ASIL

We recommend to subscribe the IPO with DCF based Jun-21 TP of Rs.44

Equity Research | Food & Personal Care Products | Monday, 5 October, 2020

We recommend to subscribe the IPO at Rs.30 with a DCF based Jun-21 TP of Rs.44 which provides an upside potential of 47% relative to its floor price of Rs30

The registration process of eligible investors has already been commenced from 1st Oct 2020 and will close at 3:00 pm on 7th Oct 2020

Bidding dates are from 6th Oct 2020 to 7th Oct 2020 (From 9:00 am to 5:00 pm)

Dates of public subscription are from 14th Oct 2020 to 15th Oct 2020 from 9:00 am to 5:00 pm

Company Overview

Agha Steel Industries (ASIL) started its commercial operations on 1st January 2012, producing Billets and Rebars at an installed capacity of 250,000 MT p.a. and 150,000 MT p.a. respectively. The Company only deals in graded steel and now operates at an annual Billets and Rebars production capacity of 450,000 MT p.a. and 250,000 MT p.a. respectively and has a market share of more than 3%, according to the management of the Company.

Purpose of the Issue

The company wants to raise Rs3.6bn by issuing 120mn shares at the floor price of Rs30 per share. The principal purpose of the issue is to increase its capacity and also continue its technological advancement by installing a state of the art and first in Pakistan Mi.Da. Rolling Mill.

Mi.Da. rolling mill would bring cost & time efficiencies for the company as the uninterrupted production cycle from raw material to finished product, and the extreme compactness of the technological area will allow ASIL to be one of the most cost-efficient plants in Pakistan. The total project cost of PKR 7.04 Billion shall be financed at the project D/E ratio of 49:51.

Details of the utilization of debt and equity proceeds are given below:

Particular	PKR (bn)	Usage	%
IPO Proceeds	3.60		51
L.T Debt	1.74	Expansion & Working Capital	25
S.T Debt	1.70		24
Total	**7.04**	**Total**	**100**

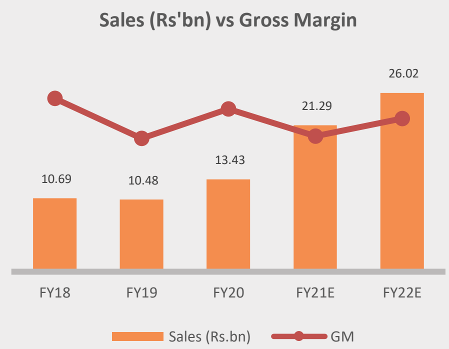
Industry Overview

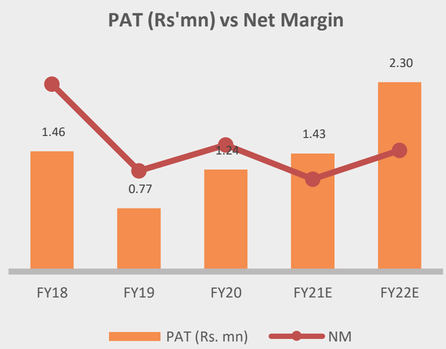
Steel Sector being heavily dependent on imported raw material is a highly leveraged sector. The overall economic slowdown prior to the COVID 19 lockdown has had a negative impact on the construction sector as well as the steel sector of Pakistan. Pakistan's steel industry has suffered due to the sudden outbreak of the pandemic, which has disturbed the pace of work on public sector developmental projects and CPEC.

Construction being the backbone of the industry was a special concern for economic policymakers. During the COVID lockdown, the economic measure was taken by the Government whereby the offer rate was reduced to 7%. Reduced rates financing and deferment of liabilities were introduced, the high leverage steel sector was the biggest beneficiary of the said relief measures. Also, with certain tax benefit schemes introduced in the construction sector, the demand in the post COIVD scenario for the steel sector is on the higher side.

Key Statistics

Symbol	ASIL
TP - Jun 21	44.00
Floor Price	30.00
Upside	47%
Free Float (mn)	120
Market Cap. (Rs.mn)	172,823





Sources: ACPL Research, Company Financials, PSX,

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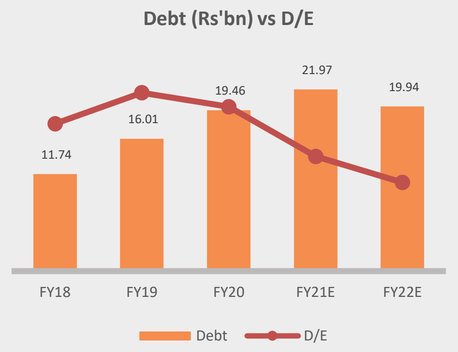
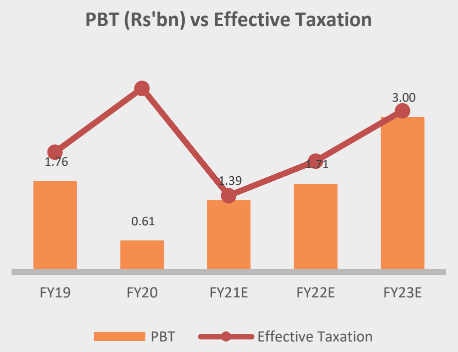
Key Statistics





