



The Pakistan Credit Rating Agency Limited

Rating Report

Islamabad Feeds (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Sep-2019	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Among the largest agro based segments in Pakistan, poultry holds a prominent place. Poultry feed manufacturing formally started in Pakistan in early 1960's as home mixtures as well as in commercial feed mills. Today, there are around ~ 350 feed mills with annual production capacity of around 8 MMT. Increase in income levels and expanding population, pushes demand for poultry. However, higher conversion ratio has stagnated volumetric growth. This remains a competitive business where volumes and margins are function of timeliness and cost of procuring raw material along with favorable supply chain dynamics of various feed mills.

The ratings reflect Islamabad Feeds established poultry in the poultry industry with its sponsors and associates having presence in other poultry segments including hatchery, broiler and layer farms. The Company's topline remains strong and mainly comprises broiler and layer feeds. The Company has diversified into broiler chicken and eggs sales, though their respective contribution remains small in overall revenues. The Company procures Soybean meal from local market, however, is exposed to inherent price volatility risk after rupee depreciation. The Company's margins remain thin; but, inline with industry players with modest profitability. The Company's financial risk profile is characterized by modest coverages, stretched working capital cycle and high leveraging. Procuring maize in bulk due to seasonal constraints leads to high holding period and increased financing requirement. Going forward, the rising interest rate scenario could exert pressure on the financial profile of the Company. However, the management is working on a gradual reduction in the short term borrowings.

The ratings are dependent on the management's ability to prudently manage liquidity and working capital requirements. The management's ability to build profitable volumes remains critical for the ratings. Envisioned improvement in business and financial profile along with effective changes in governance framework would be beneficial. Significant deterioration in coverages and/or margins will have negative impact on the ratings.

Disclosure

Name of Rated Entity	Islamabad Feeds (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Criteria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study Poultry Feed(Mar-19)
Rating Analysts	Silwat Malik silwat.malik@pacra.com +92-42-35869504

Profile

Legal Structure Islamabad Feeds (Pvt.) Limited was incorporated as a Private Limited Company in Pakistan, in Aug 2008.

Background Islamabad Feeds (Pvt.) Limited is an established player in the poultry industry, comprising poultry farms and feed mills. The sponsors of the Company started poultry business in 1981 and integrated by setting up poultry feed mill, poultry farms and hatcheries. The Company set up its first feed mill in Rewat in 2008, which became formally operational in 2010. Second feed mill was setup in Okara in 2017.

Operations Islamabad Feeds is primarily engaged in the production and sale of poultry feed through its two feed mills, located in Rewat and Okara. Units I and II have combined installed capacity of 550,000 MT per annum, utilized upto 52%. The Company has also set up its poultry farms, for broiler chicken, in Lahore, Multan, Okara, Muree, Hyderabad, Karachi and Attock. In FY18, layer farms spanning over 100 kanal were set up at the cost of PKR 400mln. The bird placement capacity of these farms is around 300,000. The Group's registered office is located in Satellite Town, Rawalpindi. To manage operations, the Company sales offices are present in Lahore, Islamabad and Karachi.

Ownership

Ownership Structure Majority ownership of Islamabad Feeds resides with Dr. Muhammad Aslam (99%). His wife owns the remaining share (1%).

Stability Ownership structure of the business is seen as stable as no changes in ownership are expected. The second generation is gradually being inducted in the business. However, transition to next generation remains to be seen.

Business Acumen The Company is a venture of Islamabad Group which has an established presence in Pakistan's poultry and poultry feed industry. The Group's flagship entity, Islamabad Feeds, has grown to become one of the Country's leading feed mills catering to its clients in the poultry industry.

Financial Strength The sponsors have high net worth and their willingness to support the business bodes well for the Company.

Governance

Board Structure Islamabad Feeds BoD comprises one Executive Director and one Non-Executive Director belonging to the sponsoring family. Small size of the Board and absence of independent oversight indicates significant room for improvement in the Company's governance framework.

Members' Profile The Board's Chairman, Dr. Muhammad Aslam, is a Doctor of Veterinary Medicine and has an overall experience of over four decades in poultry and integrated businesses. He is the Chairman of Pakistan Poultry Association and also a member of Punjab Poultry Board. The Non-Executive Director, has an overall experience of above three decades in the field of education. She has been associated with the Company's Board for 12 years.

Board Effectiveness There are no sub-committees of the Board. During FY19, the Board met informally to discuss pertinent matters. Minutes of these meetings are maintained. However, these are not in detail.

Financial Transparency Islamabad Feeds external auditors, M/s Muniff Ziauddin & Co. Chartered Accountants, have expressed an unqualified opinion on the Company's financial statements for the year ended June 30, 2018. The firm has been QCR rated by ICAP and is in 'Category A' of SBP panel of auditors.

