S&P Global
Ratings

RatingsDirect®

Research Update:

UAE-Based Ittihad International Investment LLC Assigned 'B+' Rating; Outlook Stable

November 28, 2023

Rating Action Overview

- Through its diversified portfolio across the printing and writing paper, tissue paper, metal converting, and building materials industries, as well as business and environmental services, among other activities, we expect Emirati conglomerate Ittihad International Investment (Ittihad) will record sales of United Arab Emirates dirham (AED) 10.4 billion and S&P Global Ratings-adjusted EBITDA of AED500 million in 2023.
- We consider Ittihad's end-market diversification, favorable cost-positioning in its paper operations, logistic advantages, and highly liquid copper inventories as supportive of the rating. We view the commoditized nature of some of the group's products, the limited size of its stand-alone operations, and the geographic concentration of its assets as offsetting factors.
- We assigned our 'B+' long-term issuer credit rating to Ittihad and our 'B+' issue rating to the $350 million sukuk that Ittihad International Ltd. issued in November 2023. The ratings are in line with the preliminary ratings we assigned on Oct. 31, 2023, and follow the close of the transaction and our review of the final documentation.
- The stable outlook reflects our expectation of high leverage of around 7.5x and negative free operating cash flow (FOCF) of AED40 million–AED50 million at end-2023, due to working capital needs. The outlook also reflects that the rating will be supported by the ramp-up of Ittihad's new paper mill and recovery in the infrastructure and building materials industries.

PRIMARY CREDIT ANALYST

Lina Sanchez
Frankfurt
+4901622104469
lina.sanchez
@spglobal.com

SECONDARY CONTACT

Sapna Jagtiani
Dubai
+ 97143727122
sapna.jagtiani
@spglobal.com

Rating Action Rationale

The commoditized nature of most of Ittihad's products, its limited scale (in terms of EBITDA), geographic asset concentration, and high customer and supplier concentration will weigh on its business risk profile. In our opinion, printing and writing paper, tissue paper (jumbo rolls especially), and some building materials are highly commoditized and limit Ittihad's pricing power; these segments contributed close to 75% of the group's EBITDA in 2022. Ittihad's scale is modest (EBITDA of AED506 million in 2022, or roughly $140 million) especially considering the size of its stand-alone subsidiaries. We think this makes them vulnerable to high-impact, unforeseen events. We also identify risks from the group's asset concentration in the United Arab Emirates

(UAE) and from the reliance on a few pulp suppliers, but we believe this reflects the concentration of the pulp market. Most of Ittihad's printing and writing paper is sold to three large distributors, which, in our opinion, creates some concentration. That said, end-clients are more diversified, with no customer contributing more than 15% of revenue. We understand the printing and writing paper industry is still growing in the Middle East and North Africa (MENA region), which we view as credit positive. However, we do not rule out that, in the medium or long term, the industry could start to decline due to environmental concerns and further digitalization, mirroring the current trend in Europe and the Americas. These factors lead us to assess Ittihad's business risk profile as weak.

That said, Ittihad's favorable cost base, strong market positioning, robust asset base, and significant market entry barriers support its business risk profile. We take into account the group's solid reputation and leading market position in the printing and writing paper industry (about 40% of EBITDA in 2022), as well as its strong position in tissue paper production (roughly 20%). This is supported by its proximity to customers, which reduces lead times, and a favorable cost-positioning that limits competition. We consider Ittihad's printing and writing paper, and tissue paper assets to be well invested and cost competitive. Additional cost benefits arise from the group's bargaining power as a pulp buyer (due to the procurement synergies between Ittihad's paper and tissue paper operations) and its favorable geographic footprint with broad accessibility to ports and low shipping costs. We also believe that high start-up costs in the paper industry act as a barrier to entry.

We assess Ittihad's financial risk profile as highly leveraged. In 2023, we expect adjusted debt to EBITDA of about 7.5x, from 6.5x in 2022. As per our methodology for issuers we assess as having a weak business risk profile, we do not net cash from our debt calculation. We incorporate in our assessment the group's new $350 million sukuk issuance which Ittihad destined to debt refinancing. We therefore consider that the transaction was broadly neutral to leverage but note that it simplified the group's capital structure. Pro forma the transaction, the group's debt includes the $350 million sukuk, loans for approximately AED524 million (chiefly financing from an export credit agency [ECA] facility) and close to AED1.7 billion of debt under working capital facilities. In 2024, we forecast leverage will improve toward 6.5x-7.0x as we expect EBITDA growth (supported by market share gains in the paper business and geographic expansion in the health care business) and further working capital loans repayments. We believe this will offset additional debt the group plans to raise under an ECA facility to fund the expansion of its tissue paper operations in Saudi Arabia.

