The Pakistan Credit Rating Agency Limited

Rating Report

Gharibwal Cement Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Sep-2019	A-	A2	Stable	Maintain	-
29-Mar-2019	A-	A2	Stable	Maintain	-
16-Nov-2018	A-	A2	Stable	Maintain	-
04-May-2018	A-	A2	Stable	Maintain	-
20-Nov-2017	A-	A2	Stable	Maintain	-
06-Jun-2017	A-	A2	Stable	Maintain	-
04-Oct-2016	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Gharibwal Cement's strength in its key markets. The Company has a market share of 4% in the north region with annual cement capacity of 2.1mln tons. The company focuses on geographies closer to the plant location; Gujranwala division remained company's home market. During FY19, industry dynamics especially for cement players operating in north region have shifted significantly on account of fluctuating cement prices, increase in FED on coal import and depreciation in Pak Rupee against other currencies. Along with these factors, slow local demand has affected the company's sales whereby cement dispatch declined to 1.1mln tons in 9MFY19 (9MFY18: 1.4mln tons). Owing to current muted demand, the company decided to delay its capacity enhancement plan by two years. The company's business profile remained adequate on account of aforementioned factors while margins and profitability witnessed decline. However, margins remained better when compared with other small players of the industry. The financial risk matrix is expected to improve as leveraging is expected to remain at same level owing to delay in expansion; coverage improved YoY. The ratings draw comfort from sponsor families, having prime focus of the company.

The ratings are dependent on upholding of the company's business vis-à-vis financial risk profile in current economic scenario. Industry's dynamics encompassing expected challenges of supply glut, substantial decline in local demand or deterioration in cement prices will negatively affect the ratings.

Disclosure

Name of Rated Entity	Gharibwal Cement Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Crtieria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study | Cement(Apr-19)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure Gharibwal Cement Limited – the flagship company of Gharibwal Group – was incorporated in 1960 as Public Limited Company and commenced operations in 1965 and is listed on Pakistan Stock Exchange.

Background Way back in 1970's, the company was nationalized like other peers. Subsequently, after two decades (1992), in the wake of industries' privatization, Mr. Tausif Peracha and Mr. Abdur Rafiq Khan – a foreign entrepreneur – acquired majority stake in Gharibwal Cement. Since then, both have been associated with company.

Operations Gharibwal Cement's registered office is located in Pace Tower Lahore and production facility is located in Ismailwal, Tehsil Pind Dadan Khan, District Chakwal. Gharibwal Cement Limited enhanced grinding capacity by adding new vertical mill of cement, in which company has increased its capacity to 13,680 t.p.d of grinding mill.

Ownership

Ownership Structure Gharibwal Cement is a family owned business with majority stake held by two families. Peracha family owns ~56% while Khan family holds 32% equity stake in the company; all through individuals. However, Mr. Muhammad Tousif Peracha (single key shareholder) is identified as the man at the last mile.

Stability Tacit understanding between shareholding families necessitates formal documentation.

Business Acumen Mr. Muhammad Tousif Peracha and Mr. Abdur Rafique Khan have been together for more than three decades and are partners in different business ventures internationally – mainly shipping and real estate business. They have no blood relation but had been family friends since many past years.

Financial Strength Gharibwal Group has interests in glass manufacturing, lubricants, and real estate projects locally and shipping and truck manufacturing in Nigeria.

Governance

Board Structure The overall control of the company vests in seven member's board of directors including the Chairman - Mian Nazir Ahmed Peracha, and the CEO - Mr. Muhammad Tousif Peracha. While two independent members. Out of five, there are two executive directors – the CEO and a director– and three non-executive directors.

Members' Profile Board members carry adequate experience; though challenge to management decisions is limited.

Board Effectiveness Two committees, Audit and Human Resource and Remuneration, are in place to assist the board on relevant matters.

Financial Transparency M/s Kreston Hyder Bhimji and Co. Chartered accountants, 'A' category SBP panel member, are the external auditor for the company. They have performed interim review on financial statements for six months ending Dec, 2018.

Management

Organizational Structure The organizational structure of the company is divided into eight key functions. These include i) Operations and Projects, ii) Procurement, iii) Finance, iv) Marketing/ Commercial, v) Technical Advisory, vi) Information Technology, vii) Administration/ HR, and viii) Internal Audit. The Director Operations and Projects, supported by GM Works and his team, resides at Plant. All functional heads report to the CEO except Internal Audit, who reports to the Audit Committee.

