The Pakistan Credit Rating Agency Limited

Rating Report

Irfan Noman Brothers (Pvt.) Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
10-Oct-2022	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Rice is among the five major crops of Pakistan and is the second main staple food, after wheat. The segment contributes about 3.5% in agriculture value addition and 0.7% to GDP. Local consumption includes ~95% of basmati rice and ~5% non-basmati. The major players in rice exports include Pakistan, India, Thailand, and Vietnam. Pakistan is in direct competition with India, while Thailand and Vietnamese rice are considered premium. During FY22, rice crop area increased to ~3.4mln Hec (FY21: ~3.3mln Hec), reflecting an increase of ~3%. Rice production increased by ~6%, standing at ~8.9mln MT in FY22 (FY21: ~8.4mln MT). New higher-yielding hybrid rice varieties, improved agronomic practices, and increased planting area, as farmers shift out of cotton, are factors driving the increased production. Around ~4mln MT of rice is consumed locally, while, the remaining is exported. During FY22, Pakistan exports increased to ~USD 2.5bln (FY21: ~USD 2bln). Going forward, 2022 floods are anticipated to cause ~12% loss to the forecasted rice production for FY23. However, the rupee depreciation is anticipated to compensate for reduction in export volumes.
The ratings reflect Irfan Noman Brothers (Pvt.) Limited's ('Irfan Noman' or 'the Company') leading position in the rice exporter's market of the country with substantial business volumes. The Company enjoys a strong relative position. The Company has enhanced its production over the years leading to higher volumetric sales resulting in improved financial performance by two-folds during FY22. The Company strategizes on customer retention and maintaining the market share. The Company has a comparative edge and benefits from economies of scale amidst increase in costs. Subsequently, margins, and in turn profitability witnessed a significant increase during FY22. The ratings derive comfort from the Company's relatively high market share over the years. The Company has also plans to diversify its product base, lately by adding volumes of basmati rice to its exports and the move towards value-added rice products, which is expected to be beneficial in the long-term. Sponsors' invested efforts are reflected in the development of a corporate culture through enhanced business practices and direct involvement in key functions of the Company. Furthermore, the willingness of the sponsors' to ensure exponential growth in the Company provides comfort to the ratings.

The ratings are dependent upon the sustenance of business volumes under the current challenging environment. As the global economy undergoes distress, business sustainability emerges as the key challenge for exporters, along with the floods leading to agricultural losses. Meanwhile, keeping up with a stable financial risk profile, particularly debt servicing capacity, remains imperative for ratings. Further envisioned improvements in qualitative factors, going forward, remain imperative for the ratings.

Disclosure

Name of Rated Entity	Irfan Noman Brothers (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 | Rice(Oct-21)
Rating Analysts	Ahmad Faraz Arif | ahmad.faraz@pacra.com | +92-42-35869504

Profile

Legal Structure Irfan Noman Brothers (Private) Limited (‘the Company’) was incorporated in Feb-98 as a Private Limited Company under the Companies Ordinance, 1984 (now Companies Act, 2017).

Background Mr. Mukhtar Ahmad Sheikh, former Chairman of Rice Millers and Supplier Association, established a rice mill in 1960s and laid foundations of the Irfan Noman Group (‘the Group’). Over the years the Group managed to gain prominence in the rice sector and established another rice mill and also established rice farms.

Operations The Company is primarily engaged in the process of processing semi-processed non-basmati rice, and basmati rice and exporting it Malaysia and other 40+ countries. The Company, in recent years, has witnessed prominent growth in its operations. The Company currently has two processing units in Port Qasim and S.I.T.E Karachi, respectively. The combined per hour processing capacity stands at 125MT and annual capacity stands at 360,000MT. The Company also possesses storage facility of 55,000MT per month. The Company has witnessed upward trajectory with regards to its processing capacity and, subsequently, volumetric increase in the quantity of rice processed (FY21: 250,000MT).

Ownership

Ownership Structure The Company’s major ownership resides with brothers Mr. Irfan Ahmad Sheikh (45.5%) and Mr. Noman Ahmad Sheikh (50%). The remaining (4.5%) stake is held by Mr. Irfan’s son, Mr. Moaz Irfan.

Stability The Company is completely owned by the sponsoring family and the structure is seen as stable as the second generation has been successfully integrated in the family business. Formal succession planning would provide additional cushion to the stability.

Business Acumen The sponsoring family have been involved in the rice export business for over 6 decades and have witnessed multiple business cycles. The current sponsors have been associated with the Company for over 2 decades and have led to the prominence of the Company as one of the largest exporters of rice in the country.

Financial Strength The sponsor holds sufficient net worth to support the Company in times of distress.

Governance

Board Structure The Company’s Board is dominated by the sponsoring family and includes three Executive Directors, and one Non-Executive Director.

