9,216	12,346	12,801
Net Cash from Operating Activities	11,308	16,754	18,775
Net Cash from InvestingActivities	(5,199)	(2,948)	(5,012)
Net Cash from Financing Activities	(6,271)	(24,096)	(2,958)
Net Cash generated during the period	(163)	(10,290)	10,805
Ratio Analysis			
Performance			
Turnover Growth	31%	11%	12%
Gross Margin	60%	54%	53%
Net Margin	27%	28%	29%
ROE	23%	19%	22%
Coverages			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	2.8	1.9	1.9
Interest Coverage (x) (FCFO/Gross Interest)	15.1	6.9	5.8
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCF(	0.8	1.3	1.7
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	61	120	124
Capital Structure (Total Debt/Total Debt+Equity)	23%	25%	39%

DEBT INSTRUMENT RATING SCALE & DEFINITIONS

The instrument rating reflects forward-looking opinion on credit worthiness of underlying debt 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 RATINGS	
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 RATINGS
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.
B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C: An inadequate capacity to ensure timely repayment.

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, a) some material identifiable event and/or b) deviation from expected trend. 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 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

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.
(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

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs)	Security	Quantum Of Security	Nature of Assets	Trustee
Sukuk	PKR 10,500mln	5	First pari-passu charge with 25% margin on all present and future fixed assets of Fatima	PKR 10,500* 125% = PKR ~13,125mln	All present and future fixed assets including land and building	National Bank of Pakistan (NBP)

SUKUK – LISTED, RATED & SECURED	
ISSUE SIZE	PKR 10,500 mln
TENOR	5 Years
PROFIT RATE	Floating rate of 6M KIBOR + 1.10% payable semi- annually.
PRINCIPAL REPAYMENT	To be redeemed in 10 equal semi-annual installments from the date of first disbursement
SECURITY	Secured by: - First pari-passu hypothecation charge over all present and future fixed assets with a minimum 25% margin; - First pari-passu mortgage over land and building with a minimum 25% margin; - Establishment of a Debt Payment Account (DPA) - Assignment over all rights and benefits of Fatima under any and all project insurance and cut-through agreements for reinsurance The Sukuk would be initially secured by ranking charge and it would be upgraded into first pari-passu within 90 days of first disbursement.

Fatima Fertilizer Compaany Limited
Facility Upto PKR 10,500,000,000

Sukuk Amount	10,500,000,000
Disbursement	10,500,000,000
Tenor	5
Grace Period	Nil
Installment Payment Frequency	Half yearly
Notional Cap Rate	25.00%

I	II	III	IV	V	VI	VII	VIII
Period	Date	Total Rental	Variable Rental	No of Days	Amount of Fixed Rental	Investment Agent's Musharaka Share	Amount of Purchase Price Outstanding
0	29-Dec-16					10,500,000,000	17,493,287,671
1	28-May-17	2,128,767,123	1,078,767,123.29	150	1,050,000,000	9,450,000,000	15,364,520,548
2	28-Nov-17	2,240,958,904	1,190,958,904.11	184	1,050,000,000	8,400,000,000	13,123,561,644
3	28-May-18	2,091,369,863	1,041,369,863.01	181	1,050,000,000	7,350,000,000	11,032,191,781
4	28-Nov-18	1,976,301,370	926,301,370	184	1,050,000,000	6,300,000,000	9,055,890,411
5	28-May-19	1,831,027,397	781,027,397	181	1,050,000,000	5,250,000,000	7,224,863,014
6	28-Nov-19	1,711,643,836	661,643,836	184	1,050,000,000	4,200,000,000	5,513,219,178
7	28-May-20	1,573,561,644	523,561,644	182	1,050,000,000	3,150,000,000	3,939,657,534
8	28-Nov-20	1,446,986,301	396,986,301	184	1,050,000,000	2,100,000,000	2,492,671,233
9	28-May-21	1,310,342,466	260,342,466	181	1,050,000,000	1,050,000,000	1,182,328,767
10	28-Nov-21	1,182,328,767	132,328,767	184	1,050,000,000	-	0
Total		17,493,287,671	6,993,287,671		10,500,000,000		