The Pakistan Credit Rating Agency Limited

Rating Report

Pakistan Oil Mills (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
09-Dec-2022	BBB+	A2	Stable	Maintain	-
10-Dec-2021	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan is among the biggest importers of edible oil, as Palm Oil is the 4th largest imported product after petroleum and LNG. The industry, including both ghee (hydrogenated oil) and cooking oil production, relies on 70% of imports in the form of edible oilseed (soy and canola, ~ 3.4 MMT) and edible oil (mostly RBD Palm Oil, ~ 3.1MMT) which accounts for 80% of the cost of production. While, only 30% of the consumption is fulfilled by locally produced oilseed (cottonseed and mustard seed, ~1.7MMT). Domestic consumption for edible oil stood around 5.1 MMT, during FY22. With a minimal surge in demand along with the inflationary pressure on oilseed import and production, edible oil production grew meagerly over ~ 2% during FY22. The industry remains affluent with steady cashflows; however, debt levels remain considerably high. Being a staple item, despite consistent inflationary pressure, the industry's volumes and profits are expected to remain stable going forward.
The ratings reflect Pakistan Oil Mills (Pvt.) Limited's ('the Company') developing brand equity for its edible oil brands (Naz, Pak, Sun, and Pure) and its association with a large industrial group that has ventured into shipbreaking, textile, and real estate. Over the years, the Company has integrated backwards into oilseed crushing along with expanding its refining capacity. With a relatively adequate market share, the Company has experienced growth in its top-line owing to stable demand growth in refined and branded edible oil and meal segments. However, the refined and branded edible oil segment remains competitive where volumes and margins are functions of timeliness and prudence of raw materials (Canola oilseed and RBD Palm olein) procurement. The Company procures raw materials in bulk due to seasonality constraints, posing an inherent price risk along with storage issues and a high holding period. This has led to a modest increase in the Company's debt levels. Moreover, the rupee depreciation and increasing interest rate environment have impacted the Company's profits leading to reduced margins. However, the Company's financial risk remains low supplemented by strong coverages and a healthy working capital cycle. Capital structure remains modest. Demonstrated support from sponsors bode well for the Company's ratings.

The ratings are dependent on the management's ability to maintain its growing business volumes while sustaining margins and profitability. Prudent management of working capital and maintaining strong coverages is critical. Effective changes in governance framework would be beneficial for the ratings. Any prolonged deterioration in revenues and/or coverages will adversely impact the ratings.

Disclosure

Name of Rated Entity	Pakistan Oil Mills (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Edible Oil(Feb-22)
Rating Analysts	Faiqa Qamar | faiqa.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Pakistan Oil Mills (Pvt.) Limited ('Pakistan Oil Mills' or 'the Company') was incorporated in April, 1960 as a Private Limited Company

Background Mr. Muhammad Ishaq and his son, Haji Muhammad Farooq were initially involved in furniture business. In 1960, they set up an edible oil refinery with a production capacity of 7 MT per day. The Company's production facility, located in Kotri, Sindh, currently has oilseed crushing capacity of 400 MT per day and refining capacity of 280 MT of vegetable oil/ghee per day.

Operations Pakistan Oil Mills is primarily engaged in the process of seed filtering and crushing, refining of vegetable oil/ghee by mechanical and chemical processes. The Company primarily sells vegetable oil/ghee, canola meal, and other byproducts including laundry soap. During 6MCY22, the Company produced 34,027 MT of vegetable oil/ghee resulting in capacity utilization of ~ 41%. The decrease was mainly due to lower import volumes impacted by rupee depreciation. Furthermore, the Company operates in branded edible oil segment, namely Naz cooking oil/ghee, Pak cooking oil/ghee, Sun cooking oil/ghee, and Pure cooking oil/ghee.

Ownership

Ownership Structure The Company's major ownership resides with the family of Mr. Haji Muhammad Farooq. The major stake resides with his two sons Mr. Muhammad Masood Pervez (~ 64%) and Mr. Muhammad Usman (~ 33%). The remaining stake resides with Mr. Masood's sons, Mr. Mohsin Masood (~ 2%) and Mr. Abu Bakr Masood (~ 1%).

Stability The Company is completely owned by the sponsoring family. The Company's succession plan is formally documented indicating the stability of the ownership structure.

Business Acumen The sponsors have been involved in multiple businesses in edible oil, textile, ship breaking, and automobiles. Mr. Masood Pervez, the CEO of the Company and Fimcotex Industries (Pvt.) Limited, have over 30 years of experience in the edible oil and textile segment. Mr. Usman is the Director of Usman Steels (Pvt.) Limited and has over 3 decades of experience in real estate and ship breaking segments

Financial Strength The sponsors hold sufficient net worth to support the Company in times of distress. Furthermore, sponsors also benefit from multiple ventures and companies that provide substantial strength.

