



The Pakistan Credit Rating Agency Limited

Rating Report

Sadiq Feeds (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
20-Mar-2019	BBB+	A2	Stable	Maintain	-
18-Sep-2018	BBB+	A2	Stable	Maintain	-
22-Mar-2018	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Poultry feed manufacturing formally started in Pakistan in early 1960's. Poultry feed is produced by commercial feed mills and home mixtures. There are ~ 350 poultry feed mills, with annual production capacity of around 10 MMT. Income levels and expanding population, pushes demand for poultry however, higher conversion ratio, volumetric growth has stagnated to an extent. However, this remains a competitive business where volumes and margins are function of timeliness and cost of raw material procurement and supply competition amongst different feed mills.

The ratings reflect Sadiq Feeds association with an established poultry group, named Sadiq Group. The Company is part of the Group's integrated poultry chain – oil/meal, feed and poultry. Topline is concentrated towards broiler feed and major sale to group's own companies. Moreover, procuring maize in bulk due to seasonal constraints, highlights inherent price risk of raw material along with storage issues and high holding period. Margins remain thin with modest profitability. The Company's financial risk profile is characterized by high leverage mainly for working capital requirements, and modest coverages. To manage this, management is working to a) gradually reduce short term borrowings and b) reprofile its debt mix with some switch towards long-term borrowings. This, along with better cashflows, is expected to manage financial risk.

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. Envisaged improvement in business and financial profile along with effective changes in governance framework would be beneficial. Significant deterioration in coverages or margins impact the ratings.

Disclosure

Name of Rated Entity	Sadiq Feeds (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 Poultry Feed(Mar-19)
Rating Analysts	Adnan Dilawar adnan@pacra.com +92-42-35869504



Profile

Legal Structure Sadiq Feeds (Pvt.) Ltd. was incorporated on July 07, 2005, as a Private Limited Company.

Background Sadiq 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.

Operations Sadiq Feeds produces three different type of feeds namely; i) poultry feed, ii) strain specific layer feed and iii) cattle feed for birds and livestock of different types and age groups. The Company has two feed mills situated in Mandra and Sahiwal, with a production capacity of 70MT per hour and 130 MT per hour, respectively.

Ownership

Ownership Structure Sadiq Feeds major shareholding vests with Dr. Muhammad Sadiq (70%); followed by his two sons, Mr. Asif Zubair (15%) and Mr. Salman Sadiq (15%). While ownership is not expected to change, the Company is in the process of re-structuring assets in it's Group among associated entities.

Stability Ownership of the business is seen as stable as the major ownership vests with Dr. M. Sadiq. While ownership is not expected to change, the Company is in the process of re-structuring assets in it's Group among associated entities.

Business Acumen Sadiq Group has experienced multiple business cycles, maintaining 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 Sadiq Group. All are operating in various segments.

Financial Strength Sadiq Group has consolidated asset base of ~PKR 35bln supported by an equity of the ~PKR 10.5bln as at end Jun' 2018. Through its diverse set of businesses, it has generating a turnover of ~PKR 43bln and a pre-tax bottom line of ~PKR 948mln in FY18.

Governance

Board Structure Sadiq Feeds 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 FY18, four Board meetings, with full/majority attendance, were held to discuss pertinent matters and make strategic decisions.

Financial Transparency Sadiq Feeds external auditors, Muniff Ziauddin and Co Chartered Accountants, have expressed an unqualified opinion on the financial reports for FY18. 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 Feeds 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.

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 Feeds, internal audit department has been established at group level to ensure internal controls. The Company's both feed mills are fully automated.

Business Risk

Industry Dynamics Poultry feed manufacturing formally started in Pakistan in early 1960's. Poultry feed is produced by commercial feed mills and home mixtures. There are ~ 350 poultry feed mills, with annual production capacity of around 10 MMT. Income levels and expanding population, pushes demand for poultry however, higher conversion ratio, volumetric growth has stagnated to an extent.

Relative Position Sadiq Feeds is among the market leaders in Pakistan's poultry feed industry, with a market share of 15% approximately. Out of Punjab's annual feed production of 7.6 MMT, Sadiq Feeds alone produces 1.7 MMT of poultry feed.

