The Pakistan Credit Rating Agency Limited

Rating Report

Engro Eximp Agriproducts (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jun-2019	A-	A2	Stable	Maintain	-
27-Dec-2018	A-	A2	Stable	Maintain	-
28-Jun-2018	A-	A2	Stable	Maintain	-
29-Dec-2017	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect the strength of ownership structure of the company: Engro Eximp is a wholly owned subsidiary of Engro Corp, the parent company and one of the largest conglomerate in Pakistan (rated AA+ by PACRA). The CEO of Engro Corp is also the Chairman of Engro Eximp. Ratings take comfort from the strong corporate governance framework of the group. The company has successfully managed to achieve its break even in later CY18. Profits have sustained since then, after suffering from huge losses in the past. Reversal of previously occurred impairment losses bears a significant contribution towards the profits. Dealing in a product – ‘basmati’- a high priced commodity has assisted the company in avoiding the unfavorable effects of the industry. The financial risk profile has also recovered adequately.

The ratings are dependent upon growth in business volume and redemption of profits. Adherence to sound financial discipline while strengthening debt servicing capacity through improved cash position is vital for the ratings. Positive outcome of the future projects and sustainability of profits remain a catalyst for the business

Disclosure	
Name of Rated Entity	Engro Eximp Agriproducts (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Rice(Dec-18)
Rating Analysts	Raniya Tanawar | raniya.tanawar@pacra.com | +92-42-35869504

Profile

Legal Structure Engro Eximp Agriproducts (Pvt.) Ltd. (herein referred to as "Engro Eximp" or "the company") is a Private Limited Company.

Background The company was incorporated on November 3, 2009. It entered into the rice processing business in 2010 with a view to bring value addition to the agriculture sector of the country.

Operations The Company procures high standard of paddy from the farmer and after processing those, exports the prepared rice to business to business customers across the globe. The principal activity of the company is processing, export and trade of rice. With a primary focus on buying rice paddy from farmers rather than middlemen, the Company's inclusive business model concentrates on improving the competitiveness of Basmati rice for farmers to ensure enhanced yield/acre and reduction in cost of production/ton to benefit the farmers. The company operates with an advanced integrated processing plant having a design capacity of 144,000 tons for milling and 3 months design capacity of 270,000 tons for drying.

Ownership

Ownership Structure Engro Eximp is a wholly owned subsidiary of Engro Corporation.

Stability Being a subsidiary of a renowned Multinational Corporation of Pakistan - Engro Corp, is the key driving force of stability for the company.

Business Acumen Engro Corporation, the parent company, is one of the largest conglomerates of Pakistan, having diversified businesses in fertilizer, food, chemical storage & handling, trading, digital technologies, mining, energy and petrochemicals sector.

Financial Strength Robust sponsorship continues to add strength to the financial muscle of the company.

Governance

Board Structure Engro Eximp has a three member Board of directors, including the Chairman and the CEO. Governance reflects status of a private limited entity which is necessitated to evolve as the business size grows.

Members' Profile Mr. Ghias Khan - Chairman of the board, is also the CEO of Engro Corp. Other members on the board are Mr. Imran Anwer, CEO - Engro Polymer & Chemicals and Mr. Mazhar Hasnani, Head of Strategy and Corporate Finance, Engro Corp.

Board Effectiveness The board is currently aligned with the private status of the company. Board meetings are conducted on a quarterly basis where company's financial performance and other pertinent matters are reviewed.

Financial Transparency A.F. Ferguson & Co. Chartered Accountants - one of the big four firms, are the Auditors for Engro Eximp. They gave an unqualified opinion on the financial statements for the year ended December 31, 2018.

Management

Organizational Structure Engro Eximp has a regime of clear reporting lines. The board's reporting line terminates into the CEO while the departmental heads report to the Director Consumer Agri-business.

Management Team The company's management palette is enriched with highly experienced members associated with the group for long. Mr. Danial Ali, a graduate from a reputed institute has been recently appointed as the CFO. He has been deploying his valuable services in various roles within the Engro group, as well as in Engro Eximp for more than 12 years.

Effectiveness In pursuance of effective business management, Engro Eximp has a culture of weekly management committee meetings, which comprises all heads of the department and the CEO. A Corporate planning meeting is also held every year for ensuring performance management.

