The Pakistan Credit Rating Agency Limited

Rating Report

Kohat Cement Company Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
26-Jan-2023	A	A1	Positive	Maintain	-
27-Jan-2022	A	A1	Positive	Maintain	-
12-Feb-2021	A	A1	Stable	Maintain	-
13-Feb-2020	A	A1	Stable	Maintain	-
28-Sep-2019	A	A1	Stable	Maintain	-
29-Mar-2019	A	A1	Stable	Maintain	-
22-Nov-2018	A	A1	Stable	Maintain	-
04-May-2018	A	A1	Stable	Maintain	-
29-Dec-2017	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Kohat Cement’s ratings incorporates its stable market position along with strong operational history. As of FY22, the Company occupies 7% share of total volumes sold during the period. Overall, the Cement sector reported a decline of 7.8% in total dispatches with significant contribution from decline in exports. Local dispatches dwindled by 0.9% on an annual basis. Similar trend was witnessed in quarterly dispatches of the current fiscal year with an overall decline of ~25% from the same quarter previous year. Going forward, the trend is expected to continue throughout the remaining fiscal year owing to economic constraints and political uncertainty. Additionally, the inflationary pressure is further driving the demand for Cement downwards. During FY22, the Company’s local dispatches were recorded at 3.55mln tons (FY21: 3.56mln tons) showing a negligible change. However, exports declined by 95.64% owing to the demand shrink in Afghanistan. Similar trend was witnessed in 1QFY23, with local dispatches declining by 20.2% and export dispatches by 65.8% compared to same period previous year. Alternatively, the Company’s Net Revenues increased (1QFY23: PKR 8,853mln, FY22: 32,877mln, FY21: PKR 24,057mln) owing to price hikes throughout the period. The Company successfully passed on the increase in cost to the customers resulting in improving margins. Furthermore, the Company’s low leveraged structure (12%) combined with negligible finance led to better profitability over the period. The Company has procured land for its planned greenfield expansion of 7,800-10,000 TPD near Khushab. The plant and equipment will be sourced once the economic conditions improve. Going forward, with declining trend in the cement sector, it is vital for the Company to maintain efficient utilization while maintaining its margins.

The company’s fairly low leveraging, healthy liquid investment book provides comfort to the ratings. Company owns investment properties having a book value of ~PKR 4.1bln which strengthens the financial profile. The ratings are dependent on upholding of company’s market position in addition to sustenance of business volumes and margins along with good governance practices. The company's strategy to keep a moderate level of leveraging remains important for the ratings.

Disclosure	
Name of Rated Entity	Kohat Cement Company Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Cement(Mar-22)
Rating Analysts	Hashim Yazdani | hashim.yazdani@pacra.com | +92-42-35869504

Profile

Legal Structure Kohat Cement Company Limited (Kohat Cement) a subsidiary of ANS Capital (Pvt.) Ltd is a public listed company established in 1984 by State Cement of Pakistan. Subsequent to its privatization in 1992, the company was taken over by new management headed by Mr. Aizaz Sheikh. The company is listed on Pakistan Stock Exchange (PSX).

Background The registered office and the factory are located in Kohat, whereas the Head Office is located in Lahore. In 1995, the company underwent an extensive BMR program and the capacity of the plant was enhanced to 1,800tpd. Afterwards, in 2005 a White Cement Plant was established followed by a Grey Cement Plant in 2007. Furthermore, a power plant with capacity of 22.6MW was added in 2009.

Operations Kohat Cement is engaged in the production and sale of cement. The Company's products include Grey Cement and White Cement. Company has an installed capacity of approximately 5.0mln tons per annum. Two separate production lines (for grey and white cement) allows the company to have a broader product slate.

Ownership

Ownership Structure Kohat Cement is majority owned by sponsor family through ANS Capital (Pvt.) Limited (~55%) where, the ownership of ANS Capital (Pvt). Ltd. resides equally between Mr. Aizaz & Mr. Nadeem Atta sheikh. The other major proportion of shareholding is of Mrs. Hijab Tariq (widow of late Mr. Tariq Atta) owns ~17%.

Stability Kohat Cement's ownership structure is seen stable with no major changes over the years.

Business Acumen The sponsors, especially the Chief Executive, has interests vested in various sectors through holding company. Furthermore, the sponsors have been in the Cement manufacturing business from the past 38 years which is an evidence of their expertise in the sector.

Financial Strength Kohat Cement being the flagship entity of sponsors, 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's board of directors - including the Chief Executive – Nadeem Atta Sheikh. The board comprises of 5 Non-Executive, 1 Executive and 2 Independent members.

Members' Profile Mr. Aizaz Mansoor is the chairman of the board. The board members' have good business acumen on the back of significant local industry exposure in several sectors. The board meetings minutes are formally maintained reflecting good participation by the members present. Mr. Ahmed Sajjad Khan and Mr. Talha Saeed Ahmed were elected as independent directors and associated with the board since Jun, 2019.

