RATING REPORT

Lucky Cement Limited (LCL)

REPORT DATE:
May 03, 2021

RATING ANALYST:
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Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA+	A-1+	AA+	A-1+
Rating Outlook	Stable		Stable	
Rating Date	*Mau 03, 2021*		*February 19, 2020*	

COMPANY INFORMATION	
Incorporated in 1993	**External auditors:** A. F. Ferguson & Co. Chartered Accountants
Public Limited Company	**Chairman:** Mr. Muhammad Yunus Tabba
Key Shareholders (with stake 5% or more):	**CEO:** Mr. Muhammad Ali Tabba
- ***Directors and Spouse- 19.48%*** - ***Sponsors- 18.34%*** - ***Associated Companies, Undertakings & related parties- 22.54%*** - ***Mutual Funds- 5.85%*** - ***General Public (Local) - 10.95%*** - ***General Public (Foreign) - 12.19%***	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria ***(April 2019)*** https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Lucky Cement Limited

OVERVIEW OF THE INSTITUTION

Lucky Cement Limited (LCL) was incorporated on September 18, 1993 as a public limited company. LCL is listed on Pakistan Stock Exchange Limited as well as London Stock Exchange, with the head office situated in Karachi, and regional office located in Pezu, KPK. Further, the Company's liaison offices are situated in Islamabad, Quetta, Multan, D.I.Khan, Lahore and Peshawar. The company has two production facilities at Pezu, District Lakki Marwat in Khyber Pakhtunkhwa and at Main Super Highway in Karachi, Sindh. The company is engaged in manufacturing, selling and marketing of cement.

Profile of Chairman

Mr. Muhammad Yunus Tabba possesses more than 50 years of experience spanning across various sectors. He has also been awarded "Businessman of the year" by the Chamber of Commerce several times during his career. Furthermore, in recognition of his services rendered in the field of entrepreneurship and public service, he has been bestowed with the award of "Sitara-e-Imtiaz" by the President of Islamic Republic of Pakistan.

Profile of CEO

Mr. Muhammad Ali Tabba also serves as the CEO of Yunus Textile Mills Ltd (YTML), a state-of-the-art home textile mill and the largest exporter of home textile products from Pakistan. Mr. Tabba also serves in the capacity of

RATING RATIONALE

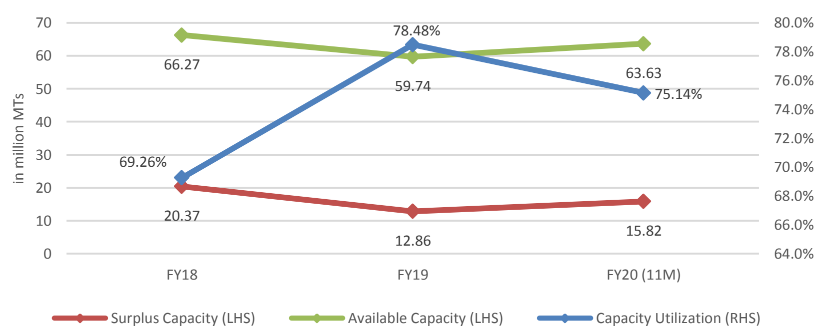
Lucky Cement Limited ('LCL' or 'the Company') was incorporated in 1993 and is one of the largest cement manufacturers in Pakistan. The Company comes under the umbrella of Yunus Brothers Group (YBG), which is among one of the biggest conglomerates of Pakistan. LCL is listed on Pakistan Stock Exchange (PSX) while it has also issued Global Depository Receipts (GDRs) listed on London Stock Exchange (LSE).

LCL has a Cement production capacity of 12.15m MT p.a. located in Karachi and Pezu (KPK province), increasing from 9.35m MT p.a. as a new facility, featuring a capacity of 2.8m MT p.a. at Pezu, was added during the year FY20. The company has its own captive power plant of 180MW and also produces energy through Waste Heat Recovery (WHR), Refuse Derived Fuel (RFD) and Tyre Derived Fuel (TDF).

On foreign operations, LCL has 1.74 MT p.a. cement grinding plant in Basra, Iraq and 1.18 MT p.a. fully integrated cement plant in Congo. Additionally, 1.20 MT p.a. cement production facility in Samawah, Iraq has recently commenced its commercial operations in March, 2021. Adding all above, overseas cement production capacity now stands at 4.12 MT p.a.

