The Pakistan Credit Rating Agency Limited

Rating Report

Qadir Agro Industries (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Mar-2022	BB+	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan's edible oil industry is heavily reliant on imports since oilseeds account for ~80% of the cost of production. Edible oil is the country’s 2nd largest import after petroleum. Pakistan’s total oil and fats consumption is ~ 5 million metric tons per annum and its per capita consumption is ~22 kg. Consumption is met by 70% (~3.3 MMT) of edible oil import. The remaining 30% (~1.7 MMT) of edible oil is produced from oilseeds (local ~ 3.5MMT, imported ~ 3.1 MMT). Additionally, low domestic oilseed production in Pakistan caused by a distortion in support price mechanism and lower yields have pushed farmers away from oilseed, further increasing dependence on imports. On the supply side, the key raw materials – oilseed and RBD palm oil – are imported primarily from USA, Brazil, and Malaysia. Moreover, raw material prices have continued to inflate amid supply uncertainties and historically low global inventory levels, along with rupee devaluation impacting importers. Subsequently, prices of cooking oil and vegetable ghee have remained on the higher side. Going forward, sales are expected to remain stable. Margins and profitability are expected to improve for players and costs will be offset by the increased demand and in turn prices. The rating reflects Qadir Agro Industries (Pvt.) Limited’s (‘the Company’) developing position in the country's edible oil and poultry feed sectors. The Company's financial performance has remained varied over the years owing to the relatively small market share. Lately, the Company has integrated into poultry feed by setting up a limited capacity feed mill. Margins have also showcased a variation over the years but generally remained on the lower side. Inventory management system and related efficiencies would require the Company’s attention to keep its working capital costs low. Being an importer of oilseeds, the Company remains exposed to the inherent risk related to currency fluctuations and prices of raw material. Forward integration and value addition initiatives could help elevate performance and margins. The Company has an adequate financial risk profile. The Company's debt book majorly comprises short-term running finance availed to fund its working capital needs. The Company's coverages remain adequate, however, any further debt-load and increased finance costs could stretch the interest/debt coverage and capital structure.

The ratings are dependent on the management's ability to prudently improve margins, profitability, and financial profile of the Company. Meanwhile, strengthening governance practices will have a positive impact on the ratings. Any deterioration in debt coverages leading to higher financial risk or substantial losses will adversely impact ratings.

Disclosure

Name of Rated Entity	Qadir Agro Industries (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Edible Oil(Feb-22)
Rating Analysts	Ahmad Faraz Arif | ahmad.faraz@pacra.com | +92-42-35869504

Profile

Legal Structure Qadir Agro Industries (Pvt.) Limited ('the Company') was incorporated in July, 1987 as a Private Limited Company.

Background Mr. Khawaja Mehr Baksh and his son, Mr. Khawaja Muhammad Shehzad laid the foundations of the Company by setting up a small crushing unit in the 1980s. Over the years the Company has been able to enhance its capacity and also venture into poultry feed by setting up a feed mill in Jul-2018.

Operations The Company is primarily engaged in the process of seed filtering, crushing and solvent extraction. The Company primarily sells soybean oil/meal, canola oil/meal and poultry feed. The Company has seed crushing capacity of 250MT per day. The capacity of the poultry feed mill currently stands at 15MT per hour.

Ownership

Ownership Structure The Company's major ownership resides with Khawaja Mehr Baksh (~34%) and his sons, Khawaja Muhammad Shehzad (~33%) and Khawaja Muhammad Omer (~33%).

Stability The Company is completely owned by the sponsoring family and the structure is seen as stable.

Business Acumen The sponsors have been involved in multiple businesses in textile, edible oil and poultry feed. The sponsors have ventured into textile by purchasing a cotton factory. The sponsors also own Roomi Industries (Pvt.) Limited, a solvent extraction unit.

Financial Strength The sponsors hold adequate net worth to support the Company in times of distress.

Governance

Board Structure The Company's BoD 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. The overall control of the Company vests with the Board's Chairman.

Members' Profile The Board's Chairman, Mr. Khawaja Mehr Baksh, has been associated with the Company since 1987 and has an overall experience of 5 decades in textile, edible oil, and poultry feed.

