



The Pakistan Credit Rating Agency Limited

## Rating Report

### National Foods Limited

#### Report Contents

1. Rating Analysis
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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
19-Apr-2024	AA-	A1	Stable	Maintain	-
20-Apr-2023	AA-	A1	Stable	Maintain	-
19-Apr-2022	AA-	A1	Stable	Maintain	-
19-Apr-2021	AA-	A1	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

National Foods Limited's (NFL's) established presence since 1970 and strategic diversification into 13 product categories with around 300 SKUs underscore its sustainable financial trajectory. NFL's calculated entry into the branded spice market has solidified its leadership in Pakistan's food sector. The company's focus on creditworthiness and effective use of brand equity signifies adept navigation in both local and global markets. Despite the prevalence of unbranded products in Pakistan posing a credit risk, NFL's shift towards branded goods suggests credit-positive potential. Globally, NFL's proactive approach maintains its credit standing amidst intense competition, particularly in the condiment space against Indian entities. NFL's dedication to fiscal prudence and market adaptability anchors its positive credit profile. Its Dubai-based subsidiary, NF-DMCC, along with NEI in Canada, caters to the Middle eastern, North American and European markets, reflecting its international operational strength.

National Foods has exhibited a strong financial performance, with a ~10% increase in its topline during FY23 ascending to PKR ~29.6 bln (FY22: ~26.8 bln) backed by price and volumetric growth. The company's strategic initiatives and operational efficiencies have contributed to a Gross Margin of ~34.6% (FY22: ~33.4 bln, an Operating Margin of ~9.2% (FY22: ~8.9), and a Net Margin of ~7.4% (FY22: ~7.3%). The Return on Assets and Return on Equity were at ~9.66% (FY22: ~11.4) and ~31.2% (FY22: ~32.8%), respectively. National Foods Limited's (NFL's) rating affirmation is predicated on the company's robust franchise value, underscored by a commanding market share and potent brand equity in its principal product segments. The intrinsic worth of the franchise is pivotal, enabling NFL to strategically extend its brand equity into new product categories, which is instrumental in propelling the company towards the fulfilment of its ambitious growth projections set forth by the management. The executive team at National Foods has consistently demonstrated astute capital management and a steadfast commitment to sustaining a strong credit profile. The company's prudent financial policies, coupled with its agility in adapting to market fluctuations, and adherence to international standards in nutrition, health, wellness, quality and customer satisfaction provide a solid foundation for the continuation of the current rating.

The ratings reflect the management's competence in sustaining profit margins and expanding market share. The realization of strategic growth initiatives is pivotal. Diligent management of working capital, along with the preservation of adequate cash flows and coverage ratios, is crucial for maintaining the ratings.

#### Disclosure

<b>Name of Rated Entity</b>	National Foods Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Rating(Jul-23),Methodology   Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology   Rating Modifiers(Apr-23)
<b>Related Research</b>	Sector Study   Food Products(Dec-23)
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## Profile

**Legal Structure** National Foods Limited ('National Foods' or 'the Company') is a public listed company, incorporated in 1970.

**Background** In 1970, Mr. Abdul Majeed (late) and Mr. Waqar Hasan (late) established National Foods to introduce branded and packaged spices by acquiring National Foods Laboratories. In 1986, second production facility was setup in SITE. Third new facility was setup in Port Qasim, in 2006. The Company entered in the international market through a wholly owned subsidiary, National Foods DMCC (NFL DMCC), a UAE based company, in 2013. Through NFL DMCC, the Company invested in National Epicure Inc. (Canada). In 2015, fourth production facility was setup in Gujranwala. Later, National Epicure Inc. acquired 60% interest in A-1 Cash & Carry, a company based in Canada.

**Operations** The Company is primarily engaged in manufacturing convenience food products with a portfolio of 13 categories in 300 different products. The production facilities are located in Port Qasim, Nooriabad, and M-3 Industrial City, Faisalabad. The Company is exporting products to ~ 40 countries across ~ 5 continents, through NFL DMCC. During FY23, the Company's production declined by 6.5% to 101.083MT (FY2: 108.104MT) as a result of ongoing expansion activities throughout the year.