Board Effectiveness Kohat Cement has two committees: 1) Audit committee and 2) Human resource & Remuneration Committee (HR&R) to assist the management in related matters. Furthermore, the board conducts regular meetings as needed during the year to discuss and advise on matters relating to Company's financial and operational performance.

Financial Transparency KPMG Taseer Hadi & Co., Chartered Accountants conduct the external audit services for Kohat Cement. 'KPMG' is in '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 June 30th, 2022.

Management

Organizational Structure Currently, the organizational structure is divided into fourteen main functions. The functions reporting to CEO are as follows: 1) Sales & Marketing, 2) Administration, 3) HR, 4) Planning & Development, 5) Finance & Accounts 6) Works. However, the functions reporting to GM Works are: 1) Production, 2) Electrical, 3) Quality Control, 4) Power Plants, 5) Technical & Purchase, 6) Maintenance, 7) Works and 8) Material and Mining.

Management Team Mr. Nadeem Atta, the CEO, is associated with the company since the last 28 years. The CEO is supported by a team of experienced individuals equipped with necessary technical skills and relevant industry exposure.

Effectiveness The Chief Executive Officer and Executive Director are supported by a team of experienced professionals at key management positions.

MIS Kohat Cement has strong technology infrastructure with reasonably defined policies and procedures. The company's current operational modules include marketing, supply chain and financial modules with comprehensive MIS quality. Various system generated reports including the Cash flow/investment portfolio, daily management report, and daily production summary and sale variance report which are reviewed by top management.

Control Environment Kohat Cement's plant is located in Kohat, in North Region. The fuel requirement is met mainly through coal imported from South Africa, Indonesia, Afghanistan and local coal. The kiln can operate on coal only. To cater the power needs, the company has 82MW of connection from WAPDA and generators of 22MW for captive power generation. Furthermore, the company has 25MW waste heat recovery power plant.

Business Risk

Industry Dynamics Cement sector's production capacity is recorded above ~69mln tons in FY22. Almost ~76% of the operational plants are located in the North Region, while remaining~24% capacity is located in the South Region. Due to the ongoing economic constraints and political instability in the country, cement industry has also faced decline in dispatches during FY22. The supply was adversely affected by the nationwide floods that disturbed supply lines along with slow down in the construction industry leading to a fall in demand. During FY22, overall dispatches including local and export were recorded at 52.89mln MT (FY21: 57.43mln MT) registering a decline of 7.9%. Major decline of 43.6% was witnessed in the exports while local dispatches declined by 1%. Decline in exports were witnessed due to worldwide inflation and unfavorable pricing to export.

Relative Position In terms of installed capacity, Kohat Cement occupies 7.0% of the total installed capacity of the country i.e., approx. 70MTPA. With its installed capacity of ~5.0MTPA, Kohat Cement is categorized as a medium player with significant presence in the North region. As of volumes sold during FY22 and 1QFY23, Kohat Cement occupies 7.0% market share of the cement industry.

Revenues Revenues improved during FY22 on account of higher pricing. The Company reported Net sales of PKR 32,877mln during FY22 (FY21: PKR 24,057mln) with a net increase of 37% as a result of inflation. Same result was witnessed in 1QFY23 where Net Sales were recorded at PKR 8,853mln (1QFY22: PKR 6,804mln).

Margins Kohat Cement margins have continuously improved since 2021 with an upward trajectory. The Company reported Gross Profit Margin of 31.3% during 1QFY23 (FY22: 29.8%, FY21: 24.8%). Similarly, Net Profit Margins improved significantly to 20.2% during 1QFY23 from 15.3% in FY22 (FY21: 14.5%). The decline in finance cost over the years have added positively to the Net Profit Margins.

Sustainability Although there has been a current slowdown in the economy and the cementsector leading to reduced sold volumes. As the economy picks up pace with government spending in PSDP, the cement sector will revive. The Company has also announced Greenfield expansion of 7,800 TPD in Khaushab, Punjab. The work on the expansion is yet to begin but once completed will give further opportunity to capture the market share in south region.

Financial Risk

Working Capital During 1QFY23, Kohat's working capital requirements represented by net cash cycle (net working capital days) - a function of inventory, receivables and payables - stood at 8 days (FY22: 8 days). The slight increase in inventory days (1QFY23: 16 days, FY22: 14 days) was on account of accumulated inventory as a result of flooding. The Company is able to manage the requirement primarily through internal resources on account of robust cashflows. Hence, the Company has zero reliance on STB as on Sept 2022.

Coverages FCFO further improved to PKR 9,888mln during FY22 (FY21: PKR 6,575mln) leading to better coverages during the period. Similarly, FCFO for 1QFY23 stood at PKR 2,855mln. EBITDA/Finance Cost was recorded at 18.5x during 1QFY23 (FY22: 20.6x, FY21: 14.1x). Coverages show significant improvement due to low reliance on borrowings leading to negligible finance cost.

