



The Pakistan Credit Rating Agency Limited

## Rating Report

### Fatima Fertilizer Company Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jan-2022	AA	A1+	Stable	Upgrade	-
30-Jul-2021	AA-	A1+	Stable	Maintain	-
19-Aug-2020	AA-	A1+	Stable	Maintain	-
21-Aug-2019	AA-	A1+	Stable	Maintain	-
19-Feb-2019	AA-	A1+	Stable	Maintain	-
01-Nov-2018	AA-	A1+	Stable	Maintain	-
08-Aug-2017	AA-	A1+	Stable	Maintain	-
11-Nov-2016	AA-	A1+	Stable	Maintain	-

#### Rating Rationale and Key Rating Drivers

Pakistan has an agrarian economy, thus fulfills around ~ 84% of its fertilizer requirement through local production while the remaining is met through imports. The Country's total fertilizer production capacity stands at around ~ 7.1mln MT of Urea and CAN and ~ 1.7mln MT of DAP, NP, and NPK. In CY21, Urea's offtake stood at ~6.3mln MT. The availability of urea was estimated on the basis of the Economic Coordination Committee's decision that allows urea plants to operate on subsidized LNG up to Mar-22. Unavailability of LNG has created supply uncertainty of urea for the ongoing Rabi Season 2021-2022, thus the Federal Government has decided to import 0.1mln MT of urea from China. Meanwhile, DAP's offtake stood at 2.5mln MT. Despite the increase in gas prices, overall margins of the industry remained healthy mainly due to the increase in prices of fertilizer products. In the international market, prices of Urea and DAP witnessed an upward trend supported by increased demand. Going forward, the industry's outlook is expected to remain satisfactory.

The ratings reflect Fatima Fertilizer Company Limited's ('Fatima' or 'the Company') association with strong business Groups, Fatima Group and Arif Habib Group. The Company holds the highest market share in NP and CAN. Furthermore, after the acquisition of the Pakarab Fertilizer's plants (Ammonia, Urea, Nitric Acid, Nitro Phosphate, Calcium Ammonium Nitrate, and Clean Development Mechanism) the Company has increased its overall market standing. The Company's topline comprising mainly of Urea, NP, and CAN has witnessed phenomenal growth driven by increased sales volumes during 9MCY21 post the acquisition. The Company has maintained healthy margins over the years owing to efficient operations and having a dedicated gas supply line from Mari fields. Despite the expiration of concessionary gas, the Company's performance is anticipated to remain optimal owing to the volumetric growth. The Company has continuously invested in optimizing its production plants and reaps the benefits of having increased utilization and higher run time of its production facilities. Moreover, income from the trading portfolio provides limited support to the Company's bottom line. The Company's financial profile is characterized by modestly leveraged capital structure, very strong coverages, and efficient management of working capital. Ratings draw comfort from business acumen from the sponsors and strong governance framework.

The ratings are dependent on the Company's ability to sustain its margins and healthy coverages while maintaining cushion and adherence to strong financial discipline. Substantial deterioration in margins and profitability would adversely impact the ratings.

#### Disclosure

<b>Name of Rated Entity</b>	Fatima Fertilizer Company Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Rating(Jun-21),Criteria   Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria   Rating Modifiers(Jun-21)
<b>Related Research</b>	Sector Study   Fertilizer(Jan-21)
<b>Rating Analysts</b>	Faiqa Qamar   faiqa.qamar@pacra.com   +92-42-35869504

## Profile

**Legal Structure** Fatima Fertilizer Company Limited ('Fatima Fertilizer' or 'the Company') was incorporated in Dec-03 as a public company under the repealed Companies Ordinance, 1984 (now Companies Act, 2017). The Company got listed on the Pakistan Stock Exchange (PSX) in 2010.

**Background** The Company was formed by a joint venture between two major business groups in Pakistan namely, Fatima Group and Arif Habib Group. The Company's first venture, a fully integrated fertilizer production facility, was initiated in 2006 in Sadiqabad, Punjab. The facility commenced operations in 2011. The Company later acquired production plants in Sheikhpura and Multan.