## Ownership

**Ownership Structure** NFL's major ownership lies with Sponsors through associate entity i.e., ATC Holdings (Pvt.) Limited (~34%), and Directors and their family members has ~39% stake. General public holds also hold sizeable chunk (~11%) in the Company's ownership. Remaining ~16% of the shares resides with financial institutions and foreign companies.

**Stability** Ownership of the Company seems stable as majority shareholding vests with the sponsoring family.

**Business Acumen** The sponsors have been operating in the industry for more than five decades and have very strong industry knowledge. Today, the Company is a leading player in Pakistan's multi-category food segment.

**Financial Strength** NFL is a sound Company that has diversified into various food segments. As at FY23, NFL has consolidated equity of PKR 13.2bln. Moreover, the group is managing an asset base of ~PKR 39.2bln. Through its diverse set of business, it is generating a turnover of ~PKR 64.3bln and posted a PAT of ~PKR 3.8bln.

## Governance

**Board Structure** The BoD comprises 7 members. There are three Non-Executive Directors, two Executive Directors and two Independent Directors. The BoD is dominated by the Sponsoring family.

**Members' Profile** Mr. Zahid Majeed is Chairman of National Foods and ATC Holding's BoD since April 20, 2022. All members of the BoD have significantly diversified experience and have been associated with the Company's BoD for a long span of time.

**Board Effectiveness** The board comprises of Audit Committee and Human Resource & Remuneration Committee. Board minutes are formally documented.

**Financial Transparency** The Company has appointed KPMG Taseer Hadi as its external auditors. The firm has expressed an unqualified opinion on the financial statements of the Company for the year ended Jun-23. The firm has been appointed as the Company's auditor since 2017.

## Management

**Organizational Structure** The Company's organizational structure reflects clear reporting lines and is split between the production site and head office. The Company operates through eight main departments: Finance, HR & Industrial Relations, Supply Chain, Marketing, Sales, Innovation and R&D, IT, and Internal Audit. All functional heads report to the Company's CEO, who then reports to the BoD. However, Head of Internal Audit and HR administratively reports to the CEO and functionally to the Board Audit and HR & Remuneration Committee, respectively.

**Management Team** Mr. Abrar Hasan, CEO of the Company, has an overall experience of more than three decades. He is also on the BoD of multiple other companies and holds membership of key associations. Mr. Zahid Majeed, CEO of NFL DMCC, heads the international operations and is associated with the Company since 1987.

**Effectiveness** The Company's management ensures effectiveness through its Management Committee. The Committee meets periodically to monitor the Company's performance. Minutes of these meetings are well documented.

**MIS** The company has recently transitioned to S/4 HANA for the generation of MIS and operational reports, updating from the previous ERP software, SAP ECC6.

**Control Environment** The Company has Halal certification and all products are ISO 22000 certified. The internal audit function is co-sourced to EY Ford Rhodes.

## Business Risk

**Industry Dynamics** In Pakistan, the domestic convenience food market is growing, with a 7.64% CAGR forecast for 2024-2028. Distribution meets international standards in cities, but expansion opportunities exist in smaller areas. Retail is fragmented; however, large chains are emerging, potentially changing consumer habits. The CPI's year-on-year increase is 23.06% as of February 2024, signaling a slowdown in inflation. This impacts consumer spending, especially on convenience foods, as price hikes in essentials continue. Companies must adapt to these economic shifts to maintain market share.

**Relative Position** The Company has high brand recognition in recipe mixes/spices & ingredients, ketchups, pickles, salt and jellies as they are the market leader. Although, National Foods holds a strong position in the dessert segment, it is yet to establish a notable presence in the product category of Snacks.

