



The Pakistan Credit Rating Agency Limited

Rating Report

Ismail Industries Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
31-Dec-2018	A	A1	Stable	Maintain	-
29-Jun-2018	A	A1	Stable	Maintain	-
30-Dec-2017	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Ismail Industries Limited is one of the leading confectionery, snacks and biscuit manufacturing company. The ratings reflect the Company's strong presence in the confectionery through established brands (Candyland and Bisconni) and packaged food industry. Growing middle class, coupled with capacity enhancements, have led to significant growth in revenues over the years. Ratings draw strength from the Company's diversified revenue stream supported through plastic film manufacturing units. Moreover, supplementary dividend income from investments provide support to the Company's profitability. Aggressive marketing campaigns to promote new products and increasing raw material costs, aggravated by rupee devaluation, have put margins under some pressure. Nonetheless, the Company has been able to maintain a sound business profile. Meanwhile, Ismail Industries maintains a strong financial profile, despite a leveraged capital structure, characterized by robust working capital management and adequate coverages.

The ratings are dependent on upholding of the Company's business as well as financial risk profile. The company plans to further diversify by expanding its plastic films segment. Additionally, it plans to invest further in associated companies. Prudent management of expansion and investment related debt to meet financial obligations will remain a key factor for future rating movement.

Disclosure

Name of Rated Entity	Ismail Industries 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 Consumer Goods(Dec-18)
Rating Analysts	Adnan Dilawar adnan@pacra.com +92-42-35869504

Profile

Legal Structure Ismail Industries Limited (the Company) is a public listed company.

Background The Company was founded by Mr. Muhammad Ismail, along with both his brothers. It was incorporated in June, 1988 as a private limited company and was subsequently converted into a public listed company in November, 1988. The Company commenced operations by launching its flagship brand 'CandyLand' and has since been able to expand, both, horizontally and vertically. It entered the biscuits market in 2002 and has set-up two Cast Polypropylene manufacturing plants under 'Astroflims'. The first plant became operational in 2003, whereas the second came online in 2014. Additionally, a BOPET (Biaxially-Oriented Polyethylene Terephthalate) plant was set up in 2010. Moreover, the Company penetrated the snacks industry in 2006.

Operations The Company has its head office located in Karachi with eight production facilities concentrated in three locations – HUB, Port Qasim and Sundar. During FY18, production for food and film stood at 81,628 and 26,726, respectively.

Ownership

Ownership Structure Major shareholding of the Company lies with Ismail Family (99%) through Mr. Muhammad Ismail (29%), Mr. Miftah Ismail (31%), Ms. Almas Maqsood (33%) and associates (6%). Remaining shareholding is split between the general public.

Stability During the year the board decided to convert Sponsors' outstanding loan worth ~PKR 902mln into equity by way of further issue of shares. The matter is in process and is expected to be completed by June 2019.

Business Acumen Sponsors have been operating in the industry for over three decades and are considered to have a strong business acumen.

Financial Strength In addition to being one of the major players in the confectionery, biscuits and snacks industry, the Group has interests in plastic films and wind power. During FY18, the Company had a consolidated asset base of ~PKR 23,851mln.

Governance

Board Structure The Company's Board of Directors is dominated by the sponsoring family and consists of nine members, including, the Chairman, four non-executive directors, three executive directors and one independent director.

Members' Profile The Board members have strong profiles and specialize in industrial engineering and economics, in addition to confectionery, biscuits and snacks.

Board Effectiveness The Company has in place two Board committees, namely, Human Resources and Remuneration Committee and Audit Committee. During FY18, the Board met eight times, with high attendance of members.

Financial Transparency Grant Thornton Anjum Rehman Chartered Accountants are the auditors of the Company. They have given an unqualified opinion on the Company.

Management

Organizational Structure The Company's organizational structure is divided into five main departments, all of whom are reportable to the CEO. Management is split based on brands and three major functions, which are supply chain, sales and finance & accounts. Operations of Bisconni and Snackcity are headed by one individual, whereas Candyland is headed by a separate individual.

