



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
21-Jan-2020	BBB+	A2	Stable	Maintain	-
22-Jul-2019	BBB+	A2	Stable	Maintain	-
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

Among the largest agro based segments in Pakistan, poultry holds a prominent place. Poultry feed manufacturing formally started in Pakistan in the early 1960's as home mixtures as well as in commercial feed mills. Today, there are around ~ 350 feed mills, with annual production capacity of around 8 MMT. Increase in income levels and expanding population, pushes demand for poultry. However, higher conversion ratio has stagnated volumetric growth. This remains a competitive business where volumes and margins are function of timeliness and cost of procuring raw material along with favorable supply chain dynamics of various feed mills. The industry has inherent risk of disease and mortality, which could lead to delinquencies by buyers.

The ratings reflect Sadiq Feeds association with an established poultry group, 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 sales to group companies. Moreover, procuring raw material in bulk due to seasonal constraints, highlights inherent price risk along with storage issues and high holding period. The company has adequate business margins, in line with peers and modest profitability. The Company's financial risk profile is characterized by modest coverages. However, leveraging remains high, mainly on account of working capital requirements. In high interest rate scenario, this exerts pressure on the financial profile of the Company. The management is working on a gradual reduction in the short term borrowings by re-profiling the debt mix. This, along with better cash flows, is expected to improve coverages.

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 will have negative impact on 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-19),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria Rating Modifier(Jun-19)
Related Research	Sector Study Poultry Feed(Jan-20)
Rating Analysts	Faiqa Qamar faiqa.qamar@pacra.com +92-42-35869504

Profile

Legal Structure Sadiq Feeds (Pvt.) Ltd. (Sadiq Feed or 'the Company') 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. In FY19, utilization level improved to 36% on the back of increased demand from Group's companies.

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 sponsors have re-structured assets in it's Group among associated entities in FY19.

Stability Ownership of the business is seen as stable as the major ownership vests with Dr. M. Sadiq. Group assets have been distributed among two sons of Dr. Sadiq.

Business Acumen Sadiq Group has experienced multiple business cycles, showing strong business acumen of sponsors. The Group's broiler farms are among the highest chick producers in Pakistan. Currently, there are seven companies, one AoP and one trust working under Sadiq Group. All are operating in various segments.

Financial Strength Sadiq Group has consolidated asset base of ~ PKR 43bln supported by an equity of ~ PKR 12bln as at end Jun'19. Through its diverse set of businesses, it has generating a turnover of ~ PKR 50bln.

Governance

Board Structure Sadiq Feeds Board, comprising three members, is dominated by the sponsoring family. The Company's Board lacks independence, indicating room for improvement in 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 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 FY19, four Board meetings, with full 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 FY19. The firm has been QCR rated by ICAP and is 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 by Sidat Hyder, are used at the Group level. However, for internal dissemination, information is documented as and 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. At present, poultry feed is produced by commercial feed mills as well as home mixtures. There are 350 poultry feed mills, making country's annual production capacity of around 8 MMT. The industry directly drives its demand from poultry – chicken and eggs consumption. With growing income levels and expanding population, the demand for poultry is expected to grow modestly. The industry is experiencing ~4 to 5% growth.

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 1.6 MMT of poultry feed.

Revenues Sadiq Feeds sales mix comprises broiler feed, breeder feed and layer feed. Moreover, ~ 20 – 25% revenue comes from Group Companies (which includes Sadiq Poultry, Sadiq Poultry Farms, Salman Poultry, Zubair Feeds) providing a captive market. During FY19, the Company's revenue posted an increase of 15% (FY19: PKR 25 bln, FY18: PKR 21 bln) The increase in revenue is attributable to increase in prices and a relatively higher off-take. Revenue clocked in at PKR 6.8 bln during 3MFY20 (3MFY19: 6bln) showing an increase of 11.5%

Margins Gross margins improved during FY19, to 7.3% from 6.8% in FY18 (3MFY20 ~ 7.5%, 3MFY19 ~ 6.7%), despite the increase in imported raw material cost due to rupee depreciation. The improvement in margins is on account of transferring costs to customers in a timely manner. Operating margins improved as the company was fairly able to cut its operating costs (FY19: 5.5%, FY18: 5.2%, 3MFY20: 5.6%, 3MFY19: 5%). Consistent borrowings to meet maize & other raw material procurement needs, kept the finance costs high. Net profit margins, although thin, showed improvement from 0.5% in FY18 to 0.7% in FY19. (3MFY19: 0.8%, 3MFY20: 1.7%). The Company posted net income of PKR 162mln in FY19 (FY18: PKR 102mln). The profitability stood at PKR 115mln in the 3MFY20 (3MFY19: PKR 48mln).

Sustainability Going forward, Sadiq Feeds aims to better 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 high net working capital days, emanating predominantly from high raw material inventory days (maize) as it is procured seasonally (FY19: 185 days, FY18: 195days, 3MFY20 :172days, 3MFY19: 183days). Sales are mostly on credit basis, with an average debtor days of 67 days in FY19 (FY18: 42days). Owing to high reliance on external finance for working capital needs, the Company has little cushion at trade level. the rising trade receivables exposes the Company to default by customers. However, sales to group companies provide comfort to an extent.