MIS The Company has an ERP software implemented for their safety management, financial management and inventory management.

Control Environment Engro Eximp being a subsidiary of Engro Corp, follows the best practices and has the highest number of quality certifications among rice players in Pakistan.

Business Risk

Industry Dynamics Pakistan's Rice industry is an instrumentalist segment in the overall economy as it is one of the five major crops of the country and a contributor to the national exports revenue. After wheat, it is Pakistan's second main staple food crop. Major factors affecting rice production include water availability, area of cultivation, crop yield and the governing policies and initiatives. and During FY19, rice crop area decreased by ~3.1% to 2.8 million hectares compared to last year. The production stood at 7.2 million tonnes as against 7.5 million tonnes last year, short by ~3.3%, mainly due to decrease in area cultivated, dry weather and shortage of water.The maximum contribution from the Rice sector in country's foreign exchequer is from non-basmati rice exports, as basmati rice is locally consumed and minimal quantity is exported.

Relative Position The past couple of years have been difficult for Engro Eximp as it was recovering from the after effects of over trading. CY18 brought fortune for the business as it returned to stability. The business is still in the initial growth phase, therefore market share is relatively very small (less than ~5%).

Revenues The Company has successfully regained its business position which it originally had. In the Year CY16 and CY17, the company scaled up its operations. In CY18, the company achieved a total husking of 34,540 tons of paddy (CY17: 19,978 tons) and processed 21,430 tons of rice (CY17: 25,263 tons). It exported 18,105 tons of rice in CY18 (CY17: 11,950 tons). ~94% of the rice exports are to the European Market, an edge of selling high priced basmati rice. In CY18, topline clocked in at PKR~2.5mln which is an increase of ~45% YoY while for 3MCY19 it stood at PKR~760mln. The company is expected to surpass the PKR~3bln mark in the going year.

Margins The company managed to regain its profitability margins in CY18 after enduring losses for three consecutive years. Engro Eximp posted a net profit of PKR~333mln in CY18 (3MCY19: 6mln), which is largely contributed by the reversal of impairment (PKR ~314mln). Previously, the company suffered losses, as the business fundamentals were being scaled, with a recorded post-tax loss of PKR~281mln in CY17 and PKR~475mln loss in CY16. Sustainable profit yield is pivotal for the company.

Sustainability As the business turned around to stable financial results in CY18, it is now expected to explore new business attributes. The company plans on exporting non-basmati rice as part of its pilot project which is expected to generate inflows of PKR~55mln. With an idea of diversification, the company also plans to test export trade of fruits.

Financial Risk

Working Capital Working capital needs are derived from receivables and inventory days. Cash conversion cycle is linked to the rice seasonality element. In CY18, net working capital days stood at ~232 days which are on the higher side of the industry average (CY17:~213 days). The increase is because of elevated inventory levels; 3MCY19: PKR~1,549mln (CY18: PKR ~1,729mln, CY17: PKR~1,369mln). Funding needs are mainly fulfilled through short term borrowings: 3MCY19: PKR~1,849mln, (CY18: PKR~1,873mln, CY17: PKR~1,612mln).

Coverages The return of profits enabled the company to produce positive FCFO of PKR~250mln during CY18 (3MCY19: PKR ~71mln) as against previous years of negative FCFO (CY17: PKR -210mln, CY16: PKR -353mln). As a result, coverages observed a sign of relief (Interest coverage: (3MCY19; ~1.6x, CY18: ~2.3x, CY17:` (3.7x).