Management Team Mr. Munsarim Saifullah acts as the Chief Executive Officer of the Company. He has been associated with the Company since its inception and is a close associate of the sponsors'. He holds a bachelors in engineering and has been a vital component in establishing the Company's state-of-the-art production facility. He is aided by Mr. Ghulam Farooq, who acts as executive director finance and company secretary. He has been with the Company for more than 15 years and is a fellow of the Chartered Institute of Secretaries.

Effectiveness The Company has no management committees in place. However, financial accounts are discussed among management to review monthly activity.

MIS The Company maintains a comprehensive MIS reporting system to facilitate effective management. It recently deployed SAP as its Enterprise Resource Planning system with implementation of all modules except the Human Resources module.

Control Environment The Company's internal audit department has basic internal controls required to ensure compliance and efficiency. Moreover, the Company employs strict quality control measures at its production facilities, with all products being ISO 22000 certified.

Business Risk

Industry Dynamics The confectionery, biscuits and snacks industry in Pakistan is largely dominated by domestic players and is highly price elastic. Distinction between products lies in mass marketing. Pakistan has a large retail base though highly fragmented and dominated by small retailers, competing in terms of location, personal relationships and product ranges etc.

Relative Position Ismail Industries Limited is one of the leading players in the industry with high market penetration and brand recognition. The Company's confectionery brand 'CandyLand' is the market leader in the industry. Moreover, it is the third largest manufacturer of biscuits which are sold under the brand 'Bisconni' and the second largest in snacks with its brand 'SnackCity', after Lays.

Revenues The Company sources its revenue from two segments – food and plastic films. Major portion of revenue emanates from food sales which accounted for ~79% of total revenue in FY18. During FY18, sales clocked in at ~PKR 23,906mln, depicting ~22% growth over the preceding year. Growth can be attributed to higher volumetric sales. Revenue from foods grew by 26% on the back of increased exports and higher sales made in the domestic market. Similarly, revenue from plastic films grew by ~12% owing to increased local sales. During 3MFY19, owing to impact of aggressive advertising, growth pattern persisted and the Company posted revenues worth ~PKR 6,821mln, an increase of ~39% YoY.

Margins During FY18, the Company was able to improve gross margins to 22% (FY17: 19%). Increased margins can be explained by a reduction in the price of some raw materials (sugar) and various costs cutting strategies implemented by the Company, such as, reformulation of products and changing the net weight of products. However, due to aggressive marketing campaigns to promote the launch of its new product 'FLO', operating margins declined slightly and stood at ~8.7% (FY17: 9.2%). Additionally, re-launch of the Company's product 'Novella' further augmented marketing costs. The Company's profitability is supported by supplementary dividend income and scrap sales, which helped maintain net profit margin at ~6%. During 3MFY19 gross margin suffered slightly due to high price of imported raw materials owing to rupee devaluation and stood at 23% (3MFY18: 24%). However, the Company was able to improve operating margin to ~11% in 3MFY19 (3MFY18: 10%) as it eased off promotional activities.

Sustainability Going forward, the Company plans to enhance its BOPET film production capacity by 36,000 tons per year, bringing total capacity to 54,000 tons per year. The plant is expected to commence operations in 2019 – 2020 and will be financed through long term loans. Moreover, the Company is expected to invest ~PKR 1.5bln in its associates.

Financial Risk

Working Capital The Company finances its working capital through a mix of internal cash generation and short-term borrowings. Due to effective stock management, the Company was able to improve Net Working Capital Days, bringing it down to 85 days in FY18 (FY17: 105 days). Moreover, the Company maintains a healthy cushion to borrow additional funds, if any situation arises. During 3MFY19, the Company maintained a strong position on working capital management and was able to improve it to 80 days.

Coverages Owing to improved profitability and lower interest costs, the Company was able to improve interest coverage to 4.4x in FY18 as compared to 3.4x in FY17. Additionally, income from associates helped marginally improve total debt coverage, standing at 0.9x in FY18 (FY17: 1.0x). The Company maintained elevation in coverage ratios through 3MFY19 and posted interest and debt coverage of 4.8x and 1.2x, respectively.

