



The Pakistan Credit Rating Agency Limited

Rating Report

Sadiq Oil (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Sep-2018	BBB	A2	Stable	Maintain	-
22-Mar-2018	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan is a leading consumer of edible oils - a function of its population and eating habits. With ~ 4MMT annual demand, Pakistan is the 4th largest market for edible oil. This is primary through imports (~ 86% of total consumption), wherein ~80% (of total imports) is in the form of finished product and for the rest oil seed is imported that is refined locally. Pakistan's edible oil refinery industry, currently producing ~1.2 MMT of oil and ~3MMT of meal for cattle/poultry feed industry, is on a good growth path.

The rating reflects Sadiq Oil's association with an established poultry group, named SB Group. The group has significant presence along poultry supply chain and Sadiq Oil is supporting its vertical integration strategy. At present, Sadiq Oil is experiencing growth in sales, on the back of capacity expansion. Although margins are currently squeezed, these are expected to improve once expansion in extraction capacities will be streamlined. This would also result in the rise of production volumes. Inventory management system and related efficiencies would require the company's attention to keep its working capital costs low. Rising topline on account of bulk semi-refined oil sale as well as management's focus on meal sale within group would enhance the profitability prospects. However, being an importer of oilseeds (Soybean, Canola and Sunflower) in Pakistan, there is an inherent risk involved of currency fluctuations and prices of raw material, leading to reductions in margins. Financial risk profile of the company is characterized by high leveraging – both to fund increasing working capital needs and expansion cost.

The ratings are dependent on the management's ability to prudently manage the liquidity and debt profile of the company, particularly working capital, while improving business margins. Comfort is drawn from the company's commitment to reduce reliance on external funding. Envisaged improvement in business and financial profile along with effective changes in governance framework would be good.

Disclosure

Name of Rated Entity	Sadiq Oil (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Food and Allied Edible Oil(Mar-18)
Rating Analysts	Shahzad Saleem shahzad@pacra.com +92-42-35869504

Profile

Legal Structure Sadiq Oil Extraction (Pvt.) Ltd. was incorporated in 2013 as a Private Limited Company.

Background SB Group came into existence as a small scale family business and became formally operational in Apr, 1975. Today, the Group is known as one of the leaders in poultry operating under the brand name of Sadiq Brothers.

Operations Sadiq Oil primarily extracts and produces two different products in three variants. These include: i) Semi-refined Soybean oil and refined Soy Meal, ii) Semi-refined Canola Oil and refined Canola Meal and iii) Semi-refined Sunflower Oil and refined Sunflower Meal. The Company has two solvent extraction facilities having a crushing capacity of 500 tons per day. While the chemical refinery can semi-refine the edible oil up to 300 tons per day. Recently, the Company set upped a physical refinery with a refining capacity of 200 MT per day.

Ownership

Ownership Structure Sadiq Oil's major shareholding vests with Dr. Muhammad Sadiq (70%); followed by his two sons, Mr. Asif Zubair (15%) and Mr. Salman Sadiq (15%).

Stability Ownership of the business is seen as stable as the major ownership vests with Dr. M. Sadiq.

Business Acumen SB Group has experienced multiple business cycles and have maintained their league since 1975. The Group's broiler farms are among the highest chick producers in Pakistan. Currently, there are six companies and one trust working under SB Group. All are operating in various segments.

Financial Strength At the end of 9MFY18, SB Group has consolidated equity of the PKR 6.5bln. Moreover, group is managing an asset base of above PKR 29bln. Through its diverse set of businesses, it is generating a turnover of above PKR 28bln and a pre-tax bottom line of PKR 729mln in 9M.

Governance

Board Structure Sadiq Oil's Board, comprising three members, is dominated by the sponsoring family. The Company's Board lack independence, indicating room for improvement in company's governance framework.

Members' Profile All the BoD members have relevant expertise. Dr. Muhammad Sadiq, Board's Chairman, holds a DVM degree and has four decades of experience in poultry and integrated businesses. The Company's Directors, Mr. Asif Zubair and Mr. Salman Sadiq, are US graduates and have an experience of more than 10 years.

Board Effectiveness Keeping in view the size of the Board, absence of sub-committees may not impact Board's effectiveness. During 9M's, 3 Board meetings, with full/majority attendance, were held to discuss pertinent matters and make strategic decisions.

Financial Transparency Sadiq Oil's external auditors, Muniff Ziauddin and Co Chartered Accountants, have expressed an unqualified opinion on the financial reports for FY17. The firm has been QCR rated by ICAP and are in Category 'A' of SBP panel.

Management

Organizational Structure The Company's sales and production are monitored by GM Production. Whereas, support departments work as shared services for the Group. All departments eventually report to the CEO.

Management Team Sadiq Oil's management comprise experienced professionals. Dr. Muhammad Sadiq, Group's CEO, has headed several national and international forums and is also recognized as a leading authority on poultry sciences and avian welfare.