Members’ Profile Mr. Irfan Ahmad Sheikh is the Chairman of the Board and has been associated with the Company since 1998. He has extensive experience in the rice sector and has attended multiple conferences both local, and abroad. Furthermore, he has also been involved research and seed development of rice.

Board Effectiveness The Board is supported by its sub-committees, the Audit Committee, and the Human Resource & Remuneration Committee. Both sub-committees are headed by Executive Directors. The Board and its sub-committees meet on need-basis and the minutes of the meetings are adequately documented.

Financial Transparency The external auditors of the Company, Rahman Sarfraz Rahim Iqbal Rafiq Chartered Accountants, have expressed an unqualified opinion on the financial statements of the Company for the year ended Jun-21. The firm is QCR rated placed in category ‘A’ of the SBP’s panel of auditors.

Management

Organizational Structure The Company has optimized its organizational structure as per the operational needs. The Company operates through functions of Finance, Procurement, Internal Audit, Production, Sales, HR & Admin.

Management Team Mr. Noman Ahmad Sheikh is the CEO of the Company and has been associated with the Company since 1998. He has extensive experience in the rice sector and has attended multiple conferences both local, and abroad. Furthermore, he has also been involved research and seed development of rice.

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

MIS The Company has a customized ERP system in place installed by Sidat Hyder & Co. MIS reports are regularly generated and reviewed by the Management for operational efficiency and decision-making.

Control Environment The Company has an inhouse internal audit department which ensures compliance with the Company’s policies and procedures.

Business Risk

Industry Dynamics During FY22, rice cropped area increased to ~3.4mln Hec (FY21: ~3.3mln Hec), reflecting an increase of ~3%. Rice production increased by ~6%, standing at ~8.9mln MT in FY22 (FY21: ~8.4mln MT). New higher-yielding hybrid rice varieties, improved agronomic practices and increased planting area, as farmers shift out of cotton, are factors driving the increased production. Around ~4mln MT of rice is consumed locally, while, ~5.2mln MT is exported. During FY22, Pakistan exports increased to ~USD 2.5bln (FY21: ~USD 2bln). Going forward, 2022 floods are expected to have destroyed approximately 12% of the nation's rice crop. However, the rupee depreciation is expected to compensate for reduction in export volumes.

Relative Position The Company is a leading player in the country’s rice exporters market and holds approximately 5% market share in terms of sales and 6% market share in terms of production.

Revenues The Company mainly generates revenue by exporting non-basmati rice variants majorly to Malaysia, China, Africa and minorly to other destinations. The Company’s revenues have witnessed upward trajectory, lately, owing to the increases in both prices and volumes. The Company’s sales mix contains ~71% of non-basmati rice and ~29% of basmati rice. Of the total sales, exports contribute ~93% and local sales contribute ~7%. During FY22, the Company posted revenue of PKR 17bln, witnessing 66% increase aided by increase in the prices, devaluation of the PKR, and increase in sales volumes.

Margins The Company is exposed to price changes risk because of the export-oriented nature. Subsequently, the Company’s margins have witnessed mixed trend over the years. During FY22, the Company’s gross margin witnessed increase as the Company benefited from higher selling prices and stood at 11.7% (FY21:8.7%).On operational level, the Company’s margins witnessed similar trend. Operating margin stood at 4.1% during FY22 (FY21: 1.9%). At net level, the Company’s net income witnessed significant increase and stood at PKR 405mln during FY22 (FY21: PKR 13mln). Subsequently, the Company’s net margin improved and stood at 2.4% during FY22 (FY21: 0.1%).

Sustainability The sponsors are planning to add storage and processing facility at Faisalabad, Punjab to increase the Company’s footing in the basmati sector.

Financial Risk

Working Capital The Company’s working capital management is supported through long-term loans -TERF & LTTF (~7% of total debt) and short-term Export Refinancing Facility- Part II (~93% of total debt). The Company’s inventory days were kept at 46 days in FY22 (FY21: 61 days) In terms of receivable days, the Company efficiently manages receivables cycle and receivable days have been kept at 30 days in FY22 (FY21: 27 days). The Company, by timely clearing payable dues has kept payable days to minimal. Overall, the Company’s net cash cycle stood at 70 days in FY22 (FY21: 82 days). However, the Company has insufficient room to borrow against trade assets. Short-term trade leverage and total short-term total leverage remained negative.

Coverages Free cash flows increased significantly and stood at PKR 463mln in FY22 (FY21: PKR 171mln). The finance cost stood at PKR 132mln in FY22 (FY21: PKR 113mln). As a result, interest cover improved and stood at 4.3x in FY22 (FY21: 1.9x). The Company’s debt coverage witnessed similar improvement and stood at 2.6x in FY22 (FY21: 0.3x). Going forward, the coverages are expected to remain adequate and the improvement in FY22 is expected to be sustained owing to favorable industry dynamics for rice exporters.

