The Pakistan Credit Rating Agency Limited

Rating Report

Reliance International Commodities Export

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
20-Aug-2019	BB	B	Stable	Maintain	-
18-Feb-2019	BB	B	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect the emergence of the Reliance International Commodity Exports ("Reliance") as a growing IRRI rice exporter. In line with the overall industry changing the trend, Reliance has shifted its export sales mix from China to African countries in the recent past. This has not only reaped better top-line growth but enlarged its cash conversion cycle. Reliance has marked its presence in African regions through two distribution entities. The company is committed to increasing its foreign footing. Presence in the local market remains indifferent. Profitability margins, that have a perceptible impact on the ratings, are low as compared to peers. The company's topline and profitability is expected to be sanguine, as also expected from the reported financial statements. Reliance's debt book solely comprises Export Refinancing Facility availed to fund its working capital needs. During FY19, rice crop area stood at 2.8 million hectares. The production stood at 7.2 million tonnes as against 7.5 million tonnes last year, short by ~3.3%. During FY19, Pakistan exported a total of 4.097 million metric tons of rice compared to some 4.082 million metric tons in the corresponding period of FY18.

The ratings are dependent on Reliance's ability to sustain business profile and yield better profit margins. Meanwhile, prudent working capital management is imperative.

Disclosure	
Name of Rated Entity	Reliance International Commodities Export
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Crtieria_LT ST Relationship_FY19(Jun-19)
Related Research	Sector Study | Rice(Dec-18)
Rating Analysts	Muhammad Usman | muhammad.usman@pacra.com | +92-42-35869504

Profile

Legal Structure The Reliance International Commodity Exports (Reliance) is a sole proprietorship.

Background Mr. Gada Hussain Mahesar started the business in 1958. As the business grew over the period, Mr. Gada Hussain established second rice husking plant in 1977 and the third in 1993. Reliance International Commodity Exports is run by his elder son, Mr. Arif Hussain.

Operations The primary business of Reliance is the processing and sale of rice. Reliance purchases both raw rice and paddy, and converts them into finished products at the rice mill in Karachi. Reliance's revenue comes from the export of rice to African countries and from local sales.

Ownership

Ownership Structure Reliance is a sole proprietorship, wholly owned by Mr. Arif Hussain.

Stability The ownership structure of Reliance is expected to remain the same for the forseeable period.

Business Acumen Mr. Arif Hussain has a strong understanding of the rice sector. He is running his business from the past two decades. Mr. Arif has served as the president of Sindh & Baluchistan Rice Millers Association from 2007-2010 and 2010-2013.

Financial Strength Reliance International Commodity is the main business of Mr. Arif. He owns all the assets of the proprietorship. Dependence of sponsor on one business reduces the owner's ability to support Reliance in time of need.

Governance

Board Structure As Reliance is a sole proprietorship managed by a single person, it does not have a formal board structure.

Members' Profile Mr. Arif is the only person responsible for the governance of Reliance.

Board Effectiveness Reliance does not have any board committees. Establishment of the board committees is essential for the improvement of the overall governance structure of Reliance.

Financial Transparency Reliance does not have an internal audit department in place. Reliance's external auditors, Sajid & Co, have expressed an unqualified opinion on the financial reports for FY19. The firm is not QCR rated by ICAP and do not have any listing in SBP panel. Financial transparency is considered weak due to the non-existence of the internal audit department and non-QCR rating of external auditors.

Management

Organizational Structure Both head office and the rice mill are located in Karachi. Managers at both locations are responsible for management of relevant affairs. Both mangers report to Mr. Arif Hussain.

Management Team Ms. Afshan Munir is a qualified and experienced professional with the experience of ~15 years. She is associated with the company for ~5 years. Mr. Fida Hussain is also a well experienced person. He is associated with Reliance for ~15 years.

Effectiveness Currently, Reliance does not have any formal management committees. All pertinent issues are resolved at department levels with the consent of the CEO.

MIS Reliance uses Tele ERP as its main software for preparation of financial accounts. Reliance needs to focus on deploying a software solution with a proper technology framework.

Control Environment The overall structure of Reliance is divided into two main departments - finance and rice mill. One individual at each site is responsible for the management of the operations. Strong counter check and supervision is needed to improve the overall control environment of Reliance.

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. During FY19, rice crop area decreased by ~3.1% to 2.8 million hectares as 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 a decrease in area cultivated. 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 Demand for rice in both local and international markets is expected to remain steady owing to the nature of the basic commodity. Reliance is a relatively small player in the rice industry. As Mr. Arif's family has been in the rice business for several years, The company's ability to manage its supply chain is good. Furthermore, Reliance is committed to increasing its international presence and the establishment of trading Reliance for the said purpose is a step in the right direction.

Revenues Reliance witnessed ~15% YoY growth in revenue during twelve months period ended Apr-19. Topline clocked in at PKR ~2,701 million (Apr-18: PKR ~2,346 million). Growth in revenue came on the backdrop of strong demand from African countries. Reliance sales mix comprises majorly IRRI-6 non-basmati rice.