Management Team The management is equipped with necessary skill set and technical skills required. The board has lately approved new positions which are not yet finalized. Few changes in management structure, in order to bring efficiency in overall group structure, are expected

Effectiveness The management is supported by four committees: – (i) Core Executive, (ii) Risk Management, (iii) Investor Relation, and (v) Finance and Policy Committee.

MIS Deploys Microsoft Dynamic G.P 2015 as operating software; quality of MIS reporting considered good.

Control Environment Plant – a mix of European and Chinese technology. Gharibwal Cement has several sources to cater its power requirements (57MW).

Business Risk

Industry Dynamics Cement industry is divided into North and South region – majority (76%) operational capacity exists in North region. Industry has achieved its majority capacity expansions in last two years of around 14mln tons per annum. During FY19, north region witnessed 5% and 18% decline in local and export dispatches respectively attributable to contractionary fiscal policy, slowdown in large infrastructural activities and low demand from Afghanistan and India (export avenues). South region witnessed uptrend in dispatches which is correlated with longevity of export window available through sea. Industry dynamics has changed significantly driven by unsustainable cement prices (especially in north region) on account of supply glut recently created, muted demand and ruppee depreciation. Cement players witnessed significant dip in margins on account of aforementioned factors. Currently, leveraging of industry is moderate (31% as at end-Mar19) but increased interest rates has amplified the stress on financial risk profile of players. 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 as demand front deemed to stay weak for at least upcoming one year.

Relative Position Gharibwal Cement is among middle-tier cement players with an operational capacity of 2.1mln tpa. Over last few years, the company commenced some projects in order to gain overall efficiency which included raw material conveyer belt, setting up a WHRPP and lately commenced cement grinding mill. The company announced production expansion capacity, however, by taking into account lately developed industry dynamics the expansion is currently on hold.

Revenues In 9MFY19, company's revenues decreased by ~4% YOY to stand at PKR 8.2bln (FY18: 11.4bln) because of decline in cement sales volume by 17%. Topline mix is predominantly skewed towards local sales. Key reason being the plant's location, whereby local sales can secure margins, local sales are more profitable than exports. During 9MFY19, local dispatches have slimmed down by 2% (FY18: 9%; FY17: 7%; FY16: 11%). Export volumes has witnessed downtrend – an industry wide phenomenon – the contribution of exports in overall revenues is nominal. The Company's interest income was increased to PKR 27mln (9MFY18: PKR 20mln, FY18: PKR 26mln, FY17: 62mln) owing to the presence of settlement of markup on repayments in previous years. Financial charges reported an inclining trend; attributable to payment of outstanding debt level and increase in borrowing rate. Resultantly, the company reported a significant reduction in net income of 9MFY19: PKR 820mln (FY18: PKR 1.5bln, FY17: 2.3bln), down -20% YOY.

Margins Margins decreased 9MFY19: 23%(9MFY18: 24%) operating: 9MFY19: 19.5% (9MFY18: 20.8%) due to the increase in the prices of fuel, energy and also the fluctuation in cement prices. EBITDA Margin also inched down to 27.5% (9MFY18: 27.7%).

Sustainability Going forward, the company is planning to focus on fully utilizing its current capacity and achieving overall efficiency in manufacturing process. Previously, the company announced capacity expansion of 1mln tpa – effective capacity will reach at 10,000 tpd post expansion. The project cost is estimated to be PKR 6.5bln with debt equity ratio of 50:50. Owing to the current economic pressures, the company has delayed the expansion for some years.

Financial Risk

Working Capital Gharibwal Cement's working capital requirements are a function of its inventory and payables, for which the company currently relies on mix of internal cashflows and short term borrowings. Net cash cycle improved to (22) days at end-Mar19; on account of delayed payments to creditors. Current ratio was 0.9x in June 18 marginally increased to 1.0x in 9MFY19. The company has approved short term advance to facility up to PKR 500mln to its associated Company BGL at a markup @ 3 months KIBOR plus 3.5% p.a outstanding balance includes markup receivable.

Coverages Gharibwal Cement's absolute EBITDA is largely maintained at (end-Mar19: PKR 2.2bln, end-Mar18: PKR 2.3bln) owing to sustained profitability. Coverages remained adequate while debt payable slightly improved to 1.5 years (FY18: 2.5 years)

Capitalization During 9MFY19, the capital structure of the company slightly improved as total debt to debt plus equity ratio at 21% (FY18: 26%) attributable to the repayments. During FY18, company announced a dividend of total 15% (PKR 1.5 per share) amounting to PKR 939mln. Going forward, debt levels are not expected to rise.