Symbol	FY21E PE
ASTL	23.91x
MUGHAL	17.82x
Average	**20.87x**
ASIL	12.07x
Discount	**42%**

Sources: ACPL Research, Company Financials,

Financial Performance

ASIL has a promising track record of financial performance with consistent growth in revenues and profitability. The company has successfully been able to grow its revenues and earnings at a 5-year CAGR of 10% and 13% respectively in FY20. The company, especially in FY20, has outperformed its competitors by posting a tremendous earnings growth of 61% YoY as compared to the earnings growth of its listed competitors ASTL (-3532% YoY) and MUGHAL (-57% YoY). The reason behind this is the use of low-cost scrap steel as the raw material and selling the final product to institutional clients at a premium price (premium price is charged as the company provides a credit period of around 100 days which also inflates the working capital requirement) which enables the company to maintain a gross margin of around 23.7% in FY20 as compared to the gross margins of ASTL (7.5%) and MUGHAL (9.6%) during the same period.

Going forward, we expect the revenues and earnings of the company to grow at a 4-year CAGR of 26% on account of the planned expansion, higher cost-efficiency due to the installation of new technology (Mi.Da. Rolling Mill), and growing demand amid the post-COVID-19 scenario.

Investment Rationale

The Company possesses 45-ton Eccentric Bottom Tapping (“EBT”) Electric Arc Furnace (“EAF”) with ladle refining furnace and has Cut to Length (“CTL”) facility allowing it to cast molten steel in a 3 strand continuous casting machine and enabling the Company to produce customized lengths of Billets and Rebars. The ability to produce Rebars of different grades and sizes from the same production facility allows the Company to adjust its production mix with respect to the demand in the market.

Furthermore, savings of 20%-25% of the total electricity cost, less labor-intensive, and higher efficiency in terms of yield recovery are some of the competitive advantages the company has by having an electric arc furnace instead of an induction furnace.

Moreover, the demand growth is expected to increase ahead in the post-COVID-scenario which is clearly evident by the cement dispatches which have grown by 22% YoY in 1QFY21. The growth prospects are highly probable amid SBP’s efforts to stimulate the economy by keeping the real interest rate negative and the recent construction package announced by the Prime Minister of Pakistan to restart the development and reindustrialization. Furthermore, social measures being undertaken such as the “Naya Pakistan Housing Scheme”, construction of dams for water conservation and measures being taken to ensure energy and food security will underpin steel demand in the future.

Valuation

The superior performance of the company allows it to trade at a premium multiple as compared to its listed competitors. However, the FY21E PE of ASIL stands at 12.07x at a floor price of Rs.30 as compared to the peers’ average of 20.87x. Therefore, we recommend to **SUBSCRIBE** the IPO at Rs.30 with a DCF based Jun-21 TP of Rs.44 which provides an upside potential of 47%.

Key Risks to Valuation

- Higher than expected increase in working capital requirement
- Higher than expected depreciation of PKR
- Prolonged Covid-19 scenario

Financial Projections

Rupees' millions	FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
Net sales	10,688	10,482	13,427	21,295	26,019	29,132	33,578
Cost of sale	7,995	8,451	10,158	17,095	20,225	22,394	26,285
Gross profit	**2,693**	**2,031**	**3,269**	**4,200**	**5,794**	**6,738**	**7,293**
Administrative Expenses	180	208	202	246	279	303	330
Selling And Distribution	219	124	153	201	233	259	285
Operating Profit	**2,295**	**1,700**	**2,914**	**3,754**	**5,283**	**6,176**	**6,678**
Other Income/ (Expense)	- 113	42	178	13	- 58	- 290	- 336
Finance cost	419	1,135	1,703	2,060	2,228	2,030	1,885
Profit before taxation	1,763	607	1,390	1,707	2,997	3,856	4,458
Taxation	307	- 162	154	275	702	1,120	1,346
Profit after taxation	**1,456**	**769**	**1,236**	**1,432**	**2,295**	**2,736**	**3,111**
EPS	**2.53**	**1.33**	**2.14**	**2.49**	**3.98**	**4.75**	**5.40**

