



The Pakistan Credit Rating Agency Limited

Rating Report

National Foods Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
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 ('National Foods' or 'the Company') was established in 1970 with an objective to introduce branded and packaged spices. Today, the Company offers a diversified product portfolio of 11 product categories and almost 250 SKUs. National Foods is Pakistan's leading player in the multi-category food market and holds sizeable brand equity in most of its product categories, both - in local and export market. Locally, unbranded segment always had sizeable presence in the market. However, over the years, an opportunity for expansion has risen in the branded segment. Globally, India has been a major competitor in condiment segment.

National Foods operates in the global market via its wholly-owned subsidiary, National Foods DMCC (NFL DMCC), which is based in the UAE. The investment in A1 Cash & Carry, facilitated by National Epicure Inc. (Canada), a wholly-owned subsidiary of NFL DMCC, has enabled the necessary diversification and considerable growth over the years. The Company derives strength from its holding company structure and stable international operations.

National Foods enjoy a sound risk profile and continues to increase its topline backed by price and volumetric growth. Increase in export sales prices has also supported this growth. The Company has maintained stability in healthy margins and profitability trend; despite raw materials remain price sensitive and marketing expenses were noticeably high. Competition in the recipe mixes segment remains considerably high; however, the management reflects confidence in holding the current performance pattern. Ratings draw strength from the Company's strong financial profile represented by a modestly leveraged capital structure, stable coverages and efficient management of working capital cycle. Also, the profitability at a consolidated level is significantly promising. Moreover, sponsors' business acumen and their widespread reach remains beneficial for the ratings. Strong governance framework further adds strength to the Company's profile

The ratings are dependent upon the management's ability to sustain margins while improving its market share. Materialization of growth activities remain critical. Prudent management of the working capital, maintaining sufficient cash flows and coverages remain imperative for the ratings

Disclosure

Name of Rated Entity	National Foods 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 Food Products(Dec-22)
Rating Analysts	Faiqa Qamar faiqa.qamar@pacra.com +92-42-35869504

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 11 categories in 250 SKUs. The production facilities are located in Port Qasim, SITE, Nooriabad, and Gujranwala. The Company is exporting products to ~ 40 countries across ~ 5 continents, through NF DMCC. During FY22, the Company's total production remained stable at 108,104MT of mixed food products.

Ownership

Ownership Structure National Foods major (~ 57%) ownership lies with sponsors through ATC Holdings (Pvt.) Ltd. (~34%) and individual family members (~23%). Directors and their family members hold ~16% stake while, Foreign Companies hold ~15% shares. While, the remaining ~12% of the shares resides with general public

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 over five decades and have very strong industry knowledge. Today, the Company is a leading player in Pakistan's multi-category food segment

Financial Strength National Foods is prime vehicle for the wealth of sponsoring family. On consolidated basis, the Company has an equity base of ~PKR 9.6bln with asset base of ~PKR 31bln, as at 1H FY23. The Company generated a consolidated revenue of ~PKR 26bln and posted a PAT of ~PKR 1.2bln during 1H FY23.

Governance

Board Structure The BoD comprises 7 members. There are four Non-Executive Directors, one Executive Director 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 During FY22, six BoD meetings were convened with majority attendance. Minutes were formally documented. The BoD is assisted by Board Audit Committee and Human Resource & Remuneration Committee. During 1H FY23, one BoD meeting has been convened.

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-22. 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 ~ three decades. He is also on the BoD of ATC Holdings (Pvt.) Ltd. and Cherat Packaging Ltd. 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 To generate MIS and operational reports, ERP software, SAP ECC6 is used.

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 convenience food market is mainly controlled by products produced domestically. This industry is fiercely competitive and the products are sensitive to changes in prices. The market operates with unbranded segment as a sizeable player. The food industry in Pakistan is growing at a rapid pace (CAGR of 6.6% during 2020-2025) due to increasing population, urbanization, and changing lifestyles. Lately, Pakistan's CPI has increased by ~32% in Feb-23 YoY, mainly due to significant increases in food, beverage, and transportation prices, rising by over 45%. This has affect the demand for convenience food products in the retail market. Going forward, industry's cashflow and liquidity is expected to remain stable.

