The Pakistan Credit Rating Agency Limited

AGP LIMITED

INSTRUMENT RATING REPORT

	CURRENT [NOV-17]	INITIAL [JUL-17]
Privately Placed, Secured Sukuk (PKR 2,448mln)	A	A
Outlook	Stable	Stable

REPORT CONTENTS

NOVEMBER 2017

About the Sukuk

- AGP Limited (AGP) has issued (Jun'17) a privately placed and secured Sukuk of ~PKR 2.4bln in order to refinance its long-term debt.
- With a tenor of 5 years, the Sukuk's principal and profit (3MK+1.3%) will be paid in 20 equal quarterly installments, starting from the 3rd month of issue date (Sep'17). As of Sept-17, an amount of PKR 2.28bln is outstanding.
- The instrument is secured through first pari passu charges over all present and future non-current assets (~PKR 3.1bln) of AGP and Aspin Pharma (associate).

Profile and Ownership

- AGP is an public unlisted pharmaceutical company, operating in Pakistan since 1989
- Product portfolio comprises over 117 variants of 53 products, including star products such as 'Ceclor', 'Rigix', 'Osnate', and recently launched 'MyHep'.
- Majority owned by OBS Group (OBS) (57.9%), followed by strategic partners: Muller & Phipps (M&P), Baltoro Growth Fund (BGF), Bank Alfalah Ltd, High Q Pharmaceuticals (Pvt.) Ltd and JS Bank.
- OBS Pakistan and M&P Pakistan intends to offer 20m and 15m shares accumulating to 12.5% stake respectively as offer for sale (OFS) to public from their total shareholdings.

Governance and Management

- The company is governed by a seven-member BoD comprising four representatives of OBS Group, and one each of M&P and BGF, with a recent induction of one independent director.
- The Chairman, Mr. Tariq Moinuddin - the brains and owner of OBS Group - is a qualified CPA having over 30 years of domestic and international experience, including 18 years in pharmaceutical industry.
- MD & CEO, Ms. Nusrat Munshi, joined AGP in 2007 as Director Finance. She has 26 years of experience; a decade in the pharmaceutical industry. She is assisted by experienced management team having long association with AGP.

Systems and Controls

- AGP has implemented and is using all key modules of SAP (ERP suite) which provides a real-time end-to-end integrated solution for all operations including finance, sales and marketing, production and quality management and human capital management.
- Prompt availability of MIS for higher management's use.

Performance

- During 6MCY17, topline (PKR 2,343mln) grew by 7.4% YoY.
- Improved core margins in 6MCY17 (gross: 60%, operating: 38%) on the back of (i) procurement of APIs at comparatively lower cost in bulk quantities majorly from India and China, and (ii) lower factory overheads due to operational efficiencies.
- Bottom-line increase to PKR 603mln, resulting from strong revenue growth with net margin rising to ~26% (6MCY16: ~23%).

Business Strategy

- AGP is positioned to derive benefits from group synergies in the form of (i) bulk discounts for suppliers of raw materials, (ii) better bank relationship, and (iii) strength-wise parking of products.
- Strategic alliance with Mylan, USA (World 2nd largest generic drugs manufacturer) to promote their complete portfolio in Pakistan.
- Recent plans for expansion of operational capacity and nutraceutical plant from internal generation would contribute in AGP's revenue growth in future.
- Recent change of distributor, to M&P, is expected to increase outreach on the back of better experience of distributor, wider branch network, and superior technology.
- Five new products were launched in CY16, with seven new products launched in CY17 to date. AGP targeting to launch six products every year going forward.

Financial Risk

- Borrowings largely comprise long-term debt procured by Appollo to finance the acquisition of AGPP and AGPH. During the year, the company replaced its entire long-term debt with Sukuk; PKR ~2.4bln outstanding at end-Jun17, which would improve its coverages.
- Though AGP's free cash flows (FCFO) are strong, debt service coverage remains adequate (end-Jun17: 1.9x) owing to size of principal and interest repayments.
- Going forward, AGP is committed to expand its operations with internal cash generation and without expanding its current debt levels. Thus, it would result in improved debt coverage ratios on account of strong cashflows.

