



The Pakistan Credit Rating Agency Limited

Rating Report

K.K. Rice Mills (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
01-Mar-2019	BB+	A3	Stable	Upgrade	-
27-Dec-2018	BB	B	Stable	Maintain	-
28-Jun-2018	BB	B	Stable	Maintain	-
08-Jan-2018	BB	B	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings capture the fresh injection of PKR ~ 175mln in the company as subordinated loan. The sponsor have expressed undertaking to keep the amount as such or convert it into paid-up capital. The ratings incorporate the improving market positioning of the company, also reflected from the recent reported numbers. In line with the industry, KK Rice Mills also benefited from the improved performance of country's rice segment attributed by ban of Indian Rice that eventually helped rice players improve their margins. KK Rice Mills has adopted a top-line centric approach targeting Middle East and the African region. The company is going through business expansion and the management expects to generate the maximum fruit of the expansion. Henceforth, another expansion comes into play as Company's new plant is expected to be operational by March'19. Timely promotion of the product at the right price is essential. Compared to establish corporate, the board oversight and control environment are desirous of further improvement.

The ratings are dependent upon the maintained business volume and profitability. Adherence to sound financial discipline while debt servicing capacity through cash position is vital for the ratings

Disclosure

Name of Rated Entity	K.K. Rice Mills (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 Rice(Dec-18)
Rating Analysts	Raniya Tanawar raniya.tanawar@pacra.com +92-42-35869504

Profile

Legal Structure KK Rice Mills (Pvt.) Ltd, incorporated in 2009, is a privately owned unlisted company.

Background Formerly, before the incorporation of KK Rice (pvt) ltd, the operations were carried as a sole proprietor under the name of KK Commodities. KK Rice Mills Pvt Ltd received a license to export from Rice Export Association (REAP) in September 2009.

Operations KK Rice Mills has two manufacturing plants located at two different locations, in Karachi and Hyderabad. The plant in Karachi is located at Port Qasim whereas the plant in Hyderabad is located at Nooriabad. The two manufacturing plants at Port Qasim and Port Nooriabad have their own respective production capacities. The plant located at Port Qasim has two specialized equipment's, i) Muyang Plant and ii) Buhler Plant each having the production capacity of 131,000 tons. Company also has machinery for Boiling, Husking and Silking are installed at Nooriabad.

Ownership

Ownership Structure The majority shareholding of the company is held by Mr. Chela Ram, 60% holding whereas the remaining is equally shared among the executive directors. One of them being an active and the other passive.

Stability Dealing in a commodity that has growing demand, 'non-basmati rice', ensures company's long existence in the market as one of the top players.

Business Acumen Mr. Chela Ram, - is the man at the last mile and Ms Kami Bai is his wife. Mr. Dileep Kumar is the nephew of Mr. Chela Ram. He comes from an entrepreneurial background, his family has been in commodity trading since last three generations and are well known veterans in trading of rice, wheat and sugar.

Financial Strength Strong presence in the market and sponsors backing has paved ways for the company to sustain financially sound. The company's Director Mr. Chela Ram has recently injected PKR 175mln subordinated loan which is intended to be converted into equity.

Governance

Board Structure The board consists of three members, all three of them being director shareholders. Ms Khami Bai is a passive director.

Members' Profile Mr. Chela Ram Kewlani, CEO KK Rice, is a B.A. qualified experienced professional, who has been with the company since its inception. He was the Chairman of Pakistan Hindu Council from 2014-2016 and has also served as the Senior Vice Chairman of Rice Export Association of Pakistan.

Board Effectiveness The board meeting takes place twice a year, once before and once after the audit is performed. The meeting is minute by the HR and Admin Manager, Ms. Sadaf Ahmer. Absence of independent director posts lack of governance.

Financial Transparency S.M Rehan & Co. Chartered Accountants are the auditors for the KK Rice Mills (Pvt.) Ltd. Neither the audit firm doesn't satisfy the QCR ratings nor does it is classified in any of the categories defined by the State Bank of Pakistan. The auditors issued an unqualified opinion on the company's financial statements for the year ended June 30, 2018.

Management

Organizational Structure KK Rice has defined business structure and thorough line of management. All head of the department's report to CEO.

Management Team The management team comprises of six members, including the CFO - Dileep Kumar. Mr. Dileep Kumar is a rice specialist and has been associated with the company for more than two decades. The Company also has a Director Finance, Mr. Tulsi Das Kewlani, who was responsible for overseeing the local business matters but now he has been transferred to Benin to cope with financial issues.

Effectiveness Other senior management personnel with exception to a couple of directors (Director International Business and Director Finance) have significant professional experience. Management meetings take place on half yearly basis.

MIS The Company has an ERP system in place at the Head Office and in the factories. The existing in-house ERP solution is Oracle Financial having four modules i)Accounts Payable ii) Accounts Receivable iii) General Ledger iv) Supply Chain Management.

Control Environment KK Rice has no committee to oversee and monitor the corporate governance rules and regulations, posing concerns over the internal controls of the company.

Business Risk

Industry Dynamics Pakistan's Rice industry continue to be instrumental for the Agriculture sector of the country. However, the total contribution to the GDP is meagre clocking in at 0.6%. There are around 150 silky plants and more than 1500 husking plants. Only one company named MATCO is listed in the Pakistan Stock Exchange. The Rice cultivation area is 2.9 million hectares. Production of rice is ~7 million Tons and the consumption is ~3 million Tons. The maximum contribution from the Rice sector in country's foreign exchequer is from non-basmati rice exports: marked USD 2bln in FY18.

