



The Pakistan Credit Rating Agency Limited

Rating Report

Amreli Steels Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
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	-
27-Mar-2017	A	A1	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect Amreli Steels' 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). The Company has achieved capacity expansion of melting and rebar manufacturing capacity to 400,000 tpa and 605,000 tpa respectively. This will be enhanced to 600,000 and 1,105,000 for melting and rebar respectively. However, focused efforts to vigilantly channel volumes from enhanced capacity amid slow infrastructural activity remains essential for the Company. The general industry dynamics reflect weakening. Meanwhile, regulatory protection to the finished product (rebar) is an advantage for the sector. The volumetric increase (from recently added capacity) improved topline but margins declined - an industry wide phenomenon - attributable to increased raw material prices, depreciating Pak rupee and significant rise in distribution costs incurred by the company. The financial risk profile deteriorated owing to decline in coverages attributable to sizable increase in finance costs. Going forward, upholding business profile remain vital for the ratings. The ratings draw comfort from strong business acumen of Amreli Steels' sponsors - Akberali Family.

The ratings are dependent on the management's ability to uphold its business vis-à-vis financial risk profile. Utilization of enhanced capacity and improved margins are vital. Moreover, prudent management of financial affairs remains important.

Disclosure

Name of Rated Entity	Amreli Steels 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 Steel(Mar-19)
Rating Analysts	Sehar Fatima sehar.fatima@pacra.com +92-42-35869504

Profile

Legal Structure Amreli Steels Limited is a public limited company listed on Pakistan Stock Exchange since December 2015 and is traded under the section of Engineering.

Background Amreli Steels' rebar production facility is situated at S.I.T.E Karachi and the melt shop is situated in industrial zone at Dhabaji, Port Qasim. Expansion equating to a total of PKR 1bln is ongoing on steel melt shop at dhabaji to increase capacity from 400,000tpa to 600,000tpa. During FY18, commencement of commercial operations of the new rolling mill at Dhabaji increased the rebar production capacity of Amreli to 605,000 tons p.a (FY17:180,000 tons p.a).

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). All Xtreme bars are cut in standard sizes of 12-16 meters. Amreli Steels has the largest billet manufacturing plant in Pakistan with a capacity of producing 400,000 tons of billets. The SMS Plant produces billets in sizes ranging from 100x100mmsq to 200x200mmsq. The Company's entire power need is being fulfilled by K-Electric.

Ownership

Ownership Structure The company is majority (75%) owned by Akberali family, followed by Financial Institutions (18%), and general public (~7%).

Stability The Company's ownership structure witnessed minor changes post IPO. However, majority stake will rest 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 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 on the company.

Board Effectiveness There are two board committees in place, these include: (i) Audit, and (ii) Human Resource & Remuneration. Audit Committee comprises two independent members and one non-executive director from sponsoring family. In FY18, four board meetings were held. Attendance of board members in these 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 year ended 30th, June 2018.

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 i) Marketing, ii) Govt. and Public Relations, iii) Information Technology, iv) Corporate Affairs & Liaison, v) New Businesses, and vi) CSR and communication reports to COO-Strategy. Other eight functions; i) Sales, ii) Finance, iii) Supply Chain, iv) Admin & IR, v) Plant Operations, vi) Human Resource, vii) Security and Vigilance, ix) Environmental Health & Safety are reporting to COO-Operations and CFO. Internal audit function reports to Audit Committee.

Management Team Mr. Shayan Akberali, the elder son of Mr. Abbas Akberali, is lately appointed CEO. He is an engineer by profession and has been associated with the company since last two decades. Mr. Hadi Akberali, the younger son, has been promoted to the position of COO – Strategy. Mr. Fazal Ahmed, the previous CFO has been promoted as 'COO – Operations and CFO'.

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 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 include sales and collection, production, major customers receivables report, and quality inspection report.

