The Pakistan Credit Rating Agency Limited

Rating Report

Nishat Paper Products Company Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
17-Feb-2023	A	A1	Stable	Maintain	-
17-Feb-2022	A	A1	Stable	Maintain	-
17-Feb-2021	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Nishat Paper Products Co Ltd.'s ("NPPCL" or the "Company") ratings reflect the strong sponsor profile, satisfactory market position, and adequate financial profile of the Company. The demand for the cement packaging segment is directly linked with cement dispatches. The latest period reported a reduction in cement production reflecting an economic downturn. The increase in prices of all the construction materials has impacted demand for cement as well. However, cement's demand is expected to come in the full circle once the macro-level fundamentals improve. Through, industry-wide volumetric decrease in sales has been reported but the selling prices have absorbed the impact too much extent. While considering the depleting revenues of the country, the supply chain of the Company has also been impacted as the raw material is ~95% imported. However, being the subsidiary of D.G. Khan Cement Company Limited, NPPCL derives strength and economies of scale from the parent company, which bodes well for the ratings. Furthermore, the industry is also diverging more towards PP bags as these are less costly compared to KP bags. Currently, the Company has a production capacity of 220mln bags/per annum and operating at a capacity level of ~40% during FY22 (FY21: ~60%).
The Company has maintained adequate margins and profitability. The top line of the Company decreased by ~22.9% during FY22. The Company has generated a topline of ~ PKR 3,070mln in FY22 as compared to ~PKR 3,980mln in FY21. During FY22, Nishat Paper Products Company Limited generated a humble bottom line of ~PKR 292mln (FY21: ~PKR 525mln). The decline in profitability is attributable to PKR depreciation and increased commodity prices and finance cost. The Company has leveraged capital structure. Long-term debt is related to expansion activities, whereas short-term debt has increased substantially pursuant to slow movement in receivables. However, the majority of receivables are from the related party which gives comfort to the credit risk. Going forward, the Company is planning to diversify its revenue stream by introducing a new product line that would support the Company in stable profitability.

The ratings would remain dependent upon the company's ability to sustain its healthy business profile amidststrong competition, herein, effective and prudent management of financial risk indicators remainimportant. Moreover, upholding of governance framework is vital.

Disclosure

Name of Rated Entity	Nishat Paper Products Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Paper and Packaging(Nov-22)
Rating Analysts	Muhammad Atif Chaudhry | Atif.Chaudhry@pacra.com | +92-42-35869504

Profile

Legal Structure Nishat Paper Products Company Ltd("NPPCL" or the "Company") is a Public Limited Company incorporated under the repealed Companies Ordinance 1984, on 23 July, 2004.

Background Nishat Paper Products Company Ltd was a Joint venture project of Nishat with Shuaiba Paper Products Company Ltd. Kuwait (Shuaiba). The Primary purpose of the project was the vertical integration in Cement business for supply of paper sacks for cement packaging. D G Khan Cement Company Ltd. (DGKCC) and Shuaiba entered into an agreement on 12th June 2004 for setting up a paper sack plant in Pakistan, but later in June 2008, Nishat acquired the stake from Shuaiba Paper. Now NPPCL is subsidiary of D.G. Khan Cement Company Ltd.

Operations The Company is engaged in the manufacturing and sale of paper packaging material with annual production capacity of 220 million bags. The plant is situated adjacent to D.G. Khan Kairpur cement unit, in District Chakwal, in close proximity of some other big cement producers.

Ownership

Ownership Structure NPPCL shareholding is primarily vests with DG Khan Cement (55%) and Nishat Mills Ltd (25%). Among the sponsoring family, major ownership is with Mrs. Naz Mansha 6%, Mr Umer Mansha and Mr Hassan Mansha 4% each. Nishat Mills Ltd has 25% of shareholding in DG Khan Cement. Thus ultimate shareholding remained with Nishat Group.

Stability Nishat being largest and most diversified Industrial house in South East Asia, with assets base over PKR 300 bln. Whereas, DG Khan cement is one of the largest cement players in the industry.

Business Acumen Nishat is considered at par with multinationals operating locally in terms of its quality of products, services and management skills. The sponsors through their vast experience, have become reliable partner for the packaging industry. Mian Mansha, man behind the whole setup of Nishat Group, has a long success story which provides a strong base for the NPPCL.

Financial Strength The Financial strength of the sponsors is sufficient to support the Company in the times of crises. DG Khan Cement is AA-/A1+rated by PACRA. DG Khan Cement has ~PKR 136.5bln assets and ~PKR 69.9bln equity with a revenue of ~PKR 58bln during FY22.

