



The Pakistan Credit Rating Agency Limited

**Rating Report**

**Pioneer Cement Limited**

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Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Sep-2019	A	A1	Negative	Maintain	-
29-Mar-2019	A	A1	Stable	Maintain	-
18-Dec-2018	A	A1	Stable	Maintain	-
07-May-2018	A	A1	Stable	Maintain	-
28-Dec-2017	A	A1	Stable	Maintain	-
21-Jun-2017	A	A1	Stable	Maintain	-
02-Nov-2016	A	A1	Stable	Initial	-

**Rating Rationale and Key Rating Drivers**

The revision in the outlook is attributable to the decline in margins, pressure on profitability and financial risk matrix. Pioneer Cement has been operating a single manufacturing facility. The Company’s sales are majorly driven by local market fundamental – trend followed by all cement players in north region. During FY19, industry dynamics especially for cement players operating in north region have shifted significantly on account of fluctuating cement prices, increase in FED on coal import and depreciation in Pak Rupee against other currencies. Along with these factors, slow local demand has affected the company's sales. The Company is pursuing announced brown-field expansion – clinker 2.4mln tpa – expected to commence in a month or so. Also, 12MW WHRPP and 24MW coal power plant are part of this project - deemed to bring operational efficiencies. The Company's business performance in muted; local demand remains vital with focus on sustaining margins. Optimal capacity utilization and adequate channeling of volumes from upcoming new line are necessary to support financial risk profile. Leveraging has surged on account of debt-driven expansion. The ratings draw comfort from sponsor's financial strength.

The ratings are dependent on the management's ability to (i) improve margins, and (ii) optimal utilization of existing line. Timely repayment of long term financing is essential for the ratings. The company's business performance in current stretched economic scenario - challenges on demand front - remains vital.

Disclosure	
<b>Name of Rated Entity</b>	Pioneer Cement Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Criteria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
<b>Related Research</b>	Sector Study   Cement(Apr-19)
<b>Rating Analysts</b>	Usama Zubair   usama.zubair@pacra.com   +92-42-35869504

## Profile

**Legal Structure** Pioneer Cement is a listed Company with its shares traded on Pakistan Stock Exchange Limited (PSX). The Company's shares are quoted under the Cement Sector.

**Background** Pioneer Cement was incorporated in 1986. It is headquartered in Lahore, Pakistan and the manufacturing facility is located at Chenki-District Khushab. Its location in central Punjab allows easy and fast approach to market. The main markets of the company are adjoining areas of Punjab and Khyber-Pakhtunkhwa. Pioneer operates with two production lines having a combined annual cement capacity of 2.09mln tons (CoD: Line I - 1994, Line II - 2006).

**Operations** Pioneer Cement is engaged in the manufacturing and sale of Ordinary Portland Cement. The company has a limited product slate and currently it is selling Ordinary Portland Cement (OPC).

## Ownership

**Ownership Structure** Vision Holding Middle East Limited (VHMEL) is an offshore SPV of Vision Holding Trust (VHT). VHMEL holds majority stake (47%) in Pioneer Cement and remaining shares of the company are held by various financial institutions and general public.

**Stability** Ownership structure of the Company is seen as stable as no ownership changes are expected in near future. Majority stake will rest with the Vision Holding Middle East Limited (VHMEL).

**Business Acumen** Vision holding trust is 100% owned by Mr. Habibullah Khan – a renowned foreign entrepreneur. Apart from Cement, trust maintains interest in several sectors. The sponsors having a diversifiable universe of investments is considered to be a positive sign.

**Financial Strength** Given that Pioneer is a flagship entity of the sponsor, willingness to support the company in case the needs arises is considered high; also supplemented by access to capital markets.

## Governance

**Board Structure** The overall control of the company vests in eight member board of directors (BoD), including the CEO and three independent directors. Mr. Arif Hamid Dar last year was appointed Chief Executive Officer with effect from July 01, 2018.

**Members' Profile** Board members carry requisite technical skills which is abetted by diversified professional background of board members. Board meeting minutes are formally maintained and the attendance is considered good which bodes well for overall governance framework of the company.

**Board Effectiveness** The board has two committees to oversee the company's financial matters. These committees include: 1) Audit, and 2) Human Resource & Remuneration (HR&R). This is in compliance with the Code of Corporate Governance.

