The Pakistan Credit Rating Agency Limited

Rating Report

Sadiq Poultry (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
22-Jul-2019	A-	A1	Stable	Maintain	-
20-Mar-2019	A-	A1	Stable	Maintain	-
18-Sep-2018	A-	A1	Stable	Maintain	-
22-Mar-2018	A-	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Poultry is one of the largest agro based segment in Pakistan, accounting both domestic & commercial poultry. With an investment of almost PKR 700bln in FY18, industry has posted an annual growth of 10%. Pakistan is sufficient in poultry meat and egg production. However, lacks in per capita protein consumption remains low when compared to the world's average.

The ratings reflect Sadiq Poultry’s association with an established vertically integrated poultry group, named Sadiq Group. The Company has an established profile in its business and enjoys the lead position in broiler, chicken, eggs and day old chicks segment. After significant expansion in capacities, topline posted an increase; however, remains concentrated towards day old chicks. Business margins improved as the management was able to keep the costs under control and managed to reap economies of scale. Nevertheless, the Company remains exposed to volatility in prices and contingent health risk associated to its product (live chicken stock and eggs). Procuring feed in bulk from Group’s own company create synergies. The Company’s financial risk profile is characterized by moderate leverage and adequate coverage ratios. The loan mix is skewed towards short term borrowings to fulfill the working capital requirements.

The ratings are dependent on the management's ability to prudently mange the business risk for of perishable consumer products, while sustaining business margins. Moreover, governance framework needs attention. Meanwhile, prudent management of working capital and maintaining strong coverages remain critical.

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

Profile

Legal Structure Sadiq Poultry (Pvt.) Ltd. was incorporated on July 07, 2005 as a Private Limited Company.

Background Sadiq Group came into existence as a small scale family business and became formally operational in Apr, 1975. Today, the Group is known as one of the leaders in poultry operating under the brand name of Sadiq.

Operations The Company is primarily operating poultry breeding units/farms, broiler production farms, commercial egg production and layer units, poultry hatcheries, livestock pharmaceuticals, grain storage and livestock feeds, paper pulp tray production plant and organic fertilizer plants. During the year, the Company leased it's fixed assets to it's associated entities, Salman Poultry and Zubair Feeds; along with transfer of inventory as a part of Group level business re-structuring.

Ownership

Ownership Structure Sadiq Poultry's major shareholding vests with Dr. Muhammad Sadiq (70%); followed by his two sons, Mr. Asif Zubair (15%) and Mr. Salman Sadiq (15%).

Stability Ownership of the business is seen as stable as the major ownership vests with Dr. M. Sadiq. While ownership is not expected to change, the Company is in the process of re-structuring assets among associated entities in the Group.

Business Acumen Sadiq Group has experienced multiple business cycles, maintaining their league since 1975. The Group's broiler farms are among the highest chick producers in Pakistan. Currently, there are six Companies and one Trust working under Sadiq Group. All Companies are operating in various segments.

Financial Strength Sadiq Group has consolidated asset base of ~PKR 35bln supported by an equity of the ~PKR 10.5bln as at end Jun'18. Through its diverse set of businesses, it has generating a turnover of ~PKR 43bln and a pre-tax bottom line of ~PKR 948mln in FY18.

Governance

Board Structure Sadiq Poultry's Board, comprising three members, is dominated by the sponsoring family. The Company's Board lack independence, indicating room for improvement in the Company's governance framework.

Members' Profile All the BoD members have relevant expertise. Dr. Muhammad Sadiq, Board's Chairman, holds a DVM degree and has four decades of experience in poultry and integrated businesses. Mr. Asif Zubair and Mr. Salman Ssdiq, Directors of the Company, are US graduates and have an experience of more than 10 years.

Board Effectiveness Keeping in view the size of the Board, absence of sub-committees may not impact Board's effectiveness. During 9MFY19, ? Board meetings, with full/majority attendance, were held to discuss pertinent matters and make strategic decisions.

Financial Transparency Sadiq Poultry's external auditors, Muniff Ziauddin and Co. Chartered Accountants, have expressed an unqualified opinion on the financialreports for FY18. The firm has been QCR rated by ICAP and are in Category 'A' of SBP panel.