Governance

Board Structure The Board consists of seven members. There is also a female representation on the board. There are four executive directors, and two non-executive directors on Board. But no Independent representation. However, being the subsidiary of a listed company independence oversight is compensated.

Members' Profile The Board, with a diversified background and expertise of its members, is a key source of oversight and guidance for the management. The Chairman, Mian Raza Mansha, also holds the position of CEO in the company. He has been associated with the Company since last 16 years.

Board Effectiveness The minutes of the Board meetings are well documented. The Board has no formal committees to assist the board.The quality of minutes reflects the involvement of all directors in the agenda items. Total four meetings were held during the outgoing year and attendance was well sufficient in the meetings.

Financial Transparency M/s KPMG Taseer Hadi & Co. are the external auditors of the company. They have expressed an unqualified opinion on the financial reports for FY22. The firm is QCR rated by ICAP and is in the A Category of SBP's panel of auditors.

Management

Organizational Structure To perform well, NPPCL has structured and organized its organogram as per the operational needs. The Company operates through Procurement, Sales and Marketing, Finance and Accounting, production and Technical department and Administration Departments.

Management Team The Company has a set of experienced & professional management. The Company's CEO, Mian Raza Mansha has more than 24 years diversified professional experience in various business sectors including Banking, Textile, Power, Cement, Insurance, Hotels, Properties, Natural Gas, Agriculture, Dairy etc. He received his Bachelor degree from the University of Pennsylvania, USA. Currently he is on the Board of ten other companies.

Effectiveness Management's effectiveness and efficiency can be ensured through the presence of management committees. At NPPCL, management committees are not in place. Thus, indicating a room for improvement.

MIS NPPCL manufacturing facilities in Chakwal is connected with the Company's Head Office in Lahore through an ERP(Oracle based customized system). To facilitate the management, various reports related to Finance, Sales, HR, Production and Import are generated on daily and monthly basis. Other customized reports can be generated on ad hoc basis. Frequecny of these reports may alter as per the managements requirement.

Control Environment The Company has an internal audit function in place, with effective mechanism for identification, assessment and reporting of all types of risks arising out of the business operations. This function is necessary to provides support, guidance and monitoring of the internally placed SOPs along with conducting Gap Analysis for evaluating already placed policies and procedures.

Business Risk

Industry Dynamics Pakistan's packaging industry consists of four major segments, paper, plastic, tinplate and glass. Paper and plastic segments occupy the major share in total market. NCCPL operates under paper segment of the Industry. The demand of this segment is directly correlated with cement production. The segment's direct costs consist largely of imported raw materials. Therefore, volatility in exchange rates and international price trends has an impact on costs. The international price of major raw material has significantly increased. Henceforth, the industry is also focusing on pp bags as these are less costly compared to KP bags. The average margins of the paper packaging industry have shown a positive trend since FY21, with average gross margins rising from ~13% in FY21 to ~16% in FY22.

Relative Position NPPCL is one of the main players in the industry. Large market players in the paper segment are Cherat Packing Ltd (production capacity 660mln bags/annum), Thal Ltd (production capacity 356mln bags/annm). The utilization capacity of the plant is ~40% during FY22.

Revenues The Company generates revenue by selling paper sacks to cement manufactures. Major customers are DG Khan Cement, Best Way cement, Lucky Cement, Attock Cement, Kohat Cement, and Maple leaf Cement. Top 3 Customers are generating more than ~80% of the total revenue. DG Khan Cement contributes above ~50% of total revenue. During FY22, the Company generated a revenue of ~PKR 3.07bln vs ~PKR 3.98bln during FY21, showing decrease of ~29.6% YoY.

Margins Kraft paper and Chemical wood pulp is one of the main raw materials in production of paper packaging. Approximately 95% of raw material is imported across the world. The variation in exchange rate has a significant impact on the cost part. The Company production is demand based, the overall revenue are decreased due to decrease in production. Significant increase in cost of sales resulted a decrease in the Company's gross margins (FY22: ~21.8% vs FY21: ~25%). In the result, Net Margin also decreased to ~9.5% FY22 vs ~13.2% FY21.

Sustainability The Company is a subsidiary of DG Khan Cement and came into existence as a result of vertical integration into supply chain line. The main purpose of the Company is to supply packaging material to the parent Company.

Financial Risk

Working Capital The Company's working capital management is supported through short-term running finance facility obtained from a consortium of banks. NPPCL inventory days stood on higher side at ~89 days during FY22 (FY21: ~66 days), the receivable days increased to ~163 days (FY:21 ~153 days), this is due to overall conservative market condition. Resultantly, the net working capital days significantly increased to ~248 days during FY21 (FY20: ~218 days).

