



The Pakistan Credit Rating Agency Limited

Rating Report

Engro Corporation Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2018	AA+	A1+	Stable	Maintain	-
27-Jun-2018	AA+	A1+	Stable	Upgrade	-
17-May-2017	AA	A1+	Stable	Maintain	-
22-Dec-2016	AA	A1+	Stable	Maintain	-
22-Dec-2015	AA	A1+	Stable	Upgrade	-

Rating Rationale and Key Rating Drivers

The ratings reflect Engro Corporation's ('Engro Corp') very strong risk profile. The HoldCo's diverse pool of investments previously under its three strategic pillars i.e. fertilizer, consumer goods and energy have been re-aligned to four strategic pillars i.e. agri-solutions, consumer, energy infrastructure and petrochemicals. Significant liquid resources post divestment of sizable stake in Efoods, EFert and Elengy Terminal allow Engro Corp to explore various investment avenues.

Engro Corp's existing portfolio has shown significant growth. While, EFert and EVopak continue as stable cash producers, EPolymer and Elengy have also joined the ranks. This has added the much needed diversity to the HoldCo's revenue streams which would further strengthen with increase in dividends.

Of late EPolymer has made a major turnaround owing to fundamental changes in the international industry dynamics supplemented by operational efficiencies. Given the strong demand in the local markets and the company's fortified position in the PVC industry, EPolymer is expected to reap full benefits of its planned expansion. Engro Corp has sizeable investment in energy chain through Engro Energy. Here, coal mining along with coal based power plant are the key projects.

Engro Corp is operating at a modest leverage signifying low financial risk. Its strategy to limit debt levels to fifty percent of its equity(excluding sovereign linked debt) at group level give comfort to its current ratings. The ratings also recognize the HoldCo's re-alignment of its organizational structure, which allows greater control over the strategic direction of its subsidiaries.

The ratings are dependent on the management's ability to execute its envisaged strategy of growth and expansion. Sustainability in the performance of subsidiaries as envisaged along with effective management of financial profile on a group-wide basis remains important.

Disclosure

Name of Rated Entity	Engro Corporation Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18),Methodology Holding Company (Jun-18)
Related Research	Sector Study Holding Company(Aug-18)
Rating Analysts	Adnan Dilawar adnan@pacra.com +92-42-35869504



Profile

Legal Structure Engro Corporation Limited is a public limited company listed on the Pakistan Stock Exchange. The Company is incorporated in Pakistan under the repealed Companies Ordinance, 1984 (now Companies Act, 2017).

Background Engro Corporation Limited was established in 1965 under the name Esso Pakistan Fertilizer Company Limited following the discovery of Mari gas field. Post exit of its foreign partners, it was renamed as Engro Chemical Pakistan Limited. To capitalize on its diverse status, it was converted to a holding company; Engro Corporation Limited in 2010.

Operations The principal activity of the Company is to manage investments in subsidiary companies, associated companies and joint ventures. It is engaged in fertilizers, PVC resin manufacturing and marketing, food, energy, LNG and chemical terminal and storage businesses.

Ownership

Ownership Structure As at Dec '17, Dawood Group holds a major stake of 45% in Engro Corp mainly through Dawood Hercules Corporation Limited (37%) and the rest through other corporate entities (7%) and individuals (1%). 14% is held by financial institutions and 41% is held by other corporate entities, general public and others.

Stability Ownership of the business is seen as stable as the major ownership vests with the sponsors i.e. Dawood Family.

Business Acumen DH Group is a conglomerate with over three generations of experience in commercial and social enterprises. Currently, the Group has interests in various sectors of the economy including Fertilizers, Foods, Power Generation, Technology, Financial Services, Chemical Storage, and Petrochemicals. Strong affiliation and technical track record with international JVs have added to the success of the companies within the Group.

Financial Strength Dawood Group's main holding companies are DH Corp and Dawood Lawrencepur Limited. The Groups' main investments in Engro Corp are consolidated in DH Corp while investments in energy sector are consolidated in Dawood Lawrencepur Limited. In addition, the Group's businesses include Cyan Limited (a listed entity, engaged in making equity investments in companies with high growth potential). Engro Corp has a strong consolidated asset base of ~ PKR373bln supported by an equity base of ~ PKR 181bln as at Sept-18. Consolidated Revenue stood at ~ PKR 115bln for 9MCY18.

Governance

Board Structure BoD has ten members. All except the CEO are non- executive. It has two independent members including one female director.