Margins The company's gross margin slightly dropped in percentage terms - Apr-19: 3.8%, as compared to the corresponding period Apr-18: 4% - standing at PKR ~103mln (Apr-18: PKR ~94mln). Gross profit increased due to the increase in sales to African countries as they have more bargaining power compared to China. The net profit of the company reached PKR ~61mln at the end Apr-19 as compared to PKR ~53mln at end Apr-18.

Sustainability Reliance is committed to strengthening its distribution network in African markets. To achieve that, Reliance is planning to establish more distribution companies in Africa. Further, Reliance is keen to improve its overall organizational structure and is in the process of changing its legal structure from sole proprietorship to a private limited company.

Financial Risk

Working Capital The company maintains a strong position in working capital management. However, owing to high inventory levels and trade receivables, net working capital days remained elevated and stood at 112 days at end Apr-19 (Apr-18: 95 days). The increase is due to the inclination of Reliance's exports to African countries that have a larger cash conversion cycle as compared to the Chinese market.

Coverages Free cash flow from operations (FCFO) increased by PKR ~8 million during twelve months period, clocking in at PKR ~78 million (Apr-18: PKR ~70 million). The interest coverage ratio increased to 4.3x at end Apr-19 (Apr-18: 4x) despite the increase in gross interest expense which was recorded at PKR ~18.3mln during Apr-19 (Apr-18: PKR ~17.4mln).

Capitalization Reliance has ~75% leveraged capital structure. Total debt of Reliance at the end of Apr-19 clocked in at PKR~657 million as compared to PKR~698 million at the end of Apr-18. All liabilities are short term, particularly export refinances facility, to fund working capital needs.

The Pakistan Credit Rating Agency Limited

Reliance International Commodity Exports

PKR mln

BALANCE SHEET	Apr-19 12M	Apr-18 12M	Apr-17 12M	Apr-16 12M
Non-Current Assets	**30**	**29**	**31**	**33**
Investments (Incl. Associates)	-	-	-	-
Equity	-	-	-	-
Fixed Income	-	-	-	-
Current Assets	**854**	**943**	**414**	**250**
Inventory	513	91	259	185
Trade Receivables	299	752	122	55
Others	41	99	33	9
Total Assets	**884**	**972**	**445**	**283**
Debt/Borrowings	**657**	**698**	**312**	**175**
Short-Term	657	698	312	175
Long-Term (Incl. Current Maturity of Long-Term Debt)	-	-	-	-
Other Short-Term Liabilities	3	2	2	2
Other Long-Term Liabilities	-	-	-	-
Shareholder's Equity	**224**	**271**	**131**	**106**
Total Liabilities & Equity	**884**	**972**	**445**	**283**
INCOME STATEMENT				
Turnover	**2,701**	**2,346**	**2,133**	**2,015**
Gross Profit	103	94	75	67
Net Other Income	-	-	-	-
Financial Charges	(18)	(17)	(7)	(9)
Net Income	**61**	**53**	**47**	**39**
CASH FLOW STATEMENT				
Free Cash Flow from Operations (FCFO)	78	70	49	41
Total Cashflows (TCF)	78	70	49	41
Net Cash changes in Working Capital	(23)	(524)	(154)	(57)
Net Cash from Operating Activities	55	(455)	(105)	(16)
Net Cash from InvestingActivities	12	100	-	(10)
Net Cash from Financing Activities	(66)	358	115	28
Net Cash generated during the period	1	4	10	2
RATIO ANALYSIS				
Performance				
Turnover Growth (vs SPLY)	15%	10%	6%	-6%
Gross Margin	4%	4%	4%	3%
Net Margin	2%	2%	2%	2%
ROE	25%	26%	39%	37%
Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	4.3	4.0	6.5	4.7
Interest Coverage (X) (FCFO/Gross Interest)	4.3	4.0	6.5	4.7
Debt Payback (Years) (Total Debt (excluding Covered Short Term Borrowings) / FCFO)	11.1	13.3	7.5	5.4
Capital Structure (Total Debt/Total Debt+Equity)				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	112	95	53	43
Capital Structure (Total Debt/Total Debt+Equity)	75%	72%	70%	62%

Credit Rating Scale & Definitions

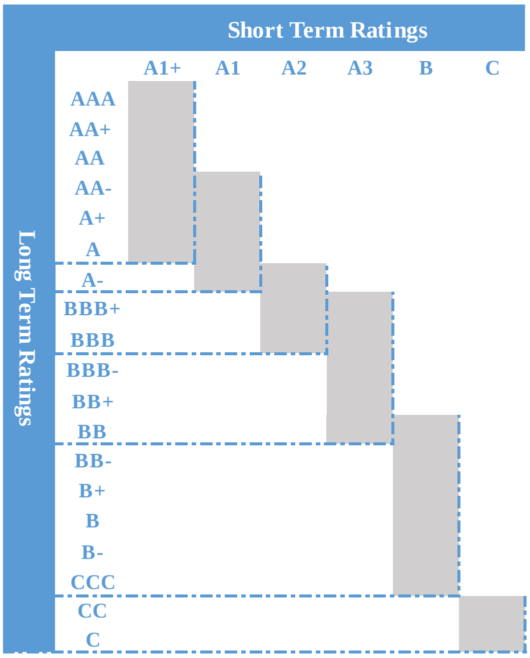
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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