Coverages In FY22, the Company's FCFO's stood at ~PKR 519mln decreasing from ~PKR 837mln in FY21. The FCFO/Finance cost also showed a decrease from ~4.3x of coverage at end of FY21 to ~ 3.0x at end of FY22; however, this is still a healthy coverage level for the Company. While the Company does take on both shortterm and long-term financing from financial institutions, the strategy is to keep the Company mainly equity-focused, thus the finance cost is planned to be on a manageable scale moving forward.

Capitalization The Company has a moderate-leveraged structure, with long-term liabilities being ~28.7% of equity at end of FY22 and ~37.8% of equity at end of FY21. Its gearing ratio has decreased from ~61.7% at the end of FY21 to ~40.2% at the end of FY22, while it has remained at ~66.8% in FY20.

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Financial Summary
PKR mln

Nishat Paper Products Company Limited Paper and Packaginig	Jun-22 12M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	1,338	1,399	1,441	1,501
2 Investments	0	0	-	-
3 Related Party Exposure	190	173	144	144
4 Current Assets	2,903	4,371	3,598	3,821
a Inventories	*811*	*683*	*766*	*1,496*
b Trade Receivables	*1,030*	*1,715*	*1,630*	*844*
5 Total Assets	4,431	5,943	5,183	5,466
6 Current Liabilities	408	332	404	493
a Trade Payables	*36*	*25*	*14*	*16*
7 Borrowings	1,492	3,297	3,060	3,360
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	314	268	195	209
10 Net Assets	2,216	2,046	1,524	1,404
11 Shareholders' Equity	2,216	2,046	1,524	1,404
B INCOME STATEMENT				
1 Sales	3,070	3,980	4,273	4,057
a Cost of Good Sold	*(2,400)*	*(2,986)*	*(3,588)*	*(3,567)*
2 Gross Profit	670	994	685	490
a Operating Expenses	(54)	(31)	(14)	(14)
3 Operating Profit	616	963	671	475
a Non Operating Income or (Expense)	*(11)*	*(52)*	*(41)*	*(53)*
4 Profit or (Loss) before Interest and Tax	605	911	630	422
a Total Finance Cost	*(173)*	*(197)*	*(449)*	*(298)*
b Taxation	*(140)*	*(189)*	*(50)*	*(65)*
6 Net Income Or (Loss)	292	525	131	59
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*519*	*837*	*656*	*235*
b Net Cash from Operating Activities before Working Capital Changes	*346*	*595*	*232*	*9*
c Changes in Working Capital	*570*	*219*	*80*	*(1,355)*
1 Net Cash provided by Operating Activities	917	814	312	(1,345)
2 Net Cash (Used in) or Available From Investing Activities	(35)	(31)	(11)	(13)
3 Net Cash (Used in) or Available From Financing Activities	(261)	(20)	(132)	223
4 Net Cash generated or (Used) during the period	622	763	169	(1,135)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-22.9%	-6.9%	5.3%	35.5%
b Gross Profit Margin	21.8%	25.0%	16.0%	12.1%
c Net Profit Margin	9.5%	13.2%	3.1%	1.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	35.5%	26.5%	17.2%	-27.6%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	13.7%	29.4%	9.0%	4.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	252	220	202	168
b Net Working Capital (Average Days)	248	218	201	166
c Current Ratio (Current Assets / Current Liabilities)	7.1	13.1	8.9	7.7
3 Coverages				
a EBITDA / Finance Cost	3.5	5.0	1.5	1.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.4	0.8	0.7	0.4
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.5	2.1	5.9	-15.5
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	40.2%	61.7%	66.8%	70.5%
b Interest or Markup Payable (Days)	40.2	44.2	0.0	0.0
c Entity Average Borrowing Rate	7.1%	6.1%	13.9%	11.0%

Credit Rating

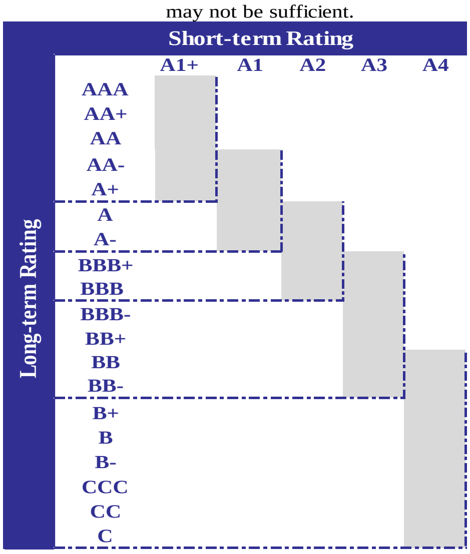
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

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

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

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

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

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 | Clause 11-(A)(p).
(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