Board Effectiveness The Board lacks formal sub-committees. The minutes of Board meetings are adequately documented.

Financial Transparency The external auditors of the Company, Waqas and Co. Chartered Accountants, have expressed an unqualified opinion on the financial statements of the Company for the year ended Dec-20. The firm is neither QCR rated nor in SBP's panel of auditors.

Management

Organizational Structure The Company has a linear organizational structure. The Company operates through three functions: Production, Finance, Sales & Marketing. All functional managers report to the Company's CEO, who makes all pertinent decisions. As the Company's CEO is responsible for the whole unit, thus highlighting the key man risk of management.

Management Team Mr. Khawaja Muhammad Shehzad, the CEO of the Company, has over 30 years of experience in the edible oil and textile segment. He is an MBA and also looks over the Company's procurement and import of edible oil seeds.

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

MIS The Company's reports are mostly excel based for the management to review.

Control Environment The Company lacks internal audit function.

Business Risk

Industry Dynamics Pakistan's edible oil industry is heavily reliant on imports since oilseeds account for ~80% of the cost of production. Edible oil is the country's 2nd largest import after petroleum. Consumption is met by 70% (~3.3 MMT) of edible oil import. The remaining 30% (~1.7 MMT) of edible oil is produced from oilseeds (local ~ 3.5MMT, imported ~ 3.1MMT). Since Dec-20, raw material prices have continued to inflate amid supply uncertainties and historically low global inventory levels, along with rupee devaluation impacting importers. The price of Palm Oil stood at 990.27 USD/MT in Jan-21 followed by an increase of 36% to 1,348.07 USD/MT on Nov-21. Similarly, the price of Soybean oilseed stood at 576 USD/MT in Jan-21 and 600 USD/MT in Jun-21. Subsequently, prices of cooking oil and vegetable ghee have remained on the higher side.

Relative Position The Company has a market share of less than ~1% in terms of revenue and production in edible oil segment.

Revenues The Company mainly generates revenue by selling poultry feed (~38%), soybean meal (~22%), followed by canola/soybean/rapeseed oil and meal (~40%). During FY21, the Company generated revenue of PKR 4,519mln, witnessing more than two-folds increase (FY20: PKR 2,049mln) mainly due to the increase in prices and volumetric sales of poultry feed and soybean meal. Lately, the Company has benefited from both volumetric and prices increase in edible oil products as well owing to high demand post pandemic.

Margins The Company is exposed to foreign currency risk as soybean and canola oilseeds are imported. The import price has volatility depending on the demand and supply mechanics. During FY21 , the Company's gross margin decreased YoY and stood at 3.2% (FY20: 5.3%) owing to the jump in import costs. On operational level, the Company's margins witnessed similar trend. Operating margin stood at 2.5% in FY21 (FY20: 4.1%). At net level, the Company's net income stood at PKR 25mln during FY21 (FY20: PKR 12mln) indicating low profitability. Subsequently, the Company's net margin stood at 0.5% in FY21 (FY20: 0.6%).

Sustainability The sponsors are planning to increase the capacity of the poultry feed to 30MT per hour during the current year.

Financial Risk

Working Capital The Company's inventory days were kept at 65 days in FY21 (FY20: 152 days). In terms of receivable days, the Company efficiently manages receivable cycle and receivable days have been kept at 17 days in FY21 (FY20: 9 days). The Company, payable days improved in FY21 and stood at 17 days in FY21 (FY20: 43 days). Overall, the Company's net cash cycle stood at 64 days in FY21 (FY20: 118 days) Furthermore, the Company also has no room to borrow against short-term trade assets.

Coverages The Company's coverages have remained adequate through the years. Free cash flows stood at PKR 61mln in FY21 (FY20: PKR 32mln). The Company finance cost stood at PKR 38mln in FY21 (FY20: PKR 45mln). As a result, interest cover stood at 1.6x in FY21 (FY20: 0.7x). The Company has not obtained any long-term debt so the debt coverage remains the same as interest coverage ratio.