FOCF will be negative in 2023-2024, before recovering in 2025 on the back of investment benefits. We forecast negative FOCF of AED40 million-AED50 million in 2023 (from positive AED454 million in 2022 and AED363 million in 2021) mainly due to a sizable working-capital-related outflow of about AED240 million driven by higher readily marketable inventories. The expansion of the tissue paper business in Saudi Arabia, which will cost roughly AED320 million and is planned to start in 2024, will cut into cash generation during that year. Consequently, we estimate negative FOCF of AED170 million in 2024, and this reinforces our view that liquidity is rather limited for the rating level. Still, we assume that, once investments become profitable in 2025-2026, FOCF should improve toward AED120 million, gradually supporting the liquidity position. We note that the execution of the expansion project in Saudi Arabia is conditional on obtaining funding. We understand that management is well advanced in the process.

We believe the company's diversification and highly liquid copper inventories are credit positive. Our business risk profile assessment primarily reflects Ittihad's printing and writing paper and tissue paper businesses, which together contributed around 60% of EBITDA in 2022. The remaining 40% has typically been very fragmented, so we do not fully capture it in our approach. We think that Ittihad's exposure to business and environmental services industries, in which it benefits from stable, counter-cyclical operations backed by long-term contracts with local public entities, helps offset the potential volatility of the paper and tissue paper industry. Additionally, we consider that the liquid nature of Ittihad's pre-sold copper inventories partly offsets the high utilization of working capital facilities to fund raw materials procurement. As of end-June 2023, readily marketable copper inventories amounted to approximately AED780 million (roughly one-quarter of Ittihad's pro forma total debt). We reflect those two credit strengths--the stronger business diversification than typical companies of a similar size and the highly liquid nature of copper inventories--in a one-notch positive comparative rating adjustment.

The ratings are in line with the preliminary ratings we assigned on Oct. 31, 2023, and follow the close of the transaction and our review of the final documentation.

Outlook

The stable outlook reflects our expectation of high leverage of around 7.5x and negative FOCF of AED40 million–AED50 million at end-2023, due to working capital needs. The outlook also reflects that the rating will be supported by the ramp-up of Ittihad's new paper mill and recovery in the infrastructure and building materials industries, but also the improvement of the liquidity position in 2024.

Downside scenario

We could lower the rating in the next 12 months if:

- Ittihad is unable to reduce adjusted debt to EBITDA sustainably below 7.0x. This could happen, for example, in case of lower demand for Ittihad's products or difficulties to pass-through higher raw material prices in a timely manner;
- The company deviates from its financial or dividend policy, resulting in large debt-funded shareholder distributions or acquisitions; or
- Liquidity further weakens or we believed that adjusted liquidity sources to uses are unlikely to improve to about 1.0x as per our calculations in the short-term; this could happen for instance in case of substantial short-term debt maturities or working capital outflows.

Upside scenario

We view an upgrade as unlikely in the next 12 months, given the company's business risk assessment, structural reliance on short-term funding, and leverage level. In the long term, any upside would most likely stem from:

- Sustained robust credit metrics, with adjusted leverage declining sustainably below 5.0x and EBITDA interest coverage of around 3x;
- Meaningfully positive FOCF; and

- A sustainable improvement in the liquidity buffer such that adjusted liquidity sources comfortably exceed liquidity uses by 1.2x as we describe for adequate liquidity.

Company Description

Headquartered in Abu Dhabi, Ittihad International Investment is a multi-industry private holding group with a diversified investment portfolio. In 2022, Ittihad's sales reached AED11 billion (2021: AED9.3 billion) and its adjusted EBITDA AED506 million (2021: AED281.6 million). Ittihad has 8,000 employees across 20 companies with a primary focus on the MENA region and emerging markets.