Governance

Board Structure The Company's Board comprises three Executive Directors. All three directors are from the sponsoring family. Lack of independent oversight and diversity indicates a room for improvement in the Company's governance structure.

Members' Profile The Board's Chairman, Mr. Masood Pervez, also the CEO of the Company, has been associated with the Company since 1978. He was the president of Hyderabad Chamber of Commerce, Trade & Industries and is a life member of FPCCI. Mr. Usman, Director of Usman Steels (Pvt.) Limited, has been associated with the Company for over 3 decades. Mr. Mohsin Masood has joined the Company's Board a year ago.

Board Effectiveness The Board lacks formal sub-committees. During 6MCY22, there were 3 meetings and attendance remained full. The minutes of Board meetings are adequately documented.

Financial Transparency The external auditors of the Company, Shah and Co. Chartered Accountants have expressed an unqualified opinion on the financial statements of the Company for the year ended Dec-21. The firm is not QCR rated. Lately, the Company has appointed Rehman Sarfaraz Rahim Iqbal Rafiq Chartered Accountants as its external auditors . The firm is QCR rated and in SBP's panel of auditors in the "A 'category.

Management

Organizational Structure The organizational structure has been optimized as per the operational needs. The Company operates through four functions: Production, Finance, Sales & Marketing, and Procurement. All functional managers' report to the Company's CEO.

Management Team Mr. Masood Pervez, the CEO of the Company and Fimcotex Industries (Pvt.) Limited, has overall 40 years of experience in the edible oil and textile segment. He is assisted by a team of experienced professionals.

Effectiveness There are no management committees in place. Management meets on need basis to ensure efficiency of the Company's operations.

MIS The Company uses an ERP (Oracle) software as per its needs. The software is regularly monitored by an inhouse IT function. Reports are prepared on need-basis for the management and Directors.

Control Environment To ensure operational efficiency, the Company has setup an internal audit function, which implements and monitors the policies and procedures of the Company.

Business Risk

Industry Dynamics Edible oil is Pakistan's 2nd largest import after petroleum. The industry, including both ghee (hydrogenated oil) and cooking oil production, relies on 70% of imports in the form of edible oilseed (soy and canola, ~ 3.4 MMT) and edible oil (mostly RBD Palm Oil, ~ 3.1MMT) which accounts for 80% of the cost of production. While, only 30% of the consumption is fulfilled by locally produced oilseed (cottonseed and mustard seed, ~1.7MMT). Domestic consumption for edible oil stood around 5.1 MMT, during FY22. With a minimal surge in demand along with the inflationary pressure on oilseed import and production, edible oil production grew meagerly over ~ 2% during FY22. The industry remains affluent with steady cashflows; however, debt levels remain considerably high. Being a staple item, despite consistent inflationary pressure, the industry's volumes and profits are expected to remain stable going forward.

Relative Position The Company has a market share of ~1% in terms of revenue.

Revenues The Company mainly generates revenue by selling vegetable oil/ghee (~93%) and canola meal (~6%) followed by laundry soap (~ 0.4%) and other by-products (~ 0.6%). During 6MCY22, the Company generated a revenue of ~PKR 16bln, witnessing an increase of ~150% (6MCY21: PKR 6bln) as the Company has benefited from volumetric and price increase in edible oil products owing to high demand.

Margins During 6MCY22, the Company's gross margin decreased YoY and stood at ~8% (6MCY21: ~11%) owing to an increase in the import costs. On an operational level, the Company's margins witnessed a similar trend. Operating margin stood at ~6% during 6MCY22 (6MCY21: ~9%) backed by an increase in administrative expenses (6MCY22: PKR 204mln, 6MCY21: 151mln). At net level, the Company's net income stood at PKR 472mln during 6MCY22 (6MCY21: PKR 370mln). However, high finance cost amidst interest rates hike resulted in low profitability margin (6MCY22: ~2.8%, 6MCY21: ~4%).

Sustainability The sponsors are planning to add flour mill in the Company. New land in Kotri, Sindh has been acquired for the said purpose.

Financial Risk

Working Capital The Company's working capital management is supported through short-term running finance facility obtained from commercial banks. The Company's inventory days were kept at 43 days as of 6MCY22 (6MCY21: 37 days) due to excessive procurement. Receivable days have been kept at 9 days as of 6MCY22 (6MCY21: 18 days) by proactive collection of payments. Payable days stood at 2 days as of 6MCY22 (6MCY21: 4 days) due to cash purchase. Overall, the Company's net cash cycle stood at 52 days as of 6MCY22 (6MCY21: 51 days).

Coverages The Company's interest cover is a function of free cash flows and finance costs. Free cash flows improved due to better profitability and stood at PKR 594mln as of 6MCY22 (6MCY21: PKR 417mln). The Company finance cost increased and stood at PKR 25mln as of 6MCY22 (6MCY21: PKR 7mln). As a result, interest cover posted a dip and stood at ~3.1x as of 6MCY22 (6MCY21: ~16.1x). Core and Total interest cover also posted a dip and stood at ~3.1x each as of 6MCY22 due to increase finance cost.