<u>Sector Update</u>

- During FY20, the cement industry offtake recorded marginal uptick of 2% to 47.812 m MT p.a., on the back of strong growth (~20%) in export dispatches.
- The industry capacity utilization depicted improvement in FY19, when available industry capacity had dropped; however, as some capacity enhancement projects came online in FY20, in addition to the pandemic-induced slowdown, the capacity utilization was affected, as reflected in the figure below.



in million MTs	*FY18*	*FY19*	*FY20*	*H1'FY20*	*H1'FY21*
Local dispatches	41.147	40.235	39.965	20.373	23.615
Export dispatches	4.746	6.522	7.847	4.377	5.022
Total	**45.893**	**46.757**	**47.812**	**24.750**	**28.637**

- With domestic dispatches remaining stagnant in FY20 (YoY), the 2% growth in aggregate dispatches entirely emanated from the growth in export dispatches. Export dispatches, subsequent to posting strong growth of 38% in FY19, continued with the momentum, with growth coming in at 20% for FY20. The growth in export dispatches entirely emanated from exports sales to Afghanistan.
- Subsequent to year-end FY20, the LSM index posted growth of 37% in H1'FY21. Both local and export cement dispatches displayed an increase of 15.9% and 14.7%,

Vice Chairman on the Board of ICI Pakistan Limited and is also the Chairman of KIA Lucky Motors. Moreover, Mr. Tabba also serves in the role of Chairman Lucky Electric Power Company Limited. Mr. Muhammad Ali Tabba was awarded the "Sitara-e-Imtiaz" by the President of Islamic Republic of Pakistan in 2018.

respectively, vis-à-vis SPLY. Resultantly, overall volume increased by 15.7%, vis-à-vis SPLY.

- Resumption in economic activities after Covid-19 lockdown, better macroeconomic indicators and construction package announced by the GoP contributed in the uptick of local cement demand during H1'FY21.
- The industry's future outlook is positive, in view of the infrastructure projects in the pipeline. Downside risk to profitability of cement industry participants is likely to emanate from further more than expected elongation of the pandemic and potential lockdown situation. Furthemore, so far, interest rates have remained at low level of 7%, albeit potential increase in the same, would impact the demand and profitability of the cement companies.

Operational Update

Capacity Utilization	*FY19*	*FY20*	*H1'FY21*
Cement	73.1%	60.4%*	75.3%
Clinker	85.3%	58.9%	76.0%

** Based on actual capacity available, instead of year-end capacity*

- Given the new capacity of 2.8m MT p.a., which was available for half of FY20, the capacity utilization of the company was affected. As per management, the lower capacity utilization can be attributed to higher clinker exports, planned maintenance shutdown and lower demand on account of the pandemic-induced slowdown
- Given improved demand dynamics observed in H1'FY21, the capacity utilization has depicted improvement.

in million MTs	*FY18*	*FY19*	*FY20*	*1HFY20*	*1HFY21*
Local dispatches	6.686	5.854	5.463	2.594	3.662
Export dispatches	1.131	1.820	2.162	1.083	1.335
Total	**7.817**	**7.674**	**7.625**	**3.677**	**4.997**

- LCL's local cement dispatches clocked in at 5.463mn MTs in FY20 (FY19: 5.854mn MTs), down by 7% YoY; this was following another contraction in FY19 of 12% and in tandem with the downturn in industry's local dispatches. LCL's share in the local dispatches has decreased from 16.2% in FY18 to 13.7% in FY20.
- On the other hand, LCL has managed to tap exports market and increased its offtake to 2.162mn MTs in FY20 compared to 1.820mn MTs a year earlier. The company has grown its share in the export market from 23.8% in FY18 to 27.6% in FY20.
- Dispatches have started to rebound as local demand grew in tandem with the pickup in economic activities, which has translated in an increase of 41% in local dispatches during H1'FY21, vis-à-vis SPLY. Total dispatches of the company grew by 36% during H1'FY21. The company has managed to increase its market share in the domestic market to 15.5% in H1'FY21.
- On exports market front, LCL is also catering the demand in Sri-Lankan market in addition to Bangladesh and China. LCL has a regional office in Colombo and appointed two more dealers in order to expand market reach. The company is actively targeting new geographical locations in order to increase its presence in global market.