Management

Organizational Structure The Company operates through Finance, Accounts, Production, Sales & Marketing, Human Resource, IT and Internal Audit division. Both feed mills are monitored by their respective Managers, who reports to the GM Production. All Departmental Heads report to the Company's CEO, enabling him to make the key strategic decisions. The key person risk exists but is mitigated by engagement of a larger team.

Management Team Islamabad Feeds has an experienced & professional management. The Company's CEO, Dr. Muhammad Aslam, is a Doctor of Veterinary Medicine and has an overall experience of over four decades in poultry and integrated businesses. Dr. Munawwar Ali, GM Production, has an overall experience of above three decades and has been associated with the Group from past 30 years. Mr. Muhammad Sajjad, CFO, has an overall experience of 25 years and has been associated with the Group from almost 20 years.

Effectiveness At Islamabad Feeds, six management committees are formally in place; namely, audit, finance, sales and recovery, production, broiler farms and layer farms. These committees meet informally to discuss pertinent matters and minutes are maintained. However, these are not in detail.

MIS Sidat Hyder has installed Oracle as an enterprise resource software, customized as per the industry needs for the Company. This enables the senior management to monitor and generate reports about inventory, sales, receivables and payables side. These reports are generated on daily, weekly and monthly basis.

Control Environment To ensure operational efficiency, the Company has setup an internal audit function to implement the policies and procedures. This function conducts regular pre and post audits to monitor the policies and procedures implemented at Islamabad Feeds.

Business Risk

Industry Dynamics Poultry feed manufacturing formally started in Pakistan in early 1960's. At present, poultry feed is produced by commercial feed mills as well as home mixtures. There are 350 poultry feed mills, making country's annual production capacity of around 8 MMT. This industry directly drives its demand from poultry – chicken and eggs consumption. With growing income levels and expanding population, the industry is experiencing ~4 to 5% growth.

Relative Position Islamabad Feeds has secured prominent position in the market due to its high FCR, culminating in higher demand for their product. The Company is ranked among the first tier players of poultry feed industry

Revenues Islamabad Feeds generate revenue by manufacturing and selling variants of poultry feed (92%), Broiler (4%) and Eggs (3%). The Company generates 82% of its revenue from the country's central region with top ten customer having a revenue share of ~ 44%. Feed is sold to local poultry farms directly (22%) and through network of agents (78%) on credit. The Company generates 20-25% of revenue by selling feed to Associated Company – Islamabad Farms. The Company's top line witnessed a dwindling trend. In FY19, revenues were supported by increase in prices and better volumes clocking in at PKR 14.5bln (FY18: PKR 11.8bln), witnessing an increase of 23% (YoY).

Margins The input cost raw material - soybean meal, increased due to rupee depreciation. However, the Company was able to pass on the higher cost in a timely manner, leading to improved gross margins (FY19: 7.3%, FY18: 6.4%). Similarly, the management kept the production and overheads expenses under control, resulting in better operating margins (FY19: 5.7%, FY18: 4.7%).

Sustainability Going forward, the management plans to increase the utilization level strengthening the Company's sales. The Company intends to vertically integrate into solvent extraction business. The management is eyeing to set up more farms for broiler and layer birds under Islamabad Feeds and Islamabad Farms. This will primarily be financed through internal cashflows.

Financial Risk

Working Capital Islamabad Feeds working capital needs originates from financing and storing maize and soybean meal in bulk. High inventory levels, kept the working capital days on the higher side (FY19: 150 days, FY18: 173 days). The Company procures raw materials on credit. The Company generally receives payment from buyers upon maturity and sale of flock of birds (FY19: 40 days, FY18: 42 days). The Company's receivable days came down slightly (FY19: 51 days, FY18: 59 days) as it tightened the credit terms. Adequate room exists at net trade level.

Coverages In FY19, the interest cover remain stable, however improved over time (FY19: 1.7x, FY18: 1.7x). This was supported by increase in free cash flows (FY19: PKR 844mln, FY18: PKR 623mln). However, finance cost rose (FY19: PKR 501mln, FY18: PKR 373mln) significantly due to increased borrowings and higher interest rates. This led a slight dip in the Company's core and total coverage ratios (Core and Total Coverage: FY19: 1.5x, FY18: 1.6x).

