The Pakistan Credit Rating Agency Limited

Rating Report

Kohat Cement Company Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jan-2022	A	A1	Positive	Maintain	-
12-Feb-2021	A	A1	Stable	Maintain	-
13-Feb-2020	A	A1	Stable	Maintain	-
28-Sep-2019	A	A1	Stable	Maintain	-
29-Mar-2019	A	A1	Stable	Maintain	-
22-Nov-2018	A	A1	Stable	Maintain	-
04-May-2018	A	A1	Stable	Maintain	-
29-Dec-2017	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Kohat Cement's ratings reflect its good market position in cement industry. The company's market share in north region rose to 9.6% after successful completion of brown-field expansion of 2.3mln tpa, last year. The Cement sector's dispatches have recorded splendid growth and surged by 21% in FY21 as demand in the domestic market accelerated. Export is another avenue. Industry-wide exports have gone up as a new export window is created in the Bangladesh market. The industry's future demand outlook is positive, in view of the infrastructure projects in the pipeline. The Company's revenues witnessed an increase (1QFY22: PKR 6.8bln, FY21: PKR 24bln, FY20: PKR 11.3bln) attributed to an uptick in sales volumes, positive price indicators and, reinvigorating economy. Margins in 1QFY22 also improved on account of recently added more efficient Line-IV. Company aims to optimally utilize the recently expanded line IV, in order to cut off direct cost. The Company managed to recoup previous losses and reported profits of PKR 1.3bln and PKR 3.5bln in 1QFY22 and FY21 respectively. BMR of Line-III is underway that would cost ~PKR 650mln, and will be financed through equity. Company's leverging has reduced as the repayments of long term loan for line IV has started taking the debt/equity ratio in a comfortable position ~19% in 1QFY22 (FY21: 21.4%, FY20: 27%). In order to participate in current boom in cement industry management has announced further green field expansion of 7,800-10,000 TPD, near Khushab. Estimated cost of project is ~PKR 28bln out of which ~60% will be debt financed. Financial Close is expected to be achieved by Mar-22. The company has an available short term limit of ~PKR 3.3 billion out of which ~86% remained unutilized which shows company's low reliance on short term borrowings. The company's fairly low leveraging, healthy liquid investment book provides comfort to the ratings. Company own investment properties along with a significant amount of liquid assets having a book value of ~PKR 4.1bln and ~PKR 5.3bln respectively, which mitigates the financial risk factor to a large extent.

The ratings are dependent on upholding of company's market position in addition to sustenance of business volumes and margins along with good governance practices. The company's strategy to keep a moderate level of leveraging remains imporatnt for the ratings. .

Disclosure

Name of Rated Entity	Kohat Cement Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Cement(Mar-21)
Rating Analysts	Bazah Tul Qamar | bazahtul.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Kohat Cement Company Limited (Kohat Cement) a subsidiary of ANS Capital (Pvt.) Ltd is a public listed company established in 1984 by State Cement of Pakistan. Subsequent to its privatization in 1992, the company was taken over by new management headed by Mr. Aizaz Sheikh. The company is listed on Pakistan Stock Exchange (PSX).

Background The registered office and the factory are located in Kohat, whereas the Head Office is located in Lahore. In 1995, the company underwent an extensive BMR program and the capacity of the plant was enhanced to 1,800tpd. Afterwards, in 2005 a White Cement Plant was established followed by a Grey Cement Plant in 2007. Furthermore, a power plant with capacity of 22.6MW was added in 2009.

Operations Kohat Cement is engaged in the production and sale of cement. The Company's products include Grey Cement and White Cement. Company has an installed capacity of 5.3mln tons per annum. Two separate production lines (for grey and white cement) allows the company to have a broader product slate.

Ownership

Ownership Structure Kohat Cement is majority owned by sponsor family through ANS Capital (Pvt.) Limited (~55%) where, the ownership of ANS Capital (Pvt). Ltd. resides equally between Mr. Aizaz & Mr. Nadeem Atta sheikh. The other major proportion of shareholding is of Mrs. Hijab Tariq (widow of late Mr. Tariq Atta) owns ~17%.

Stability : Kohat Cement's ownership structure is seen stable as no major ownership changes are expected in near future.

Business Acumen The sponsors, especially the Chief Executive, has interests vested in various sectors through holding company. This strengthens the sponsor's business acumen.

Financial Strength Kohat Cement being the flagship entity of sponsors, 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 eight member's board of directors - including the Chief Executive – Nadeem Atta Sheikh. Other than Chief Executive, Mr. Aizaz Mansoor is the chairman of the board. All board members are from sponsoring family, including two independent members Mr. M. Ahmed Sajjad Khan & Mr. Talha Saeed Ahmed.