	FY19	*FY20*	*1H'FY20*	*1H'FY21*
Net Sales	**48,021**	**41,871**	**21,211**	**30,075**
Gross Profit	**13,984**	**6,077**	**3,224**	**8,585**
Gross Margin (%)	**29.1%**	**14.5%**	**15.2%**	**28.5%**
Operating Profit	**12,246**	**3,996**	**2,247**	**5,673**
Operating Margin (%)	**25.5%**	**9.5%**	**10.6%**	**18.9%**
Profit After Tax	**10,490**	**3,344**	**1,937**	**4,541**
Net Margin (%)	**21.8%**	**8.0%**	**9.1%**	**15.1%**

- As illustrated in the table above, LCL's topline revenue contracted by 13% YoY. Furthermore, the sales mix has shifted towards export sales, which comprised 20% of the gross revenues vis-à-vis 15% in FY19.

- The margins of the company depicted a consistent drop in the last 2 years mainly due to weak macroeconomic conditions and high interest rate environment.
- Note that, the cement industry has done capacity expansion of around 10mn MTs during the last 2 years which created excess supply situation giving way to high price competition.
- Furthermore, part of the reason for why the margins came in lower, is the tilt towards exports sales, where pricing is relatively lower than domestic sales.

<u>Key Rating Drivers</u>

Strong sponsorship profile and diversified long term investment portfolio of LCL is a key rating driver. Other Income from assets also diversifying earning avenues

- LCL is a part of Yunus Brother Group (YBG) which is a leading conglomerate with strong financial profile and has diverse presence across multiple sectors including Cement, Power Generation, Chemicals, Automobile, Entertainment, Textile, Hospitality, Food & Commodities and others.
- Ratings assigned to LCL draw support from strong financial profile and diversified presence of sponsor. Long term investments amounted to 50.2b as at Dec'21, representing 35% (FY20: 35%, FY19: 27%) of the total assets.
- During FY20, LCL has invested Rs. 19.5b in Lucky Electric Power Company Limited (LEPCL) – a 660MW coal based power plant in Karachi. This investment has further increased to Rs. 22.5b as at 1HFY21, due to which LCL has mobilized long term debt on its balance sheet.
- LCL earned other income of Rs. 3.19b in FY20 (FY19: Rs. 3.24b) and Rs.836m in H1'FY21.

Other Income	FY19	FY20
Income from non-financial assets	**431,235**	**162,986**
Income from financial assets		
-Dividend from subsidiary	457,000	1,162,684
-Dividend from associate	183,410	122,273
-Dividend from mutual fund	37,503	200,861
-Income from deposits	2,132,516	1,537,055
Grand Total	**3,241,682**	**3,185,859**

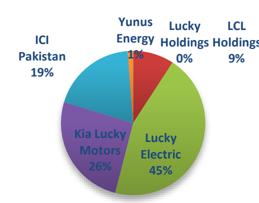


Figure 1: Breakup of Investment in Associates/Subsidiaries (Dec'20)

Strong liquidity profile and comfortable cash flow coverage

- Over the years, LCL has consistently generated healthy cash flow from operations which has resulted in accumulation of surplus liquidity. Excess cash flow has allowed the Company to undertake significant investments and capital expenditure over the last three years from internally generated cash.
- The company's cash flow coverage indicators are considered to be very comfortable. The cashflow generated in H1'FY21 (annualized), provides debt coverage of 1.3x, which means that the company can cover the entire debt on the balance sheet from a single year's cash flow generation, with a cushion.