Source: ACPL Research, Company Financials

Horizontal Analysis

	FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
Net sales		-1.9%	28.1%	58.6%	22.2%	12.0%	15.3%
Cost of sale		5.7%	20.2%	68.3%	18.3%	10.7%	17.4%
Gross profit		**-24.6%**	**60.9%**	**28.5%**	**38.0%**	**16.3%**	**8.2%**
Administrative Expenses		15.7%	-2.8%	21.6%	13.3%	8.8%	8.9%
Selling And Distribution		-43.5%	24.0%	30.9%	16.2%	11.2%	10.0%
Operating Profit		**-25.9%**	**71.4%**	**28.8%**	**40.7%**	**16.9%**	**8.1%**
Other Income/ (Expense)		-137.0%	325.9%	-92.6%	-536.5%	-403.3%	-15.6%
Finance cost		170.9%	50.1%	21.0%	8.2%	-8.9%	-7.2%
Profit before taxation		-65.6%	129.0%	22.8%	75.6%	-28.7%	-15.6%
Taxation		-152.8%	195.1%	78.4%	155.5%	59.6%	20.2%
Profit after taxation		-47.2%	**60.7%**	**15.9%**	**60.3%**	**19.2%**	**13.7%**
EPS		**-47.2%**	**60.7%**	**15.9%**	**60.3%**	**19.2%**	**13.7%**

Source: ACPL Research, Company Financials

Key Ratios

Profitability Ratios		FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
GP Margin	%	25.20	19.38	23.66	19.72	22.27	23.13	21.72
OP Margin	%	21.47	16.21	21.70	17.63	20.30	21.20	19.89
NP Margin	%	13.62	7.33	9.20	6.72	8.82	9.39	9.27
ROE	%	26.57	12.43	15.14	10.85	14.82	15.01	14.58
ROCE	%	21.23	13.11	19.77	19.61	28.58	30.00	28.36
ROA	%	7.47	3.14	4.12	3.79	5.99	7.23	8.28

Liquidity Ratios		FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
Current	x	1.11	1.20	1.08	1.18	1.21	1.33	1.60
Acid-test	x	0.33	0.32	0.28	0.33	0.39	0.45	0.62
Cash to current liab.	x	0.00	0.02	0.00	0.01	0.03	0.01	0.01

Activity Ratios		FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
Inventory Turnover	x	2	1	2	2	2	2	3
Receivables Days		102	117	104	100	100	100	100
Inventory Days		236	335	310	280	250	220	170
Payables Days		24	23	48	30	30	30	30
Operating Cycle		313	429	366	350	350	350	350

Investment Ratios		FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
EPS	Rs.	2.53	1.33	2.14	2.49	3.98	4.75	5.40
DPS	Rs.	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Div. Yield	%	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Dividend Cover	x	0.00	0.00	0.00	0.00	0.00	0.00	0.00
BVPS	Rs.	15.16	17.11	22.58	28.93	26.88	31.63	37.03
Payout	%	0.00	0.00	0.00	0.00	0.00	0.00	0.00
Retention	%	100.00	100.00	100.00	100.00	100.00	100.00	100.00
No. of Shares	'mn	361	361	361	456	576	576	576
P/E		11.87	22.48	13.99	12.07	7.53	6.32	5.55
Sales per share		29.57	29.00	37.15	46.69	45.17	50.57	58.29
P/BV		1.98	1.75	1.33	1.04	1.12	0.95	0.81
Price to Sales		1.01	1.03	0.81	0.64	0.66	0.59	0.51

Gearing Ratios		FY18A	FY19A	FY20A	FY21E	FY22E	FY23E	FY24E
Debt to Equity	x	2.14	2.59	2.39	1.67	1.29	0.91	0.61
L.T. Debt to Equity	x	0.58	0.91	0.83	0.40	0.14	0.04	0.02
Interest Cover	x	5.21	1.53	1.82	1.83	2.35	2.90	3.37

Source: ACPL Research, Company Financials

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DEFINITION OF TERMS

TP	Target Price	CAGR	Compound Annual Growth Rate	FCF	Free Cash Flows
FCFE	Free Cash Flows to Equity	FCFF	Free Cash Flows to Firm	DCF	Discounted Cash Flows
PE	Price to Earnings Ratio	PB	Price to Book Ratio	BVPS	Book Value Per Share
EPS	Earnings Per Share	DPS	Dividend Per Share	ROE	Return of Equity
ROA	Return on Assets	SOTP	Sum of the Parts	LDCP	Last Day Closing Price

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II. Dividend Discount Model
III. Relative Valuation Model
IV. Sum of Parts Valuation

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BUY	Greater than 15%
HOLD	Between -5% to 15%
SELL	Less than and equal to -5%

Sector Rating	Sector Outlook
Overweight	Positive
Market Weight	Neutral
Underweight	Negative

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