Coverages During FY19, interest coverage dropped due to increase in finance costs (FY19: 1.2x, FY18: 1.5x). Total and core coverage reduced to 1x in FY19 from 1.1x in FY18. During 3MFY20, interest cover remained stable (3MFY20: 1.4x, 3MFY19: 1.4x) . An improved free cash flow from operations led to better Core and Total coverage (3MFY20: 1.2x, 3MFY19: 1x). The Company's coverage ratios remain modest though.

Capitalization Sadiq Feeds has a highly leveraged capital structure. Total debt comprises 94% short term borrowings and 6% long term borrowings in FY19. Current business activity levels and need for credit facility has kept the leverage on the higher side. Current maturities are expected be settled through internal cash flows.



The Pakistan Credit Rating Agency Limited

Financial Summary

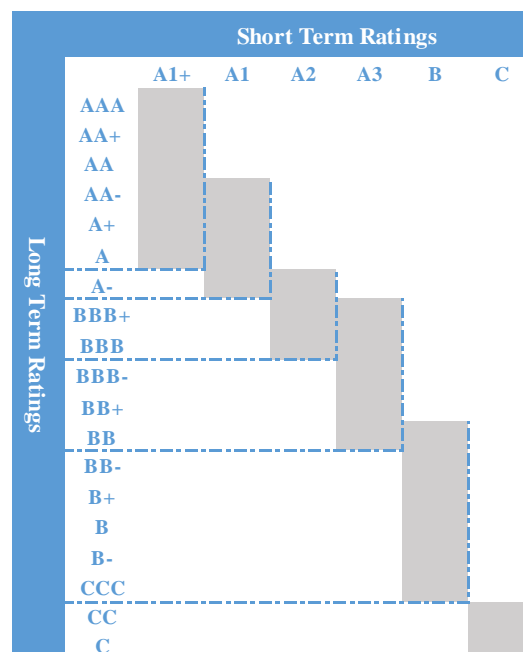
PKR mln

Sadiq Feeds Private Limited Food and Allied	Sep-19 3M	Jun-19 12M	Jun-18 12M	Jun-17 12M
A BALANCE SHEET				
1 Non-Current Assets	1,628	1,650	1,583	1,635
2 Investments	5	5	-	-
3 Related Party Exposure	-	-	-	9
4 Current Assets	16,864	17,191	14,231	13,552
a Inventories	10,540	10,576	8,754	10,862
b Trade Receivables	5,204	5,514	3,587	1,389
5 Total Assets	18,497	18,846	15,814	15,196
6 Current Liabilities	4,341	4,194	1,950	1,716
a Trade Payables	3,036	2,903	469	1,248
7 Borrowings	10,407	11,009	10,391	10,109
8 Related Party Exposure	-	9	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	3,749	3,634	3,473	3,371
11 Shareholders' Equity	3,749	3,634	3,473	3,371
B INCOME STATEMENT				
1 Sales	6,876	24,674	21,404	17,913
a Cost of Good Sold	(6,362)	(22,861)	(19,942)	(16,640)
2 Gross Profit	514	1,812	1,462	1,273
a Operating Expenses	(125)	(468)	(356)	(288)
3 Operating Profit	388	1,345	1,106	985
a Non Operating Income or (Expense)	111	110	(17)	(8)
4 Profit or (Loss) before Interest and Tax	499	1,455	1,088	977
a Total Finance Cost	(385)	(1,190)	(855)	(856)
b Taxation	-	(103)	(132)	(42)
6 Net Income Or (Loss)	115	162	102	79
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	533	1,419	1,169	994
b Net Cash from Operating Activities before Working Capital Changes	197	390	316	147
c Changes in Working Capital	429	(716)	(406)	2,137
1 Net Cash provided by Operating Activities	626	(326)	(90)	2,284
2 Net Cash (Used in) or Available From Investing Activities	(32)	(264)	(69)	(56)
3 Net Cash (Used in) or Available From Financing Activities	(602)	611	220	(2,279)
4 Net Cash generated or (Used) during the period	(8)	21	61	(50)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	11.5%	15.3%	19.5%	-12.0%
b Gross Profit Margin	7.5%	7.3%	6.8%	7.1%
c Net Profit Margin	1.7%	0.7%	0.5%	0.4%
d Cash Conversion Efficiency (EBITDA/Sales)	8.2%	6.4%	6.0%	6.6%
e Return on Equity (ROE)	12.4%	4.6%	3.0%	2.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	211	210	210	266
b Net Working Capital (Average Days)	172	185	195	245
c Current Ratio (Total Current Assets/Total Current Liabilities)	3.9	4.1	7.3	7.9
3 Coverages				
a EBITDA / Finance Cost	1.5	1.4	1.7	1.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.2	1.0	1.1	0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.9	2.3	2.3	4.6
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	73.5%	75.2%	75.0%	75.0%
b Interest or Markup Payable (Days)	89.6	103.6	78.9	79.5
c Average Borrowing Rate	14.2%	10.7%	7.4%	6.6%

Credit Rating Scale & Definitions

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

Long Term Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
AA+	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.	A1	A strong capacity for timely repayment.
AA		A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
AA-		A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A+	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
A		C	An inadequate capacity to ensure timely repayment.
A-			
BBB+	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.		
BBB			
BBB-			
BB+	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.		
BB			
BB-			
B+	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.		
B			
B-			
CCC	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.		
CC			
C			
D	Obligations are currently in default.		



Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.	Rating Watch Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.	Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.	Withdrawn A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.	Harmonization A change in rating due to revision in applicable methodology or underlying scale.
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(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)

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- 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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- (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)
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- (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)
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- (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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