The Pakistan Credit Rating Agency Limited

Rating Report

Ismail Industries Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
14-Dec-2020	A	A1	Stable	Maintain	-
27-Dec-2019	A	A1	Stable	Maintain	-
28-Jun-2019	A	A1	Stable	Maintain	-
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

The ratings reflect the Ismail Industries Limited's (Ismail Industries or 'the Company') strong presence in confectionery, biscuits and plastic film manufacturing through established brands (Candyland, Bisconni, Snackcity and Astro Films). Growing middle class, coupled with timely capacity enhancements, have led to significant growth in revenues of the Company in the recent past. The ratings draw strength from the Company's diversified revenue stream, supported by the plastic film manufacturing segment. The Company was able to sustain its revenues, owing to aggressive marketing campaigns and introduction of new food products. The food industry remain exemption from the lockdown implemented by the Government to control the spread of COVID-19. However, demand of non-essential food products remain low due to the lockdown as schools and limited movement of people. The Company maintained its margins at the gross level, despite cost-push inflation and rupee depreciation. High marketing costs, coupled with increased finance costs resulted in a relatively low bottom-line. However, significant share of profit was received from its associate company. Nonetheless, business profile remains strong. Ismail Industries' strategic investments in its associated companies is expected to support the bottom-line, going forward. Meanwhile, despite a leveraged capital structure, the Company maintains a strong financial profile, through strong working capital management and adequate coverages.

The ratings are dependent on continued revenue growth and maintenance of margins. Prudent management of expansion and investment-related debt in order to meet financial obligations will be important. Decline in coverages and/or erosion of margins may have a negative impact on ratings.

Disclosure	
Name of Rated Entity	Ismail Industries Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Food Products(Dec-19)
Rating Analysts	Faiqa Qamar | faiqa.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Ismail Industries Limited (Ismail Industries or 'the Company') was incorporated as a public listed company in 1989. The Company is listed on the Pakistan Stock Exchange..

Background Ismail Industries Limited was incorporated as a public listed company in 1989. The Company was founded by Mr. Muhammad Ismail along with his brothers. 'Candyland', which operates in the confectionary segment, is the flagship brand of the Company. The Company established the brand 'Bisconni' in 2002 and 'Snackcity' in 2006. The Company also produces CPP, BOPP and BOPET films under the brand name 'Astro Films'.

Operations The Company manufactures and sells confectionery, biscuits, snacks and plastic films under the brand names of CandyLand, Bisconni, SnackCity and Astro Films. Its head office is located in Karachi, while production facilities are located in Hub, Port Qasim and Sundar. Astro Films produce CPP, BOPP and BOPET at an installed capacity of 54,000MT. The Company is enhancing its BOPET production capacity, increasing the overall film capacity to 70,000MT per annum.

Ownership

Ownership Structure Major shareholding of the Company lies with the Ismail Family (~99%) through Mr. Muhammad Ismail (~16%), Mr. Miftah Ismail (~31%), Ms. Almas Maqsood, wife of Maqsood Ismail, (~33%), Mr. Ahmed Muhammad (~15%) and associates (~4%). Remaining shareholding is held by the general public.

Stability The ownership structure is stable as the Ismail family owns majority shares of the Company. Mr. Muhammad Ismail has been leading the Company for several years and has vast experience in the industry.

Business Acumen The sponsors have been operating in the industry for over three decades and have very strong industry knowledge.

Financial Strength In addition to being a major player in the confectionery, biscuits and snacks industry, the Group has interests in plastic films and wind power sectors

Governance

Board Structure The Company's Board of Directors is dominated by the sponsoring family and consists of seven members, including the Chairman, two non-executivedirectors, two executive directors and two independent directors.

Members' Profile The Board members have strong profiles and specialize in diverse fields such as industrial engineering and economics, in addition to having strong knowledge of the confectionery, biscuits and snacks industry.

Board Effectiveness The Company has formed two Board committees, namely, i) Human Resource and Remuneration Committee, and ii) Audit Committee. Minutes of the meetings were well recorded and reflected adequate participation and discussion from members including independent directors.

Financial Transparency Grant Thorton Anjum Rehman Chartered Accountants are the external auditors of the Company. They gave an unqualified opinion on the Company's financial statements for the year ended June 30, 2020.

Management

Organizational Structure The Company has a well-defined organizational structure that is divided according to the main brands. Functions such as Accounts & Finance, HR, IT and Supply Chain are common to the entire organization while Sales and Marketing departments are specific for each brand.

Management Team Mr. Munsarim Saifullah is the Group CEO. He is a close associate of the sponsors and has been involved with the Company since its inception. He holds a Bachelor's degree in Engineering, in addition to having significant experience in production and engineering. Moreover, he has been instrumental in the Company's success over the decades. Mr. Saifullah is aided by a team of experienced professionals.

Effectiveness The Company has no management committees in place. However, members of the senior management regularly communicate and discuss ongoing issues and upcoming plans relating to relevant brands and management functions.