Capitalization The Company has an aggressive capital structure, represented by a leveraging ratio of ~60% in 3MFY19. Total debt taken up by the Company stood at ~PKR 12,178mln, rising by ~3% as compared to FY18 (~PKR 11,854mln). Debt taken up is inclined towards short-term borrowings, representing 53% of total debt. The Company utilized long-term borrowings to finance various capacity enhancements and investment opportunities.

Ismail Industries Limited
BALANCE SHEET

	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	3MFY19 Unaudited	Annual Audited	Annual Audited	Annual Audited
Non-Current Assets	10,917	10,994	10,430	8,035
Investments (incl. Associates)	3,238	3,560	3,926	4,310
Equity	3,238	3,560	3,926	4,310
Debt Securities (incl. income funds)	-	-	-	-
Current Assets	8,921	8,518	7,883	8,259
Inventory	5,044	4,970	4,864	5,750
Trade Receivables	1,781	1,566	1,443	1,621
Others	2,096	1,982	1,577	888
Total Assets	23,076	23,072	22,239	20,604
Debt	12,178	11,854	12,635	11,128
Short-term	4,214	4,191	3,783	4,448
Long-term (incl. Current Maturity of Long-Term debt)	7,964	7,663	8,851	6,680
Other Short-term Liabilities	1,330	1,665	1,217	1,774
Other Long-term Liabilities	1,531	1,431	1,213	800
Shareholder's Equity	8,037	8,122	7,174	6,901
Total Liabilities & Equity	23,076	23,072	22,239	20,604

INCOME STATEMENT

Turnover	6,821	23,906	19,605	17,008
Gross Profit	1,576	5,361	3,721	3,109
Other Income	5	372	516	541
Financial Charges	(190)	(618)	(671)	(798)
Net Income	392	1,412	1,166	1,002

Cashflow Statement

Free Cashflow from Operations (FCFO)	904	2,735	2,285	2,155
Net Cash changes in Working Capital	(994)	(111)	273	(433)
Net Cash from Operating Activities	(294)	2,376	2,262	1,157
Net Cash from Investing Activities	(20)	(1,401)	(3,145)	(2,237)
Net Cash from Financing Activities	324	(956)	838	1,110
Net Cash generated during the period	10	19	(45)	31

Ratio Analysis
Performance

Turnover Growth	38.5%	21.9%	15.3%	38.9%
Gross Margin	23.1%	22.4%	19.0%	18.3%
Net Margin	5.7%	5.9%	5.9%	5.9%
ROE	10.0%	35.6%	16.3%	14.5%

Coverages

Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	0.8	0.9	0.9	0.6
Interest Coverage (x) (FCFO/Gross Interest)	7.5	3.5	3.8	2.7
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross It	2.8	3.6	5.5	4.9

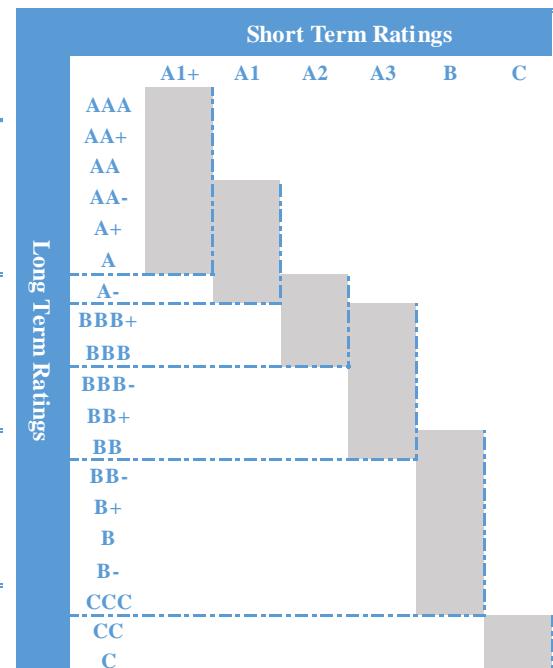
Liquidity

Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	80	85	105	117
Capital Structure (Total Debt/Total Debt+Equity)	60.2%	59.3%	63.8%	61.7%

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+	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.
AA		A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
AA-		A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
A		C	An inadequate capacity to ensure timely repayment.
A-			
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			
BBB-			
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			
BB-			
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			
B-			
CCC	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.		
CC			
C			
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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Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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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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