**Financial Transparency** M/s EY Ford Rhodes Chartered Accountants conducted the external audit services for Pioneer. They're in a 'A' category of SBP list of external auditors and has a QCR rating. They have expressed unqualified opinion on the financial statements for the year ended 30th June, 2018. The same performed interim review on the financial statements for the six months ending December, 2018.

## Management

**Organizational Structure** Pioneer Cement has a lean organization structure with the company's operations grouped under nine key functions. These include i) Administration, ii) Corporate Affairs, iii) Finance, iv) Human Resource, v) Information Technology, vi) Marketing, vii) Operations, viii) Supply Chain and ix) Internal Audit. All functional heads report to the CEO except for internal audit, which reports directly to the Audit committee of the board (in compliance with the requirement of law for listed companies).

**Management Team** During FY18, Mr. Syed Mazhar Iqbal retired from the position of MD/CEO resulting in appointment of Mr. Arif Hamid Dar as the new CEO. He is an experienced individual with diversified experience from several sectors including Auto, Fertilizer and Cement.

**Effectiveness** The CEO is supported by experienced professionals at key management positions having a long-term association with the company.

**MIS** Pioneer has deployed an oracle based ERP solution. The company's current operational modules include i) Inventory, ii) Purchasing, iii) Payables, iv) Receivables, v) Cash Management, vi) Fixed Assets, vii) General Ledger, and viii) Order Management.

**Control Environment** Pioneer's plant comprises of two lines wherein, Line I is a European technology (FLSmidth), and Line II is a mix of European and Chinese technology. Accredited with ISO 9001: 2008 and ISO 14001:2004 certification, Pioneer deploys advance technology to ensure production of quality cement.

## Business Risk

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

**Relative Position** Pioneer Cement is a mid-tier cement player, operating in north region. The company has operational cement capacity of 2.0mln tons per annum with existing market share of 4.5% in the north region. Furthermore, the company has announced clinker capacity expansion of 2.4mln tpa.

**Revenues** During 9MFY19, Revenue of PKR 7.4bln was recorded (9MFY18: PKR 7.5bln), down by 0.2% YoY. Sales mix remained tilted towards local market - in line with industry trend followed in north region. The company's capacity utilization level declined to 67% (9MFY18: 78%) – below the average capacity utilization level of the industry. Other income inched up to PKR 44mln (9MFY18: PKR 15mln) attributable to uptick in policy rate. Finance costs increased to PKR 288mln (9MFY18: PKR 79mln) on account of significant increase in long term finance. Consequently, PAT stood at PKR 825mln (9MFY18: PKR 1.15bln), down by 28% YoY.

**Margins** Pioneer's margins have significantly declined over the past year (gross: 23.5%, 9MFY18: 27.5%, operating: 9MFY19: 18.4%, 9MFY18: 25.0%). EBITDA margin also witnessed a dip YoY (9MFY19: 26.5%, 9MFY18: 31.8%) against industry average of 27%. Margins deterioration is a trend witnessed in performance of all players operating in north region primarily on account of instability in cement prices, muted local demand, increase in FED on coal import and Rupee Depreciation.

**Sustainability** The progress work on the under construction projects is at full swing. Most of the materials and equipment have already been received at the factory. Mechanical and electrical work is being carried out on parallel basis. The management is confident to achieve the commercial operations within the stipulated timelines. The production line will have an annual clinker capacity of 2.4mln tons. In addition to this, the company will establish coal based power plant (24MW) and WHRP. The estimated cost of these projects is PKR 25bln. The debt equity proportion will be 72:28 and new cement line is expected to commence in upcoming few months.

## Financial Risk

**Working Capital** Pioneer's working capital requirements represented by net cash cycle (net working capital days) – a function of inventory, receivables and payables - decreased to negative 32days (9MFY18: 9days). Cash cycle decreased on account of increase in payable days (9MFY19: 65days; 9FY18: 12days). The requirements were met through a mix of internal cash generation and short term borrowings. As at end-Mar19, STBs stood at PKR 4.4bln (9MFY19: PKR 1.3bln) attributable to enhanced working capital requirements.

**Coverages** During 9MFY19, FCFO remained largely same at PKR 1.6bln (9MFY18: PKR 1.5bln). Interest and Core coverage declined to 5.8x and 2.7x (end-Jun18: 16.9x and 3.3x) attributable to enhanced finance cost.

