

AMRELI STEELS LIMITED (ASL)
RATINGS (MAY 2011)

	NEW	PREVIOUS
SUKUK (PKR 880 MLN)	A-	A-
PRIVATELY PLACED, SECURED		

FINANCIAL DATA

PKR (mln)

	Mar-11*	Jun-10	Jun-09
Total Assets	7,212	5,552	4,931
Equity	3,275	2,570	1,741
Turnover	3,636	4,103	4,056
Net Income	37	104	(481)
EBITDA	300	368	(66)
EBITDA Interest Cover (x)	1.16	0.87	(0.16)
FCFO/Gross Interest+Current maturity+Uncovered ST borrowing	0.77	0.47	(0.07)
Total Debt/Total Debt+Equity (%)	51	51	60

* Based on unaudited accounts for nine months ended Mar 31, 2011.

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RATING RATIONALE AND KEY DRIVERS

- The rating reflects the established franchise of the company in reinforcement steel bars manufacturing segment. The rating incorporates continuing demonstrated commitment of sponsors – Akberali Family. However, financial profile of the company remains weak owing to lower profitability and constrained cash flows, resulting in weak debt servicing coverages. Cognizant of this, the management is making efforts to revamp its financial discipline while bringing efficiency in overall plant operations. In addition, commissioning of billet manufacturing plant would help company to ensure stable raw material supply while improving its re-bar capacity utilization and margins. Meanwhile, the rating draws comfort from grace period and staggered repayment structure of Sukuk, wherein cash flows are expected to improve post integration of new plant.
- The rating is dependent upon the company's ability to timely execute its planned integration while strengthening overall business and financial profile. Meanwhile, material increase in leveraging wherein sponsors fall short of fresh injection to sustain an adequate capital structure may negatively impact the rating.

SUKUK ISSUE

- The company issued a Sukuk of PKR 880mln in December 2009 to re-profile its short term borrowings, which were earlier used to finance ASL's backward integration project. The issue is for a term of seven years including a grace period of two years. The profit is payable at 3 month KIBOR plus 250bps quarterly in arrears.
- The security structure of the instrument entails first pari passu charge on all present and future fixed assets of ASL (equal to total principal amount) whereas 25% margin amount shall be covered through a charge on current assets. In addition, ASL would maintain a reserve with the agent bank, equivalent to one installment, in equal amounts over a period of one quarter for the upcoming quarterly installment. At least 24% of the Issue amount would be redeemed during a period of three years starting after the grace period (Dec-11) and the balance amount in sixth and seventh year in equal quarterly installments

ASSESSMENT

- ASL is principally involved in manufacturing and sale of reinforcement bars – rebars, which are utilized for construction purposes. Steel billets are used as the raw material for rebars. Historically, Pakistan Steel Mills (PSM) has remained the major supplier of billets. However, during 9MFY11 ASL procured majority of its raw material from small private sector billet manufacturers and imports owing to non operational PSM. Though lately improved, shortage of billets coupled with lower availability of required working capital kept ASL's capacity utilization at relatively lower level (9MFY11: 56%; FY10: 46%). Sales volumes, as a result, remained low. Nevertheless, overall profitability of the company has improved vis-a-vis last year on account of sustained margins and reduction in financial charges. Given a low margin business, growth in volumes remain critical to achieve desired profitability.
- The company is currently in the process of setting up a billet manufacturing plant with a capacity of 190,000 tons. The cost of the plant is ~PKR 3,500 mln and is expected to come online within FY11. This vertical integration is expected to help the company a) attain a smooth supply of raw materials, b) achieve an optimal level of capacity utilization, c) supplement its revenues through sale of surplus billets, and d) improve its margins. Interest cost would remain an important concern as significant portion (around 50%) of this project is financed through borrowing. However, lately, the company has obtained fresh borrowing at lower than existing borrowing cost, resulting in reduction in average interest rate.
- ASL, as part of its plan to improve systems and process has taken various initiatives interalia, improving MIS reporting, though gradually, and formulation of various management committees to strengthen its control mechanism. The company intends to harmonize its organizational structure with clear delegation of responsibilities and improved governance structure.
- Despite the fact that cash flows of the company still remain weak, the company managed to service its debt obligations mainly because of financial support from the sponsors. Company's borrowings are a mix of foreign and local debt. Though the company would require lower capex in near to medium term, working capital requirements would increase owing to expected improvement in capacity utilization. Therefore, the company is expected to remain leveraged. Nevertheless, the rating draws comfort from built in grace periods and favorable interest rate on a sizable portion of company's borrowing. Going forward, given expected improvement in profitability and the sponsors' commitment to maintain an optimal mix of debt and equity, coverages are expected to improve.

PROFILE

- ASL was incorporated in 1984 and is fully owned by Akberali Family. AkberAli family is engaged in steel and allied businesses since early forties. The company uses modern technology for producing high quality steel bars according to British and American standards, with an installed capacity of 150,000 tons per annum.
- ASL's three member board is family dominated. Mr. Abbas Akberali, the CEO of the company, is a metallurgical engineer and holds an MBA degree from Columbia University, USA. He has around four decades of experience in local and the Middle-East markets. He is assisted by a team of relatively young but well-qualified professionals. Currently, few changes are being contemplated at top management positions by the sponsoring family.