Capitalization The debt of the Company comprises 100% short-term borrowings. Total debt of the Company stood at PKR 3,497mln as of 6MCY22 (6MCY21: PKR 1,489) against an equity base of PKR 3,990mln (6MCY21: PKR 4,228mln). The leveraging ratio remains moderate, however, deteriorated and stood at ~47% in 6MCY22 (6MCY21: ~26%) due to an increase in short-term debt.

The Pakistan Credit Rating Agency Limited

Pakistan Oil Mills	Jun-22	Dec-21	Jun-21	Dec-20
Edible Oil	6M	12M	6M	12M
A BALANCE SHEET				
1 Non-Current Assets	811	816	773	454
2 Investments	-	-	-	-
3 Related Party Exposure	854	936	1,657	1,185
4 Current Assets	6,397	7,262	3,724	3,507
a Inventories	*2,286*	*5,177*	*1,094*	*1,538*
b Trade Receivables	*623*	*429*	*930*	*307*
5 Total Assets	8,062	9,014	6,154	5,146
6 Current Liabilities	575	360	436	413
a Trade Payables	*160*	*153*	*150*	*114*
7 Borrowings	3,457	4,333	1,489	1,043
8 Related Party Exposure	40	158	-	232
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	3,990	4,162	4,228	3,458
11 Shareholders' Equity	3,990	4,162	4,228	3,458
B INCOME STATEMENT				
1 Sales	16,002	13,515	6,408	9,591
a Cost of Good Sold	*(14,702)*	*(12,531)*	*(5,674)*	*(8,838)*
2 Gross Profit	1,300	984	733	752
a Operating Expenses	(383)	(333)	(157)	(224)
3 Operating Profit	917	651	576	529
a Non Operating Income or (Expense)	*(50)*	*(24)*	*(25)*	*(25)*
4 Profit or (Loss) before Interest and Tax	867	627	551	504
a Total Finance Cost	*(189)*	*(120)*	*(26)*	*(166)*
b Taxation	*(206)*	*(203)*	*(155)*	*(95)*
6 Net Income Or (Loss)	472	304	370	243
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*594*	*383*	*417*	*316*
b Net Cash from Operating Activities before Working Capital Changes	*568*	*335*	*409*	*290*
c Changes in Working Capital	*(2,452)*	*(3,794)*	*(534)*	*1,901*
1 Net Cash provided by Operating Activities	(1,883)	(3,459)	(124)	2,191
2 Net Cash (Used in) or Available From Investing Activities	(148)	(420)	(347)	(21)
3 Net Cash (Used in) or Available From Financing Activities	1,941	3,217	615	(1,759)
4 Net Cash generated or (Used) during the period	(91)	(662)	144	410
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	136.8%	40.9%	33.6%	-3.0%
b Gross Profit Margin	8.1%	7.3%	11.4%	7.8%
c Net Profit Margin	2.9%	2.2%	5.8%	2.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	-11.6%	-25.2%	-1.8%	23.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	23.1%	8.0%	19.3%	7.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	50	101	55	107
b Net Working Capital (Average Days)	48	97	51	103
c Current Ratio (Current Assets / Current Liabilities)	11.1	20.2	8.5	8.5
3 Coverages				
a EBITDA / Finance Cost	4.2	4.9	22.2	2.5
b FCFO / Finance Cost+CMLTB+Excess STB	3.1	3.2	16.1	1.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.0	0.6	0.0	1.5
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	46.7%	51.9%	26.0%	26.9%
b Interest or Markup Payable (Days)	25.2	173.0	7.2	18.3
c Entity Average Borrowing Rate	12.0%	5.0%	3.7%	7.7%

Credit Rating

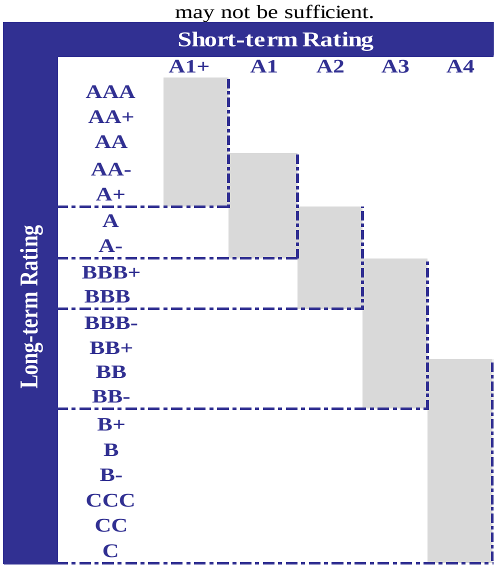
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 Rating

Scale	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
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 surveill 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):

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

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

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