The Pakistan Credit Rating Agency Limited

Rating Report

Amreli Steels Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
05-Jul-2021	A-	A2	Stable	Maintain	-
02-Sep-2020	A-	A2	Stable	Maintain	-
24-Sep-2019	A-	A2	Stable	Downgrade	-
25-Mar-2019	A	A1	Stable	Maintain	-
18-Dec-2018	A	A1	Stable	Maintain	-
14-Jun-2018	A	A1	Stable	Maintain	-
29-Dec-2017	A	A1	Stable	Maintain	-
27-Mar-2017	A	A1	Stable	Maintain	-
28-Oct-2016	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Amreli Steels has good business profile on account of the company's market positioning in the industry. The Company produces two key products: i) steel billets, ii) rebars including a) Grade 60 Deformed Steel bars and b) Xtreme bars (G-500W). The Company achieved capacity expansion of melting from 400,000 tons to 600,000 tons in June 2019 and rebars manufacturing capacity from 180,000 tons to 605,000 tons in June 2018. Rebar capacity will be further enhanced to 1,105,000; however the project is currently at halt for quite some time now on account of tough previous years in term of observed contracted economy. The company being 'Champion in selling Rebars' intends not to compromise on its quality and working to increase its footprint in other regions. Steel Industry dynamics reflect healthy prospects with notable growth in demand on the back of increased private sector spending. The governing bodies also took several measures to boost economy that provided supportive measures including curtailed policy rates, stabilized exchange rate and availability of subsidized financing. However; raw material costs witnessed historically increased prices which has a squeezing impact on margins. Meanwhile, the commencement of announced PSDP funded projects is going to contribute towards strong demand to strengthen the cashflows in near future. The volumetric increase (from recently added capacity to capture augmented demand) improved topline but margins did not reflect the wholesome increase due to a proportionate increase in costs. Amreli's financial risk matrix is stretched where the debt to equity ratio stands at around ~59.7% owing to the significant reliance on long term & short term financing for day-to-day working capital requirements. The ratings reflect better margins and recovered profitability in recent reported quarter post FY20 losses. The performance trend depicting revival after a dip witnessed till last fiscal year. Going forward, the management is expected to focus on optimal capacity utilization to achieve economies of scale and increase its market share while aligning the financial matrix to repay the principal amount of loan.

The ratings draw comfort from the strong business acumen of Amreli Steels' sponsors - Akberali Family. The ratings are dependent on the management's ability to uphold in difficult times and improve its business vis-àvis financial risk profile while operating in a flourishing economy. Utilization of enhanced capacity while capturing increased demand and sustained margins are vital. Moreover, prudent management of financial affairs proven vital in the sustainability of the Company.

Disclosure

Name of Rated Entity	Amreli Steels Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Steel(Sep-20)
Rating Analysts	Anam Waqas Ghayour | anam.waqas@pacra.com | +92-42-35869504

Profile

Legal Structure Amreli Steels Limited, a public limited company incorporated in 1984 under the Companies Ordinance and is traded under the section of Engineering.

Background Amreli Steels' rebar production facility situated at S.I.T.E Karachi is spread over an area of 2.2 acres of land. The facility has an automated re-rolling arrangement with a production capacity of 180,000 tons p.a. The melt shop is situated in industrial zone at Dhabeji, Port Qasim; and is constructed on 65 acres of land.

Operations Amreli Steels produces two key products: i) steel billets, ii) rebars including a) Grade 60 Deformed Steel bars and b) Xtreme bars (G-500W). Amreli Steels has the largest billet manufacturing plant in Pakistan with a capacity of producing 600,000 tons. The Company's entire power need is being fulfilled by K-Electric.

Ownership

Ownership Structure Presently, the company is majority (75%) owned by Akberali family, followed by Financial Institutions (6%), and general public (19%).

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 a seven-member board of directors, wherein four are from sponsoring family including the Chairman and CEO, while three are independent members.

Members' Profile Amreli arranges orientation courses for its directors on as and when required basis. The incoming directors are also provided with appropriate briefing and orientation material to equip them with first-hand knowledge of the company.

Board Effectiveness There are two board committees in place, these include: (i) Audit, and (ii) Human Resource & Remuneration. The audit committee comprises two independent members and one non-executive director. In FY20, six board meetings were held. Attendance of board members is also considered good.

Financial Transparency M/s EY Ford Rhodes, Chartered Accountants, classified in category 'A' by SBP and having a QCR rating, are the external auditors of the company. They have expressed an unqualified opinion for the financial statements of the year ended 30th, June 2020.

Management

Organizational Structure Amreli has a multi-tier organizational structure. Including two senior positions i) COO-Strategy and ii) COO-Operations and Chief Financial Officer and six functions namely; Marketing, Govt. and Public Relations, Information Technology, Corporate Affairs & Liaison, New Businesses, and CSR and communication reports to COO-Strategy.

