The Pakistan Credit Rating Agency Limited

Rating Report

Fauji Cement Company Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
15-Mar-2023	AA-	A1	Stable	Upgrade	-
15-Mar-2022	A+	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Fauji Cement Company Limited (FCCL) ratings upgrade are derived from its association with Fauji Foundation along with its improved market position, financial and operational performance, cost optimization measures and synergies attained from merger of Askari Cement Limited with and into FCCL in July 2021. The cement industry capacity utilization in FY22 remained at 76%, with a slight decrease of 8% in the overall cement dispatches (FY22: 52.9mln MT, FY21: 57.4mln MT). The drop in dispatches is mainly attributable to cement exports. Similar declining trend was witnessed at the start of FY23, owing to various challenges including the aftermaths of floods, rising interest rates, high inflation, increase in commodity prices and cuts in overall development spending by the government. This led to an overall decline in industry volumes by 21% to 21.8mln MT in 1HFY23 as compared to 27.5mln MT in 1HFY22. Going forward, the demand is expected to rebound as the impact of flooding is receded and dispatch to large projects mainly hydropower dams picked up. FCCL operates three manufacturing facilities with a production capacity of approx. 8.4mln MTPA. Currently, the Company occupies 12% market share in terms of dispatches, making it the third largest cement manufacturer in the country. The management expects to maintain its industry ranking in future. As a result of successful merger, during FY22 the Company reported cumulative dispatches of 5.6mln MT (FY21: 3.5mln MT). Alternatively, during 1HFY23 the Company sold 2.5mln MT of cement, registering a decline of 15% YoY. Amid declining industry performance, Revenues for 1HFY23 were recorded at PKR 33,673mln (1HFY22: PKR 25,346mln). The increase in revenues during the period was backed by price hikes to reflect the increase in input prices especially fuel and power. Likewise, reported Net Income exhibited an upward trajectory as a result of synergies through the merger and cost optimization measures implemented by the management. FCCL's margins have shown significant improvement and are aligned to its peers in the large cement manufacturers. Furthermore, the Company is working towards establishing its Greenfield expansion project of 6,825 TPD cement, near DG Khan which is expected to become operational by Dec'23. The Company has successfully procured significant portion of the machinery which is on the site. Upon completion of the project, the Company will have access to the southern region of Punjab, Balochistan and some parts of Sindh which would further complement its market presence. The Company keeps a moderately leveraged financial profile, with potential increase due to expansion but is expected to remain under 40% of its Equity.

The ratings remain dependent on upholding company's market position along with sustenance of business volumes, margins and achieving optimal utilization of production capacities. Going forward, sustainability in profits for timely repayment of debt remains vital.

Disclosure

Name of Rated Entity	Fauji 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 Fauji Cement Company Limited (FCCL), is a public listed company established in 1992. The company is listed on Pakistan Stock Exchange (PSX). The Company has been set up with the primary objective of manufacturing, selling and exporting of different types of Cement products.

Background The Company started its operations in 1997 with the production capacity of 3,885 tons per day (TPD), which was enhanced to over 11,865 TPD, with addition of second production Line in 2011, with annual total production capacity of 3.5mln MT of cement. Upon successful merger with Askari Cement Limited in July 2021 along with completion of expansion of Nizampur line, the Company's annual capacity has increased to approx. 8.4mln MT.

Operations Currently the Company is operating at three locations including Attock (2 lines), Nizampur (3 lines) and Wah (1 line). The Company is one of the leading producers of a wide range of quality cement including ordinary Portland cement and other specialized cement(s) in Pakistan.

Ownership

Ownership Structure FCCL is majority owned by its sponsor Fauji Foundation and other group companies (67%) while remaining is held by General public (17%) and Financial institutions (16%).

Stability Fauji Foundation (also known as Fauji Group or FFG), is amongst the largest business conglomerate in Pakistan which "Earns to Serve" the interests of ex-servicemen, basically a Charitable Trust founded in 1954 for the welfare of the ex-servicemen and their dependents.

Business Acumen Fauji Foundation is amongst the leading business conglomerates in Pakistan with investment in different sectors including Banking, Cement, Power, Fertilizer, Oil Exploration and Foods. The group has been operating in the cement sector since three decades which is an evidence of their strong business acumen.

Financial Strength Financial Strength of the sponsors is considered strong enough, through above mentioned associated and fully owned projects.

Governance

Board Structure The overall control of the company vests in eight member's board of directors - including the Chief Executive – Mr. Qamar Haris Manzoor. The board comprises of 5 Non-Executive Directors while 3 are Independent Directors.