**Revenues** The Company has maintained its growth trajectory in revenues since commencing operations in 1970. During FY23, revenue posted a growth of ~10.3% and stood at ~PKR 30bln (FY22: ~PKR 27bln). Exports remained stable and stood ~PKR 2.4bln (FY22: ~PKR 2.2bln). During 1HFY24, the Company posted revenue of PKR 15,587m (1HFY22: ~PKR 11,896m), an increase of ~31.11%, driven by higher volumes sold locally.

**Margins** Gross and operating margin stood at 34.6% and 9.2% in FY23 (FY22: 33.4% and 8.9%), respectively, on the back of efficient supply chain management. The Company's net profit witnessed an increase of ~15% and stood at ~PKR 2.18bln (FY22: ~PKR 1.9bln). Net profit margin remained almost same and stood at 7.4% (FY22: 7.3%) higher turnover, mainly due to higher sales which effect was reduced by the hike in finance cost. During 1HFY24, the Company's gross margin dropped to ~32. % due to majorly to increase in energy costs compared to ~35.4% during 1HFY23. Moreover, operating margin decreased to ~5.6% (1HFY23: 6.8%) due to increased operating and marketing expenses. In addition, net profit margin witnessed a fall and stood at ~1.4% during 1HFY24 (1HFY23: 4.1%).

**Sustainability** National Food Limited's (NFL) strategic maneuvers reflect a forward-thinking approach that aligns with long-term financial stability and growth. The investment in a state-of-the-art facility in Faisalabad is indicative of NFL's commitment to enhancing its production capabilities and also serves as a catalyst for synergy enhancement, which is likely to improve its competitive edge and market share. The establishment of facility in Faisalabad is set to enhance the logistics infrastructure within the Punjab region, streamlining distribution networks and facilitating swifter, more efficient delivery of goods.

## Financial Risk

**Working Capital** The Company's net working capital days posted an increase in FY23 and stood at 108 days (FY22: 89 days) owing to increase in inventory days (FY23: 101 days, FY22: 79 days), receivable days remain stable (FY23: 22 days, FY22: 22 days). Trade payable days posted an improvement (FY23: 15 days, FY22: 12 days) due to revision in credit terms. In 1HFY24, the Company's net working capital days stood at 118 days (1HFY23: 118 days).

**Coverages** FCFO stood at ~PKR 3.2bln in FY23 (FY22: ~PKR 2.9bln), with an increase of ~10%. Finance cost increased by 3.3 times to PKR 599m (FY22: PKR 180m) on the back of higher interest rates. Subsequently, interest cover abated to 5.6x (FY22: 20.4x). Core and total coverages posted a drop and stood at (FY23: 4.8x each, FY22: 5.2x each) due to higher interest rates. During 1HFY24, the Company's interest coverage ratio decreased to 1.5x (1HFY23: 5x). Moreover, the core and total operating coverage ratio increased to 1.4x each during 1HFY24, respectively. (1HFY23: 3.8x each).

**Capitalization** NFL has National Foods has a moderately leveraged capital structure with a debt-to-equity ratio of ~52% (FY22: ~43.3%). In FY23, Total debt stood at ~PKR 8.1bln (FY22: ~PKR 5bln), comprising major increase in long term debt (FY23: PKR 3,073m, FY22: PKR 273m). However, low-cost borrowing, Export Refinance Facility from SBP, benefits the Company. In 1HFY24, the leveraging ratio increased to ~61% compared to ~59.4% in 1HFY23, primarily driven by funding obtained from banks amounting to ~PKR 3.5bln at 3MK+ 0.01% to 3MK+ 0.4%.



National Foods Limited	Dec-23	Jun-23	Dec-22	Jun-22	Jun-21
Food Products	6M	12M	6M	12M	12M