Members' Profile The Board is chaired by Mr Hussain Dawood, the patriarch of Dawood Family. He is a Pakistani businessman and ardent philanthropist and chairs an array of profit and not-for- profit ventures. Lately, Khawaja Iqbal Hassan, Rizwan Diwan and Raihan Merchant have been elected as directors in place of Muneer Kamal, Imran Sayeed and Inam-ur-Rehman. All members are seasoned professionals having experience in energy, chemical, technology and financial sectors.

Board Effectiveness The BoD has three committees to assist the board in governing the affairs of the company. These comprise: a) Board People's Committee, b) Board Audit Committee, and c) Board Investment Committee. During CY18, BoD met eight times, Audit Committee met six times, People's Committee ten times and Investment Committee eight times.

Financial Transparency Engro Corp's External Auditors are A.F. Ferguson & Co since 2010 and have issued an unmodified auditor's report on CY17 financial statements.

Management

Organizational Structure The Company has instituted a well-designed organizational structure comprising of separate departments for Finance, Strategy, Information Systems, Internal Audit, Human Resources, Engro Central and Technical, Corporate Communication, Legal and Public Affairs. The subsidiaries have independent management teams and organizational structure. This structure specifically caters to monitoring performance of its subsidiaries, devising strategy and HR policy for the Group as a whole.

Management Team Mr. Ghias Khan took over as CEO in Dec '16. He has been associated with Dawood group for over fifteen years.

Effectiveness Engro Corp has an Executive Committee (ExCom) which is chaired by the CEO. The members of the committee include CEOs of its' subsidiary companies, the Engro Corp's CFO, CHRO and CSO which enables efficacious management of the Group as a whole. Further, Engro Corp established a CFO Forum, which is chaired by the CFO of Engro Corp and includes CFO's of all subsidiaries.

MIS Engro Corp generates a standardized MIS report for its Board members quarterly - Dashboard - which provides a structured breakdown of information on predetermined key indicators (including business performance evaluation, significant business related events, health and safety statistics for each subsidiary and human resource utilization) for the Company as a whole as well as each Group entity individually.

Control Environment Internal Audit Department (IAD) has been established at all Engro Group companies which reports to the Board Audit Committee of the Company.

Business Risk

Industry Dynamics Holding companies are an emerging phenomena in Pakistan. Some operating companies that held strategic investments, for the purpose of diversification and growth, eventually de-merged from their operations and structured itself so that holding companies could concentrate their investments for the purpose of business growth and diversification.

Relative Position Engro Corp's enjoys a sizable position in the universe of Holding Companies. The Company's fertilizer business is ranked among top fifty fertilizer manufacturers in the world. The dairy business is the market leader in Pakistan's UHT market and number 2 dairy dessert brand serving over 12 million consumers. In Chemical Storage and Handling business, the Company has set up Pakistan's first LNG receiving terminal, and an integrated bulk liquid chemical & LPG terminal. The energy side of the Company is operating Pakistan's first 217MW power plant on permeate gas. The mining business in a JV with the Government of Sindh and CMEC, is developing Pakistan's first open-pit coal mine.

Revenues The Company's standalone topline comprises dividend and royalty income from its subsidiaries and joint ventures. Dividend income decreased by 10% amounting to PKR 6.8bln in 9MCY18 (9MCY17: PKR 7.6bln). Royalty income increased by 27% closing in at PKR 680mln in 9MCY18 (9MCY17: PKR 536mln). Consolidated revenue grew by 33% from PKR 86bln in 9MCY17 to PKR 115bln in 9MCY18 on the back of improved fertilizers and petrochemicals performance.

Margins On a standalone basis, Operating Margin decreased to 26% for 9MCY18 as compared to 28% same period last year, owing to lower dividend income and increased administrative expenses. Other income supported the bottom line by PKR 3,398mln which is derived from money market instruments. As a result, Net Profit Margin increased to 94% for 9MCY18 as compared to 80% same period last year owing to lower effective tax rate and finance cost. On a consolidated basis, Gross Profit Margin increased to 31% for 9MCY18 as compared 28% same period last year. In line with this increase, Net Profit increased to 16% for 9MCY18 as compared to 13% same period last year. This increase is due to increase in topline on the back of improved performance of fertilizers and petrochemicals segments.