Rating Rationale

The ratings reflect AGP's strong business fundamentals. The pharmaceutical industry has witnessed a high rate of sustained growth over the years. Cost-efficiencies as well as demand inelasticity are benefiting the industry players. While product pricing has been a challenge, the new CPI-linked pricing criteria has allowed an increase in prices with respect to inflation, indicating a positive sign. At the same time, AGP's core profitability is strong; any downward revision in margins must remain range-bound. Cash flows - strong and sizeable - are adequate to service the debt initially procured by the incumbent sponsors – OBS Group – to acquire the company in 2014. With the recent debt re-profiling, debt servicing ability has improved further. Ongoing process of listing, through offer for sale by central sponsors would bode well from governance and transparency perspective. Expansion strategies and strategic alliance with Mylan, USA to promote their product portfolio in Pakistan should enable volumetric growth. Presence of OBS Group in the pharmaceutical sector provides strength, in the form of group synergies, to AGP's positioning within the industry.

Key Rating Drivers

The ratings are dependent on continued sustainability of profits and market share. Adequacy of cash flows and availability of alternative resources to make debt-related payment remains important. Meanwhile, compliance with internally-defined leveraging metrics is a prerequisite. Moreover, the instrument rating is dependent upon upholding of all major covenants.

Industry Snapshot

Pharmaceutical Industry in Pakistan comprises 672 players, of which 27 are multinationals (MNCs) having 34% market share. The market is dominated by top 9 players (43% market share). MNCs are taking exit from Pakistan due to pricing issues. CPI-linked pricing criteria, notified in Jul-16, allowed the industry to increase drug prices with respect to inflation, indicating a positive sign going forward.

AGP Limited

PKR mln

BALANCE SHEET	30-Jun-17	31-Dec-16	31-Dec-15	31-Dec-14
	6M	CY	CY	May-Dec14 (consolidated)
Non-Current Assets	6,889	6,804	6,801	6,809
Current Assets	1,420	1,709	1,546	1,007
Total Assets	**8,308**	**8,513**	**8,347**	**7,817**
Shareholder's Equity	4,880	4,277	3,190	2,547
Debt	2,757	3,391	4,484	4,462
Other Liabilities	671	845	673	808
Total Liabilities & Equity	**8,308**	**8,513**	**8,347**	**7,817**

INCOME STATEMENT	30-Jun-17	31-Dec-16	31-Dec-15	31-Dec-14
Turnover	**2,343**	**4,206**	**3,748**	**1,453**
Gross Profit	1,405	2,460	2,162	842
Other Income	(43)	(60)	(49)	(344)
Financial Charges	(176)	(361)	(515)	(266)
Net Income	**603**	**1,087**	**643**	**(253)**

Cashflow Statement	30-Jun-17	31-Dec-16	31-Dec-15	31-Dec-14
Free Cashflow from Operations (FCFO)	809	1,418	1,106	(306)
Net Cash changes in Working Capital	(166)	43	(22)	91
Net Cash from Operating Activities	367	1,043	506	(230)
Net Cash from InvestingActivities	(140)	(106)	(108)	(6,954)
Net Cash from Financing Activities	(633)	(1,094)	10	7,274
Net Cash generated during the period	(406)	(157)	408	90

RATIO ANALYSIS	30-Jun-17	31-Dec-16	31-Dec-15	31-Dec-14
Performance				
Turnover Growth	7.4%	12.2%	50.5% **2**	N/A
Gross Margin	60.0%	58.5%	57.7%	58.0%
Growth in Profitability (PAT)	20.1%	69.0%	353.9%	N/A
ROE (based on average Equity during the period)	26.4%	29.1%	22.4%	-21.2%
Coverages				
Debt Service Coverage (times) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.9	0.9	0.7	-1.2
Capital Structure (Total Debt/Total Debt+Equity)	36.1%	44.2%	58.4%	63.7%

Notes:
1. Consolidated figures as stated (for comparison) in Appollo Pharma Annual Report CY15.
2. For growth calculation, CY14 turnover is prorated based on 7 months' sales of consolidated figures.

The Pakistan Credit Rating Agency Limited

STANDARD RATING SCALES & 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 or 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.** "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.

