



The Pakistan Credit Rating Agency Limited

## Rating Report

### Hi-Tech Feeds (Pvt.) Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
16-Jul-2020	BBB-	A3	Developing	Maintain	YES
17-Jul-2019	BBB-	A3	Stable	Maintain	-
15-Jan-2019	BBB-	A3	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

The global feed industry can be valued at around ~\$460bln, with poultry (~\$166bln) constituting ~36% of the total industry. Pakistan has an installed production capacity of ~ 8mln MT of poultry feed annually with a total of ~150 registered feed mills and ~200 unregistered feed mills catering to it. The industry generates an estimated annual revenue of ~ PKR 100bln from local sales to poultry farms. Lately, due to Covid-19 outbreak, restaurants, marriage halls and other public places have been closed. This, along with no exports of poultry products, have led to supply glut in local market. Prices of poultry products have posted a dip despite being an essential food item due to lower demand with many poultry farms becoming non-operational. Subsequently, sale of feed and recovery from farms is expected to remain under pressure. Although feed producers have sufficient inventory, lower sales and liquidity crunch are expected to significantly impact industry players. Recent SBP measures will provide some respite in the short-time. However, prolonged closure of key revenue generating channels will affect sales in the entire poultry chain.

The ratings reflect Hi-Tech Feeds (Pvt.) Limited association is with an established poultry group, Hi-Tech Group. The Company is part of Group's integrated poultry chain – oil/meal, feed and poultry – and enjoys a moderate market share with good Feed Conversion Ratio. The Company remains exposed to inherent risks in the feed industry emanating from raw material price changes and lately low demand due to COVID-19 outbreak. Although the Company enjoyed good margins and profitability in 9MFY20, sales have slowed down considerably in the 4QFY20 subsequent to lockdown leading to lower capacity utilization and off take. This trend is expected to continue until lockdown eases and demand centers (restaurants, banquet halls etc.) reopen. The Company piled up raw material inventory, procured on cash, in anticipation of higher prices. This led to stretched working capital requirement, with receivable days also high, met through short-term borrowings. The Company had a moderately leveraged capital structure, while coverages remain stretched. The ratings have been put on "Rating Watch" as COVID-19 outbreak and lockdown has adversely impacted industry prospects and created uncertainty. PACRA will monitor the prevailing situation and update the ratings accordingly.

The ratings are dependent on the management's ability to sustain its operations and improve capacity utilization. Maintaining strict working capital discipline through prudent inventory management and rationalizing significantly high receivable days and ensuing borrowings remain critical. Any significant deterioration in margins and/or prolonged low sales cycle will have negative impact on the ratings. Support from sponsors and other group entities is important.

#### Disclosure

<b>Name of Rated Entity</b>	Hi-Tech Feeds (Pvt.) Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Ratings(Jun-19),Methodology   Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria   Rating Modifier(Jun-19)
<b>Related Research</b>	Sector Study   Poultry Feed(Jan-20)
<b>Rating Analysts</b>	Faiqa Qamar   faiqa.qamar@pacra.com   +92-42-35869504

## Profile

**Legal Structure** Hi-Tech Feeds (Pvt.) Limited ('Hi-Tech Feeds' or 'the Company') is incorporated as a Private Limited Company.

**Background** In 1980, the Sponsors started from small scale poultry breeder business and later diversified vertically across the poultry supply chain. Today, the Group has poultry feed mills, poultry farms, rice processing unit, edible oil mill and a veterinary pharmaceutical unit. Hi-Tech Feeds' became operational in 1985 when the Company set up its first feed mill in Lahore. Another feed mill was setup in Sahiwal in 2009.

**Operations** Hi-Tech Feeds is primarily engaged in the production and sale of poultry feed for breeder chicks, broiler and layers. The Company has two feed production units. Unit I, located in Lahore, manufactures feed at an installed capacity of 100 MT per hour. While, Unit II, located in Sahiwal, has an installed capacity of 90 MT per hour. The combined annual capacity of the Company is 396,000 MT per year. In 9MFY20, Hi-Tech Feeds produced 157,613 MT feed, which translates into capacity utilization of ~53%. Feed production units employ modern technologies and the Company is considered a high quality feed manufacturer.