Capitalization Borrowings including CMLTB amounting to PKR 3,956mln (FY22: PKR 4,251mln). As a result, leveraging stood at 12.0%. Going forward, the company's leveraging is expected to increase in pursuit of expansion. However, it is expected to be comfortably managed through healthy cash flows.

PKR mln

Kohat Cement Company Limited	Sep-22	Jun-22	Jun-21	Jun-20
Cement	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	21,241	21,441	22,102	22,827
2 Investments	14,018	14,258	7,136	3,852
3 Related Party Exposure	-	-	-	-
4 Current Assets	10,453	7,652	6,849	5,198
a Inventories	*1,586*	*1,456*	*1,113*	*1,016*
b Trade Receivables	*673*	*916*	*984*	*494*
5 Total Assets	45,711	43,351	36,087	31,877
6 Current Liabilities	8,979	8,416	5,927	4,677
a Trade Payables	*1,800*	*1,325*	*1,672*	*1,278*
7 Borrowings	3,956	4,251	6,051	6,989
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	3,745	3,437	1,885	1,485
10 Net Assets	29,031	27,246	22,223	18,727
11 Shareholders' Equity	29,031	27,246	22,224	18,727
B INCOME STATEMENT				
1 Sales	8,853	32,877	24,057	11,300
a Cost of Good Sold	*(6,082)*	*(23,065)*	*(18,092)*	*(11,325)*
2 Gross Profit	2,771	9,812	5,965	(24)
a Operating Expenses	(125)	(476)	(408)	(303)
3 Operating Profit	2,645	9,336	5,558	(327)
a Non Operating Income or (Expense)	*178*	*127*	*(155)*	*179*
4 Profit or (Loss) before Interest and Tax	2,823	9,463	5,403	(148)
a Total Finance Cost	*(173)*	*(538)*	*(517)*	*(409)*
b Taxation	*(865)*	*(3,901)*	*(1,388)*	*114*
6 Net Income Or (Loss)	1,785	5,024	3,498	(444)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*2,855*	*9,888*	*6,575*	*175*
b Net Cash from Operating Activities before Working Capital Changes	*2,711*	*9,374*	*5,975*	*(127)*
c Changes in Working Capital	*(1,203)*	*(1,192)*	*(886)*	*(376)*
1 Net Cash provided by Operating Activities	1,508	8,181	5,089	(502)
2 Net Cash (Used in) or Available From Investing Activities	255	(7,093)	(3,950)	(19)
3 Net Cash (Used in) or Available From Financing Activities	(296)	(1,805)	(943)	839
4 Net Cash generated or (Used) during the period	1,467	(717)	196	318
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	7.7%	36.7%	112.9%	-27.8%
b Gross Profit Margin	31.3%	29.8%	24.8%	-0.2%
c Net Profit Margin	20.2%	15.3%	14.5%	-3.9%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	18.7%	26.4%	23.6%	-1.8%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	25.2%	20.1%	16.7%	-2.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	24	25	27	47
b Net Working Capital (Average Days)	8	8	5	17
c Current Ratio (Current Assets / Current Liabilities)	1.2	0.9	1.2	1.1
3 Coverages				
a EBITDA / Finance Cost	18.5	20.6	14.1	1.6
b FCFO / Finance Cost+CMLTB+Excess STB	6.6	6.2	4.0	0.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.4	0.5	0.9	-29.0
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	12.0%	13.5%	21.4%	27.2%
b Interest or Markup Payable (Days)	89.7	100.7	91.3	193.8
c Entity Average Borrowing Rate	14.5%	9.9%	7.6%	6.0%

Credit Rating

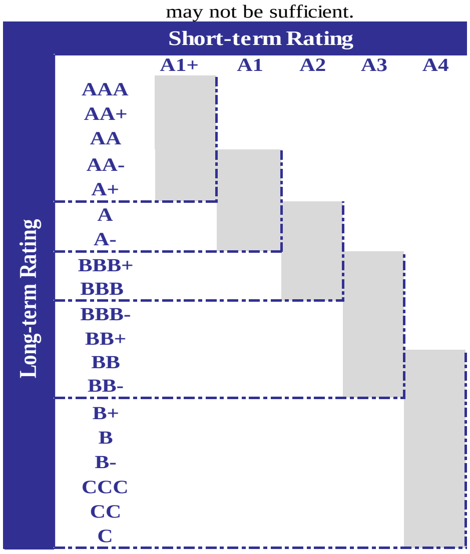
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

Disclaimer: PACRA has used due care in preparation of this document. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information. Contents of PACRA documents may be used, with due care and in the right context, with credit to PACRA. Our reports and ratings constitute opinions, not recommendations to buy or to sell.

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
(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA's prior written consent