Control Environment The Company has internal control systems and procedures in place to ensure the quality of goods produced on a continuing basis.

Business Risk

Industry Dynamics Domestic steel industry is undergoing expansions announced in previous government's regime. With the commencement of capacity expansions, industry player's performance in current scenario of slowdown in infrastructure projects remains vital. Regulatory protections in form of increased anti-dumping duties is a positive. However, improved business performance and margins is essential for industry players in era of growing interest rate, exchange rate and expected inflationary environment in foreseeable future.

Relative Position Amreli is one of the larger players in domestic steel industry. The company is undergoing capacity expansion, in phases, which will enhance company's footprint and market positioning.

Revenues During 1HFY19, topline surged by 97% YoY to stand at PKR 12.3bln (1HFY18: PKR 6.2bln,) mainly because of part-materializing of capacities. The company's operating expenses (administrative and marketing expenses) rose by 29% and a massive 110% respectively. Consequently, the company posted operating profit of PKR 1.0bln (FY18: PKR 1.9bln; FY17: PKR 1.8bln). Furthermore, finance cost witnessed sizable increase to PKR 490mln (FY18: PKR 476mln; 1HFY18: PKR 207mln) driven by increase in long-term and short-term finance coupled with hike in key policy rate. Hence despite volumetric growth in topline, PAT stood at PKR 516mln (1HFY18: 524mln).

Margins Amreli's margins witnessed decline (Gross: 1HFY19: ~12%, FY18: ~18%, FY17: ~19%, Operating: 1HFY19: ~8%, FY18: 13%, FY17: 14%). In addition to company's higher operating costs, upward trend in international scrap prices (~30%) during FY18 contributed towards slimming business margins.

Sustainability Going forward, as of Nov'18 the board has also approved the third phase of expansion plan for setting up an additional rolling mill at Dhabaji to further expand its rebar manufacturing facility from 605,000mt/p.a (FY17: 180,000mt/p.a) to 1,105,000mt/p.a. Meanwhile, the management is continuing its marketing efforts to expand its geographical footprint.

Financial Risk

Working Capital During 1HFY19, Amreli's working capital requirements represented by net cash cycle (function of inventory, receivables and payables) decreased to 149days (end- Jun18: 164days) driven by decrease in inventory days (1HFY19: 119days; FY18: 128days). The company manages its working capital requirements through mix of internally generated cash and short term borrowings. On account of stretched working capital cycle, the company's short term borrowings increased significantly by 38% (1HFY19: PKR 9,271mln; FY18: PKR 8,399mln).

Coverages During 1HFY19, EBITDA increased by 31% YOY, standing at PKR 1.3bln (end-Dec17: PKR ~1bln). FCFO increased by 34% YOY to PKR 1,120; (1HFY18: PKR 835mln). However, surge in finance cost(~137% YOY) weakened coverage (interest: end-Dec18: ~2.3x; end-Jun18: ~4.3x ; debt service: end-Dec18: ~1.0x; end-Jun18: ~1.6x). Going forward, vigilant utilization of enhanced capacity is vital for comfortable repayment of long term debt.

Capitalization Over the last few years, the company has been operating at a low leveraged capital structure. During 1HFY19, leveraging stood at ~50% (end Jun18 ~47%). Out of total debt, ~74% pertains to short-term (end-Jun18: ~74%; end-Jun17: ~80%). The company's equity base improved over the last few years to PKR ~13bln.