Management Team Mr. Shayan Akberali, the elder son of Mr. Abbas Akberali, is lately appointed CEO - an engineer by profession and has been associated with the company for the last two decades. Mr. Hadi Akberali, the younger son, has been 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 the following operational modules, i) Production planning, ii) Material Management, iii) Sales and Distribution, iv) Finance, v) Controlling, and vi) Human Capital Management including success factor module. Reports generated on daily basis.

Control Environment Amreli has obtained ISO-9001 certification from Lloyd's Register Quality Assurance, which shows that the company's manufacturing processes and procedures are in conformity with international standards.

Business Risk

Industry Dynamics The domestic steel industry has undergone through recent expansion phase. With the reviving economy post-pandemic and the Govt. supportive initiatives to induce growth, steel sector is predicting better prospects in near future in concurrence with the reported growth in allied sectors including cement & construction sector. Regulatory protections in form of increased anti-dumping duties also considered a positive indicator. Whilst, sustained market share, improved business performance and margins are essential for industry players in an era of the stable key policy rate, supportive industry dynamics and flourished demands in the region.

Relative Position Amreli Steels is one of the leading players specifically in south region and is known for its quality in the domestic steel industry. The Company's strategies to geographically diversify its operation are currently holding up and remains vital to enhance its market share over the periods.

Revenues During 3QFY21, topline surged by ~29% YoY to stand at PKR 27.6bln (FY20: PKR 26.5bln; 3QFY20: PKR 21.4bln,) mainly driven by relatively induced demand which is evident from economy due to stimulated economic activity. The company's operating expenses (administrative and distribution expenses) decreased by ~22% and ~12% respectively, mainly attributable to recently launched "The state of the art warehousing facility" in Lahore to reduce transportation cost. During 3QFY21, finance cost witnessed a sizable decrease to stand at PKR 1,231mln (FY20: PKR 2,299mln; FY19: PKR 1,241mln) driven by stagnant long-term and short-term finance – attributable to decline in borrowing requirements – coupled with stagnant key policy rate. Hence, along with the volumetric growth in topline, Amreli Steels booked profit of PKR 926mln, emerged from losses of PKR (1,129mln) reported in FY20.

Margins Amreli Steel's margins witnessed notable surge (Gross: 3QFY21: ~12% FY20: ~7%, FY19: ~9%, FY18: ~18%, Operating: 3QFY21: ~8% FY20: ~3%, FY19: ~4.2%, FY18: 13%; Net: 3QFY21: ~3% FY20: ~-0.4%, FY19: ~0.1%, FY18: ~10%). However, there is an upward trend witnessed in international scrap prices along with energy cost contributed to the higher cost of sales, but effective cost management along with higher sales volumes contributed towards better margins.

Sustainability Amreli's vision to provide quality and innovation that also evident by the successful launch of 8mm rebar last year is going to strengthen its footprint on industrial landscape. Amreli Steels has recently expanded its rebar manufacturing facility under Phase-I and now actively working on improvement of distribution channels in order to capture the demand insight. Moving forward, active development on Governmental projects under PSDP funding including Naya Pakistan Housing Schemes and execution of CPEC projects will contribute to the existing private sector's driven demand. Moreover, Company's geographical diversification to enhance its market share remains vital for its performance.

Financial Risk

Working Capital During 3QFY21, Amreli Steel's working capital requirements represented by net cash cycle (function of inventory, receivables and payables) increased to 133days (end- Jun20: 153days) driven by decrease in inventory days (3QFY21: 88days; FY20: 101days). The company manages its working capital requirements through mix of internally generated cash and short-term borrowings & long-term borrowings. However, on account of better cashflows from operations, the company reduced its reliance on short term borrowings which drove relatively decreased figure (3QFY21: PKR 10.9bln; FY20: PKR 11.9bln; FY19: PKR 9.1bln). The company's liquidity profile stands at comfortable levels (Current ratio: (3QFY21: 3.3x; FY20; 3x).

Coverages During 3QFY21, EBITDA surged up by ~57% on period basis, standing at PKR 2,589mln (end-Jun20: PKR 1,654mln). FCFO also followed the growth trend by ~84% on period wise basis to stand at PKR 2,223mln; (end-Jun20: PKR 1,605mln). Consequently, stagnant in finance costs & enriched FCFO resulted in better coverage (interest: end-Mar21: ~2.0x; end-Jun20: ~0.6x; debt service: end-Mar21: ~1.0x; end-Jun20: ~0.4x).