Members' Profile The board members' have good business acumen on the back of significant local industry exposure in several sectors. The board meetings minutes are formally maintained reflecting good participation by the members present. Mr. Ahmed Sajjad Khan and Mr. Talha Saeed Ahmed were elected as independent directors and associated with the board since Jun, 2019.

Board Effectiveness Kohat Cement has two committees: 1) Audit committee and 2) Human resource & Remuneration Committee (HR&R); this is in compliance with the Code of Corporate Governance.

Financial Transparency KPMG Taseer Hadi & Co., Chartered Accountants conduct the external audit services for Kohat Cement. 'KPMG' is in 'A' category of SBP list of external auditors and has a QCR rating.

Management

Organizational Structure Currently, the organizational structure is divided into fourteen main functions. The functions reporting to CEO are as follows: 1) Sales & Marketing, 2) Administration, 3) HR, 4) Planning & Development, 5) Finance & Accounts 6) Works. However, the functions reporting to GM Works are: 1) Production, 2) Electrical, 3) Quality Control, 4) Power Plants, 5) Technical & Purchase, 6) Maintenance, 7) Works and 8) Material and Mining.

Management Team Mr. Nadeem Atta, the CEO, is associated with the company since the last 28 years. The CEO is supported by a team of experienced individuals equipped with necessary technical skills and relevant industry exposure

Effectiveness The Chief Executive Officer and Executive Director are supported by a team of experienced professionals at key management positions.

MIS Kohat Cement has strong technology infrastructure with reasonably defined policies and procedures. The company's current operational modules include marketing, supply chain and financial modules with comprehensive MIS quality. Various system generated reports including the Cash flow/investment portfolio, daily management report, and daily production summary and sale variance report which are reviewed by top management.

Control Environment Kohat Cement's plant is located in Kohat, in North Region. The fuel requirement is met mainly through coal imported from South Africa and Indonesia. The kiln can operate on coal only. The total energy requirements of the company for FY21), are 65MW. To cater the power needs, the company has 82MW of connection from WAPDA and generators of 22MW for captive power generation. Furthermore, the company has 25MW waste heat recovery power plant.

Business Risk

Industry Dynamics Irrespective of the apprehensions caused by COVID-19, Pakistan's cement industry has continued to grow on the back of well in time government initiatives. Package included amnesty scheme, tax exemptions and Rs 36 billion subsidy for Naya Pakistan Housing Scheme. Further, banks were directed to increase construction sector loans to 5% of their total loan book and FED reduction on cement from Rs 2/kg to Rs 1.5/kg have given impetus to this industry. A significant increase in Foreign Direct Investment (FDI)1 and Long-Term Financing Facility (LTFF)2 for construction sector also bodes well for the sector. Total cement dispatches in FY 2021 stood at 57.4 mln MT as against 47.8mln MT last year. Domestic consumption grew by 20%. The export trend represented a substantial growth of 18.6% during the period.

Relative Position As at end-Jun21, Kohat's market share stands at 9.6% in the north region

Revenues During 1QFY22, the Company recorded revenue of PKR 6.8bln (1QFY21: PKR 5.1bln) witnessing an increase of ~31% YoY on the back of positive price indicators. Sales mix remained tilted towards local market mainly due to healthy demand and secured margins in local market. During FY21, the Company's capacity utilization levels improved to ~73% (FY20: ~55%). Finance costs deccreased to PKR 119mln in 1QFY22 (1QFY21: PKR 138mln).

Margins Kohat's margins have improved over the past year but still remained at comfortable level (Gross: 1QFY22: ~33%, FY21: ~24.8%, FY20: -0.2%), Operating 1QFY22: ~31.04%, FY21: ~22.46% FY20: -1.3%). Also, EBITDA margin witnessed substantial increase (1QFY22: ~37%, FY21: 29%, FY20: 6%).

Sustainability The government stimulus packages for the construction industry are expected to lead the growth and recovery of Pakistan Economy. The Company has investment properties of PKR 4.1bln in 1QFY22 which can be utilised in case of any cash shortfall in upcoming expansion.

Financial Risk

Working Capital During FY21, Kohat's working capital requirements represented by net cash cycle (net working capital days) - a function of inventory, receivables aand payables - decreased to 5 days (FY20: 17 days). The Company was able to manage the requirement primarily through internal resources on account of robust cashflows. Hence, company's reliance on Short-term borrowings (STBs) remained minimal, (1QFY22: PKR 217mln, FY21: 498).

Coverages During 1QFY22, Kohat Cement's EBITDA increased by 112% YOY, standing at PKR 2,498mln. (1QFY21: PKR 1,180mln). The Company was able to maintain adequate coverage ratios on account of strong cash flows and comparatively low leveraged structure. (Interest coverage: 1QFY22: 17.7x;; 1QFY21: 6.03x, debt service: 1QFY22: 5.52x; 1QFY21: 3.88x). Going forward, with the predicted gradual addition in debt, coverages are expected to be affected but will remain inbounds of adequacy.