Amreli Steels

Listed Public Limited

BALANCE SHEET

	Dec'18	Jun'18	Jun'17	Jun'16
	6M	12M	12M	12M
a Non-Current Assets	16,217	15,692	12,403	8,600
b Investments (Incl. Associates)	15	15	15	315
Equity Instruments	-	-	-	-
Debt Instruments	15	15	15	315
c Current Assets	12,909	10,935	5,791	7,850
Inventory	8,547	7,459	3,404	4,410
Trade Receivables	2,650	1,788	1,455	2,071
Others	1,713	1,689	931	1,370
d Total Assets	29,141	26,643	18,209	16,765
e Debt/Borrowings	12,571	11,380	5,189	4,181
Short-Term	9,271	8,399	4,165	3,171
Long-Term (Incl. Current Maturity of Long-Term Debt)	3,300	2,981	1,024	1,009
Other Short-Term Liabilities	2,672	1,221	652	683
Other Long-Term Liabilities	1,155	1,162	1,222	1,212
f Shareholder's Equity	12,743	12,880	11,146	10,690
g Total Liabilities & Equity	29,141	26,643	18,209	16,765

INCOME STATEMENT

a Turnover	12,317	15,501	13,284	12,400
b Gross Profit	1,525	2,758	2,468	2,792
c Net Other Income	(18)	(102)	(115)	(169)
d Financial Charges	(490)	(476)	(252)	(330)
e Net Income	516	1,585	1,074	1,279

CASH FLOW STATEMENT

a Free Cash Flow from Operations (FCFO)	1,120	2,004	1,796	2,193
b Total Cashflows (TCF)	1,120	2,004	1,796	2,193
c Net Cash changes in Working Capital	(1,602)	(4,223)	1,854	(3,195)
d Net Cash from Operating Activities	(892)	(2,614)	3,406	(1,354)
e Net Cash from Investing Activities	(854)	(2,924)	(4,133)	(1,293)
f Net Cash from Financing Activities	1,689	5,599	416	2,949
g Net Cash generated during the period	(57)	62	(312)	301

RATIO ANALYSIS

a Performance				
Turnover Growth	59%	17%	7%	-14%
Gross Margin	12%	18%	19%	23%
Net Margin	4%	10%	8%	10%
ROE	8%	13%	10%	15%
b Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+U	1.0	1.6	3.2	2.7
Interest Coverage (X) (FCFO/Gross Interest)	2.3	4.3	7.3	6.7
Debt Payback (Years) (Total Debt (excluding Covered Short T	2.6	1.9	0.7	0.5
c Capital Structure (Total Debt/Total Debt+Equity)				
Net Cash Cycle (Inventory Days + Receivable Days - Payable D	149	164	153	143
d Capital Structure (Total Debt/Total Debt+Equity)	50%	47%	32%	28%

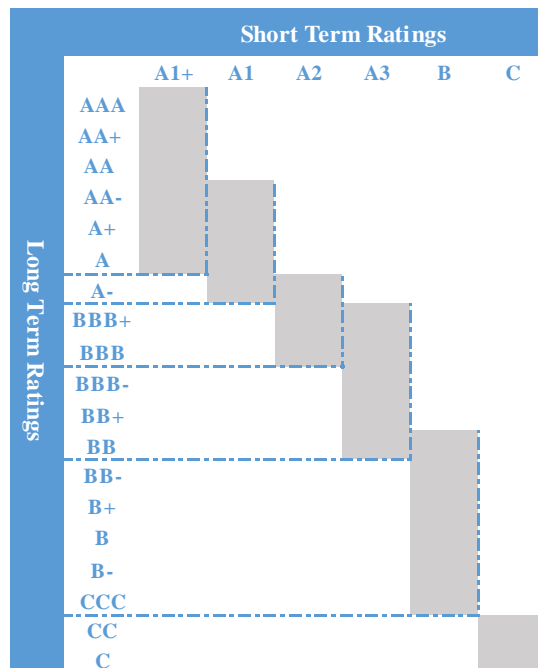
Amreli Steels

Mar-19

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+	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.
AA		A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
AA-		A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
A		C	An inadequate capacity to ensure timely repayment.
A-			
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.		
BBB			
BBB-			
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.		
BB			
BB-			
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.		
B			
B-			
CCC	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.		
CC			
C			
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.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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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- (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)

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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)

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)

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