MIS The Company has installed SAP to streamline the flow of information within the Company. However, the Company faced challenges during SAP implementation. Most of these issues have now been resolved and it is expected that flow of information will improve, going forward.

Control Environment The Company employs strict quality control measures at its production facilities, with all products being ISO 22000 certified. The Company has also received Halal certifications from SANHA. The Company has an effective internal audit department which reports to the Audit Committee, reflecting well on the overall control environment.

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 it is highly fragmented and dominated by small retailers. Post Covid-19, the food industry remain exempted from lockdown implemented by the Government. However, there was a detrimental impact on demand of non-essential food products due to the lockdown as schools, shops and Malls remained closed. The measures announced by SBP, including rate cut of 625bps, eased some pressure.

Relative Position Ismail Industries is one of the leading players in the industry. Its flagship brand 'Candyland' is the market leader in the confectionery segment. The 'Bisconni' brand is the third-largest in the biscuit segment while 'Snackcity' is one of several players in the snacks segment who trail the market leader 'Lays'. 'Astro Films' is a major player in the film packaging segment.

Revenues The Company earns its revenue from two segments, namely i) Food, and ii) Plastic films, in the local and export markets. Major portion of revenue emanates from food sales, which accounted for ~78% of total revenue. Local sales generates ~89% of the total revenue. During FY20, overall sales grew by ~10% and stood at ~PKR 33,218mln (FY19: ~PKR 30,091mln). This growth was attributable to food segment (~13%), supported by volumes due to increased marketing efforts. During 1QFY21, the Company posted revenues of ~PKR 9,755mln (1QFY20: ~PKR 8,020mln), an increase of ~18% YoY, driven by a significant increase in export sales.

Margins During FY20, gross margins remained stable at ~21% (FY19: ~21%), despite an increase in inflation and rupee devaluation. However, the operating margin witnessed a decline (FY20: ~6%, FY19: ~7%) owing to higher selling and marketing expenses. Meanwhile, the finance costs increased to ~PKR 1,156mln (FY19: ~PKR 906mln). The Company's bottom-line was supported by significant returns provided by the associates. The Company posted a stable net profit margin of ~3% (FY19: 3%). In 1QFY21, gross and operating margins declined slightly to ~20% and ~7%, respectively. Meanwhile, net profit margin improved to ~3% (1QFY20: ~2%) as a result of lower finance cost.

Sustainability Ismail Industries is currently enhancing its BOPET film production capacity by 36,000MT per annum. The new line is expected to achieve COD in Nov-20. New production lines are also being added for CandyLand.

Financial Risk

Working Capital During FY20, the Company's inventory days remained stable to 62 days (FY19: 61 days). The Company's trade receivables emanate mostly from the plastics segment and sales to departmental stores as remaining food segment sales are made on a cash basis. Trade receivable days increased to 33 days in FY20 (FY19: 26 days). Meanwhile, trade payable days increased to 20 days (FY19: 14 days) owing to delay in payments to its creditors. Consequently, net working capital days deteriorated to 96 days (FY19: 87 days). The Company had a short-term trade leverage of ~19% in FY20 (FY19: ~24%), showing adequate room to borrow. In 1QFY21, the net working capital days observed an improvement to 88 days (1QFY20: 95 days) on the back of efficient inventory management.

Coverages In FY20, the Company's free cash flows from operations decreased to ~PKR 2,820mln (FY19: ~PKR 3,078mln) on the back of lower profitability. Meanwhile, total finance cost increased (FY20: ~PKR 1,151mln, FY19: ~PKR 906mln). Consequently, the Company's interest coverage ratio declined to 2.5x (FY19: 3.5x). Debt coverage ratio improved slightly to 1.3x (FY19: 1.1x) due to lower current maturity of long-term debt. During 1QFY21, the Company's interest cover (1QFY21: 4.9x,1QFY20: 3.3x) and debt cover (1QFY21: 1.5x, 1QFY20:1.2x) witnessed an improvement due to increased cash flows.

Capitalization The Company has a highly leveraged capital structure with a leveraging ratio of ~68%. Short term borrowings constitutes ~32% of total borrowings in FY20. The higher leveraging was due to an increase in long-term borrowings (FY20: ~PKR 13,605mln, FY19: ~PKR 6,289mln), used to finance new production lines in CandyLand and Astro Films. In 1QFY21, the leveraging ratio observed a slight increase to ~69% as the Company continued to obtain long-term borrowings to fund capex.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Ismail Industries Limited	Sep-20	Jun-20	Sep-19	Jun-19	Jun-18
Food Products	3M	12M	3M	12M	12M

