



The Pakistan Credit Rating Agency Limited

PAK ELEKTRON LIMITED

ENTITY RATINGS REPORT

	NEW [JAN-18]	PREVIOUS [APR-17]
ENTITY		
Long-Term	A+	A+
Short-Term	A1	A1
Sukuk II (PKR 1,100mln)	A+	A+
Privately Placed Sukuk (PKR 1,500mln)	AA-	-
Outlook	Stable	Stable

REPORT CONTENTS

1. RATING ANALYSIS
2. FINANCIAL INFORMATION
3. RATING SCALE
4. REGULATORY AND SUPPLEMENTARY DISCLOSURE

JANUARY 2018

Profile & Ownership

- Pak Elektron Limited (PEL), listed on Pakistan Stock Exchange, was established in 1956.
- Flagship Company of the Saigol Group (SG) engaged in manufacturing and sale of home appliances, and electrical and power equipment.
- PEL is majority owned by Saigol Group (50%), which has interests in energy and textile sectors.

Governance

- BoD comprises ten members including six nominees of Saigol Group; including CEO, three nominees of National Bank of Pakistan, and one nominee of National Investment Trust Limited.
- Nominees of Saigol group comprising three executives (including two family members) and three non-executive directors (including two family members).
- Mr. Naseem Saigol, a chemical engineer by profession, is the chairman of the board and the group.

Management

- Organizational structure divided in two divisions; Appliances and Power.
- Mr. Murad Saigol is Chief Executive Officer of the Company. In Oct-16 he was appointed for an additional three year term.
- Mr. Zeid Saigol is the Director Operations of Power Division.
- Mr. Manzar Hasan, the CFO of the Company, has ample experience with the Company, and is an integral part of the team.
- Experienced and stable management team.

Systems & Controls

- Successfully implemented Oracle Financials, Supply Chain, HR, and Payroll.
- Currently implementing Oracle Discrete Manufacturing, Business Intelligence, and Enterprise Asset Management.

Business Risk

- During 9MCY17, PEL topline witnessed a 25% YoY growth mainly due to local sales (33% increase YoY basis). However, heavy discounts led the net sales growth at 16% on YoY basis.
- Sales in the Appliances Division are dominated by Refrigerators (9MCY17: 67%; CY16: 82%; CY15: 83%), followed by Air Conditioners (9MCY17: 19%; CY16: 8%; CY15: 5%). and Deep Freezers (9MCY17: 10%; CY16: 8%; CY15: 9%).
- Power Division's sales are spearheaded by Distribution Transformers (9MCY17: 47%; CY16: 45%; CY15: 35%), followed by Switch Gears (9MCY17: 17%; CY16: 15%; CY15: 14%) and Energy meters (9MCY17: 11%; CY16: 5%; CY15: 5%).
- EPC business of the entity covers 21% share of the power division worth PKR 2,026mln.
- Rise in topline resulted in 14% increase in gross margins (CY16: 31%; CY15: 30%).The declining margin emanated from higher discounts provided to maintain market share.
- An increase of 3% in financial charges and 19% in taxation lead to a slight decrease in the Company's profit after tax on YoY basis (9MCY17: PKR 2,972mln; CY16: PKR 3,670; 9MCY16: PKR 3,006mln; CY15: PKR 2,880mln).
- The management would focus on increasing market share in its high margin products mainly refrigerators and air conditioners in appliances segment, and distribution transformers and energy meters in power segment.

Financial Risk

- Significant working capital requirement; a facet of high inventory and receivable days (Net cash cycle: 9MCY17: 207 days; CY16: 219 days; CY15: 213 days).
- During 9MCY17, a slight increase in Company's FCFO is witnessed (9MCY17: 4,997mln; CY16: PKR 5,584mln; 9MCY16: PKR 4,953mln; CY15: PKR 5,468mln). These high cash flows provide significant debt coverage (9MCY17: 1.9x; CY16: 1.7x; CY15: 1.5x).
- To meet the working capital needs Company's debt level is increased leaving the debt to debt plus equity (net of revaluation surplus) to 38% (end-Dec16: 35%; end-Dec15: 45.7%).
- The Company intends to sustain its total debt up to PKR 14bln by end-Dec 2018.

Sukuks

- PEL intends to issue PPS of PKR 1,500mln, having a tenor of 15 months with a partial/ full call option after 12 months. The instrument carries a profit rate of 3MK + 105bps with quarterly payments.
- Sukuk II was issued in Mar08 for PKR 1,100mln. The instrument has a life till March 2019. The profit on issue, payable quarterly, is at 3MK + 100bps with a floor of 8%.
- PEL issued short-term, unsecured Commercial Paper (CP) of PKR 1,200mln to finance its working capital requirements. CP, having a tenor of 9 months, carries a profit rate of 9MK + 125bps. The redemption will be at face value at the time of maturity.

RATING RATIONALE

The ratings reflect PEL's strong business profile in its respective markets - Appliances and Power - supplemented by its strong brand. The Company, while aiming to diversify its product base, has continued to focus on improving technology in its key revenue generating products. This resulted in higher sales volumes. The performance of the Company is well supported by healthy business margins, though profits sustained given expansionary market strategy. Cashflows remained largely stable, while supporting the debt servicing ability of the company at satisfactory level.

High working capital needs emanating from long inventory and receivables cycle expose the Company to financial risk. While the management's focused efforts provided relief. Comfort is drawn from sponsors' support to manage these needs (former equity injection and retention of profits). Meanwhile, the Company has articulated an adequate debt management policy a) total debt would be restricted to 2.5 times of free cash flows [end-Sep17: 1.2x] and b) short-term borrowings would not exceed 50% of net working capital needs [end-Dec16: 39%].