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Financial Summary
PKR mln

Gharibwal Cement Limited	Mar-19	Jun-18	Jun-17	Jun-16
Cement	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	18,618	19,251	18,768	15,491
2 Investments	-	-	20	104
3 Related Party Exposure	329	250	250	249
4 Current Assets	3,920	3,342	2,578	2,208
a Inventories	*901*	*632*	*625*	*423*
b Trade Receivables	*604*	*557*	*509*	*360*
5 Total Assets	22,868	22,843	21,615	18,052
6 Current Liabilities	3,996	3,701	3,452	2,522
a Trade Payables	*2,084*	*1,960*	*1,167*	*373*
7 Borrowings	3,391	4,338	4,506	3,892
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	2,771	2,313	2,275	1,566
10 Net Assets	12,710	12,491	11,381	10,071
11 Shareholders' Equity	12,710	12,491	11,381	10,071
B INCOME STATEMENT				
1 Sales	8,276	11,484	11,223	10,522
a Cost of Good Sold	*(6,355)*	*(8,772)*	*(7,369)*	*(6,350)*
2 Gross Profit	1,921	2,712	3,854	4,172
a Operating Expenses	(305)	(410)	(348)	(328)
3 Operating Profit	1,615	2,303	3,506	3,844
a Non Operating Income or (Expense)	*(59)*	*(90)*	*(153)*	*129*
4 Profit or (Loss) before Interest and Tax	1,556	2,213	3,353	3,973
a Total Finance Cost	*(356)*	*(430)*	*(308)*	*(279)*
b Taxation	*(380)*	*(274)*	*(761)*	*(1,014)*
6 Net Income Or (Loss)	820	1,510	2,284	2,681
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,031*	*2,285*	*3,692*	*4,075*
b Net Cash from Operating Activities before Working Capital Changes	*1,814*	*1,913*	*3,116*	*3,453*
c Changes in Working Capital	*(126)*	*577*	*375*	*(552)*
1 Net Cash provided by Operating Activities	1,688	2,490	3,491	2,901
2 Net Cash (Used in) or Available From Investing Activities	(169)	(1,337)	(3,816)	(2,648)
3 Net Cash (Used in) or Available From Financing Activities	(1,532)	(1,169)	(61)	(46)
4 Net Cash generated or (Used) during the period	(13)	(16)	(385)	206
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-3.9%	2.3%	6.7%	--
b Gross Profit Margin	23.2%	23.6%	34.3%	39.7%
c Net Profit Margin	9.9%	13.1%	20.3%	25.5%
d Cash Conversion Efficiency (EBITDA/Sales)	27.5%	27.3%	36.0%	40.9%
e Return on Equity (ROE)	8.7%	12.6%	21.3%	30.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	45	37	31	31
b Net Working Capital (Average Days)	-22	-13	6	10
c Current Ratio (Total Current Assets/Total Current Liabilities)	1.0	0.9	0.7	0.9
3 Coverages				
a EBITDA / Finance Cost	7.2	8.2	15.5	17.0
b FCFO / Finance Cost+CMLTB+Excess STB	1.6	1.1	1.9	4.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.5	2.5	1.6	1.1
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	21.1%	25.8%	28.4%	27.9%
b Interest or Markup Payable (Days)	79.9	39.5	85.3	65.1
c Average Borrowing Rate	10.9%	8.6%	6.2%	6.7%

Rating Scale | Corporate

2019

Credit Rating Scale & Definitions

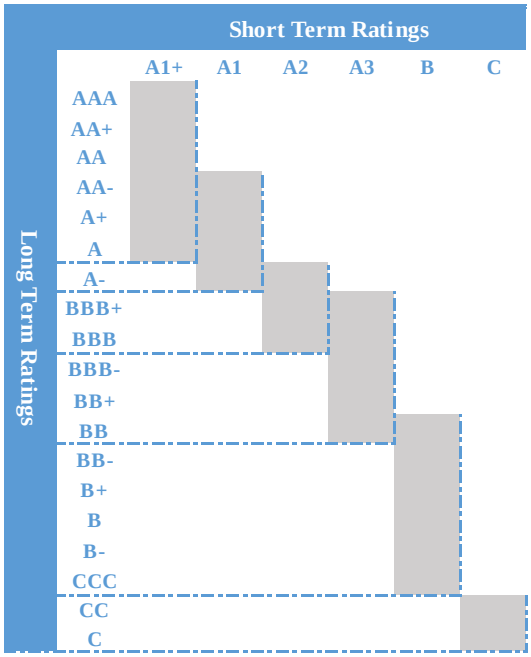
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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 Ratings

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 conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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 surveill the opinion due to lack of requisite information.

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

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