Members' Profile The board members' have good business acumen on the back of significant local industry exposure in several sectors. Mr. Waqar Ahmed Malik is the Chairman of the board. He has vast experience of different sectors and is holding the position of Chairman on different boards of the groups associated companies.

Board Effectiveness FCCL has three committees: 1) Audit committee 2) Human resource & Remuneration Committee (HR&R) and 3) Investment Committee; this is in compliance with the Code of Corporate Governance. The board along with its committees conduct regular meetings as needed to discuss matters relating to operational and financial performance of the Company.

Financial Transparency KPMG Taseer Hadi & Co, Chartered Accountants conducted the external audit services for Fauji Cement. 'KPMG Taseer Hadi & Co, Chartered Accountant 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 The organizational structure is divided into different functions. Main functions are; 1) Sales & Marketing, 2) Plant Operations 3) Finance & Accounts. 4) Internal Audit 5) Human Resource 6) Legal & Corporate Affairs and 7) Management Information System. The internal audit department reports to the Audit Committee in line with the Code of Corporate Governance.

Management Team Mr Qamar Haris Manzoor the CEO, has done his Masters in Chemical Engineer from US and holds over 36 years of experience in plant and project management. He is accompanied by a team of qualified and competent individuals who head their respective departments.

Effectiveness The management is mainly supported by seven departments (i) Management, (ii) Production, iii) Finance & Accounts (iv) Sales & Marketing, (v) IT Steering (vi) Legal & Corporate Affairs and (vii) Human Resource. The management meetings are conducted on frequent basis to ensure smooth flow of processes and resolve operational bottlenecks. The necessary information is captured in minutes.

MIS FCCL has implemented SAP (ERP) solution in the Company. The technology infrastructure with reasonably conceived and implemented policies or procedures enables the management to generate various regular and customized reports of different frequency (daily, weekly, monthly and yearly) pertaining to sales, purchase, inventory, general ledger, payroll, costing & budget and Preventive maintenance and other important financial figures.

Control Environment Fauji Cement has an in house internal audit function. HOD Internal Audit is reportable to Audit Committee. Internal Audit function is an integral part of the process and regularly apprises and monitors the implementation of financial controls and other procedures.

Business Risk

Industry Dynamics Cement sector's production capacity is recorded above ~69mln MT 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%. Similar decline was witnessed in industry volumes by 21% to 21.8mln MT in 1HFY23 as compared to 27.5mln MT in 1HFY22.

Relative Position In terms of installed cement manufacturing capacity, Fauji Cement is the third largest player in the local cement sector post merger with ACL and Nizampur expansion. With its current installed capacity of approx. 8.4mln MTPA, FCCL is categorized amongst the large players of the industry with significant presence in the North region. In terms of Volumes sold, FCCL occupies 12% market share for the half year ended Dec 2022.

Revenues During FY22, the Company sold 5.61mln MT (FY21: 3.48mln MT) of cement generating a revenue of PKR 54,243mln. However, during 1HFY23, sold volumes declined by 14% to 2.5mln MT as compared to same half previous year. Revenues for 1HFY23 were recorded at PKR 33,673mln (1HFY22: PKR 25,346mln). The increase in revenues during the period was backed by price hikes to reflect the increase in input prices especially fuel and power.

Margins Gross Profit Margin improved slightly during FY22 recorded at 26.5% (FY21: 25%) with a further improvement in 1HFY23: 27.7%. The Company was successful in passing on the increase in input prices to the customer through price hikes. Similarly, Net Profit Margin in 1HFY23 increased to 15.1% from 13.1% in June 2022 owing to better retention prices and cost optimization measures taken by the management.

Sustainability Post merger, FCCLs market presence has significantly improved as a result of increase in sold volumes. Furthermore, the Company is setting up a greenfield cement manufacturing plant of 6,825 TPD cement at Dera Ghazi Khan which will allow penetration in the South region.

Financial Risk

Working Capital During 1HFY23, FCCL working capital requirements represented by net cash cycle (net working capital days) - a function of inventory, receivables and payables - increased to 29 days (FY22: 18 days). Cash cycle days (1HFY23: 44 days; FY22: 29 days) increased on account of rise in inventory days owing to slowdown in sales as a result of flooding during the period. The Company was able to manage the requirement through internal resources along with utilization of working finance facilities. Hence, company's reliance on Short-term borrowings (STBs) stood at PKR 2,504mln as on Dec 2022 (FY22: PKR 3,218mln).

Coverages During 1HFY23, FCCL's FCFO were recorded at PKR 8,519mln as a result of better profitability. EBITDA/Finance Cost) during 1HFY23 was recorded at 11.5 (FY22: 13.6, FY21: 76.3) registering a decline owing to rise in finance cost to support expansion projects.