	FY19	FY20	1HFY21
FFO (In millions PKR)	**14,101**	**7,492**	**7,693**
FFO to Debt	**9.7x**	**1.8x**	**1.3x***
FFO to LT Debt	**NA**	**16.8x**	**3.4x***
DSCR	**967.2x**	**54.3x**	**40.8x***

**Annualized*

Low leverage indicators & conservative financial policy translate in very low financial risk profile

- Equity base of the Company has grown at a CAGR of 9% over the past five years on account of healthy internal capital generation. The company has not paid any dividend during FY20.
- Owing to a conservative financial policy, the company has historically remained debt free, while it has recently started acquiring debt in order to sponsor a long term investment subsidiary named Lucky Electric Power Company Limited. The current long term debt has taken under the TERF scheme and SBP's Salary Refinance Loan (SRF). On the other hand, short term borrowing has also increased on account of higher working capital requirements. However, quantum of the same remains modest given size of cash flows and LCL's existing equity base.
- Going forward, LCL is planning to acquire further subsidized long term debt under LTFF and TERF scheme to finance the several upcoming CAPEX projects including a new clinker line of 3.15MTPA at its Pezu Plant.

Balance Sheet Extract	*FY18*	*FY19*	*FY20*	*1HFY21*
Equity	86,367	94,318	99,184	103,732
Short term debt	-	2,900	7,931	7,050
Long term debt	-	-	507	4,525
Total debt	-	2,900	8,438	11,575
Dividend Payout Ratio	34%	20%	0%	0%

- We have incorporated the planned debt into LCL's leverage projections and expect the same to remain aligned with the threshold for the assigned rating.

Sound corporate governance framework supported by a well-designed organizational structure, experienced management team and strong disposition towards transparency and disclosures

- LCL has instituted a well-designed organizational structure comprising separate departments for key functions. All divisions have independent management teams and organizational structure. Board composition is in line with best practices while effective oversight mechanism is in place through functioning board committees. Detailed annual report disclosures reflect strong disposition towards transparency and disclosures.

Lucky Cement Limited (LCL) Appendix I

FINANCIAL SUMMARY- Unconsolidated (Rs. in m)					
BALANCE SHEET		**FY18**	**FY19**	**FY20**	**1HFY21***
Fixed Assets		40,913	57,276	60,155	60,452
Long term Investments		24,981	34,314	47,144	50,195
Stock-in-Trade + Stores and Spares		10,580	11,063	9,529	11,251
Trade Debts		2,424	2,059	3,423	2,661
Short term investments		35	1,056	2,971	10,013
Cash & Bank Balances		27,435	15,657	7,817	4,056
Total Assets		108,999	125,089	135,868	142,175
Trade and Other Payables		13,121	19,196	19,355	16,622
Long Term Debt		-	-	507	4,525
Short Term Debt		-	2,900	7,931	7,050
Total Debt		-	2,900	8,438	11,575
Paid Up Capital		3,234	3,234	3,234	3,234
Total Equity		86,367	94,318	99,184	103,732
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**H1'FY20**	**H1'FY21**
Net Sales	47,542	48,021	41,871	21,211	30,075
Gross Profit	16,952	13,984	6,077	3,224	8,585
Profit Before Tax	15,119	12,221	3,820	2,199	5,517
Profit After Tax	12,197	10,490	3,344	1,937	4,541
RATIO ANALYSIS					
Gross Margin (%)		35.7%	29.1%	14.5%	28.5%
Net Margin (%)		25.7%	21.8%	8.0%	15.1%
Net Working Capital		27,718	9,801	(488)	5,275
Adjusted FFO		16,084	14,101	7,492	7,693
FFO to Total Debt (x)		NA	9.7	1.8	1.3
FFO to Long Term Debt (x)		NA	NA	1.8	3.4*
Debt Servicing Coverage Ratio (x)		NA	967.2	54.3	40.8*
Gearing (x)		-	0.03	0.09	0.11
Leverage (x)		0.26	0.33	0.37	0.37
Current Ratio (x)		2.82	1.42	0.98	1.20
STD Coverage		NA	452%	153%	120%
ROAA (%)		11.8%	9.0%	2.6%	3.3%
ROAE (%)		14.7%	11.6%	3.5%	4.5%

**Ratios Annualized*

*** FFO Adjusted for dividend income*

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES					Appendix III
Name of Rated Entity	Lucky Cement Limited				
Sector	Cement and Construction				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	03/05/2021	AA+	A-1+	Stable	Reaffirmed
	19/02/2020	AA+	A-1+	Stable	Initial
Instrument Structure	N/A				
Statement by the Rating Team	VIS, 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(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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Due Diligence Meetings Conducted	**Name**	**Designation**	**Date**		
	S.R. Khawar	Manager Treasury	27-Mar-2021		