KEY RATING DRIVERS

The ratings take into account improving business dynamics in Appliances and Power segments apart from the Company's strengthening business risk profile. Increase in market share with sustainable cash flows have benefited the ratings. Meanwhile, close monitoring of working capital requirements and debt servicing capacity remains imperative to maintain the company's financial health; hence ratings. The Sukuk rating incorporates the management plan of keeping a sizeable cushion in its credit lines over the tenor of the instrument.

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
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.	<p>A1+: The highest capacity for timely repayment.</p> <p>A1: A strong capacity for timely repayment.</p> <p>A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.</p> <p>A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.</p> <p>B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.</p> <p>C: An inadequate capacity to ensure timely repayment.</p>
AA+	Very high credit quality. Very low expectation of credit risk.	
AA	Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	
AA-		
A+	High credit quality. Low expectation of credit risk.	
A	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.	
A-		
BBB+	Good credit quality. Currently a low expectation of credit risk.	
BBB	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.	
BBB-		
BB+	Moderate risk. Possibility of credit risk developing.	
BB	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.	
BB-		
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-		
CCC	Very high credit risk. Substantial credit risk	
CC	“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.	
C		
D	Obligations are currently in default.	

<p>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’.</p>	<p>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.</p>	<p>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.</p>	<p>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</p>
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Name of Entity

Pak Elektron Limited

Sector

Engineering

Type of Relationship

Solicited

Purpose of the Rating

Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
10-Jan-18	A+	A1	Stable	Maintain
26-Apr-17	A+	A1	Stable	Maintain
03-Dec-16	A+	A1	Stable	Upgrade
4-Dec-15	A	A1	Stable	Upgrade
12-Dec-14	A-	A2	Stable	Initial

Related Criteria and Research

Household Appliances Sector Study - Dec17
Electrical Engineering Sector Study - Dec17

Methodology:

Corporate Rating Methodology

Rating Analysts

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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

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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

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Regulatory and Supplementary Disclosure

[Name of Issuer](#)

Pak Elektron Limited

[Name of Issue](#)

Pak Elektron Limited | Sukuk II

[Sector](#)

Engineering

[Type of Relationship](#)

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[Purpose of the Rating](#)

Independent Risk Assessment

[Rating History](#)

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03-Dec-16	A+	-	Stable	Upgrade
04-Dec-15	A	-	Stable	Upgrade
06-Jan-15	A-	-	Stable	Initial

[Amortization Schedule](#)

See Annexure B

[Instrument Details](#)

Nature of Instrument	Size of Issue (PKR mln)	Tenor (yrs) including grace period of 4 years post debt restructuring	Security	Trustee
Sukuk II	1,100	10.5	First pari passu charge over all present and future fixed assets of the company	BankIslami Pakistan Limited

[Related Criteria and Research](#)

Household Appliances Sector Study | Dec-17
Electrical Distribution Sector Study | Dec-17

[Methodology](#)

Corporate Rating Methodology

[Rating Analysts](#)

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Regulatory and Supplementary Disclosure

Repayment Schedule Sukuk-II

Annexure B

SUKUK Amount (PKR '000) 1,100,000
 Period (years) 7
 Repayment Quarterly
 Pricing 3 K + 1.00% Floor at 8%

Date	Installment	Beginning Principal	Payment		Ending Principal	
			Principal	Markup		
30-Sep-08		1,100,000	-	-	1,100,000	
31-Dec-08	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-09	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-09	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-09	92	30,720	1,100,000	-	30,720	1,100,000
31-Dec-09	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-10	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-10	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-10	92	30,720	1,100,000	-	30,720	1,100,000
31-Dec-10	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-11	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-11	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-11	92	30,720	1,100,000	-	30,720	1,100,000
31-Dec-11	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-12	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-12	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-12	92	30,720	1,100,000	-	30,720	1,100,000
31-Dec-12	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-13	91	30,387	1,100,000	-	30,387	1,100,000
30-Jun-13	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-13	91	30,387	1,100,000	-	30,387	1,100,000
31-Dec-13	91	30,387	1,100,000	-	30,387	1,100,000
31-Mar-14	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-14	91	30,387	1,100,000	-	30,387	1,100,000
30-Sep-14	92	30,720	1,100,000	-	30,720	1,100,000
31-Dec-14	92	30,720	1,100,000	-	30,720	1,100,000
31-Mar-15	90	30,053	1,100,000	-	30,053	1,100,000
30-Jun-15	91	93,377	1,100,000	68,750	24,627	1,031,250
30-Sep-15	92	89,545	1,031,250	68,750	20,795	962,500
31-Dec-15	92	88,158	962,500	68,750	19,408	893,750
31-Mar-16	91	86,576	893,750	68,750	17,826	825,000
30-Jun-16	91	85,205	825,000	68,750	16,455	756,250
30-Sep-16	92	82,613	756,250	68,750	13,863	687,500
31-Dec-16	92	82,613	687,500	68,750	13,863	618,750
31-Mar-17	90	80,955	618,750	68,750	12,205	550,000
30-Jun-17	91	79,720	550,000	68,750	10,970	481,250
30-Sep-17	92	78,454	481,250	68,750	9,704	412,500
31-Dec-17	92	80,270	412,500	68,750	11,520	343,750
31-Mar-18	90	78,141	343,750	68,750	9,391	275,000
30-Jun-18	91	76,347	275,000	68,750	7,597	206,250
30-Sep-18	92	74,510	206,250	68,750	5,760	137,500
31-Dec-18	92	72,590	137,500	68,750	3,840	68,750
31-Mar-19	90	70,628	68,750	68,750	1,878	-
		2,091,422		1,100,000	991,422	

Jun16 and Sep 16 payments were made in quarter of Jun16