



The Pakistan Credit Rating Agency Limited

Rating Report

Pioneer Cement Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Dec-2018	A	A1	Stable	Maintain	-
07-May-2018	A	A1	Stable	Maintain	-
28-Dec-2017	A	A1	Stable	Maintain	-
21-Jun-2017	A	A1	Stable	Maintain	-
02-Nov-2016	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Pioneer Cement's healthy business profile. The company has been operating a single manufacturing facility. The Company's sales are majorly driven by local market fundamental – an industry wide phenomenon. During FY18, industry dynamics have shifted significantly on account of lower retention prices, surged international coal prices, increase in FED on coal import. The aforementioned factors have affected the company's sales. The upcoming energy projects (12MW WHRPP and 24MW coal power plant) are likely to assist bottom-line in future through power cost savings. The company's brown-field expansion – 2.2mln tpa – is expected to commission in 4QFY19. This will supplement company's business profile given higher capacity utilization and adequate channeling of production. The leveraging is expected to surge in medium term on account of debt-driven expansion. Timely commissioning of new line is considered vital for the ratings. The ratings also draw comfort from sponsor's financial strength.

The ratings are dependent on the management's ability to (i) uphold margins, and (ii) optimal utilization of existing lines. Timely repayment of long term financing is essential. The company's improved business performance in current stretched economic scenario - challenges on demand front - remains vital for ratings.

Disclosure

Name of Rated Entity	Pioneer Cement Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Cement(Nov-18)
Rating Analysts	Sehar Fatima sehar.fatima@pacra.com +92-42-35869504

Profile

Legal Structure Pioneer Cement is a listed Company. Its shares are traded on Pakistan Stock Exchange Limited (PSX). The Company's shares are quoted under the Cement Sector.

Background Pioneer Cement was incorporated in 1986. It is headquartered in Lahore, Pakistan and the manufacturing facility is located at Chenki-District Khushab. Its location in central Punjab allows easy and fast approach to market. The main markets of the company are Punjab and Khyber-Pakhtunkhwa. Pioneer operates with two production lines having a combined annual cement capacity of 2.09mln tons (CoD: Line I - 1994, Line II - 2006).

Operations Pioneer Cement is engaged in the manufacturing and sale of Ordinary Portland Cement. The company has a limited product slate and currently it is selling Ordinary Portland Cement (OPC).

Ownership

Ownership Structure Vision Holding Middle East Limited (VHME) is an offshore SPV of Vision Holding Trust (VHT). VHME holds majority stake (47%) in Pioneer Cement and remaining shares of the company are held by various financial institutions and general public.

Stability Ownership structure of the Company is seen as stable as no ownership changes are expected in near future. Majority stake will rest with the Vision Holding Middle East Limited (VHME).

Business Acumen Vision holding trust is 100% owned by Mr. Habibullah Khan – a renowned foreign entrepreneur. Apart from Cement, trust maintains interest in several sectors. The sponsors having a diversifiable universe of investments is considered to be a positive sign.

Financial Strength Given that Pioneer is a flagship entity of the sponsor, willingness to support the company in case the needs arises is considered high; also supplemented by access to capital markets.

Governance

Board Structure The overall control of the company vests in ten member board of directors (BoD), including the CEO and three independent directors. Mr. Arif Hamid Dar has been appointed Chief Executive Officer with effect from July 01, 2018.

Members' Profile Board members carry requisite technical skills which is abetted by diversified professional background of board members. In FY18, four board meetings were held. The meeting minutes are formally maintained and the attendance is considered good which bodes well for overall governance framework of the company.

Board Effectiveness The board has two committees to oversee the company's financial matters. These committees include: 1) Audit, and 2) Human Resource & Remuneration (HR&R). This is in compliance with the Code of Corporate Governance.