**Operations** The Company is primarily involved in manufacturing and selling variants of fertilizers and chemicals. The production facilities are all located in Punjab, Pakistan. The Company mainly produces Urea, CAN, and NP. In 3QCY21, the Company's combined actual production increased by 33% QoQ and stood at 1.84 million MT (3QCY20: 1.38mln MT) and capacity utilization remained stable at 95%.

## Ownership

**Ownership Structure** Fatima Group holds 45% of the total shares through associated companies (23%) and individuals (22%), while Arif Habib Group holds 34% through associated companies (16%) and individuals (18%). Fazal Group holds 11% through associated company (3%) and individuals (8%). The remaining shareholding lies with Financial Institutions (4%) and General Public (6%).

**Stability** Ownership of the business is stable. The second generation has been inducted into the business as well.

**Business Acumen** The sponsors have very strong business acumen. Fatima Group is one of the leading corporate groups in Pakistan, engaged in trading of commodities, manufacturing of fertilizers, textiles, sugar, mining and energy. Arif Habib Group ranks amongst the prominent financial services groups and holds interests in financial advisory, investment management, commercial banking, commodities, private equity, cement and fertilizer industries.

**Financial Strength** The Company's sponsors, Fatima Group and Arif Habib Group, have substantial financial strength.

## Governance

**Board Structure** The Company's Board comprises of seven members. The Board includes two members each from Fatima Group and Arif Habib Group, CEO of the Company and two independent directors.

**Members' Profile** The Board's Chairman, Mr. Arif Habib, has very strong business acumen and is also the Chief Executive Officer of Arif Habib Corporation Limited, the holding company of Arif Habib Group.

**Board Effectiveness** The Board is assisted by the Board Audit Committee, Human Resource and Remuneration Committee, and Nomination and Risk Management Committee. The committees meet on need basis and minutes are adequately documented.

**Financial Transparency** The External Auditors of the Company are Deloitte Yousaf Adil, Chartered Accountants rated 'A' on the SBP panel. They have expressed an unqualified opinion on the financial statements for the year ended Dec-20.

## Management

**Organizational Structure** The organizational structure has been optimized as per the operational needs. The Company operates through eight functions: Production, Finance, Marketing and Sales, Internal Audit, Business Development, Administration, Supply Chain, and Human Resource. All functional managers report to the Company's CEO except the Head of Audit who reports to the Audit Committee, and HR Director who reports to HR & Remuneration Committee.

**Management Team** Mr. Fawad Ahmed Mukhtar is the CEO of the Company. He has 30 years of experience in industrial management. He is assisted by a team of experienced professionals. Mr. Asad Murad is the Chief Operating Officer of the Company and has over 23 years of experience.

**Effectiveness** Management's effectiveness and efficiency is ensured through the presence of Executive Committee, Project Review Committee, and Enterprise Risk Management Committee.

**MIS** The Company uses an upgraded Oracle based ERP system which has been optimized as per the needs of the business.

**Control Environment** To ensure operational efficiency, the Company has setup an internal audit function, which implements and monitors the policies and procedures of the Company.

## Business Risk

**Industry Dynamics** Pakistan has an agrarian economy, thus fulfills around ~ 84% of its fertilizer requirement through local production while the remaining is met through imports. The Country's total fertilizer production capacity stands at around ~ 7.1mln MT of Urea and CAN and ~ 1.7mln MT of DAP, NP, and NPK. In CY21, Urea's offtake stood at ~6.3mln MT. The availability of urea was estimated on the basis of ECC decision to allow urea plants to operate on subsidized LNG up to Mar-22. Unavailability of LNG has created supply uncertainty of urea for the Rabi Season 2021-2022 and the Federal Government has decided to import 0.1mln MT of urea from China. Meanwhile, DAP's offtake stood at 2.5mln MT. The overall margins of the industry remained healthy despite increase in gas prices mainly due to the increase in prices of fertilizer products. In the international market, prices of Urea and DAP witnessed an upward trend supported by increased demand due to high input cost. However, the expected Government subsidy scheme would reduce DAP prices. Going forward, industry's outlook is expected to remain satisfactory.