Effectiveness Management ensure effectiveness through Technical, Interview and Operational committee, established at the Group level. Each comprises 4 members and met 3 times during 9M.

MIS Two financial software, set upped by Sidat Hyder, are used at the Group level. However, for internal dissemination, information is documented when required.

Control Environment At Sadiq Oil, internal audit department has been established at group level to ensure internal controls. The Company's entire extraction and refining facilities is fully automated.

Business Risk

Industry Dynamics Pakistan is a leading consumer of edible oils - a function of its population and eating habits. With ~4MMT annual demand, Pakistan is the 4th largest market for edible oil. This is primary through imports (~86% of total consumption), wherein ~80% (of total imports) is in the form of finished product and for the rest oil seed is imported that is refined locally. Pakistan's edible oil refinery industry, currently producing ~1.2 MMT of oil and ~3MMT of meal for cattle/poultry feed industry, is on a good growth path.

Relative Position As per the All Pakistan Solvent Extractions' Association, there are 95 solvent extraction units out of which only 30 are operational. Among these 30 companies, Sadiq Oil Extraction (Pvt.) Limited holds a share of 2%

Revenues Sadiq Oil's sales mix comprises semi-refined oil, meal and soap. During 9MFY18, Sadiq Oil generated a topline of PKR 5.6bln (FY17: PKR 4.4bln). This increase was supported by price.

Margins The Company's business margins have slightly improved (9MFY18: Gross ~7.6% and Operating ~7.2%) on the back of procuring oilseed, in bulk, before the rupee depreciated. Consistent borrowings to meet the import needs, kept the interest expenses high.

Sustainability Going forward, the Company aims to fully utilize its production capacity to keep cost in control. The management is eyeing on an early commencement of Ghee plant and Soap plant's commercial operations.

Financial Risk

Working Capital Sadiq Oil's high inventory days refers to buffer stock of at least 2 to 2.5 months. Operating with brokers on cash basis for oil sales, with a credit period of 15-25 days given for selling meal, have increased the average debtor days (23 days). Despite procuring raw materials on advance, creditor days remained moderate (4 days), leading to an inclined net cash cycle of 252 days.

Coverages Interest coverage (9MFY18: 1.5x) is a function of the Company's short term borrowings (9MCY18: PKR 3.3bln) and improved cash flows.

Capitalization With the expanding business activities and need for credit facilities have kept the leveraging to a higher side (9MFY18 ~80%).



Sadiq Oil Extraction (Pvt.) Limited

BALANCE SHEET

	31-Mar-18	31-Dec-17	30-Jun-17	30-Jun-16
	9M	6M	Annual	Annual
Non-Current Assets	915	866	715	478
Investments (Incl. Associates)	-	-	-	-
Equity	-	-	-	-
Debt Securities	-	-	-	-
Investment Property	-	-	-	-
Current Assets	3,502	4,853	1,450	1,034
Inventory	2,360	3,911	897	835
Trade Receivables	428	160	141	22
Others	714	782	412	177
Total Assets	4,417	5,719	2,165	1,511
Debt	3,387	4,232	972	615
Short-Term (STB)	3,309	4,139	966	604
Long-term (Incl. Current Maturity of Long-Term Debt - CMLTD)	78	94	7	11
Other Short-Term Liabilities	191	693	544	413
Other Long-Term Liabilities	-	-	-	-
Shareholder's Equity	839	794	649	483
Total Liabilities & Equity	4,417	5,719	2,165	1,511

INCOME STATEMENT

Turnover	5,658	3,283	4,416	2,262
Gross Profit	428	309	298	89
Other Income/(Expense)	0	(10)	(9)	0
Financial Charges	(221)	(142)	(100)	(52)
Net Income	190	145	166	19

Cashflow Statement

EBITDA	466	328	342	140
Free Cashflow from Operations (FCFO)	340	263	93	55
Net Cash changes in Working Capital	(2,304)	(3,012)	(78)	(535)
Net Cash from Operating Activities	(2,157)	(2,835)	(80)	(518)
Net Cash from Investing Activities	(242)	(193)	(303)	(47)
Net Cash from Financing Activities	2,415	3,256	357	602
Net Cash Generated during the period	16	228	(26)	37

Ratio Analysis

Performance				
Turnover Growth (same period last year)	70.9%	48.7%	95.2%	100.0%
Gross Margin	7.6%	9.4%	6.8%	3.9%
Net Margin	3.4%	4.4%	3.8%	0.9%
ROE	30.4%	29.4%	30.2%	6.0%
Coverages				
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.5	1.8	0.2	0.3
Interest Coverage (x) (FCFO/Gross Interest)	1.5	1.9	0.9	1.1
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCF)	0.5	0.4	4.0	2.0
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	252	458	75	65
Capital Structure (Total Debt/Total Debt+Equity)	80%	84%	60%	56%

Sadiq Oil Extraction (Pvt.) Limited

Credit Rating Scale & Definitions

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 Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) 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.

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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

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- 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

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- (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.
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- (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

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- (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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