Capitalization Since Jun-18, the company's leveraging enhanced mainly attributable to capacity expansion projects; however better performance enable the management to comfortably meet the repayment schedule. During 3QFY21, leveraging stood at ~60% (end-Jun20: ~63%). Out of total debt, ~62% pertains to short-term (end-Jun20: ~66%). The company's equity base improved on the back of improved profits after the reported losses in the last few periods to stand at PKR ~12.0bln (FY20: PKR 11.1bln; FY19: PKR 12.2bln).

PKR mln

Amreli Steels Ltd Infrastructure | Steels	Mar-21 9M	Jun-20 12M	Jun-19 12M	Jun-18 12M
A BALANCE SHEET				
1 Non-Current Assets	18,304	17,883	17,135	15,692
2 Investments	15	15	15	15
3 Related Party Exposure	-	-	-	-
4 Current Assets	18,173	17,572	12,460	10,935
a Inventories	*9,424*	*8,040*	*6,587*	*7,459*
b Trade Receivables	*5,375*	*4,900*	*3,403*	*1,788*
5 Total Assets	36,493	35,470	29,611	26,643
6 Current Liabilities	6,086	5,278	3,847	1,221
a Trade Payables	*705*	*487*	*242*	*107*
7 Borrowings	17,494	18,239	12,135	11,380
8 Related Party Exposure	341	341	280	-
9 Non-Current Liabilities	533	499	1,106	1,162
10 Net Assets	12,039	11,113	12,244	12,880
11 Shareholders' Equity	12,039	11,113	12,244	12,880
B INCOME STATEMENT				
1 Sales	27,228	26,532	28,596	15,501
a Cost of Good Sold	*(23,977)*	*(24,556)*	*(26,172)*	*(12,742)*
2 Gross Profit	3,251	1,976	2,424	2,758
a Operating Expenses	(1,051)	(1,185)	(1,218)	(787)
3 Operating Profit	2,200	790	1,206	1,971
a Non Operating Income or (Expense)	*(41)*	*(271)*	*(11)*	*(101)*
4 Profit or (Loss) before Interest and Tax	2,159	519	1,195	1,871
a Total Finance Cost	*(1,231)*	*(2,299)*	*(1,262)*	*(476)*
b Taxation	*(2)*	*654*	*100*	*191*
6 Net Income Or (Loss)	926	(1,127)	33	1,585
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,223*	*1,205*	*1,551*	*2,004*
b Net Cash from Operating Activities before Working Capital Changes	*735*	*(863)*	*505*	*1,609*
c Changes in Working Capital	*(1,297)*	*(3,140)*	*(801)*	*(4,223)*
1 Net Cash provided by Operating Activities	(562)	(4,003)	(296)	(2,614)
2 Net Cash (Used in) or Available From Investing Activities	(771)	(1,361)	(2,137)	(2,924)
3 Net Cash (Used in) or Available From Financing Activities	970	5,825	2,449	5,599
4 Net Cash generated or (Used) during the period	(363)	462	16	62
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	36.8%	-7.2%	84.5%	16.7%
b Gross Profit Margin	11.9%	7.4%	8.5%	17.8%
c Net Profit Margin	3.4%	-4.2%	0.1%	10.2%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	3.4%	-7.3%	2.6%	-14.3%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	10.4%	-11.1%	0.3%	14.6%
2 Working Capital Management				
a Gross Working Capital (Average Days)	139	158	123	166
b Net Working Capital (Average Days)	133	153	121	164
c Current Ratio (Current Assets / Current Liabilities)	3.0	3.3	3.2	9.0
3 Coverages				
a EBITDA / Finance Cost	2.3	0.8	1.6	5.1
b FCFO / Finance Cost+CMLTB+Excess STB	1.0	0.4	0.5	1.6
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	4.7	-7.6	12.2	1.9
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	59.7%	62.6%	50.3%	46.9%
b Interest or Markup Payable (Days)	76.8	101.4	103.7	0.0
c Entity Average Borrowing Rate	8.9%	14.7%	10.2%	6.0%

Credit Rating

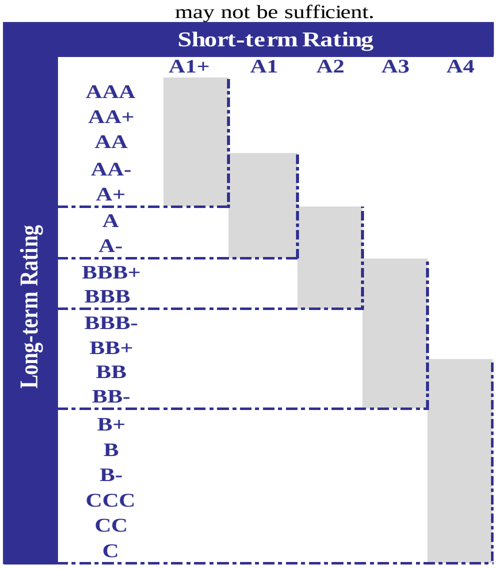
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities

a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk 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.

(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