**Relative Position** After the acquisition of the Pakarab Fertilizer's plants, the Company has increased its overall market share to 24% in terms of sales.

**Revenues** The Company's revenue comprises of Urea (34%), NP (34%), CAN (19%), DAP (12%), and Others (1%). During 3QCY21, the Company's topline stood at ~PKR 77bln (3QCY20: ~PKR 46bln) up by ~65%, primarily driven by significant increase in sales volume (Pak Arab's facility acquired in Sep-20) and the plants remaining operational for majority of the year. Furthermore, an uptick in the prices of fertilizers during 3QCY21 supplemented the increase in the Company's revenue.

**Margins** During 3QCY21, the Company's gross margin declined and stood at 43.6% (3QCY20: 46%) due to increased cost of sales as a result of cessation of concessionary gas period. Similarly, on operational level the margin slightly decreased to 34.5% (3QCY20: 34.9%). At net level, the Company's net income driven by increased turnover, closed at ~PKR 14bln (3QCY20: ~PKR 10bln) witnessing ~47% increase. Subsequently, net margin stood at 18.4% during 3QCY21 (3QCY20: 20.6%).

**Sustainability** The Company is actively evaluating alternate sources of gas with the GoP to mitigate the risk of depleting reserves.

## Financial Risk

**Working Capital** The Company's inventory days decreased to 50 days during 3QCY21 (3QCY20: 122 days) due to the efficient inventory management indicated by favorable offtake of fertilizer products. Receivable days remained stable at 32 days in 3QCY20. Payable days decreased significantly to 26 days (3QCY20: 76 days). Subsequently, the overall net cash cycle of the Company stood at 56 days in 3QCY21 (3QCY20: 78 days). The Company's short-term trade leverage and short-term leverage stood at ~33.8% and ~16.2% as of 3QCY21.

**Coverages** Free cash flows of the Company stood at ~PKR 26.2bln in 3QCY21 (3QCY20: ~PKR 14.7bln). The Company's finance cost stood at PKR 1.78bln in 3QCY21 (3QCY20: PKR 2.90bln). The increase in free cash flows and decreased finance costs resulted in significantly improved interest coverage of 19.2x in 3QCY21 (3QCY20: 5.8x). Debt coverage ratio witnessed similar trend and stood at 6.7x (3QCY20: 1.7x). Moreover, debt payback period witnessed improvement as well and stood at 0.3x (3QCY20: 1.0x).

**Capitalization** The Company has low leveraging with debt-to-debt + equity ratio standing at ~13% as of 3QCY21 (3QCY20: 27%). Total debt of the Company significantly decreased to ~PKR 14bln (3QCY20: ~PKR 30bln). The decrease represents the repayment of mainly short-term debt during the year. Overall, the capital structure of the Company remains very strong.