Management

Organizational Structure The Company's sales and production are monitored by GM Production. Whereas, support departments work as shared services for the Group. All departments eventually report to the CEO.

Management Team Sadiq Poultry's management comprise experienced professionals. Dr. Muhammad Sadiq, Group's CEO, has headed several national and international forums and is also recognized as a leading authority on poultry sciences and avian welfare.

Effectiveness Management ensures effectiveness through Technical, Interview and Operational committees, established at the Group level. Weekly meetings are held by these committees to discuss the performance and issues faced by each department.

MIS Two financial software, set up by Sidat Hyder, are used at the Group level. However, for internal dissemination, information is documented when required.

Control Environment At Sadiq Poultry, internal audit department has been established at the Group level to ensure internal controls. The Company's breeder farms, broiler farms and hatcheries are fully equipped with environmentally controlled systems.

Business Risk

Industry Dynamics Poultry is one of the largest agro based segment in Pakistan, accounting both domestic & commercial poultry. With an investment of almost PKR 700bln in FY18, industry had an annual growth of 10%. Pakistan is sufficient in poultry meat and egg production. However, lacks in per capita protein consumption remains low when compared to the world's average.

Relative Position Sadiq Poultry's has 25% share in the market. Despite being the market leader, the Company's control over the market price is negligible.

Revenues Sadiq Poultry's sales mix comprises day old chicks - 46%, table eggs - 34%, and broiler meat - 4%. The business was segregated among group companies namely Salman Poultry and Zubair Poultry. In 9MFY19, the Company's revenue posted an increase of 9% and clocked in at PKR 7.9bln (9MFY18: PKR 7.3bln). This growth was mainly due to ?

Margins Gross margins for 9MFY19 increased to ~14% due to efficiency in the production process achieved from better management control. On the other hand, price hikes in other input costs (poultry feed) was catered to by passing on the increase to customers. Operating costs remained under control leading to improved operating margin of 8% in 9MFY19 in comparison to ~ 6% in 9MFY18. Despite higher finance costs, net profit margins improved to ~ 6% in 9MFY19 in comparison to ~ 3% in 9MFY18 on the back of rental income from associated companies for leased assets.

Sustainability The Company does not plan on enhancing it's capacities in the near future.

Financial Risk

Working Capital Sadiq Poultry's net working capital days of 110 days in 9MFY19 (9MFY18: 108 days) emanate predominantly from high finished goods inventory held days (day old chicks and eggs). Average debtor days surged to 45 days in 9MFY19 from 16 days in 9MFY18 on the back of receivables from associated companies. Average creditor days increase to 22 days 9MFY19 in from 10 days in 9MFY18 to manage working capital flows. Despite the increase in working capital days, the Company maintains cushion in times borrowing lines.

Coverages The Company maintained adequate coverages with interest coverage of 5.3x during 9MFY19 on the back of improved FCFO. Core Coverage improved to 2.7x in 9MFY19 owing to lower upcoming maturities of long-term debt.