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. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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, a suspended 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, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Name of Issuer	AGP Limited
Name of Issue	AGP Limited | Sukuk
Sector	Pharmaceuticals
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Dissemination Date	Rating	Outlook	Action
7-Nov-17	A	Stable	Maintain
26-Jul-17	A	Stable	Initial
24-May-17	A	Stable	Preliminary

Instrument Details

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs)	Security	Nature of Assets	Investment Agent
Sukuk	PKR 2,448mln	5	First pari-passu charge (hypothecation and mortgage) with 20% margin on all present and future fixed assets of AGP and Aspin Pharma	Land, building, plant and machinery	Bank Islami Pakistan Limited

Amortization Schedule Refer to Annexure

Related Criteria and Research Pharmaceutical | Jan-2017

Rating Methodology
Corporate Rating Methodology
Sukuk Rating Methodology

Rating Analysts

Faizan Sufi
faizan.sufi@pacra.com
(92-42-35869504)

Rai Umar Zafar
rai.umar@pacra.com
(92-42-35869504)

Rating Team Statement

Rating Procedure
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.

Disclaimer

Rating Shopping
PACRA maintains principle of integrity in seeking rating business.
PACRA has used due care in preparation of this document. Our information has been obtained directly from the underlying entity and public 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.
Conflict of Interest
At PACRA, the analysts involved in the rating process, and members of its rating committee do not have any conflict of interest relating to the credit rating done by them.
The analysts involved in the rating process do not have any interest in a credit rating or any of its family members has any such interest.
The analysts and members of the rating committees including the external member members have disclosed all the conflict of interest, including those of their family members, if any, to the Compliance Officer PACRA.

The analysts or any of its family members do not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This is, however, not applicable on investment in securities through collective investment schemes. PACRA has established appropriate policies governing investments and trading in securities by its employees
PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities
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 ii) fee mandate - signed with the payer, which can be different from the entity.
PACRA ensures that the credit rating assigned to an entity or instrument should 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.
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 arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer.
PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so.

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.

Reporting of Misconduct
PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP.
Confidentiality
PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties.
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
None of the information in this document may 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 written consent. PACRA reports and ratings constitute opinions, not recommendations to buy or to sell

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 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

Due Date Principal	Opening Principal	Principal Repayment	Due Date Markup/ Profit	Markup/Profit Rate		Profit Payment	Installment Payable	Principal Outstanding
	PKR in mln			Base	Spread	PKR in mln		
Jun'17	2,448	0	**Drawdown**					
Sep'17	2,448	122	**3rd Month**	3M Kibor	130bps	45	168	2,326
Dec'17	2,326	122	**6th Month**	3M Kibor	130bps	43	166	2,203
Mar'18	2,203	122	**9th Month**	3M Kibor	130bps	41	163	2,081
Jun'18	2,081	122	**12th Month**	3M Kibor	130bps	39	161	1,958
Sep'18	1,958	122	**15th Month**	3M Kibor	130bps	36	159	1,836
Dec'18	1,836	122	**18th Month**	3M Kibor	130bps	34	157	1,714
Mar'19	1,714	122	**21st Month**	3M Kibor	130bps	32	154	1,591
Jun'19	1,591	122	**24th Month**	3M Kibor	130bps	30	152	1,469
Sep'19	1,469	122	**27th Month**	3M Kibor	130bps	27	150	1,346
Dec'19	1,346	122	**30th Month**	3M Kibor	130bps	25	147	1,224
Mar'20	1,224	122	**33rd Month**	3M Kibor	130bps	23	145	1,102
Jun'20	1,102	122	**36th Month**	3M Kibor	130bps	20	143	979
Sep'20	979	122	**39th Month**	3M Kibor	130bps	18	141	857
Dec'20	857	122	**42nd Month**	3M Kibor	130bps	16	138	734
Mar'21	734	122	**45th Month**	3M Kibor	130bps	14	136	612
Jun'21	612	122	**48th Month**	3M Kibor	130bps	11	134	490
Sep'21	490	122	**51st Month**	3M Kibor	130bps	9	131	367
Dec'21	367	122	**54th Month**	3M Kibor	130bps	7	129	245
Mar'22	245	122	**57th Month**	3M Kibor	130bps	5	127	122
Jun'22	122	122	**60th Month**	3M Kibor	130bps	2	125	0

`