Capitalization Islamabad Feeds has highly leveraged capital structure with debt to equity ratio at 66% on the back of relatively small equity base. In FY19, increase in short term debt was mainly to finance seasonal procurement of Maize and import Soybean meal (FY19: PKR 5bln, FY18: 4.8bln). Long term debt increased to PKR 203mln to procure biological assets.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

Islamabad Feeds (Pvt.) Ltd. Poultry Feed	Jun-19 12M	Jun-18 12M	Jun-17 12M	Jun-16 12M
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A BALANCE SHEET

1 Non-Current Assets	1,973	1,991	1,939	2,051
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	8,114	7,937	7,099	8,849
a Inventories	5,674	5,402	4,669	7,030
b Trade Receivables	2,169	1,933	1,905	1,219
5 Total Assets	10,088	9,928	9,038	10,900
6 Current Liabilities	1,754	2,300	963	941
a Trade Payables	1,310	1,894	819	719
7 Borrowings	5,326	4,912	5,434	7,454
8 Related Party Exposure	52	9	13	11
9 Non-Current Liabilities	140	140	145	157
10 Net Assets	2,816	2,567	2,483	2,336
11 Shareholders' Equity	2,816	2,567	2,483	2,336

B INCOME STATEMENT

1 Sales	14,544	11,826	13,718	15,219
a Cost of Good Sold	(13,480)	(11,069)	(12,811)	(14,248)
2 Gross Profit	1,064	756	906	972
a Operating Expenses	(236)	(205)	(214)	(202)
3 Operating Profit	828	551	692	770
a Non Operating Income or (Expense)	(2)	(11)	(14)	(2)
4 Profit or (Loss) before Interest and Tax	826	540	678	768
a Total Finance Cost	(504)	(375)	(474)	(607)
b Taxation	(73)	(81)	(59)	(37)
6 Net Income Or (Loss)	249	83	145	124

C CASH FLOW STATEMENT

a Free Cash Flows from Operations (FCFO)	844	623	803	930
b Net Cash from Operating Activities before Working Capital Changes	363	240	302	314
c Changes in Working Capital	(759)	691	1,757	(862)
1 Net Cash provided by Operating Activities	(396)	931	2,059	(548)
2 Net Cash (Used in) or Available From Investing Activities	(187)	(289)	(87)	(133)
3 Net Cash (Used in) or Available From Financing Activities	414	(522)	(2,020)	675
4 Net Cash generated or (Used) during the period	(169)	120	(48)	(6)

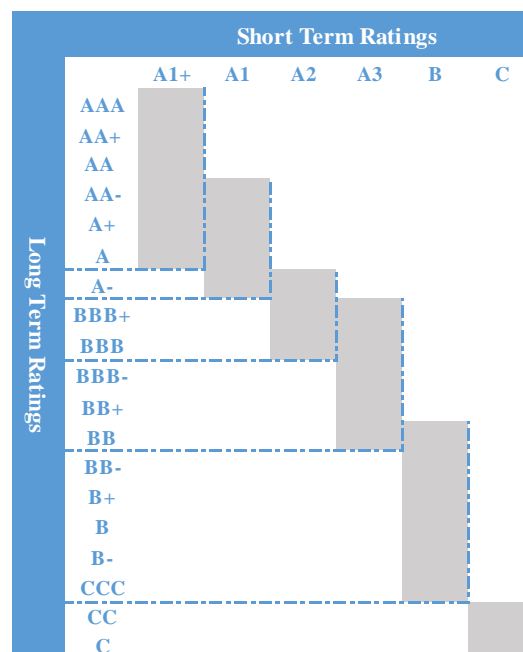
D RATIO ANALYSIS

1 Performance				
a Sales Growth (for the period)	23.0%	-13.8%	-9.9%	--
b Gross Profit Margin	7.3%	6.4%	6.6%	6.4%
c Net Profit Margin	1.7%	0.7%	1.1%	0.8%
d Cash Conversion Efficiency (EBITDA/Sales)	7.2%	5.6%	6.5%	6.2%
e Return on Equity (ROE)	9.2%	3.3%	6.0%	5.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	190	215	197	194
b Net Working Capital (Average Days)	150	173	177	177
c Current Ratio (Total Current Assets/Total Current Liabilities)	4.6	3.5	7.4	9.4
3 Coverages				
a EBITDA / Finance Cost	2.1	1.8	1.9	1.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.5	1.6	1.6	1.4
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.9	0.3	0.3	0.5
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	65.6%	65.7%	68.7%	76.2%
b Interest or Markup Payable (Days)	56.1	52.7	48.4	53.7
c Average Borrowing Rate	9.7%	7.2%	7.3%	8.1%

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



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'.	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.	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.	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.	Harmonization A change in rating due to revision in applicable methodology or underlying scale.
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Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

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- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
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- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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- (12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA’s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers’ associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst’s area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

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- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA’s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA’s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA’s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)

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