The Pakistan Credit Rating Agency Limited

Rating Report

Cherat Cement Company Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2023	A+	A1	Stable	Maintain	-
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	-

Rating Rationale and Key Rating Drivers

Cherat Cement's Ratings reflect its presence in the cement sector emanating from its decent market share (~7%) predominately in the north region. Overall, the Cement sector witnessed a negative growth of ~16% in total dispatches whereas export cement declined by ~13% during FY23. However, contrary trend was witnessed in 1QFY24, with local cement dispatches increased by ~18% and export dispatches by ~72% compared to same period previous year. The inflationary pressure during FY23 contributed towards driving the demand for Cement downwards. Going forward, the trend of sale volumes is expected to recover in FY24 owing to improvement in economic conditions. During FY23, the Company's local cement dispatches were recorded at 2.871mln tons (FY22: 3.552mln tons) registering a decline of 19%. However, during 1QFY24, the Company's local cement dispatches were recorded at 0.699mln tons (1QFY23: 0.706mln tons) registering a minor decline of ~1% despite the improvement in industry volumes. Consequently, the Company's revenues soared to PKR 10,071mln & PKR 37,386mln at the end of 1QFY24 & FY23, respectively on account of upward adjustment in cement prices (1QFY23: PKR 9,050mln, FY22: PKR 32,085mln). Company managed to improve margins in the said period on back of efficient cost management through the installed solar power plant of 13.05MW. Moreover, the BoD have approved to enhance the capacity of the solar power plant by 10.5MW leading to total installed capacity to reach 23.55MW. 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

Name of Rated Entity	Cherat Cement Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jul-23),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology | Rating Modifiers(Apr-23)
Related Research	Sector Study | Cement(Mar-23)
Rating Analysts	Ali Arslan Malik | Ali.Arslan@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 exceeding 4.5mln tons per annum, the company currently holds ~7% share in country's operational cement capacity. The company's home markets include Nowshera, Peshawar and Charsada.

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 of 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 associated with the Ghulam Faruque Group. During FY23, group revenue and total assets stood at PKR ~89.2bln and PKR ~76.5bln, respectively.

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 directors 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, nine board meetings were held. Directors' attendance in the board meetings remained strong; meeting minutes are formally maintained. Two board committees, Audit and Human Resource and Remuneration, are in place to assist the board on relevant matters.

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 FY23.

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 Mangers (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 alternate sources including 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 Pakistan has achieved GDP growth at 0.29 % in the fiscal year 2022-2023. However, this growth in the economy is not translated into cement demand and the cement industry witnessed a negative growth of 16% during the year. While, the local cement industry declined by 16%, whereas export cement declined by 13% during the financial year 2022-2023. In volume terms, total sales quantity of industry witnessed decline of 8.3 million tons (15.7%) year on year basis to 44.5 million tons. North zone registered negative growth of 6.5 million tons (16.1%) while South Zone of 1.8 million tons (14.4%). Further analysis shows that negative growth was driven by local dispatches that declined by 7.6 million tons (16.0%) while exports showed contraction by 0.7 million tons. Sales utilization of industry declined to 60% against 76% for the corresponding period last year. It was largely contributed by local sales of 54% and exports sales utilization of 6%. Quarter on Quarter total sales quantity of industry witnessed increase to 11.8 million tons (30%). North zone registered growth of 1.2 million tons (16.1%) while South Zone of 1.0 million tons (50.4%). Further analysis shows that growth was driven by exports that grew by 0.7 million ton (72%) while local dispatches showed growth of 1.5 million tons. Sales utilization of industry declined to 60% against 74% for the corresponding period last year. It was largely contributed by local sales of 51% and exports sales utilization of 9%.

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

Revenues Sales volume analysis revealed that total dispatches of the company minorly decreased by 1% in 1QFY24 as compared to the corresponding period and 19% decrease on YOY basis due to the slowdown in economic activities in the country. But considerable increase of 13% in exports on YOY basis. The sales mix remained tilted towards local sales (1QFY24: 82%, FY23: 85%, FY22: 88.5%). During 1QFY24 and FY23, the company's topline stood at PKR 10,071mln & 37,386mln respectively (FY22: PKR 32,085mln), up 17% YoY. This growth is attributed to upward adjustment in cement prices on account of higher input costs. The significant increase of ~35% in fuel and power cost caused the upward movement in sale prices.

Margins During 1QFY24, the company's margins showed upward movement on back of sale prices (GP; 1QFY24: 30.5%, FY23: 27.1%, FY22: 27.9%). Similarly, operating margins and net margins also remained intact and stands at (OM; 1QFY24: 27.6%, FY23: 24.3%, FY22: 25.2%. Net; 1QFY24: 15.2%, FY23: 11.8%, FY22: 13.9%.

Sustainability Although there has been a current slowdown in the economy and the cement sector leading to reduced sold volumes. As the economy picks up pace with government spending in PSDP, the cement sector will revive. The Company has also announced Greenfield expansion of 7,800 TPD in D.I. Khan, Punjab. The work on the expansion is yet to begin but once completed will give further opportunity to capture the market share in south region.

Financial Risk

Working Capital During 1QFY24, Cherat Cement's working capital requirements, represented by net cash cycle (net working capital days) – a function of inventory, receivables and payables – Increased to 23 days (FY23: 17 days) on basis of increase in receivables. The receivables increased to PKR 1090mln in 1QFY24 as compared to PKR 903mln in FY23 and PKR 543mln in FY22. The quantum of STBs stood at PKR 1,033mln (FY23: PKR 1,573mln) on account of enhanced working capital needs.