**Capitalization** In pursuit of expansion, the total leveraging (9MFY19: 61%, 9MFY18: 37%) increased tremendously as the Company acquired long term finance. Long term leveraging is not expected to increase any further. Short term borrowings to total borrowings also surged to 21.3% (9MFY18: 17.5%).



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Financial Summary

PKR mln

Pioneer Cement Cement	Mar-19 9M	Jun-18 12M	Jun-17 12M	Jun-16 12M
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#### A BALANCE SHEET

1 Non-Current Assets	33,665	22,962	12,281	10,431
2 Investments	912	1,086	2,694	2,425
3 Related Party Exposure	-	-	-	-
4 Current Assets	7,570	5,064	2,785	1,911
<i>a Inventories</i>	427	470	236	181
<i>b Trade Receivables</i>	510	434	225	108
5 Total Assets	42,147	29,111	17,760	14,768
6 Current Liabilities	3,457	1,636	802	1,108
<i>a Trade Payables</i>	2,703	868	182	140
7 Borrowings	21,155	10,705	2,307	645
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	4,006	3,141	2,404	2,345
10 Net Assets	13,530	13,629	12,248	10,670
11 Shareholders' Equity	13,530	13,629	12,248	10,670

#### B INCOME STATEMENT

1 Sales	7,489	10,121	10,631	9,367
<i>a Cost of Good Sold</i>	(5,730)	(7,311)	(6,203)	(5,361)
2 Gross Profit	1,759	2,811	4,428	4,005
<i>a Operating Expenses</i>	(377)	(264)	(179)	(142)
3 Operating Profit	1,381	2,546	4,250	3,864
<i>a Non Operating Income or (Expense)</i>	44	(241)	(147)	(7)
4 Profit or (Loss) before Interest and Tax	1,425	2,305	4,102	3,857
<i>a Total Finance Cost</i>	(288)	(95)	(35)	(17)
<i>b Taxation</i>	(313)	(569)	(1,152)	(1,328)
6 Net Income Or (Loss)	825	1,642	2,916	2,511

#### C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	1,589	1,521	2,915	2,667
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	783	1,325	2,907	2,641
<i>c Changes in Working Capital</i>	(61)	254	(1,164)	483
1 Net Cash provided by Operating Activities	722	1,579	1,743	3,124
2 Net Cash (Used in) or Available From Investing Activities	(10,100)	(9,051)	(2,429)	(2,729)
3 Net Cash (Used in) or Available From Financing Activities	9,540	7,656	335	(1,826)
4 Net Cash generated or (Used) during the period	161	184	(351)	(1,431)

#### D RATIO ANALYSIS

1 Performance				
<i>a Sales Growth (for the period)</i>	-1.3%	-4.8%	13.5%	11.2%
<i>b Gross Profit Margin</i>	23.5%	27.8%	41.7%	42.8%
<i>c Net Profit Margin</i>	11.0%	16.2%	27.4%	26.8%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	26.5%	30.9%	44.9%	46.1%
<i>e Return on Equity (ROE)</i>	8.1%	12.7%	25.4%	26.4%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	34	25	13	24
<i>b Net Working Capital (Average Days)</i>	-32	6	7	19
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	2.2	3.1	3.5	1.7
3 Coverages				
<i>a EBITDA / Finance Cost</i>	7.3	34.9	157.0	315.7
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	2.7	3.3	20.4	195.1
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	9.5	5.8	0.5	0.0
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	61.0%	44.0%	15.8%	5.7%
<i>b Interest or Markup Payable (Days)</i>	0.0	0.0	0.0	0.0
<i>c Average Borrowing Rate</i>	2.3%	1.4%	2.1%	1.7%

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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	
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	<b>A1+</b>	The highest capacity for timely repayment.
<b>AA+</b> <b>AA</b> <b>AA-</b>	<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.	<b>A1</b>	A strong capacity for timely repayment.
<b>A+</b> <b>A</b> <b>A-</b>	<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.	<b>A2</b>	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
<b>BBB+</b> <b>BBB</b> <b>BBB-</b>	<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.	<b>A3</b>	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
<b>BB+</b> <b>BB</b> <b>BB-</b>	<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.	<b>B</b>	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
<b>B+</b> <b>B</b> <b>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>C</b>	An inadequate capacity to ensure timely repayment.
<b>CCC</b> <b>CC</b> <b>C</b>	<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.		
<b>D</b>	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.

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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)

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- 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)
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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.
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- (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)
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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
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- (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)
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- (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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