Capitalization The Company has highly leveraged capital structure. The debt of the Company comprises 100% short-term borrowings. Total debt of the Company stood at PKR 976mln as at FY21 (FY20: PKR 873mln) against an equity base of PKR 533mln (FY20: PKR 508mln). Debt to debt plus equity ratio stood at ~65% as at FY21 (FY20: ~64%).

PKR mln

Qadir Agro Industries Edible Oil	Jun-21 12M	Jun-20 12M	Jun-19 12M	Jun-18 12M
A BALANCE SHEET				
1 Non-Current Assets	425	455	469	154
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	1,286	1,282	968	1,038
a Inventories	*605*	*994*	*712*	*767*
b Trade Receivables	*369*	*49*	*51*	*3*
5 Total Assets	1,711	1,737	1,438	1,192
6 Current Liabilities	202	356	204	278
a Trade Payables	*124*	*305*	*176*	*243*
7 Borrowings	976	873	737	776
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	533	508	496	138
11 Shareholders' Equity	533	508	496	138
B INCOME STATEMENT				
1 Sales	4,519	2,049	2,205	1,585
a Cost of Good Sold	*(4,375)*	*(1,940)*	*(2,107)*	*(1,496)*
2 Gross Profit	144	109	98	89
a Operating Expenses	(30)	(25)	(22)	(25)
3 Operating Profit	114	84	76	64
a Non Operating Income or (Expense)	*(4)*	*(2)*	*(2)*	-
4 Profit or (Loss) before Interest and Tax	110	82	74	64
a Total Finance Cost	*(38)*	*(45)*	*(30)*	*(24)*
b Taxation	*(48)*	*(25)*	*(23)*	*(21)*
6 Net Income Or (Loss)	25	12	20	19
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*61*	*32*	*43*	*46*
b Net Cash from Operating Activities before Working Capital Changes	*61*	*32*	*43*	*46*
c Changes in Working Capital	*138*	*(136)*	*(48)*	*(455)*
1 Net Cash provided by Operating Activities	199	(103)	(5)	(408)
2 Net Cash (Used in) or Available From Investing Activities	(7)	(6)	(1)	(8)
3 Net Cash (Used in) or Available From Financing Activities	(178)	136	(39)	454
4 Net Cash generated or (Used) during the period	15	26	(45)	38
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	120.5%	-7.1%	39.1%	0.0%
b Gross Profit Margin	3.2%	5.3%	4.5%	5.6%
c Net Profit Margin	0.5%	0.6%	0.9%	1.2%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	4.4%	-5.0%	-0.2%	-25.8%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	4.8%	2.4%	6.4%	14.0%
2 Working Capital Management				
a Gross Working Capital (Average Days)	81	161	127	177
b Net Working Capital (Average Days)	64	118	92	121
c Current Ratio (Current Assets / Current Liabilities)	6.4	3.6	4.7	3.7
3 Coverages				
a EBITDA / Finance Cost	2.9	1.3	2.2	2.9
b FCFO / Finance Cost+CMLTB+Excess STB	1.6	0.7	1.5	1.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.0	0.0	0.0	0.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	64.7%	63.2%	59.8%	84.9%
b Interest or Markup Payable (Days)	0.0	0.0	0.0	0.0
c Entity Average Borrowing Rate	4.0%	5.6%	3.9%	3.0%

Credit Rating

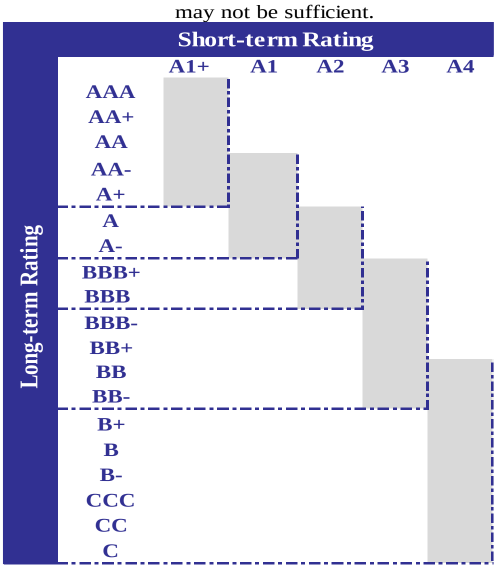
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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