



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
27-Dec-2019	AA+	A1+	Stable	Maintain	-
28-Jun-2019	AA+	A1+	Stable	Maintain	-
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	-
13-Jan-2015	AA-	A1+	Positive	Maintain	-
17-Jan-2014	AA-	A1+	Stable	Upgrade	-

Rating Rationale and Key Rating Drivers

The ratings reflect Engro Corporation's ('Engro Corp' or "the Company") established position as a conglomerate with a diverse pool of investments under four verticals: food and agriculture, petrochemicals, energy and related infrastructure, and telecommunication infrastructure. Engro Corp's various investments in diversified sectors exhibit strong performance and profitability.

Respective businesses under the Umbrella of the Holdco exhibit their strength through continued growth trajectory in 9MCY19 despite challenging economic environment. Engro Fertilizer ('Efert'), being the second largest in the fertilizer sector, increased its market share and is expected to remain stable. Engro Polymer and Chemical ('EPolymer') has a fortified position in the local PVC industry with capacity enhancements in progress and new Hydrogen Per Oxide project on the cards. The sizeable investments in the energy chain, through Engro Energy, have progressed in a timely manner. EFert, and EPolymer announced higher dividends compensating for no dividend from Engro Elengy Terminal ('Elengy') after the Group's divestment of 24% stake in the business. EVopak continued as a stable cash producer. Engro Corp has a low leveraged capital structure, very strong coverages and liquidity signifying its robust financial profile. Its ability to limit debt levels to fifty percent of its equity (excluding sovereign linked debt) at group level provides comfort to ratings. The ratings factor in HoldCo's strong organizational structure, designed to control the strategic direction of its subsidiaries, and strong governance framework.

The ratings are dependent on the management's ability to execute its envisaged strategy of growth and expansion. Sustainability in the performance of subsidiaries reflecting stable dividends and effective management of financial profile. Meanwhile, effective utilization of liquid assets to enhance investment portfolio is 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-19),PACRA_Methodology_Holding Company_FY19(Jun-19),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria Rating Modifier(Jun-19)
Related Research	Sector Study Holding Company(Aug-19)
Rating Analysts	Ayesha Malik ayesha.malik@pacra.com +92-42-35869504



Profile

Legal Structure Engro Corporation Limited ("Engro Corp" or "The Company") 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 into a holding company, Engro Corporation Limited, in 2010.

Operations The principal activity of the Company is to make and manage investments in subsidiary companies, associated companies and joint ventures. The group's business portfolio spans across various sectors including chemical fertilizers, PVC, food, power generation, coal mining and LNG storage.

Ownership

Ownership Structure Dawood Group holds ~46% stake in Engro Corp, through Dawood Hercules Corporation Limited (~37%), related corporate entities (~7%), and individuals of Dawood family (~2%). Around 15% is held by financial institutions and 40% is held by corporate entities, general public and others.

Stability Ownership of the business is seen as stable as its major shareholding 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 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's main investments in Engro Corp are consolidated in DH Corp while investments in energy sector are consolidated in Engro Corp and Dawood Lawrencepur. Engro Corp has a strong consolidated asset base of ~PKR482bln supported by an equity base of ~PKR 195bln as at Sep19. Consolidated Revenue stood at ~PKR 149bln and Profit After Tax at ~PKR101bln for the nine month period ended Sep19.

Governance

Board Structure BoD has ten members. All members, except the CEO, are non-executive. The board has three members from the Dawood family and six independent directors.

Members' Profile The Board is chaired by Mr Hussain Dawood, the patriarch of Dawood Family. He is a businessman and philanthropist and chairs an array of profit and not-for-profit ventures. During CY18, Khawaja Iqbal Hassan, Rizwan Diwan and Raihan Merchant have been elected as directors. All members are seasoned professionals with experiences in energy, chemical, technology and financial sectors, bringing a diverse range of requisite skills to the BoD.

Board Effectiveness The BoD has three committees to assist in governing the affairs of the Company. These comprise: a) Board People's Committee, b) Board Audit Committee, and c) Board Investment Committee. During 9MCY19, BoD met six times, Strong committee structure and majority of independent directors bodes well for the governance structure.

Financial Transparency The Company's External Auditors, A.F. Ferguson & Co, issued an unmodified opinion on CY18 financial statements.

Management

Organizational Structure The Company has instituted a well-designed organizational structure to cater to its needs as a HoldCo. It comprises 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 structures. This structure specifically caters to performance monitoring of subsidiaries, formulating strategy, and investments opportunities.

Management Team Mr. Ghias Khan took over as CEO in Dec16. He has been associated with Dawood group for over fifteen years and has an overall experience of more than 18 years.

Effectiveness Engro Corp has an Executive Committee, which includes CEOs of all its' subsidiary companies, Engro Corp's CFO, Chief HR Officer and Chief Secretary Officer. This is chaired by the CEO for efficacious management of the Group as a whole. Further, Engro Corp established a CFO Forum chaired by the CFO of Engro Corp and includes CFOs of all subsidiaries to discuss various finance related matters.

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 the Group.

Control Environment Internal Audit Department has been established at all Engro Group companies, which reports to the Board Audit Committee of the their respective boards as well as Engro Corp.

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 into holding companies to concentrate their investments for the purpose of business growth and diversification.

Relative Position Engro Corp has a sizable position in the universe of Holding Companies. The fertilizer business is the second largest producer in Pakistan. The PVC business is the sole producer of PVC catering to 66% of the total domestic PVC demand. The dairy business is the market leader in Pakistan's UHT market and number 2 dairy dessert brand serving over 12 million consumers. The Company operates 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. The Company is also developing Pakistan's first open-pit coal mine.