Relative Position The Company's business mainly involves exporting non-basmati rice. KK Rice is named among the leading exporters of non-basmati rice in the country. The company has a major customer base in Afro-Asian countries, with the top consumers being from Africa, Kenya, U.A.E, China and Indonesia.

Revenues As the company's export volume base increased from 140,000 metric tons to 170,000 metric tons. Company's revenue base witnessed a hike, due to international tenders, by ~39.6% YoY clocking in at PKR ~7.3bln during FY18 (FY17: PKR ~5bln), while for the 1HFY19 revenue stood at PKR ~3bln. Indonesia was the major contributor. The company's local sales were almost 0% to 1% of the total revenue in the previous three years.

Margins Company's overall margins observed improving trend; Gross margin for 1HFY19 was ~13% (FY17: ~7.8%, FY16: ~8%). The net profit for the year ended FY18 was PKR ~34mln as compared to PKR 22mln in FY17 which is 55% higher. This was mainly on account of higher revenue base in FY18 as compared to the prior years. As a result of intact operational efficacy throughout the years; cost of sales to sales ratio remained constant till FY18, during FY19 the company managed to earn its highest profits surging to PKR ~154mln on account of backward integration and cost rationalization.

Sustainability Going forward, the management eyes to acquire further market share by effective utilization of the resources and through business expansion strategies leading to a competitive edge over others. Another expansion comes in to play as Company's new plant is expected to be operational by mid-2019.

Financial Risk

Working Capital The company finances its working capital through the export refinance facility-ERF. The total approved facility is of PKR 3bln, pledged against inventory and fixed assets at a policy of at least 25% of sales in stock, out of which only PKR 250mln is unutilized, as to date. In anticipation to the future demand and sale prospects, the company's stock level have raised to 109days in 1HFY19, hence leading the working capital cycle to a higher end; ~144days (FY18: 71days, FY17: 71days, CY16: 57days). The entire working capital management is heavily supported by short term borrowings 1HFY19: ~3bln (FY18: PKR ~ 2.1bln, FY17: ~1.2bln), which comprises export refinance facility.

Coverages KK Rice enjoys an improving FCFO over the years; PKR ~125mln in FY18 as against PKR ~91mln in FY17 (1HFY19: PKR ~215mln). The increase is on account of increased profitability. After a constant pace of improved coverages in the past years ruling out interest repayment issue (FY17: 3.4x, FY16: 3.1x), K.K. Rice Mills observed a drop in its coverage (FY18: 2.8x) due to increased short term borrowings, however it improved significantly during 1HFY19 to ~5.7times.

Capitalization K.K. Rice Mills (Pvt.) Ltd capital structure comprises of short term debt and equity. Previously, the company had a long term debt representing a finance lease of vehicles, which matured during FY18. The Company also paid off the loan of PKR ~18mln during FY18, which was an unsecured loan from the director. The company long term borrowings have increased to PKR ~341mln in 1HFY19. These include PKR ~175mln injected by the sponsor Mr. Chela Ram and PKR ~101mln subsidized loan availed from JS Bank at the rate of 6% for a period of 5 Years



KK RICE Mills(Pvt.) Limited

BALANCE SHEET	31-Dec-18	30-Jun-18	30-Jun-17	30-Jun-16
	6M	Annual	Annual	Annual
Non-Current Assets	844	647	356	259
Investments (Incl. associates)	-	-	-	-
Equity	-	-	-	-
Debt	-	-	-	-
Investment property	-	-	-	-
Current Assets	3,348	2,443	1,552	1,228
Inventory	2,088	1,622	917	621
Trade Receivables	1,173	517	271	415
Others	87	304	1,257	192
Total Assets	4,191	3,091	1,908	1,487
Debt	3,421	2,213	1,289	973
Short-term	3,081	2,151	1,210	871
Long-term (Incl. Current Maturity of long-term debt)	341	61	79	102
Other shortterm liabilities	254	518	291	210
Other Longterm Liabilities	-	-	-	-
Shareholder's Equity	516	362	327	305
Total Liabilities & Equity	4,191	3,091	1,908	1,487

INCOME STATEMENT

Turnover	3,114	7,244	5,190	6,278
Gross Profit	413	566	415	517
Net Other Income	(7)	(11)	(8)	(11)
Financial Charges	(41)	(71)	(42)	(69)
Net Income	154	34	22	40

Cashflow Statement

Free Cashflow from Operations (FCFO)	215	125	91	154
Net Cash changes in Working Capital	(1,267)	(728)	(88)	(114)
Net Cash from Operating Activities	(1,052)	(668)	(43)	(32)
Net Cash from Investing Activities	(209)	(315)	(123)	(18)
Net Cash from Financing Activities	1,160	922	318	79

Ratio Analysis

Performance				
Turnover Growth	-41.2%	39.6%	-17.3%	19.5%
Gross Margin	13.2%	7.8%	8.0%	8.2%
Net Margin	5.0%	0.5%	0.4%	0.6%
ROE	59.8%	16.6%	13.7%	14.7%
Coverages				
Interest Coverage (FCFO/Gross Interest)	5.3	1.8	2.1	2.2
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	5.3	0.7	2.1	0.1
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	5.3	0.7	2.1	0.1
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest)	1.0	2.7	1.7	21.7
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	143.9	70.9	71.0	57
Capital Structure (Total Debt/Total Debt+Equity)	86.9%	86.0%	79.8%	100.0%

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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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

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- (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)
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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)
- (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)

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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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