The group operates through four divisions:

- Consumer goods: Through this division Ittihad manufactures printing and writing paper, tissue paper, and chemicals. The largest entities in this division are Ittihad Paper Mill (IPM) and Crown Paper Mill (CPM). IPM is the largest producer of uncoated woodfree paper in MENA with a total capacity of 325,000 tons per year. CPM is a producer of jumbo tissue paper rolls with a total annual capacity of roughly 100,000 tons. In 2022, the division contributed about 18% of total revenue and 60% of EBITDA.
- Infrastructure and building materials: Through this division Ittihad provides copper rods, cement, and steel bars. The main entities in this division are Union Copper Rod (UCR), Union Rebar, and National Cement Factory. It contributed about 73% of total revenue in 2022 and 15% of EBITDA.
- Business services: This division includes entities like Unison (manages radiology operations for the Ministry of Health), SOLV (delivers cleaning and environmental services), and Emirates Link Nitco (sewage facilities). The division contributed about 5% revenue in 2022 and 23% of EBITDA.
- Healthcare and other: Ittihad Group mainly supplies medical equipment through ADI, the main entity in this division. It contributed about 3% revenue in 2022 and 2% of EBITDA.

Ittihad's ultimate shareholder is Mr. Jawaan Al Khaili, a UAE entrepreneur focused on leading regional conglomerates.

Our Base-Case Scenario

Assumptions

- Abu Dhabi's real domestic GDP reducing by about 0.5% in 2023 and recovering by 3.9% in 2024.
- Revenue decline of about 5% largely driven by lower average copper prices in 2023. Copper prices are one of the main drivers of Ittihad's topline growth as its copper rods business accounts for 60%-70% of total revenues. Similarly, we expect lower revenue related to printing and writing paper, and tissue because of lower selling prices. In 2024, we expect moderate growth of about 2% because of a modest increase in copper prices.
- EBITDA margin of about 4.8% in 2023 (4.6% in 2022) supported by higher price premiums in the copper business and an improvement in building materials volumes. This will only be partly offset by lower profitability in paper and chemical segments. In 2024, we assume an EBITDA margin of 5.2% supported by market share gains for IPM and the geographic expansion of

health care business.

- Capital expenditure (capex) of AED100 million in 2023 including new machines for UCR. In 2024, we expect AED370 million–AED380 million of capex, the bulk of it relating to the expansion of CPM in Saudi Arabia. We include about AED45 million of maintenance capex per year.
- Working capital outflow of AED240 million in 2023 because of an increase in UCR inventories and higher accounts receivables at IPM (due to the ramp-up).
- Dividend payments of AED15 million annually in line with the group's dividend policy.
- A new ECA loan for about AED320 million to be signed in early December 2023 to fund expansion capex. We assume 50% of the facility will be drawn in 2024 and 50% in 2025.
- Introduction of a 9% corporate tax in UAE from 2024.
- No acquisitions.

Key metrics

Ittihad International Investment--Key metrics

Mil. AED	2021a	2022a	2023e	2024f
Revenue	9,291.6	10,966.3	10,410.2	10,562.3
EBITDA	281.6	506.0	500.0	544.0
FOCF	362.8	453.6	(44.0)	(174.9)
Debt/EBITDA (x)	12.2	6.5	7.4	6.7
FFO/debt (%)	4.1	9.1	7.9	8.7
EBITDA interest coverage (x)	2.3	2.4	2.0	2.0-2.3

a--Actual. E--Estimate. F--Forecast. AED--UAE dirham. FOCF--Free operating cash flow. FFO--Funds from operations.

Liquidity

We assess Ittihad's liquidity as less than adequate. We estimate cash sources will cover liquidity uses by about 0.7x over the next 12 months. In our view, the group's liquidity position is undermined by the large short-term repayments under working capital facilities (used to finance inventories) which, per our criteria, we consider as current debt. Nevertheless, for our qualitative assessment, we view positively Ittihad's extensive track record of renewing these facilities and its long-standing relationships with local, regional, and international banks.

We exclude from our analysis the potential expansion of the tissue paper activities in Saudi Arabia as it depends on securing financing for the project. That said, we understand that management is well advanced in the process. We also exclude the roughly AED1 billion available under working capital facilities from our liquidity sources since they are uncommitted.

We expect liquidity will improve in the coming months to levels more commensurate with Ittihad's current rating. We understand the company is working toward increasing its available committed facilities and reducing restricted cash. This is what our current stable outlook reflects.

Principal liquidity sources for the 12 months from June 30, 2023 (pro forma the transaction) include:

- Cash and cash equivalents of about AED570 million (excluding restricted cash);
- Availability under committed revolving credit facilities (RCF) of AED385 million (US$105 million equivalent);
- Funds from operations of about AED315 million; and
- Readily marketable securities of AED42 million.

Principal liquidity uses for the same period (pro forma the transaction) include:

- Debt repayments of AED1.6 billion;
- Working capital outflows (including seasonal intrayear working capital) of AED140 million; and
- Annual capex of AED50 million over the next 24 months.