Revenues The Company's standalone topline comprises of dividend and royalty income from its investments. This has increased by 12% amounting to PKR ~8bln in 9MCY19 (9MCY18: PKR ~7bln). This was driven by a QoQ surge in dividend income to PKR 7,673mln (9MCY18: PKR 6,808mln). Royalty income also showed a 15% QoQ increase clocking in at PKR 780mln (9MCY18: PKR 680mln) owing to increased turnover by EFerts.

Margins On a standalone basis, operating margin decreased to 72% in 9MCY19 (9MCY18: 81%) owing to relatively higher administrative expenses. Income from money market instruments, lower effective tax rate and finance cost supported the bottom line to stand at ~PKR 9,424mln for 9MCY19 (~PKR 9,046mln for 9MCY18). On a consolidated basis, gross profit margin increased slightly to 30% for 9MCY19 (9MCY18: 29%) on the back of improved performance of Epolymer and EFert. However, significant increase in finance costs led net profit margin to post a dip by 1% on consolidated basis.

Sustainability During 9MCY19, energy projects were completed and a new investment of up to PKR 7.5bln in the telecom sector was announced through Enfrashare, a wholly owned subsidiary of Engro Infiniti. Further, Engro Energy Limited has announced investment in solar power plants of 50MW each in Balochistan for \$144mln, to be financed through a debt to equity ratio of 80:20 (Commercial Operation Date: Jun20).

Financial Risk

Working Capital On a consolidated basis, the Company holds sizeable liquid investment (~PKR 89bln) in the form of money market instruments. Short-term running finances availed by the Group from various banks under mark-up arrangements amounted to ~PKR 10bln (Sep19) only.

Coverages Engro Corp has sizeable liquid resources of PKR 89bln, which provide cushion against borrowings or any upcoming repayments. This is in addition to stable cash flows in form of dividends.

Capitalization Engro Corp's standalone borrowings comprise lease liabilities of PKR 856mln (9MCY19). Engro Corp's consolidated borrowing stood at ~PKR 131bln as at Sep19. Leveraging marginally increased as debt to equity moved from 40% as at Sep18 to 45% (Sep19). Increase is majorly attributable to loans in Engro Powergen Thar (Private) Limited under its on-going projects.



The Pakistan Credit Rating Agency Limited

Engro Corporation Limited (ECL) [Unconsolidated]

BALANCE SHEET

	Sep-19 9M	Dec-18 Annual	Sep-18 9M	Dec-17 Annual	Dec-16 Annual
	<i>Management</i>	<i>Audited</i>	<i>Management</i>	<i>Audited</i>	<i>Audited</i>
Non-Current Assets	2,155	623	645	515	167
Investments (Incl. associates)	87,114	89,141	86,545	85,985	88,945
Inventory	-	-	-	-	-
Total Assets	97,452	92,576	92,569	88,680	91,033
Borrowings	836	-	-	-	-
Total Liabilities (Excluding Borrowings)	11,779	7,473	9,474	5,298	6,992
Shareholder's Equity	84,837	85,103	83,095	83,383	84,040
Total Liabilities & Equity	97,452	92,576	92,569	88,680	91,032

INCOME STATEMENT

Turnover	8,454	11,233	7,488	13,891	8,306
Other Income	1,630	1,630	1,630	1,630	1,630
Operating Profit	6,111	8,228	6,072	11,957	7,179
Financial Charges	(165)	(149)	(115)	(358)	(559)
PBT	11,566	16,676	9,353	15,833	63,032
Tax	(2,142)	(3,956)	(2,307)	(4,433)	(1,168)
PAT	9,424	12,720	7,046	11,400	61,864

Cashflow Statement

EBITDA	12,121	16,889	6,104	16,329	63,057
Free Cashflow from Operations (FCFO)	11,528	15,713	4,395	14,977	63,094
Net Cash from Operating Activities	(3,494)	15,677	(2,971)	(4,753)	7,189
Net Cash from Investing Activities	(24,299)	33,197	25,064	31,536	30,667
Net Cash from Financing Activities	(6,339)	(11,101)	(3,584)	(15,009)	(14,042)

Ratio Analysis

Operating Margin	72.3%	73.2%	81.1%	86.1%	86.4%
ROE	11.1%	14.9%	8.5%	13.7%	73.6%
Capital Structure (Total Debt/Total Debt+Equity)	0.9%	0.0%	0.0%	0.0%	0.0%

Engro Corporation Limited (ECL) [Unconsolidated]

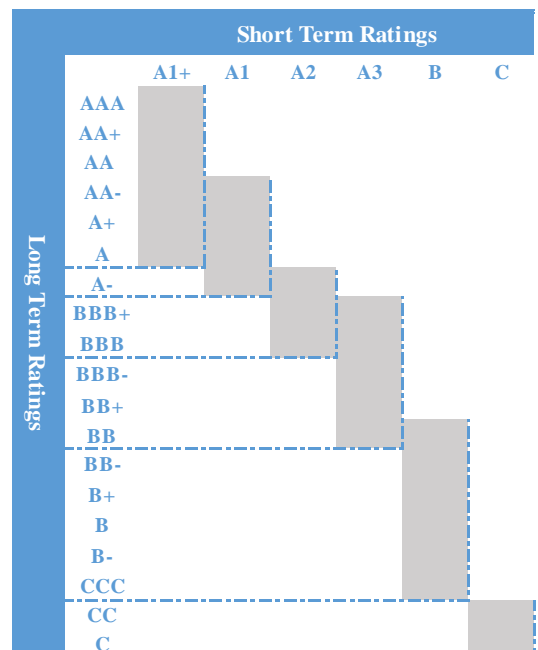
Dec-19

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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

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)

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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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