The Pakistan Credit Rating Agency Limited

FATIMA FERTILIZER COMPANY LIMITED (FATIMA)

ENTITY RATINGS REPORT

Entity	**NEW [AUG -17]**	**PREVIOUS [NOV-16]**
Long-Term	AA-	AA-
Short-Term	A1+	A1+
Outlook	Stable	Stable

AUGUST 2017

Profile & Ownership

- Fatima Fertilizer Company Limited (Fatima), incorporated in 2003, is listed on Pakistan Stock Exchange.
- Majority owned by Fatima Group (45%) and Arif Habib Group (31%); Fatima Group retains the management control.
- The group has interests in textile, sugar, mining and energy sectors and in addition owns Pakarab Fertilizer.
- Fatima owns a fertilizer complex with nameplate capacity of 1.28mln MT p.a (Urea, Can and NP combined), located at Mukhtar Garh, Rahim Yar Khan.
- There are two plants with nameplate capacity of 0.5mln MT p.a each for production of Ammonia and Nitric acid.
- Fatima Fert (formerly DH Fert) is a wholly owned subsidiary of Fatima adding 455K MT of additional capacity.

Governance and Management

- Eight member board of directors including the CEO; four representative of Fatima Group, two of Arif Habib Group and two independent members.
- The chairman of Arif Habib Group, Mr. Arif Habib, a reputed business professional, chairs the company's board.
- Mr. Fawad Ahmed Mukhtar, a seasoned entrepreneur, is the CEO of Fatima as well as of Pak Arab and Fatima Fert.

Performance

- Fatima's revenue, in CY16, continued to be driven by diversified fertilizer production; Urea (37%), CAN (34%), and NP (29%).
- Market share declined to 13% (CY15:15%), though company is the market leader in CAN (69%) and NP (60%).
- Topline grew by 12% YoY basis, wherein sizeable increase in NP sales (45%) diluted by decrease in Urea (32%) and CAN (23%).
- Commissioning of Waste Gas Boiler by April'16, boosted the energy efficiency.
- Increased offtake in the second half of CY16 compensated the previous month's impasse generating a gross profit margin of 53% (CY15: 56%).
- The company sold 123,227 tonns of Urea and CAN in the month of Dec16 leaving inventory levels at 378,081tonns (end-Nov16: 501,308).
- During CY16, Fatima's net profit stays at PKR 10bln (CY15: 9bln). Whereas, net profit margin of 29% remained highest among industry players.
- In 3MCY17, company hit the bottom line of PKR 2.2bln (3MCY16: PKR 1.1bln) on account of record quarterly sales of CAN (3MCY17:128mlntons; 3MCY15: 60mln tons), UREA (3MCY17: 99mlntons; 3MCY15: 49mln tons) and NP (3MCY17: 103mln tons; 3MCY16: 64mln tons).

Business Strategy

- Fatima envisages the optimal mix of Urea, CAN and NP to keep margins afloat
- Continue efforts in improving farmer's knowledge through providing technical assistance; conducting awareness seminars, meetings and trainings.
- Fatima envisages to have 35% shareholding in Midwest Fertilizer Corps (MFC)'s equity total worth of USD 875mln.
- Going forward, Fatima is availing the option to export Urea under the recent export quota of o.6mln tonns granted by government, which may relieve the urea inventory.

Financial Risk

- Traditionally low working capital requirement witnessed upspring due to inventory pile up; a phenomenon in line with industry. Increased working capital requirements (3MCY17: PKR 10,149mln) have been financed by hefty short term borrowings (3MCY17: 4500; PKR mln; CY16: PKR 8,011mln, CY15: PKR 10,229mln).
- Significant repayment of expensive loans with issuance of new Sukuk Certificates amounting PKR 10.5bln; the debt level remained at PKR 29,872 mln at end-Dec16 (end-Dec15: PKR 30,210mln). Debt coverage stands at 7.4times with robust debt payback of 1.7yrs.

RATING RATIONALE

The ratings reflect strong business profile of the company on the back of diversified product mix. Secure supply of gas from Mari field together with lower feed stock price (under fertilizer policy – 2001 up till July'2021), represents inherent strengths of the company compared to peers. Overall capacity utilization continued to exceed 100% (previously: 90% - 98%) based on ammonia debottlenecking. Efficiency in fuel consumption was also achieved with the installation of Waste Gas Boiler in April'16. Gross margins are healthy, with the uptick in off takes post subsidy announcement. The company faces competition from peers amidst supply surplus situation in the country, mainly on the back of improved gas situation in the country; experiencing huge inventory pile up of urea. The pending risk is being managed through allowing exports. Another risk is reduced international pricing, a significant threat to current profits. Fatima's carry over inventories and working capital needs pushed up short term borrowings, rationalized towards Dec 2016. This restricted the incremental benefit on leveraging enabled by retirement of long term borrowings. The ratings are dependent on the company's ability to maintain its cash flows.