Financial Transparency M/s EY Ford Rhodes Chartered Accountants conducted the external audit services for Pioneer. They're in a 'A' category of SBP list of external auditors and has a QCR rating. They have expressed unqualified opinion on the financial statements for the year ended 30th June, 2018.

Management

Organizational Structure Pioneer Cement has a lean organization structure with the company's operations grouped under nine key functions. These include i) Administration, ii) Corporate Affairs, iii) Finance, iv) Human Resource, v) Information Technology, vi) Marketing, vii) Operations, viii) Supply Chain and ix) Internal Audit. All functional heads report to the CEO except for internal audit, which reports directly to the Audit committee of the board (in compliance with the requirement of law for listed companies).

Management Team During FY18, Mr. Syed Mazhar Iqbal retired from the position of MD/CEO resulting in appointment of Mr. Arif Hamid Dar as the new CEO. He is an experienced individual with professional experience of several sectors of Auto, Fertilizer and Cement.

Effectiveness The CEO is supported by an experienced professionals at key management positions having a long-term association with the company.

MIS Pioneer has deployed an oracle based ERP solution. The company's current operational modules include i) Inventory, ii) Purchasing, iii) Payables, iv) Receivables, v) Cash Management, vi) Fixed Assets, vii) General Ledger, and viii) Order Management.

Control Environment Pioneer's plant comprises of two lines wherein, Line I is a European technology (FLSmidth), and Line II is a mix of European and Chinese technology. Accredited with ISO 9001: 2008 and ISO 14001:2004 certification, Pioneer deploys advance technology to ensure production of quality cement.

Business Risk

Industry Dynamics Cement industry is divided into North and South region – majority players operating in North region. Currently, cement industry is going through a phase of capacity expansion, majority of which were announced in FY16 due to surged cement demand especially driven by government announced Infrastructure projects and CPEC. Cement industry dispatches remained tilted towards locals sales, exports are minuscule part which are mainly to Afghanistan, India and through sea to some countries. Market dynamics has changed significantly in last year driven by escalation of international coal prices, rupee depreciation and unsustainable cement prices (especially in north region) on account of supply glut recently created. Cement players witnessed significant dip in margins on account of aforementioned factors. Currently, leveraging of industry is moderate but in increasing interest rates environment it is critical for cement players to vigilantly manage cost structure. Going forward – with full utilization of lately commenced plants – industry is expected to face expanded capacity challenge. Cement prices and margins are expected to stay under stress. Cement demand is expected to stay nominal (at least for upcoming two years) as new government's prerogative for infrastructure will take some time to materialize. Therefore, upcoming capacity expansion utilization will be challenging factor.

Relative Position Pioneer Cement is a mid-tier cement player, operating in north region. The company has operational clinker capacity of 1.9mln tons per annum. Furthermore, the company has announced capacity expansion of 2.4mln tpa. Consequently, company's current market share of ~3% will become 6%.

Revenues In FY18, Revenue of PKR 10.1bln was recorded (FY17: PKR 10.6bln), down by 5% YoY. Sales mix remained tilted towards local market - In line with the industry trend. The company's capacity utilization level has remained the same to 78% (FY17: 78%) – below the average capacity utilization level of the industry. However, Other income dropped to PKR 2mln (FY17: PKR 233mln) mainly due to decline in dividend income. Finance costs increased to PKR 95mln (FY17: PKR 35mln) on account of increase in debt levels. Consequently PAT stood at PKR 1.6bln (FY17: PKR 2.9bln), down by 44% YoY. During 1QFY19, the company secured topline of PKR 2.2bln.

Margins Pioneer's margins have declined over the past year but still remained inbound (gross: 1QFY19: 24%, FY18: 28%, FY17: 42%, operating: 1QFY19: 20%, FY18: 25%, FY17: 40%, EBITDA: 1QFY19: 27%, FY18: 31%, FY17: 45%). Margins deterioration is a trend witnessed throughout the cement industry for FY18 primarily on account of escalation in international coal prices and instability in cement prices.