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's revenues mainly concentrates at top 6 product categories account for ~84% of total revenue during FY22. Moreover, the Company's leading product category 'Recipe Mixes' accounted for ~56% of total revenue, reflecting high product concentration. During FY22, revenue posted a growth of ~16% and stood at ~PKR 27bln (FY21: ~PKR 23bln). Due to rupee devaluation, the export business also witnessed a healthy rise of ~14% (FY22: ~PKR 2.2bln, FY21: ~ PKR 1.9bln). During 1H FY23, the Company posted revenue of PKR 11,896mln (1H FY22: ~PKR 11,409mln), an increase of ~4.3%, driven by higher volumes sold locally. Inflationary trend may keep the revenue stream stable, even if volumes post a dip, going forward.

Margins Gross and operating margin stood at 33.4% and 8.9% during FY22 (FY21: 30.4% and 8.2%), respectively, on the back of efficient cost management. The Company's net profit witnessed an increase of ~58% and stood at ~PKR 1.9bln (FY21: ~PKR 1.2bln). Net profit margin witnessed an improvement and stood at 7.3% (FY21: 5.5%). However, in 1H FY23, the Company's gross margin increased to ~ 35.4% (1H FY22: ~ 32%), due to cost-push inflation. Nevertheless, the operating margin decreased to ~6.8% (1H FY22: ~9%) due to increased operating and marketing expenses. In addition, the net profit margin witnessed a fall and stood at ~ 4.1% during 1H FY23 (1H FY22: 7.2%). Margins may stretch due to increased procurement cost, going forward.

Sustainability To seek technology-driven growth, the Company has added a strategic wing into the Agri-Business division and has invested in a state-of-the-art facility located in Faisalabad.

Financial Risk

Working Capital In FY22, the Company's net working capital days deteriorated (FY22: 89 days, FY21: 81 days) owing to higher inventory held days (FY21: 79 days, FY20: 71 days), mainly high raw material stocks held. Early receipts slightly improved the receivable days (FY22: 22 days, FY21: 24 days). Trade payable days remain stable (FY22: 12 days, FY22: 13 days) due to timely payments. In 1H FY23, the Company's net working capital days deteriorated (1H FY23: 118 days, 1H FY22: 91 days) due to high inventory - raw material - held by the Company. Borrowing cushion is expected to remain considerable, going forward.

Coverages In FY22, despite the growth in the Company's finance cost to PKR 180mln (FY21: PKR 136mln, 33% growth in FCFO (FY22: ~PKR 2.9bln, FY21: ~PKR 2.2bln) led the interest cover to improve (FY22: 20.4x, FY21: 18.9x). Subsequently, core and total coverages posted an improvement (FY22: 5.2x each, FY21: 3.5x each). In 1H FY23, the Company's interest cover deteriorated to 5.0x (1H FY22: 20.8x) due to low profitability. However, core and total operating cover remain stable (1H FY23: 3.9x each, 1H FY22: 3.8x). Coverages may stretch further, going forward.

Capitalization In FY22, National Foods had a moderately leveraged capital structure with a debt-to-equity ratio of ~43% (FY21: ~42%). Total debt stood at ~PKR 5bln (FY21: ~PKR 4bln), comprising 86% of short-term debt to fund the working capital requirements. However, ERF from SBP, benefits the Company. In 1H FY23, the leveraging ratio increased to ~59% (1H FY22: ~47%) due to two-fold increase in total borrowing (1H FY23: PKR 8.5bln, 1H FY22: PKR 4bln). Leveraging may remain stretched, going forward.