Covenants

Requirements

The outstanding RCF include leverage covenants that cap net debt to EBITDA at various levels, the tighter one at a maximum of 5.0x. The covenant is tested annually.

Outstanding ECA facilities include leverage covenants that test net long-term debt to EBITDA and the interest coverage ratio, among others. That said, upon securing new ECA financing for the expansion of CPM, all ECA covenants will be aligned to the sukuk covenants.

The sukuk documentation only includes a limitation on indebtedness covenant that restricts additional leverage if the fixed charge coverage ratio is below 2.25x.

Compliance expectation

We expect the group to have adequate headroom under all covenants over the next 12 months.

Environmental, Social, And Governance

Environmental factors have an overall neutral influence on our credit rating analysis of Ittihad, as most of the group's EBITDA (around 60%) is generated from IPM and CPM. We view environmental risks in the paper industry as sizable given high water, chemical, and energy usage. We think this could expose companies in the sector to tighter environmental regulation. However, unlike other peers in the industry, Ittihad is not integrated in pulp production, which we believe reduces the environmental risks originating from its operations. That said, we anticipate that Ittihad could face additional environmental risks arising from its other business entities, such as cement and chemicals, but at the moment those are neutral to our credit rating assessment. We understand that Ittihad has implemented projects focused on environmental issues like water recycling and energy optimization.

Governance factors also have an overall neutral influence on our credit rating analysis. That said, with two independent members (out of five individuals) we believe the board of directors lacks significant independence from management, creating potential oversight risks. However, all decisions made by the board require a minimum of one independent member positive vote (out of three).

Issue Ratings - Subordination Risk Analysis

Capital structure

As of June 30, 2023, pro forma the sukuk issuance, Ittihad's debt includes:

- About AED1.7 billion drawn under working capital facilities;
- About AED520 million ECA loans; and
- The $350 million sukuk issued by Ittihad International Ltd.

We also include the new ECA financing of about AED320 million that will fund expansion capex and the RCF for about AED380 million (currently undrawn).

Analytical conclusions

The issue rating on Ittihad's senior unsecured $350 million sukuk is 'B+', in line with the issuer credit rating. This is because, in our view, no significant subordination risk is present in the capital structure. Per our assessment, the priority debt ratio is above our 50% threshold. That said, we believe that subordination risk remains marginal due to the upstream guarantee from the group's main subsidiaries. Our priority debt ratio considers the total secured debt in the issuer's consolidated capital structure plus the total unsecured debt issued by issuer's subsidiaries in comparison to its total consolidated debt.

Ratings Score Snapshot

Issuer Credit Rating	**B+/Stable/--**
Business risk:	Weak
Country risk	Intermediate
Industry risk	Intermediate
Competitive position	Weak
Financial risk:	Highly leveraged
Cash flow/leverage	Highly leveraged
Anchor	b
Modifiers:	
Diversification/Portfolio effect	Neutral (no impact)
Capital structure	Neutral (no impact)
Financial policy	Neutral (no impact)
Liquidity	Less than adequate (no impact)
Management and governance	Fair (no impact)
Comparable rating analysis	Positive (+1 notch)
Stand-alone credit profile:	b+

Related Criteria

- General Criteria: Environmental, Social, And Governance Principles In Credit Ratings, Oct. 10, 2021
- General Criteria: Group Rating Methodology, July 1, 2019
- Criteria | Corporates | General: Corporate Methodology: Ratios And Adjustments, April 1, 2019
- Criteria | Corporates | General: Reflecting Subordination Risk In Corporate Issue Ratings, March 28, 2018
- General Criteria: Guarantee Criteria, Oct. 21, 2016
- Criteria | Corporates | Recovery: Methodology: Jurisdiction Ranking Assessments, Jan. 20, 2016
- General Criteria: Methodology For Rating Sukuk, Jan. 19, 2015
- Criteria | Corporates | General: Methodology And Assumptions: Liquidity Descriptors For Global Corporate Issuers, Dec. 16, 2014
- Criteria | Corporates | General: Corporate Methodology, Nov. 19, 2013
- General Criteria: Methodology: Industry Risk, Nov. 19, 2013
- General Criteria: Country Risk Assessment Methodology And Assumptions, Nov. 19, 2013
- General Criteria: Methodology: Management And Governance Credit Factors For Corporate Entities, Nov. 13, 2012
- General Criteria: Principles Of Credit Ratings, Feb. 16, 2011

Ratings List

New Rating	
Ittihad International Investment LLC	
Issuer Credit Rating	B+/Stable/--
Ittihad International Ltd.	
Senior Unsecured	B+