Capitalization Engro Eximp's capital structure is dominated by short term borrowing and equity. The company's debt to equity ratio remained on higher end: CY18: ~62% (CY17:~66%) as the company's equity is undermined due to previous years loss adjustments.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Engro Eximp Agriproducts (Pvt.) Limited	Mar-19	Dec-18	Dec-17	Dec-16
Rice	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	1,220	1,226	874	936
2 Investments	-	-	-	-
3 Related Party Exposure	3	3	9	52
4 Current Assets	2,271	2,151	1,958	897
a Inventories	*1,549*	*1,729*	*1,369*	*500*
b Trade Receivables	*289*	*10*	*118*	*7*
5 Total Assets	3,494	3,380	2,841	1,885
6 Current Liabilities	308	176	230	229
a Trade Payables	*111*	*61*	*50*	*81*
7 Borrowings	1,849	1,873	1,612	377
8 Related Party Exposure	100	100	100	100
9 Non-Current Liabilities	-	-	-	1
10 Net Assets	1,237	1,231	898	1,179
11 Shareholders' Equity	1,237	1,231	898	1,179
B INCOME STATEMENT				
1 Sales	760	2,538	1,749	918
a Cost of Good Sold	*(663)*	*(2,268)*	*(1,840)*	*(1,149)*
2 Gross Profit	98	270	(90)	(231)
a Operating Expenses	(40)	(155)	(158)	(173)
3 Operating Profit	57	115	(248)	(404)
a Non Operating Income	*3*	*358*	*39*	*6*
4 Profit or (Loss) before Interest and Tax	60	473	(209)	(398)
a Total Finance Cost	*(47)*	*(116)*	*(57)*	*(75)*
b Taxation	*(7)*	*(23)*	*(15)*	*(7)*
6 Net Income Or (Loss)	6	333	(281)	(479)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*71*	*250*	*(210)*	*(353)*
b Net Cash from Operating Activities before Working Capital Changes	*38*	*151*	*(258)*	*(448)*
c Changes in Working Capital	*11*	*(329)*	*(980)*	*319*
1 Net Cash provided by Operating Activities	49	(178)	(1,238)	(129)
2 Net Cash (Used in) or Available From Investing Activities	(13)	(112)	15	12
3 Net Cash (Used in) or Available From Financing Activities	-	-	-	(443)
4 Net Cash generated or (Used) during the period	36	(291)	(1,224)	(560)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	19.8%	45.1%	90.5%	-51.2%
b Gross Profit Margin	12.8%	10.6%	-5.2%	-25.2%
c Net Profit Margin	0.8%	13.1%	-16.0%	-52.2%
d Cash Conversion Efficiency (EBITDA/Sales)	10.3%	8.4%	-11.2%	-34.4%
e Return on Equity (ROE)	2.0%	31.3%	-27.0%	-39.0%
2 Working Capital Management				
a Gross Working Capital (Average Days)	215	232	214	330
b Net Working Capital (Average Days)	204	224	200	296
c Current Ratio (Total Current Assets/Total Current Liabilities)	7.4	12.2	8.5	4.2
3 Coverages				
a EBITDA / Finance Cost	1.8	2.0	-3.6	-4.7
b FCFO / Finance Cost+CMLTB+Excess STB	1.6	2.3	-3.8	-5.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.9	0.7	-0.4	-0.2
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	61.2%	61.6%	65.6%	28.8%
b Interest or Markup Payable (Days)	0.9	0.9	0.9	0.8
c Average Borrowing Rate	8.9%	5.9%	5.0%	7.5%

Rating Scale

Credit Rating Scale & Definitions

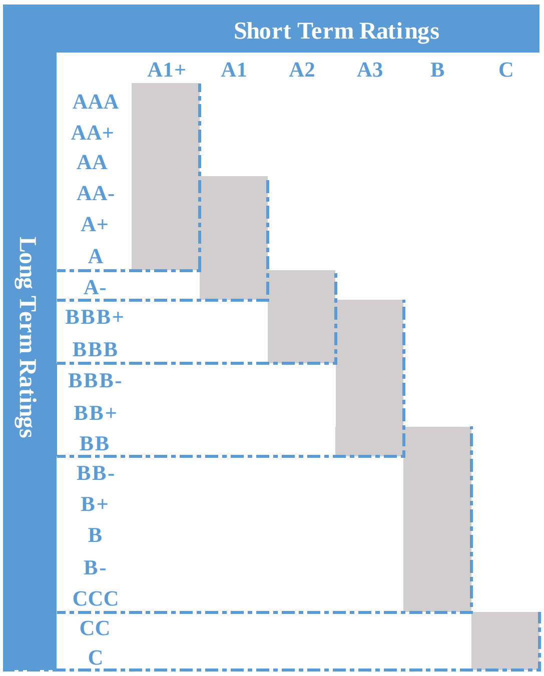
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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 Ratings

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.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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 surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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