Capitalization Over the last few years, the company operated at fairly low leveraged capital structure. However; on account of debt acquisition for expansion projects the debt to debt plus equity ratio has increased along with successful transfer of liabilities from ACL. Leveraging as of Dec 2022 stood at 32.9% (FY22: 30.3%, FY21: 9.9%).

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Financial Summary
PKR mln

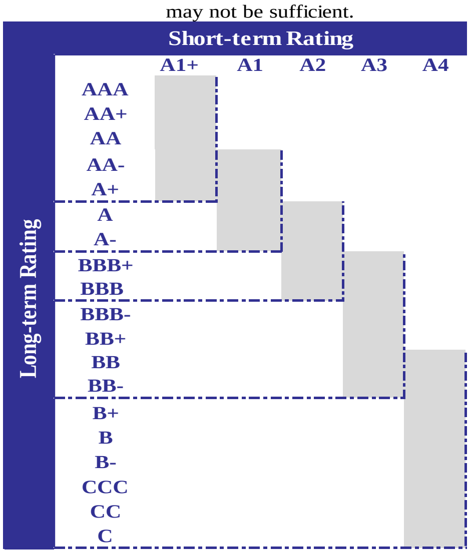
Fauji Cement Company Limited	Dec-22	Jun-22	Jun-21	Jun-20
Cement	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	98,202	85,415	21,598	22,225
2 Investments	850	3,843	4,398	-
3 Related Party Exposure	64	67	15	-
4 Current Assets	25,723	24,374	8,041	7,153
a Inventories	*5,736*	*3,698*	*1,189*	*1,188*
b Trade Receivables	*4,442*	*2,413*	*1,450*	*1,051*
5 Total Assets	124,840	113,698	34,052	29,377
6 Current Liabilities	11,655	12,696	4,143	2,986
a Trade Payables	*2,848*	*2,683*	*863*	*355*
7 Borrowings	34,370	28,266	2,568	2,702
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	8,613	7,613	4,065	3,885
10 Net Assets	70,202	65,123	23,276	19,804
11 Shareholders' Equity	70,202	65,123	23,276	19,804
B INCOME STATEMENT				
1 Sales	33,673	54,243	24,271	17,232
a Cost of Good Sold	*(24,343)*	*(39,844)*	*(18,207)*	*(16,583)*
2 Gross Profit	9,330	14,399	6,064	649
a Operating Expenses	(1,018)	(1,838)	(714)	(673)
3 Operating Profit	8,312	12,561	5,350	(24)
a Non Operating Income or (Expense)	*(131)*	*169*	*(133)*	*84*
4 Profit or (Loss) before Interest and Tax	8,181	12,730	5,217	61
a Total Finance Cost	*(898)*	*(1,202)*	*(110)*	*(234)*
b Taxation	*(2,203)*	*(4,416)*	*(1,636)*	*114*
6 Net Income Or (Loss)	5,079	7,113	3,471	(59)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*8,519*	*12,221*	*5,892*	*1,275*
b Net Cash from Operating Activities before Working Capital Changes	*8,019*	*11,236*	*5,798*	*1,043*
c Changes in Working Capital	*(3,230)*	*(4,653)*	*(153)*	*(262)*
1 Net Cash provided by Operating Activities	4,789	6,582	5,644	781
2 Net Cash (Used in) or Available From Investing Activities	(9,437)	(26,065)	(5,142)	(545)
3 Net Cash (Used in) or Available From Financing Activities	5,808	20,888	(163)	(77)
4 Net Cash generated or (Used) during the period	1,160	1,406	340	158
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	24.2%	123.5%	40.9%	-17.1%
b Gross Profit Margin	27.7%	26.5%	25.0%	3.8%
c Net Profit Margin	15.1%	13.1%	14.3%	-0.3%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	15.7%	14.0%	23.6%	5.9%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	15.1%	16.8%	16.0%	-0.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	44	29	37	44
b Net Working Capital (Average Days)	29	18	28	37
c Current Ratio (Current Assets / Current Liabilities)	2.2	1.9	1.9	2.4
3 Coverages				
a EBITDA / Finance Cost	11.5	13.6	76.3	8.2
b FCFO / Finance Cost+CMLTB+Excess STB	4.2	2.9	12.3	2.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	2.1	2.2	0.2	0.8
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	32.9%	30.3%	9.9%	12.0%
b Interest or Markup Payable (Days)	0.0	0.0	0.0	0.0

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

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

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).
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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)
(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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