Capitalization Over the last few years, the company operated at fairly low leveraged capital structure. During 1QFY22, debt to debt plus equity ratio reduced to ~18 % from 23% in 1QFY21: (FY21: ~20%). Going forward, the company's leveraging is expected to increase in pursuit of expansion. However, it is expected to be comfortably managed through healthy cash flows.

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Financial Summary
PKR mln

Kohat Cement Company Limited Cement	Sep-21 3M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	21,924	22,102	22,827	22,017
2 Investments	8,224	7,136	3,852	5,639
3 Related Party Exposure	-	-	-	-
4 Current Assets	7,863	6,849	5,198	3,659
a Inventories	*1,426*	*1,113*	*1,016*	*709*
b Trade Receivables	*905*	*984*	*494*	*714*
5 Total Assets	38,011	36,087	31,877	31,315
6 Current Liabilities	6,737	5,927	4,677	4,277
a Trade Payables	*1,709*	*1,672*	*1,278*	*629*
7 Borrowings	5,513	6,051	6,989	5,647
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	2,140	1,885	1,485	1,718
10 Net Assets	23,621	22,224	18,727	19,673
11 Shareholders' Equity	23,621	22,224	18,727	19,673
B INCOME STATEMENT				
1 Sales	6,804	24,057	11,300	15,646
a Cost of Good Sold	*(4,543)*	*(18,092)*	*(11,325)*	*(11,473)*
2 Gross Profit	2,261	5,965	(24)	4,173
a Operating Expenses	(101)	(408)	(303)	(340)
3 Operating Profit	2,160	5,558	(327)	3,834
a Non Operating Income or (Expense)	*(48)*	*(155)*	*179*	*(112)*
4 Profit or (Loss) before Interest and Tax	2,112	5,403	(148)	3,722
a Total Finance Cost	*(119)*	*(517)*	*(409)*	*(46)*
b Taxation	*(595)*	*(1,388)*	*114*	*(1,207)*
6 Net Income Or (Loss)	1,398	3,498	(444)	2,469
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,446*	*6,575*	*175*	*3,437*
b Net Cash from Operating Activities before Working Capital Changes	*2,318*	*5,975*	*(127)*	*3,098*
c Changes in Working Capital	*(550)*	*(886)*	*(376)*	*1,648*
1 Net Cash provided by Operating Activities	1,769	5,089	(502)	4,745
2 Net Cash (Used in) or Available From Investing Activities	(1,070)	(3,950)	(19)	(13,090)
3 Net Cash (Used in) or Available From Financing Activities	(540)	(943)	839	4,564
4 Net Cash generated or (Used) during the period	159	196	318	(3,781)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	13.1%	112.9%	-27.8%	16.4%
b Gross Profit Margin	33.2%	24.8%	-0.2%	26.7%
c Net Profit Margin	20.5%	14.5%	-3.9%	15.8%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	27.9%	23.6%	-1.8%	32.5%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	24.3%	16.7%	-2.4%	14.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	30	27	47	32
b Net Working Capital (Average Days)	7	5	17	10
c Current Ratio (Current Assets / Current Liabilities)	1.2	1.2	1.1	0.9
3 Coverages				
a EBITDA / Finance Cost	21.8	14.1	1.6	127.7
b FCFO / Finance Cost+CMLTB+Excess STB	6.0	4.0	0.1	3.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.6	0.9	-29.0	1.6
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	18.9%	21.4%	27.2%	22.3%
b Interest or Markup Payable (Days)	89.5	91.3	193.8	1098.5
c Entity Average Borrowing Rate	7.6%	7.8%	6.0%	1.0%

Credit Rating

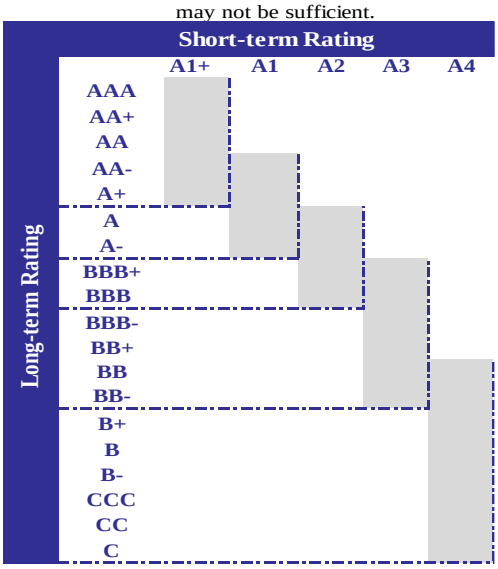
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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