Capitalization The Company has a moderately leveraged capital structure with short term borrowings comprising 75% of the total debt. As the Company settles it's long term debt the leveraging reduced to ~36% at end 9MFY19 from ~42% at end 9MFY18. Current maturities will be settled through internal cashflows. As the Company plans for no capacity enhancements in the near future, no borrowings expect for working capital requirement needs are expected.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Sadiq Poultry (Pvt.) Limited	Mar-19	Jun-18	Jun-17	Jun-16
Poultry	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	4,514	1	4,708	4,975
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	5,773	5,349	3,523	3,354
a Inventories	*2,622*	*2,358*	*2,650*	*2,375*
b Trade Receivables	*1,210*	*1,405*	*425*	*225*
5 Total Assets	10,287	5,350	8,231	8,329
6 Current Liabilities	1,971	1,546	382	734
a Trade Payables	*780*	*471*	*247*	*219*
7 Borrowings	2,827	3,281	3,141	3,167
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	440	440	441	326
10 Net Assets	5,049	83	4,267	4,102
11 Shareholders' Equity	5,049	4,556	4,281	4,126
B INCOME STATEMENT				
1 Sales	7,888	9,451	10,680	7,073
a Cost of Good Sold	*(6,773)*	*(8,202)*	*(9,469)*	*(6,146)*
2 Gross Profit	1,114	1,249	1,210	927
a Operating Expenses	(504)	(687)	(685)	(514)
3 Operating Profit	611	562	526	413
a Non Operating Income or (Expense)	*103*	*74*	*1*	*30*
4 Profit or (Loss) before Interest and Tax	714	636	527	443
a Total Finance Cost	*(215)*	*(293)*	*(237)*	*(214)*
b Taxation	*(6)*	*(68)*	*(135)*	*(117)*
6 Net Income Or (Loss)	493	275	155	111
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,145*	*1,374*	*981*	*826*
b Net Cash from Operating Activities before Working Capital Changes	*955*	*1,087*	*728*	*599*
c Changes in Working Capital	*437*	*(601)*	*(328)*	*(146)*
1 Net Cash provided by Operating Activities	1,392	486	400	453
2 Net Cash (Used in) or Available From Investing Activities	(893)	(554)	(630)	(847)
3 Net Cash (Used in) or Available From Financing Activities	(454)	121	(117)	702
4 Net Cash generated or (Used) during the period	45	53	(347)	308
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	11.3%	-11.5%	51.0%	-0.7%
b Gross Profit Margin	14.1%	13.2%	11.3%	13.1%
c Net Profit Margin	6.3%	2.9%	1.5%	1.6%
d Cash Conversion Efficiency (EBITDA/Sales)	16.3%	15.1%	9.6%	12.3%
e Return on Equity (ROE)	13.7%	6.2%	3.7%	2.7%
2 Working Capital Management				
a Gross Working Capital (Average Days)	132	132	97	175
b Net Working Capital (Average Days)	110	118	89	165
c Current Ratio (Total Current Assets/Total Current Liabilities)	2.9	3.5	9.2	4.6
3 Coverages				
a EBITDA / Finance Cost	7.4	7.5	6.3	4.1
b FCFO / Finance Cost+CMLTB+Excess STB	3.0	1.7	1.1	1.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.6	1.0	2.0	3.0
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	35.9%	41.9%	42.3%	43.4%
b Interest or Markup Payable (Days)	104.2	0.0	0.0	0.0
c Average Borrowing Rate	7.6%	6.0%	5.1%	7.8%

Rating Scale | Corporate

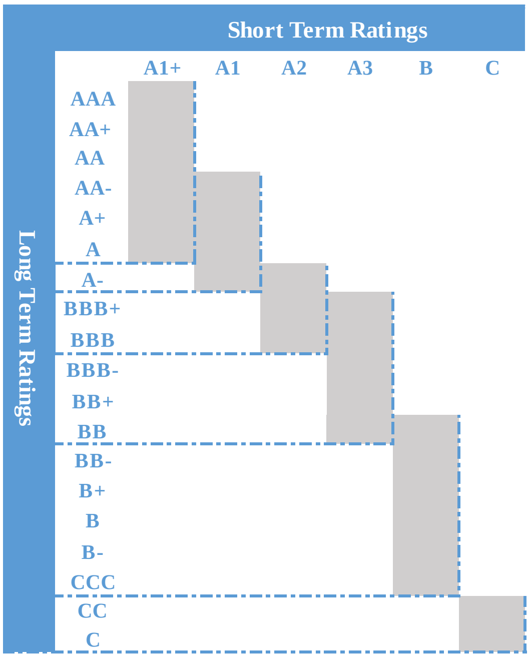
2019

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	
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA 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.
A+ A 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.
BBB+ BBB 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.
BB+ BB 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.
B+ B 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.
CCC CC C	**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.
D	Obligations are currently in default.

Short Term Ratings	
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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 surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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

Restrictions

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(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)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(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)

Independence & Conflict of interest

(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)

Monitoring and review

(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)

Proprietary Information