## Ownership

**Ownership Structure** Hi-Tech Feeds, like other Group Companies, is equally owned (25% each) by Dr. Muhammad Arshad, Dr. Abdul Qayyum, Dr. Muhammad Asim Khan and Dr. Anwar Mahmood Randhawa.

**Stability** Ownership of the business is seen as stable as equal ownership vests with the Sponsors. Moreover, the second generation has recently joined Group Companies.

**Business Acumen** Hi-Tech Group entered into the business arena in 1980. The Group's first venture was Hi-Tech Feeds (Pvt.) Limited. Later, the Group set up various business entities across poultry supply chain. The Sponsors have experienced multiple business cycles and are considered among pioneers of poultry industry.

**Financial Strength** Hi-Tech Group comprises four Companies and two Association of Persons. In FY19, Hi-Tech Group had a total annual turnover of ~PKR 28bln with an equity base of PKR 10bln. The Group generated profit after tax of PKR 399mln during the year.

## Governance

**Board Structure** Hi-Tech Feeds BoD comprises four Executive Directors, who are also the Sponsors of the Company. Absence of non-executive Director and lack of independent oversight indicates room for improvement in the Company's governance framework

**Members' Profile** All four Directors hold a veterinary degree and extensive industry knowledge. The Board's Chairman, Dr. Anwar Mahmood Randhawa, is a Doctor of Veterinary Medicine. He has overall experience of 44 years in poultry and integrated businesses.

**Board Effectiveness** During 9MFY20, the Board met informally to discuss pertinent matters and make strategic decisions, with majority attendance. However, minutes of these meeting are not formally kept. Sub-committees are not in place in the Company.

**Financial Transparency** Hi-Tech Feeds external auditors, M/s Hameed Zahid & Co. Chartered Accountants, have expressed an unqualified opinion on the financial statements of the Company for the year ended June 30, 2019. The firm has been QCR rated by ICAP but is not on any SBP panel of auditors.

## Management

**Organizational Structure** Hi-Tech Feeds operates through six departments; Procurement, Production, Marketing and Sales, Finance, Information Technology and Tax. Both of the Company's feed mills are monitored by their respective GM Productions. All Departmental Heads report to the Company's CEO, who then makes pertinent decisions. As the Company's CEO makes key decisions, reliance on him remains high.

**Management Team** Hi-Tech Feeds CEO, Dr. Muhammad Arshad, laid the foundation of the Group and set up Hi-Tech Feeds. He actively participates in many international and local seminars on poultry, feed milling and veterinary pharmaceutical industry. Mr. Abid Shiko, CFO, has an overall experience of 22 years and is associated with Hi-Tech Group from two years. Dr. Muhammad Athar, GM Production, has an overall experience of 30 years and is associated with Hi-Tech Feeds from past 28 years.

**Effectiveness** There are no formal Management committees. However, pertinent matters are discussed among the four Directors/Sponsors or department head as per requirement. No formal documentation of these discussion sessions are maintained.

**MIS** Hi-Tech Group has built a customized software in-house to monitor and generate reports relating to the Company's inventory management, sales, receivables and payables. To integrate other functions, many other modules are in the development stage. Moreover, the Company's feed manufacturing facilities are fully automated.

**Control Environment** To ensure operational efficiency, an internal audit function is placed at Group level, which implements and monitors policies and procedures of the Company. On an operational level, samples of maize, meals, medicines and manufactured feed variants are tested for quality in a well-equipped laboratory.

## Business Risk

**Industry Dynamics** The global feed industry can be valued at around ~\$460bln, with poultry (~\$166bln) constituting ~36% of the total industry. Pakistan produces ~8mlnMT of feed annually with a total of ~150 registered feed mills and ~200 unregistered feed mills catering to it. The industry directly drives its demand from poultry – chicken and eggs - feed consumption. Due to Covid-19 outbreak, restaurants, marriage halls and food courts have been closed. This, along with no exports of poultry products, has led to supply glut in local market. Prices of poultry products have posted a dip despite being an essential food item due to lower demand with many poultry farms becoming non-operational. Subsequently, demand of feed and recovery from farms is expected to remain under significant pressure.