The Pakistan Credit Rating Agency Limited

National Foods Limited Food Products	Dec-22 6M	Jun-22 12M	Dec-21 6M	Jun-21 12M	Dec-20 6M	Jun-20 12M
A BALANCE SHEET						
1 Non-Current Assets	8,393	7,233	5,503	5,192	5,063	4,930
2 Investments	1,631	1,339	747	1,031	30	30
3 Related Party Exposure	32	32	32	33	32	38
4 Current Assets	11,156	10,257	10,402	9,379	6,701	6,675
a Inventories	7,352	6,629	5,889	4,945	3,850	4,044
b Trade Receivables	833	1,949	1,273	1,277	980	1,702
5 Total Assets	21,212	18,861	16,683	15,636	11,826	11,673
6 Current Liabilities	6,589	7,146	6,216	5,787	4,612	4,661
a Trade Payables	644	751	1,029	961	666	730
7 Borrowings	8,521	4,974	4,747	4,020	2,238	1,624
8 Related Party Exposure	0	0	139	130	85	93
9 Non-Current Liabilities	276	231	220	222	255	371
10 Net Assets	5,827	6,509	5,361	5,476	4,636	4,924
11 Shareholders' Equity	5,827	6,509	5,361	5,476	4,636	4,924
B INCOME STATEMENT						
1 Sales	11,896	26,843	11,409	23,116	10,400	19,259
a Cost of Good Sold	(7,682)	(17,875)	(7,768)	(16,080)	(7,271)	(13,150)
2 Gross Profit	4,214	8,968	3,641	7,036	3,129	6,108
a Operating Expenses	(3,402)	(6,573)	(2,604)	(5,148)	(2,409)	(4,468)
3 Operating Profit	811	2,395	1,037	1,888	721	1,640
a Non Operating Income or (Expense)	131	367	127	(38)	(30)	112
4 Profit or (Loss) before Interest and Tax	942	2,762	1,164	1,850	691	1,752
a Total Finance Cost	(228)	(180)	(68)	(136)	(72)	(164)
b Taxation	(231)	(616)	(279)	(449)	(160)	(484)
6 Net Income Or (Loss)	483	1,965	817	1,265	458	1,105
C CASH FLOW STATEMENT						
a Free Cash Flows from Operations (FCFO)	921	2,990	1,239	2,250	857	2,115
b Net Cash from Operating Activities before Working Capital	830	2,881	1,172	2,109	807	1,936
c Changes in Working Capital	(914)	(1,862)	(1,419)	49	260	328
1 Net Cash provided by Operating Activities	(84)	1,019	(247)	2,158	1,066	2,264
2 Net Cash (Used in) or Available From Investing Activities	(1,751)	(2,926)	(323)	(1,743)	(402)	(817)
3 Net Cash (Used in) or Available From Financing Activities	2,414	(79)	(203)	1,697	(135)	(1,260)
4 Net Cash generated or (Used) during the period	579	(1,986)	(774)	2,112	529	187
D RATIO ANALYSIS						
1 Performance						
a Sales Growth (for the period)	-11.4%	16.1%	-1.3%	20.0%	8.0%	16.0%
b Gross Profit Margin	35.4%	33.4%	31.9%	30.4%	30.1%	31.7%
c Net Profit Margin	4.1%	7.3%	7.2%	5.5%	4.4%	5.7%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital / Net Profit)	0.1%	4.2%	-1.6%	9.9%	10.7%	12.7%
e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets / Equity)]	15.7%	32.8%	30.1%	24.3%	19.2%	23.9%
2 Working Capital Management						
a Gross Working Capital (Average Days)	129	101	107	94	93	100
b Net Working Capital (Average Days)	118	89	91	81	81	91
c Current Ratio (Current Assets / Current Liabilities)	1.7	1.4	1.7	1.6	1.5	1.4
3 Coverages						
a EBITDA / Finance Cost	6.2	23.4	24.8	22.0	16.1	16.6
b FCFO / Finance Cost+CMLTB+Excess STB	3.9	5.2	3.8	3.5	2.6	5.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fin)	2.2	0.2	0.4	0.6	0.9	0.5
4 Capital Structure						
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	59.4%	43.3%	47.0%	42.3%	32.6%	24.8%
b Interest or Markup Payable (Days)	214.2	199.6	32.8	28.1	26.7	35.9
c Entity Average Borrowing Rate	6.3%	3.4%	3.7%	5.0%	6.2%	6.8%

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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	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB-	
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.
B-	
CCC	
CC	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.
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)

2) Conflict of Interest

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- 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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- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
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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)
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- (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)

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- (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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