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Financial Summary

PKR mln

Fatima Fertilizer Company Limited Fertilizer	Sep-21 9M	Dec-20 12M	Sep-20 9M	Dec-19 12M	Dec-18 12M
<b>A BALANCE SHEET</b>					
1 Non-Current Assets	109,850	111,042	110,020	106,776	78,595
2 Investments	2,921	3,280	3,137	1,158	711
3 Related Party Exposure	10,353	6,442	6,437	6,416	10,225
4 Current Assets	50,801	36,792	37,184	40,767	20,420
a Inventories	14,433	13,531	13,367	11,518	5,028
b Trade Receivables	13,540	4,450	3,589	7,207	2,397
5 Total Assets	173,924	157,557	156,779	155,116	109,951
6 Current Liabilities	40,452	23,363	22,685	27,511	13,981
a Trade Payables	8,341	6,252	11,708	13,962	1,561
7 Borrowings	13,976	22,804	30,191	29,594	17,852
8 Related Party Exposure	-	-	-	-	-
9 Non-Current Liabilities	23,552	24,288	20,530	20,004	15,856
10 Net Assets	95,944	87,103	83,372	78,008	62,261
11 Shareholders' Equity	95,944	87,103	83,372	78,008	62,261
<b>B INCOME STATEMENT</b>					
1 Sales	76,770	71,267	46,448	74,964	45,964
a Cost of Good Sold	(43,262)	(42,473)	(25,074)	(47,065)	(19,483)
2 Gross Profit	33,508	28,795	21,375	27,899	26,481
a Operating Expenses	(7,019)	(7,259)	(5,185)	(6,579)	(5,728)
3 Operating Profit	26,489	21,535	16,190	21,320	20,754
a Non Operating Income or (Expense)	(2,222)	677	348	(366)	(793)
4 Profit or (Loss) before Interest and Tax	24,267	22,212	16,538	20,954	19,961
a Total Finance Cost	(1,776)	(3,469)	(2,902)	(3,761)	(1,450)
b Taxation	(8,400)	(5,468)	(4,073)	(5,124)	(5,238)
6 Net Income Or (Loss)	14,092	13,275	9,563	12,070	13,272
<b>C CASH FLOW STATEMENT</b>					
a Free Cash Flows from Operations (FCFO)	26,229	18,576	14,685	16,741	19,866
b Net Cash from Operating Activities before Working Capital Changes	24,411	14,841	11,516	13,582	17,620
c Changes in Working Capital	(5,924)	1,718	(313)	(6,704)	(1,912)
1 Net Cash provided by Operating Activities	18,486	16,559	11,202	6,879	15,708
2 Net Cash (Used in) or Available From Investing Activities	(6,146)	(3,489)	(2,230)	(10,322)	(10,644)
3 Net Cash (Used in) or Available From Financing Activities	(12,523)	(13,029)	(8,798)	3,241	(5,336)
4 Net Cash generated or (Used) during the period	(182)	41	174	(203)	(272)
<b>D RATIO ANALYSIS</b>					
1 Performance					
a Sales Growth (for the period)	43.6%	-4.9%	-17.4%	63.1%	0.0%
b Gross Profit Margin	43.6%	40.4%	46.0%	37.2%	57.6%
c Net Profit Margin	18.4%	18.6%	20.6%	16.1%	28.9%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	26.4%	28.5%	30.9%	13.4%	39.1%
e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/Sh	20.5%	16.1%	15.8%	17.2%	21.3%
2 Working Capital Management					
a Gross Working Capital (Average Days)	82	94	154	88	31
b Net Working Capital (Average Days)	56	42	78	51	18
c Current Ratio (Current Assets / Current Liabilities)	1.3	1.6	1.6	1.5	1.5
3 Coverages					
a EBITDA / Finance Cost	21.0	7.6	7.0	6.8	17.3
b FCFO / Finance Cost+CMLTB+Excess STB	6.7	2.0	1.7	1.3	2.6
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.3	0.7	1.0	1.2	0.7
4 Capital Structure					
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	12.7%	20.7%	26.6%	27.5%	22.3%
b Interest or Markup Payable (Days)	52.1	53.5	46.8	89.5	0.0
c Entity Average Borrowing Rate	8.8%	11.4%	12.0%	14.4%	7.7%

**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.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> 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.
AA-	
A+	
A	<b>High credit quality.</b> 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.
A-	
BBB+	
BBB	<b>Good credit quality.</b> 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-	
BB+	<b>Moderate risk.</b> 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+	
B	<b>High credit risk.</b> 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-	
CCC	
CC	<b>Very high credit risk.</b> 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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 surveil 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):

<p><b>Entities</b></p> <ul style="list-style-type: none"> <li>a) Broker Entity Rating</li> <li>b) Corporate Rating</li> <li>c) Financial Institution Rating</li> <li>d) Holding Company Rating</li> <li>e) Independent Power Producer Rating</li> <li>f) Microfinance Institution Rating</li> <li>g) Non-Banking Finance Companies (NBFCs) Rating</li> </ul>	<p><b>Instruments</b></p> <ul style="list-style-type: none"> <li>a) Basel III Compliant Debt Instrument Rating</li> <li>b) Debt Instrument Rating</li> <li>c) Sukuk Rating</li> </ul>
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(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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- (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)
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- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

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- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

### **Probability of Default**

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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