**Relative Position** Hi-Tech Feeds has secured a prominent position in the market due to its high FCR, culminating in an increased demand for its product. The Company is ranked among the second tier players of poultry feed industry with ~5% market share and FCR of ~1.5x.

**Revenues** Hi-Tech Feeds generates revenue by manufacturing and selling variants of poultry feed. In 9MFY20, the Company's topline reached to PKR 8bln witnessing a growth of ~11% on YoY basis. The Company generates a significant share of revenue from central region (53%) of the country followed by north (30%) and south (17%) regions. The growth in revenue was supported by increase in feed prices as volumes remained stagnant. The sales have slowed considerably lately as the lockdown prolongs and demand remains low.

**Margins** The Company's ability to pass on the increased raw material cost to poultry farms led to improved gross margins (9MFY20: 10.1%, FY19: 8.1%). The management kept the operating cost in control resulting in better operating margins (9MFY20: 7.7%, FY19: 5.6%). However, Hi-Tech Feeds experienced a decline in net margins (9MFY20: 0.7%, FY19: 1.4%) due to significantly higher finance cost. The Company's bottom line stood at PKR 60mln in 9MFY20 (9MFY19: PKR 100mln).

**Sustainability** The prevailing lockdown and uncertainty amidst COVID-19 outbreak has created challenges for the industry and the Company. Sustaining operations and generating cash flows will be tough in current environment as demand remains low. The situation may worsen if lockdown prolongs for a significant time.

## Financial Risk

**Working Capital** Hi-Tech Feeds working capital needs originates from financing and storing maize and soybean meal in bulk. High inventory level, kept the working capital days on the higher side (9MFY20: 131 days, 9MFY19: 96 days). Receivable days (9MFY20: 49 days, 9MFY19: 41 days) emanate from credit terms of 45-50 days as per industry norm. The Company procures raw materials on credit. However, creditor days dipped (9MFY20: 81 days, 9MFY19: 105 days) leading to stretched working capital cycle. Strict discipline in the working capital management is required to improve the short term borrowing buffer at trade level.

**Coverages** Hi-Tech Feeds interest coverage (9MFY20: 1.2x, 9MFY19: 1.9x) and core coverage (9MFY20: 0.8x, 9MFY19: 1.0x) deteriorated due to increased finance cost (9MFY20: PKR 499mln, 9MFY19: PKR 205mln), despite improvement in free cash flows (9MFY20: PKR 565mln, 9MFY19: PKR 360mln). Going forward, reduction in interest rate and SBP measures are expected to provide relief.

**Capitalization** The Company increased its short-term borrowings (9MFY20: PKR 5.8bln, 9MFY19: PKR 4.4bln) to finance working capital needs for procurement of Maize in bulk. The overall leverage improved (9MFY20: 51%, 9MFY19: 76%) despite higher borrowings due to significant increase in equity base due to revaluation of fixed assets.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