INDUSTRY

Pakistan fertilizers sector has production capacity of 6.9mln MT of urea, 0.7mln MT of DAP and 2.2mln MT of others. The industry benefits from the latent demand of its major product urea and oligopolistic market conditions. Industry is currently facing supply surplus issues because of increased capacity utilization and lower international urea price.

PKR mln

Fatima Fertilizer Limited

BALANCE SHEET	31-Mar-17	31-Dec-16	31-Dec-15	31-Dec-14
	3MCY17	CY16	CY15	CY14
Non-Current Assets	**72,812**	**73,089**	**73,150**	**68,867**
Investments (Incl. associates)	**7,970**	**7,686**	**4,806**	**3,086**
Equity	2,238	2,238	2,106	86
Debt	5,732	5,448	2,700	3,000
Current Assets	**21,628**	**29,822**	**16,833**	**11,169**
Inventory	6,370	6,243	7,003	2,681
Trade Receivables	2,266	2,116	335	448
Others	12,992	21,463	9,495	8,039
Total Assets	**102,410**	**110,597**	**94,789**	**83,121**
Debt	**10,018**	**13,529**	**17,042**	**6,975**
Short-term	4,500	8,011	10,229	600
Long-term (Inlc. Current Maturity of long-term debt)	5,518	5,518	6,812	6,375
Other shortterm liabilities	10,665	17,658	8,906	7,633
Other Longterm Liabilities	32,079	32,035	28,613	31,756
Shareholder's Equity	**49,648**	**47,374**	**40,229**	**36,757**
Total Liabilities & Equity	**102,410**	**110,597**	**94,789**	**83,121**
INCOME STATEMENT				
Turnover	**8,259**	**33,765**	**30,226**	**36,169**
Gross Profit	4,508	17,985	17,017	21,461
Other Income	-	420	349	381
Financial Charges	(497)	(2,739)	(2,379)	(3,767)
Net Income	**2,274**	**9,782**	**9,254**	**9,258**
Cashflow Statement				
Free Cashflow from Operations (FCFO)	3,668	15,976	14,139	18,666
Net Cash changes in Working Capital	3,516	12,801	12,050	15,126
Net Cash from Operating Activities	(6,633)	18,775	6,463	15,319
Net Cash from InvestingActivities	(462)	(5,012)	(7,246)	(2,784)
Net Cash from Financing Activities	(3,622)	(2,958)	130	(11,824)
Net Cash generated during the period	(10,717)	10,805	(654)	711
Ratio Analysis				
Performance				
Turnover Growth	57%	12%	-16%	8%
Gross Margin	55%	53%	56%	59%
Net Margin	28%	29%	31%	26%
ROE	19%	30%	25%	26%
Coverages				
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	2.0	2.3	1.5	1.8
Interest Coverage (x) (FCFO/Gross Interest)	7.4	5.8	5.9	5.0
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCF(	1.7	1.2	1.7	1.6
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	116	83	85	62
Capital Structure (Total Debt/Total Debt+Equity)	35%	39%	43%	40%

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

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 RATINGS

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 conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

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 surveill the opinion due to lack of requisite information

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Regulatory and Supplementary Disclosure

Rated Entity

Name of Rated Entity Fatima Fertilizer Company Limited
Sector Fertilizer
Type of Relationship Solicited

Purpose of the Rating: Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
08-Aug-17	AA-	A1+	Stable	Maintain
11-Nov-16	AA-	A1+	Stable	Maintain
12-Nov-15	AA-	A1+	Stable	Maintain
27-Nov-14	AA-	A1+	Stable	Upgrade
28-Jan-13	A+	A1	Positive	Maintain
15-Dec-11	A+	A1	Stable	Upgrade

Related Criteria and Research

Methodology: Corporate Rating Methodology
Research: Fertilizer Sector | Overview |October 2016

Rating Analysts

Sanna Khan
sanna.khan@pacra.com
(92-42-35869504)

Jhangeer Hanif
Jhangeer@pacra.com
(92-42-35869504)

Rating Team Statement

Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

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Surveillance

PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security

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PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating.

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Confidentiality

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Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter;

Prohibition

Probability of Default (PD)

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 each rating notch. These studies are available at our website (www.pacra.com). However, actual transition of a particular rating may not follow the pattern observed in the past.