Capitalization The debt of the Company comprises of 93% short-term ERF facility-Part II and 7% long-term loans -TERF and LTTF. Total debt of the Company stood at PKR 4.4bln as at FY22 (FY21: PKR 3.5bln) against an equity base of PKR 2.2bln (FY21: PKR 1.8bln). Debt to debt plus equity ratio remains on the higher side and remained stable at ~67% as at FY22 compared to the preceding financial year. Going forward, the Company’s capital structure is expected to remain similar.

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Financial Summary
PKR mln

Irfan Noman Brothers (Pvt.) Limited Rice	Jun-22 12M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	2,648	2,428	1,367	1,216
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	4,341	3,299	2,281	1,639
a Inventories	*1,697*	*2,019*	*1,369*	*1,154*
b Trade Receivables	*1,970*	*1,196*	*336*	*375*
5 Total Assets	6,988	5,727	3,647	2,855
6 Current Liabilities	598	245	266	320
a Trade Payables	*417*	*142*	*206*	*261*
7 Borrowings	4,336	3,547	2,297	1,513
8 Related Party Exposure	-	90	110	106
9 Non-Current Liabilities	33	64	53	26
10 Net Assets	2,021	1,781	921	891
11 Shareholders' Equity	2,021	1,781	921	891
B INCOME STATEMENT				
1 Sales	16,739	10,218	7,266	6,147
a Cost of Good Sold	*(14,995)*	*(9,324)*	*(6,597)*	*(5,597)*
2 Gross Profit	1,745	894	669	550
a Operating Expenses	(1,339)	(698)	(493)	(386)
3 Operating Profit	406	196	176	164
a Non Operating Income or (Expense)	*133*	*33*	*24*	*56*
4 Profit or (Loss) before Interest and Tax	539	229	200	220
a Total Finance Cost	*(129)*	*(113)*	*(77)*	*(62)*
b Taxation	*(167)*	*(102)*	*(73)*	*(61)*
6 Net Income Or (Loss)	242	14	50	97
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*425*	*171*	*194*	*197*
b Net Cash from Operating Activities before Working Capital Changes	*333*	*89*	*139*	*134*
c Changes in Working Capital	*(135)*	*(1,580)*	*(248)*	*(391)*
1 Net Cash provided by Operating Activities	198	(1,492)	(109)	(257)
2 Net Cash (Used in) or Available From Investing Activities	(376)	(535)	(212)	(173)
3 Net Cash (Used in) or Available From Financing Activities	737	1,515	788	470
4 Net Cash generated or (Used) during the period	559	(511)	466	40
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	63.8%	40.6%	18.2%	--
b Gross Profit Margin	10.4%	8.7%	9.2%	9.0%
c Net Profit Margin	1.4%	0.1%	0.7%	1.6%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	1.7%	-13.8%	-0.7%	-3.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	12.8%	1.0%	5.5%	10.9%
2 Working Capital Management				
a Gross Working Capital (Average Days)	84	88	81	91
b Net Working Capital (Average Days)	78	82	69	75
c Current Ratio (Current Assets / Current Liabilities)	7.3	13.5	8.6	5.1
3 Coverages				
a EBITDA / Finance Cost	5.6	3.0	4.6	6.7
b FCFO / Finance Cost+CMLTB+Excess STB	0.9	0.3	0.7	0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.9	7.1	2.9	1.9
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	68.2%	67.1%	72.3%	64.5%
b Interest or Markup Payable (Days)	99.3	100.9	95.4	46.6
c Entity Average Borrowing Rate	2.7%	2.9%	2.9%	2.5%

Credit Rating

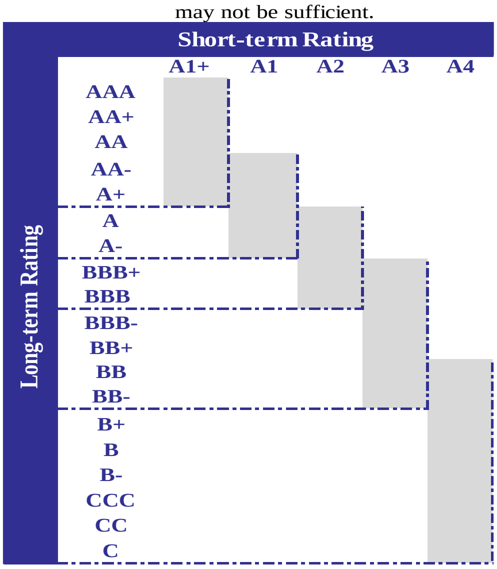
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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 | 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)
Proprietary Information