Hi-Tech Feeds (Pvt.) Limited Poultry Feeds	Mar-20 9M	Jun-19 12M	Mar-19 9M	Jun-18 12M	Jun-17 12M
<b>A BALANCE SHEET</b>					
1 Non-Current Assets	5,233	5,267	933	932	1,123
2 Investments	-	-	-	85	-
3 Related Party Exposure	766	475	1,019	882	552
4 Current Assets	7,417	7,653	6,343	5,770	5,397
a Inventories	4,798	4,743	3,937	3,488	3,409
b Trade Receivables	1,568	1,306	1,248	886	1,090
5 Total Assets	13,417	13,396	8,295	7,669	7,072
6 Current Liabilities	1,865	3,906	2,096	2,664	3,764
a Trade Payables	1,657	3,128	1,934	2,495	3,585
7 Borrowings	5,886	3,789	4,474	3,556	1,567
8 Related Party Exposure	-	-	172	-	385
9 Non-Current Liabilities	83	75	137	75	148
10 Net Assets	5,582	5,626	1,416	1,374	1,208
11 Shareholders' Equity	5,582	5,626	1,416	1,374	1,208
<b>B INCOME STATEMENT</b>					
1 Sales	8,086	9,741	7,302	8,160	8,630
a Cost of Good Sold	(7,272)	(8,953)	(6,726)	(7,460)	(8,080)
2 Gross Profit	815	788	576	699	549
a Operating Expenses	(195)	(247)	(225)	(351)	(355)
3 Operating Profit	620	541	351	348	194
a Non Operating Income or (Expense)	(0)	(1)	(6)	(36)	42
4 Profit or (Loss) before Interest and Tax	620	539	346	313	236
a Total Finance Cost	(499)	(364)	(205)	(185)	(151)
b Taxation	(61)	(34)	(41)	(19)	(1)
6 Net Income Or (Loss)	60	141	100	108	84
<b>C CASH FLOW STATEMENT</b>					
a Free Cash Flows from Operations (FCFO)	565	562	360	408	199
b Net Cash from Operating Activities before Working Capital Changes	49	310	178	238	56
c Changes in Working Capital	(1,950)	(588)	(1,450)	(1,083)	(60)
1 Net Cash provided by Operating Activities	(1,901)	(277)	(1,271)	(845)	(4)
2 Net Cash (Used in) or Available From Investing Activities	(118)	(368)	25	(521)	(180)
3 Net Cash (Used in) or Available From Financing Activities	2,097	232	917	2,305	(246)
4 Net Cash generated or (Used) during the period	78	(413)	(329)	939	(430)
<b>D RATIO ANALYSIS</b>					
<b>1 Performance</b>					
a Sales Growth (for the period)	10.7%	19.4%	19.3%	-5.4%	-14.3%
b Gross Profit Margin	10.1%	8.1%	7.9%	8.6%	6.4%
c Net Profit Margin	0.7%	1.4%	1.4%	1.3%	1.0%
d Cash Conversion Efficiency (EBITDA/Sales)	8.1%	6.2%	5.4%	5.4%	4.0%
e Return on Equity (ROE)	1.4%	4.0%	9.5%	8.4%	7.2%
<b>2 Working Capital Management</b>					
a Gross Working Capital (Average Days)	212	195	179	198	243
b Net Working Capital (Average Days)	131	90	96	62	48
c Current Ratio (Total Current Assets/Total Current Liabilities)	4.0	2.0	3.0	2.2	1.4
<b>3 Coverages</b>					
a EBITDA / Finance Cost	1.4	1.7	2.1	2.4	2.4
b FCFO / Finance Cost+CMLTB+Excess STB	0.8	1.4	1.0	0.6	1.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	2.9	0.2	1.0	2.0	3.2
<b>4 Capital Structure (Total Debt/Total Debt+Equity)</b>					
a Total Borrowings / Total Borrowings+Equity	51.3%	40.2%	76.0%	72.1%	58.4%
b Interest or Markup Payable (Days)	48.4	129.1	50.4	56.0	43.9
c Average Borrowing Rate	13.1%	9.4%	6.3%	6.9%	8.3%

**Credit Rating**

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.

Scale	Long-term Rating Definition
AAA	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> 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.
AA-	
A+	
A	<b>High credit quality.</b> 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.
A-	
BBB+	
BBB	<b>Good credit quality.</b> 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-	
BB+	<b>Moderate risk.</b> 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+	
B	<b>High credit risk.</b> 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-	
CCC	
CC	<b>Very high credit risk.</b> 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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
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.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*\*The correlation shown is indicative and, in certain cases, may not hold.*

**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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) 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.

**Surveillance.** Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

**Note.** This scale is applicable to the following methodology(s):

<p><b>Entities</b></p> <ul style="list-style-type: none"> <li>a) Broker Entity Rating</li> <li>b) Corporate Rating</li> <li>c) Financial Institution Rating</li> <li>d) Holding Company Rating</li> <li>e) Independent Power Producer Rating</li> <li>f) Microfinance Institution Rating</li> <li>g) Non-Banking Finance Companies (NBFCs) Rating</li> </ul>	<p><b>Instruments</b></p> <ul style="list-style-type: none"> <li>a) Basel III Compliant Debt Instrument Rating</li> <li>b) Debt Instrument Rating</li> <li>c) Sukuk Rating</li> </ul>
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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)

### **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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- (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)

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