Sustainability Going forward, Engro Corp is working towards delivering on projects, while exploring opportunities. Newly established dividend stream from Elengy Terminal is expected to reduce with 24% divestiture of stake in the Company.

Financial Risk

Working Capital On a consolidated basis, the Company holds sizeable liquid investment (~PKR 71bln) in the form of money market instruments, as at Sept' 18. Short-term running finances availed by the Group from various banks under mark-up arrangements amount to ~PKR 7bln.

Coverages Interest coverages improved to 7.3x as at Sept' 18 (from 5.3x as at Dec' 17) on the back improved FCFO and reduced finance cost. Engro Corp has PKR 71bln as liquid resources which provides extra cushion against the company's high quantum of borrowings.

Capitalization Engro Corp's standalone borrowings comprise Islamic Rupiya Certificates II that amount to PKR 1bln (Sept '18). These are secured Ijaratul Musha & Murabaha Sukuk certificates having a tenure of 60 months with a profit rate of 13.5% per annum payable semi-annually maturing on July 10, 2019. Engro Corp's consolidated borrowing (including current maturity of long-term debts) stood at PKR 122bln at end Sept '18 compared to PKR 101bln at end Dec '17. Leveraging increased as debt:capital moved from 37% on Dec '17 to 40% on Sept '18. Increase is majorly attributable to Engro Powergen Thar (Private) Limited under its on-going projects.



Engro Corporation Limited - Consolidated

BALANCE SHEET	30-Sep-18	30-Dec-17	30-Dec-16	31-Dec-15
	9MCY18	Annual	Annual	Annual
Non- Current Assets	191,516	164,441	142,035	134,593
Investments	102,649	102,074	34,701	17,170
Current Assets	78,661	57,437	113,597	44,529
Total Assets	372,825	323,953	290,333	196,292
Borrowings	122,329	100,932	78,653	36,993
Other Liabilities (Excluding Borrowings)	69,238	51,947	42,589	73,626
Shareholder's Equity	181,258	171,074	169,091	85,673
Total Liabilities & Equity	372,825	323,953	290,333	196,292
INCOME STATEMENT				
Turnover	114,644	128,593	157,208	184,264
Operating Profit	26,368	23,166	20,184	36,892
Other Income	3,498	9,387	67,763	1,019
Financial Charges	(3,648)	(5,131)	(6,038)	(8,425)
Net Income	17,853	16,290	73,598	17,268
Cashflow Statement				
Free Cashflow from Operations (FCFO)	26,495	27,421	21,156	39,055
Net Cash from Operating Activities	13,698	21,120	4,070	5,966
Net Cash from Investing Activities	4,381	(9,021)	1,940	25,102
Net Cash from Financing Activities	17,057	3,186	11,233	(28,300)
Ratio Analysis				
Gross Margin	31%	27%	23%	28%
ROE	10%	10%	44%	20%
FCFO/Gross Interest	7.3	5.3	3.5	4.6
LT Debt/FCFO	3.0	2.9	2.9	0.9
Total Debt/Total Debt+Equity	40%	37%	32%	30%

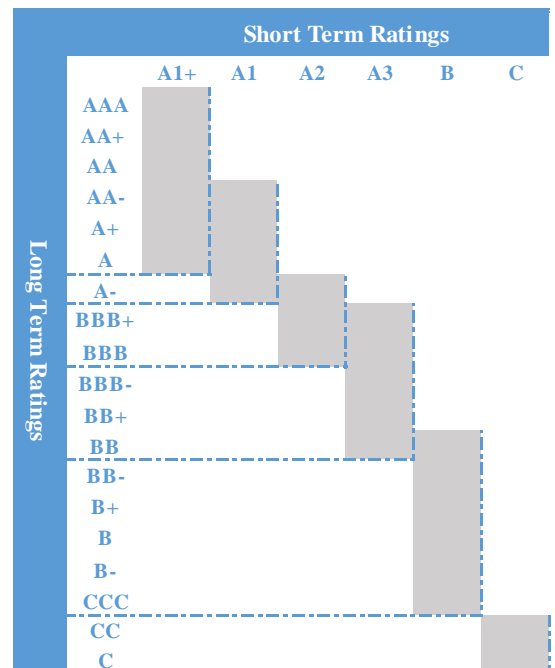
Engro Corporation Limited - Consolidated

Dec-18

Credit Rating Scale & Definitions

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

Long Term Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
AA+ 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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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

Rating Watch Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

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

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

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

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

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

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

Probability of Default

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

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