Sustainability Going forward, the management is planning to install another production line through brownfield expansion with an annual capacity of 2.4mln tons. In addition to this, the company will acquire coal based power plant (24MW) and WHRP. The estimated cost of these projects is PKR 25bln. The debt equity proportion will be 72:28 and the projects are expected to be operational by Jun-19.

Financial Risk

Working Capital Pioneer's working capital requirements represented by net cash cycle (net working capital days) – a function of inventory, receivables and payables - decreased to 6days (end-Jun17: 12days) on account of longer creditor days (FY18: 17days; FY17: 5days). The STBs stood at PKR 2.4bln (FY17: PKR 807mln). Subsequently, Current ratio dropped to 1.2x (FY17: 1.7x).

Coverages During FY18, FCFO declined to PKR 1.5bln (FY17: PKR 2.9bln) mainly due to reduced profitability. Coverages declined (Interest: FY18: 16x, FY17: 84x). Going forward, total debt will amount up to PKR 20bln, which will majorly impact the coverages of Pioneer.

Capitalization In pursuit of expansion, the leveraging (end-Jun18: 44%, end-Jun17: 16%, end-Jun16: 6%) increased tremendously YoY. Going forward, debt levels are expected to increase due to the further availing of proposed credit (PKR 10bln) by FY19. Hence, timely commencement of new line remains vital for timely repayment of debt.



Pioneer Cement Limited

BALANCE SHEET	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	3M	Annual	Annual	Annual
Non-Current Assets	26,437	22,962	12,281	10,431
Investments (Incl. associates)	1,016	1,086	2,694	2,425
Equity	-	-	-	-
Debt	937	1,007	2,623	2,356
Investment Property	79	79	71	69
Current Assets	5,774	5,064	2,785	1,911
Inventory	538	470	236	181
Trade Receivables	423	434	225	108
Others	4,814	4,160	2,324	1,621
Total Assets	33,227	29,111	17,760	14,768
Debt	14,110	10,705	2,307	645
Short-term	3,621	2,440	807	645
Long-term (Incl. Current Maturity of long-term debt)	10,489	8,266	1,500	-
Other shortterm liabilities	2,684	1,636	802	1,108
Other Longterm Liabilities	3,471	3,141	2,404	2,345
Shareholder's Equity	12,962	13,629	12,248	10,670
Total Liabilities & Equity	33,227	29,111	17,760	14,768

INCOME STATEMENT

Turnover	2,232	10,121	10,631	9,367
Gross Profit	524	2,811	4,428	4,005
Other Income	3	21	254	118
Financial Charges	(61)	(95)	(35)	(17)
Net Income	258	1,644	2,918	2,519

Cashflow Statement

EBITDA	595	3,131	4,769	4,314
Free Cashflow from Operations (FCFO)	498	1,521	2,915	2,667
Net Cash changes in Working Capital	(381)	254	(1,164)	483
Net Cash from Operating Activities	(83)	1,579	1,743	3,124
Net Cash from Investing Activities	(3,351)	(9,051)	(2,429)	(2,729)
Net Cash from Financing Activities	3,405	7,656	335	(1,826)
Net Cash generated during the period	(29)	184	(351)	(1,431)

Ratio Analysis

Performance				
Gross Margin	23.5%	27.8%	41.7%	42.8%
Net Margin	11.6%	16.2%	27.4%	26.9%
ROE	2.1%	15.0%	26.0%	25.9%
Coverages				
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.7	3.2	19.8	152.6
Interest Coverage (x) (FCFO/Gross Interest)	8.2	16.0	84.0	152.6
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCFO)	6.3	5.8	0.5	0.0
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	1	6	12	16
Capital Structure (Total Debt/Total Debt+Equity)	52.1%	44.0%	15.8%	5.7%

Credit Rating Scale & Definitions

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 Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) 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.

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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

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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)

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.
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- (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)
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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)
- (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)

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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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