A BALANCE SHEET

	Sep-20	Jun-20	Sep-19	Jun-19	Jun-18
1 Non-Current Assets	20,403	19,666	15,786	12,889	10,994
2 Investments	200	200	200	-	195
3 Related Party Exposure	5,276	5,276	3,633	3,212	3,365
4 Current Assets	11,996	12,366	11,738	10,864	8,518
a Inventories	*5,648*	*6,252*	*5,599*	*5,112*	*4,970*
b Trade Receivables	*3,584*	*3,345*	*3,172*	*2,746*	*1,566*
5 Total Assets	37,876	37,508	31,358	26,965	23,073
6 Current Liabilities	3,790	4,082	2,755	2,453	1,665
a Trade Payables	*1,532*	*2,225*	*1,415*	*1,359*	*1,001*
7 Borrowings	22,000	21,457	18,363	14,602	11,854
8 Related Party Exposure	-	-	902	902	902
9 Non-Current Liabilities	2,085	2,070	1,790	1,633	1,431
10 Net Assets	10,000	9,900	7,548	7,374	7,220
11 Shareholders' Equity	10,000	9,900	7,548	7,374	7,220

B INCOME STATEMENT

	Sep-20	Jun-20	Sep-19	Jun-19	Jun-18
1 Sales	9,755	33,218	8,020	30,091	23,906
a Cost of Good Sold	*(7,805)*	*(26,341)*	*(6,334)*	*(23,737)*	*(18,545)*
2 Gross Profit	1,950	6,878	1,686	6,354	5,361
a Operating Expenses	(1,241)	(5,063)	(957)	(4,131)	(3,277)
3 Operating Profit	710	1,815	729	2,223	2,084
a Non Operating Income or (Expense)	*(84)*	*664*	*31*	*86*	*372*
4 Profit or (Loss) before Interest and Tax	625	2,478	760	2,309	2,456
a Total Finance Cost	*(213)*	*(1,156)*	*(310)*	*(906)*	*(614)*
b Taxation	*(113)*	*(391)*	*(258)*	*(437)*	*(426)*
6 Net Income Or (Loss)	299	932	193	967	1,416

C CASH FLOW STATEMENT

	Sep-20	Jun-20	Sep-19	Jun-19	Jun-18
a Free Cash Flows from Operations (FCFO)	*1,028*	*2,820*	*981*	*3,078*	*2,739*
b Net Cash from Operating Activities before Working Capital Changes	*769*	*1,654*	*706*	*2,276*	*2,491*
c Changes in Working Capital	*(173)*	*2,578*	*(1,038)*	*(824)*	*(111)*
1 Net Cash provided by Operating Activities	596	4,232	(332)	1,452	2,380
2 Net Cash (Used in) or Available From Investing Activities	(1,112)	(8,787)	(3,601)	(3,156)	(1,405)
3 Net Cash (Used in) or Available From Financing Activities	543	4,573	3,966	1,685	(956)
4 Net Cash generated or (Used) during the period	27	19	33	(19)	19

D RATIO ANALYSIS

	Sep-20	Jun-20	Sep-19	Jun-19	Jun-18
1 Performance					
a Sales Growth (for the period)	17.5%	10.4%	6.6%	25.9%	21.9%
b Gross Profit Margin	20.0%	20.7%	21.0%	21.1%	22.4%
c Net Profit Margin	3.1%	2.8%	2.4%	3.2%	5.9%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	8.8%	16.2%	-0.7%	7.5%	11.0%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/S*	12.0%	11.0%	11.0%	14.1%	20.0%
2 Working Capital Management					
a Gross Working Capital (Average Days)	88	96	95	87	118
b Net Working Capital (Average Days)	70	76	79	73	105
c Current Ratio (Current Assets / Current Liabilities)	3.2	3.0	4.3	4.4	5.1
3 Coverages					
a EBITDA / Finance Cost	4.8	2.9	3.6	3.9	5.2
b FCFO / Finance Cost+CMLTB+Excess STB	1.5	1.3	1.2	1.1	0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	4.8	8.8	4.6	4.2	4.0
4 Capital Structure					
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	68.7%	68.4%	71.8%	67.8%	63.9%
b Interest or Markup Payable (Days)	64.7	62.2	73.2	85.8	61.7
c Entity Average Borrowing Rate	4.0%	5.8%	8.1%	6.5%	4.7%

Credit Rating

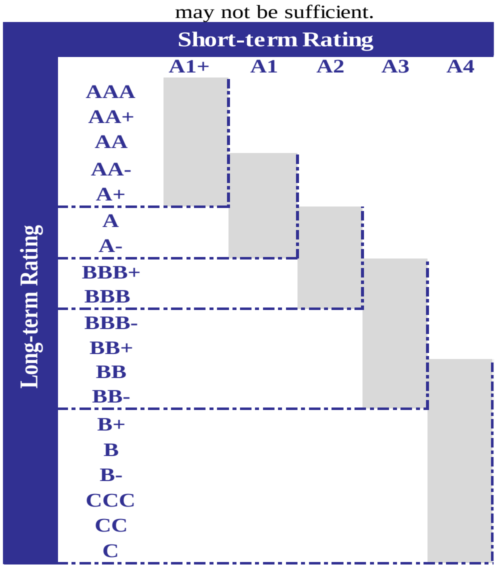
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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