#### A BALANCE SHEET

1 Non-Current Assets	11,462	9,984	8,393	7,233	5,192
2 Investments	105	937	1,631	1,339	1,031
3 Related Party Exposure	32	32	32	32	33
4 Current Assets	15,050	14,204	11,156	10,257	9,379
<i>a Inventories</i>	10,923	9,769	7,352	6,629	4,945
<i>b Trade Receivables</i>	1,174	1,570	833	1,949	1,277
5 Total Assets	26,648	25,156	21,212	18,861	15,636
6 Current Liabilities	7,860	9,018	6,589	7,146	5,787
<i>a Trade Payables</i>	1,507	1,726	644	751	961
7 Borrowings	11,267	8,106	8,521	4,974	4,020
8 Related Party Exposure	134	160	0	0	130
9 Non-Current Liabilities	222	348	276	231	222
10 Net Assets	7,164	7,525	5,827	6,509	5,476
11 Shareholders' Equity	7,164	7,525	5,827	6,509	5,476

#### B INCOME STATEMENT

1 Sales	15,587	29,603	11,896	26,843	23,116
<i>a Cost of Good Sold</i>	(10,606)	(19,361)	(7,682)	(17,875)	(16,080)
2 Gross Profit	4,981	10,242	4,214	8,968	7,036
<i>a Operating Expenses</i>	(4,101)	(7,507)	(3,402)	(6,573)	(5,148)
3 Operating Profit	880	2,735	811	2,395	1,888
<i>a Non Operating Income or (Expense)</i>	64	588	131	367	(38)
4 Profit or (Loss) before Interest and Tax	944	3,323	942	2,762	1,850
<i>a Total Finance Cost</i>	(599)	(621)	(228)	(180)	(136)
<i>b Taxation</i>	(122)	(514)	(231)	(616)	(449)
6 Net Income Or (Loss)	223	2,188	483	1,965	1,265

#### C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	848	3,273	921	2,990	2,250
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	558	3,032	830	2,881	2,109
<i>c Changes in Working Capital</i>	(2,021)	(1,459)	(914)	(1,862)	49
1 Net Cash provided by Operating Activities	(1,462)	1,573	(84)	1,019	2,158
2 Net Cash (Used in) or Available From Investing Activities	(1,008)	(3,057)	(1,751)	(2,926)	(1,743)
3 Net Cash (Used in) or Available From Financing Activities	964	876	2,414	(79)	1,697
4 Net Cash generated or (Used) during the period	(1,506)	(608)	579	(1,986)	2,112

#### D RATIO ANALYSIS

1 Performance					
<i>a Sales Growth (for the period)</i>	5.3%	10.3%	-11.4%	16.1%	0.0%
<i>b Gross Profit Margin</i>	32.0%	34.6%	35.4%	33.4%	30.4%
<i>c Net Profit Margin</i>	1.4%	7.4%	4.1%	7.3%	5.5%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-7.5%	6.1%	0.1%	4.2%	9.9%
<i>e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/Sl</i>	6.1%	31.2%	15.7%	32.8%	24.3%
2 Working Capital Management					
<i>a Gross Working Capital (Average Days)</i>	137	123	129	101	94
<i>b Net Working Capital (Average Days)</i>	118	108	118	89	81
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	1.9	1.6	1.7	1.4	1.6
3 Coverages					
<i>a EBITDA / Finance Cost</i>	2.5	6.7	6.2	23.4	22.0
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.4	4.8	3.9	5.2	3.5
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	8.3	1.2	2.2	0.2	0.6
4 Capital Structure					
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	61.1%	51.9%	59.4%	43.3%	42.3%
<i>b Interest or Markup Payable (Days)</i>	250.2	288.3	214.2	199.6	28.1
<i>c Entity Average Borrowing Rate</i>	12.2%	8.3%	6.3%	3.4%	5.0%

### Credit Rating

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.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> 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.
AA-	
A+	
A	<b>High credit quality.</b> 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.
A-	
BBB+	
BBB	<b>Good credit quality.</b> 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-	
BB+	
BB	<b>Moderate risk.</b> 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-	
B+	
B	<b>High credit risk.</b> 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-	
CCC	
CC	<b>Very high credit risk.</b> 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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
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.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



\*The correlation shown is indicative and, in certain cases, may not hold.

**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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) 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.

**Surveillance.** Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

**Note.** This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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(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)

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- 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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### **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 | Clause 11-(A)(p).
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- (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)

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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)
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- (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 | 17-(a)
- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

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