Coverages During FY23, Cherat Cement's EBITDA improved to PKR 10,843mln as compared to PKR 9,744mln in FY22 (1QFY24: PKR 3,097mln) while finance costs also witnessed significant uptick of 41% 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 7.4x at the end of 1QFY24 (FY23: 5.4x, FY22: 6.9x). Going forward, vigilant management of cashflows remains vital.

Capitalization During 1QFY24, the company's total debt stands at PKR 10,924mln (FY23: PKR 11,891mln, FY22: PKR 10,878mln). CMLTD marginally decreased to PKR 2,881mln (FY23: PKR 2,968mln). Company is regularly paying the installments. Thus, leveraging is continuously declining and stands at 32.8% at end Sep-23 (FY23: 36.3%, FY22: 49.7%) Going forward, the debt levels are not expected to rise as scheduled repayments are underway and no debt driven project is planned.

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Financial Summary
PKR mln

Cherat Cement Company Limited	Sep-23	Jun-23	Jun-22	Jun-21
Cement	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	28,857	29,029	27,658	25,687
2 Investments	2,730	-	-	-
3 Related Party Exposure	367	408	482	661
4 Current Assets	9,184	9,865	10,465	7,846
a Inventories	*2,110*	*2,280*	*926*	*1,006*
b Trade Receivables	*1,090*	*903*	*534*	*408*
5 Total Assets	41,138	39,302	38,605	34,194
6 Current Liabilities	4,473	3,628	3,643	2,850
a Trade Payables	*766*	*614*	*119*	*149*
7 Borrowings	10,924	11,891	17,082	17,153
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	3,370	2,904	563	602
10 Net Assets	22,371	20,879	17,316	13,590
11 Shareholders' Equity	22,371	20,879	17,316	13,590
B INCOME STATEMENT				
1 Sales	10,071	37,386	32,085	25,207
a Cost of Good Sold	*(7,000)*	*(27,249)*	*(23,135)*	*(18,479)*
2 Gross Profit	3,072	10,137	8,951	6,728
a Operating Expenses	(292)	(1,043)	(878)	(972)
3 Operating Profit	2,780	9,094	8,072	5,757
a Non Operating Income or (Expense)	*(75)*	*92*	*115*	*105*
4 Profit or (Loss) before Interest and Tax	2,705	9,186	8,188	5,861
a Total Finance Cost	*(425)*	*(1,914)*	*(1,359)*	*(1,524)*
b Taxation	*(748)*	*(2,868)*	*(2,373)*	*(1,132)*
6 Net Income Or (Loss)	1,533	4,404	4,456	3,205
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,980*	*10,123*	*9,022*	*7,178*
b Net Cash from Operating Activities before Working Capital Changes	*2,768*	*8,063*	*7,727*	*5,406*
c Changes in Working Capital	*1,364*	*(244)*	*(2,916)*	*(287)*
1 Net Cash provided by Operating Activities	4,132	7,819	4,811	5,120
2 Net Cash (Used in) or Available From Investing Activities	(2,934)	(2,684)	(3,506)	(1,877)
3 Net Cash (Used in) or Available From Financing Activities	(431)	(4,538)	(1,713)	(2,218)
4 Net Cash generated or (Used) during the period	766	596	(408)	1,024
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	7.8%	16.5%	27.3%	47.5%
b Gross Profit Margin	30.5%	27.1%	27.9%	26.7%
c Net Profit Margin	15.2%	11.8%	13.9%	12.7%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	43.1%	26.4%	19.0%	27.3%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	28.0%	21.3%	27.3%	24.0%
2 Working Capital Management				
a Gross Working Capital (Average Days)	29	23	16	19
b Net Working Capital (Average Days)	23	19	15	17
c Current Ratio (Current Assets / Current Liabilities)	2.1	2.7	2.9	2.8
3 Coverages				
a EBITDA / Finance Cost	7.4	5.8	7.4	5.0
b FCFO / Finance Cost+CMLTB+Excess STB	2.6	2.1	2.1	1.7
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.0	1.3	1.8	2.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	32.8%	36.3%	49.7%	55.8%
b Interest or Markup Payable (Days)	145.3	85.0	120.9	74.6
c Entity Average Borrowing Rate	12.4%	12.8%	7.9%	8.1%

Credit Rating

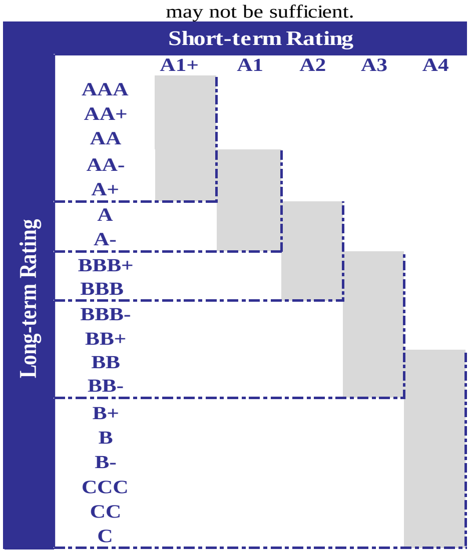
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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 | 17-(a)
(19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)
Proprietary Information