Revenues Sadiq Feeds sales mix comprises broiler feed, breeder feed and layer feed. Moreover, ~ 25 – 30% revenue comes from Group Companies (which includes Sadiq Poultry, Sadiq Poultry Farms, Salman Poultry, Zubair Poultry) providing a captive market. Revenue clocked in at PKR 12.7bln for 1HFY19 (PKR 10.2 in 1HFY18). The increase in revenue is attributable to increase in prices and a relatively higher off-take.

Margins Gross and Operating margins remained stable during 1HFY19 at ~7% and ~5%, respectively despite the increase imported raw material cost due to rupee depreciation. The stability is on account of timely increase in feed prices, transferring costs to customers. Consistent borrowings to meet maize & other raw material procurement needs, kept the finance costs high ~ PKR 853mln in FY18. Net profit margins, although thin, showed a marginal improvement from .5% in FY18 to .9% in 1HFY19.

Sustainability Going forward, Sadiq Feeds aims to fully utilize its production capacity while keeping the costs under control. No Capacity enhancements is on the cards in the near future.

Financial Risk

Working Capital Sadiq Feeds has a high networking capital days (186 days in 1HFY19). High Working capital days emanat predominantly from high raw material inventory days (maize) that is procured seasonally. Sales are mostly on credit basis, with an average debtor days of 58 days in 1HFY19 (FY18: 52days). Owing to high reliance on external finance for working capital needs, the Company has little cushion with a short-term total leverage of 11%.

Coverages Interest coverages and core coverages improved to 1.6x and 1.2x in 1HFY19 from 1.5x and 1x in FY18 despite the increase in financial costs on the back of improved FCFO. Although improvement is witnessed, the Coverages remain modest.

Capitalization The Company has a highly leveraged capital structure. Total debt comprises 93% short term borrowings and 7% long term borrowings. Current business activity levels and need for credit facility has kept the leverage on the higher side (1HFY19: 75%). Current maturities are expected to be settled through internal cashflows.



Sadiq Feeds (Pvt.) Limited

Private Limited

BALANCE SHEET

	Dec-18 6M	Jun-18 12M	Jun-17 12M	Jun-16 12M
Non-Current Assets	1,546	1,583	1,635	1,764
Investments (Incl. Associates)	-	-	-	-
Equity	-	-	-	-
Fixed Income	-	-	-	-
Current Assets	14,708	14,231	13,561	15,038
Inventory	9,985	8,754	10,862	12,312
Trade Receivables	3,700	4,421	1,629	1,884
Others	1,023	1,056	1,070	842
Total Assets	16,254	15,814	15,196	16,802
Debt/Borrowings	10,594	10,391	10,109	12,258
Short-Term	9,834	9,455	8,943	10,963
Long-Term (Incl. Current Maturity of Long-Term Debt)	760	936	1,166	1,295
Other Short-Term Liabilities	2,071	1,950	1,716	1,218
Other Long-Term Liabilities	-	-	-	34
Shareholder's Equity	3,589	3,473	3,371	3,292
Total Liabilities & Equity	16,254	15,814	15,196	16,802

INCOME STATEMENT

Turnover	12,704	21,404	17,913	20,364
Gross Profit	856	1,462	1,273	1,316
Net Other Income	(11)	(17)	(8)	(14)
Financial Charges	(473)	(855)	(856)	(849)
Net Income	114	102	79	123

CASH FLOW STATEMENT

Free Cash Flow from Operations (FCFO)	728	1,169	994	921
Total Cashflows (TCF)	728	1,169	994	921
Net Cash changes in Working Capital	(399)	(406)	2,137	(3,155)
Net Cash from Operating Activities	(97)	(90)	2,284	(3,131)
Net Cash from Investing Activities	(52)	(69)	(56)	(127)
Net Cash from Financing Activities	204	220	(2,279)	3,351
Net Cash generated during the period	54	61	(50)	93

RATIO ANALYSIS

Performance

Turnover Growth (vs SPLY)	24%	19%	-12%	-10%
Gross Margin	7%	7%	7%	6%
Net Margin	1%	0%	0%	1%
ROE	6%	3%	2%	4%

Coverages

Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.2	1.0	0.8	0.9
Interest Coverage (X) (FCFO/Gross Interest)	1.5	1.4	1.2	1.1

Capital Structure (Total Debt/Total Debt+Equity)

Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	186	204	250	209
Capital Structure (Total Debt/Total Debt+Equity)	75%	74%	75%	79%

Sadiq Feeds (Pvt.) Limited

Feb-19

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.
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- (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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