The Pakistan Credit Rating Agency Limited

Rating Report

Hi-Tech Feeds (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
15-Sep-2021	BBB-	A3	Stable	Maintain	-
19-Jan-2021	BBB-	A3	Stable	Maintain	-
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

Globally, the poultry feed production stood at 1.2bln MT in 2020, up by 1% from 2019. Pakistan's annual poultry feed production is around ~3.5mln MT, with ~150 registered feed mills and ~200 unregistered feed mills catering to it. The industry generates an annual turnover of ~PKR 396bln (Jun-20). At the beginning of the COVID-19 pandemic, the closure of restaurants/marriage halls and export avenues led to a supply glut of poultry products in the local market. However, as business avenues became operational, demand for poultry products improved. Lately, a visible surge was also observed in feed and poultry product prices. This, along with SBP's interest rate cut along with deferment and/or restructuring option provided sufficient respite to the industry players. An uptick in prices and demand dynamics are expected if the hospitality segment remains operational.
The ratings reflect Hi-Tech Feeds (Pvt.) Limited's ('the Company') association 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 remained exposed to inherent risks in the feed industry emanated from raw material price changes and low demand amidst the Covid-19 pandemic. Lately, the increasing demand and prices of poultry products has eased some pressure off the Company, however, the optimum production and sales levels are anticipated if demand avenues (banquet halls, dine-in restaurants) remain operational and demand uncertainties subside. Although the Company enjoyed stable margins and profitability, sales remained slightly lower leading to lower capacity utilization and off take. Moreover, the Company's ability to pass on the increased raw material cost to poultry farms led to improved margins. Further, the rate cut by SBP improved the Company's profitability and in turn cashflows. The Company has piled up raw material inventory, procured on cash, in anticipation of higher prices. This led to stretched working capital requirements, with receivable days also high, met through short-term borrowings. The Company had a moderately leveraged capital structure, while coverages remain adequate.

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 a negative impact on the ratings. Support from sponsors and other group entities is important.

Disclosure

Name of Rated Entity	Hi-Tech Feeds (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Poultry Feed(Jan-21)
Rating Analysts	Faiqa Qamar | faiqa.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Hi-Tech Feeds (Pvt.) Limited ('Hi-Tech Feeds' or 'the Company') was incorporated in 1985 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, Hi-Tech Group ('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 with capacity utilization standing at ~50%.

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 The sponsors have substantial financial strength and the Group has several business entities across the poultry supply chain.

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 FY20, the Board met informally four times 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, 2020. The firm has been QCR rated by ICAP but is not in the SBP's 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. Dr. Muhammad Athar, GM Production, has an overall experience of over 3 decades. He has been associated with Hi-Tech Feeds from past 29 years.

Effectiveness There are no formal Management committees. However, pertinent matters are discussed among the four Directors/Sponsors or departmental heads as per requirement. No formal documentation of these discussions is 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 Pakistan's annual poultry feed production is around ~3.5mln MT, with ~150 registered feed mills and ~200 unregistered feed mills catering to it. The industry generates an annual turnover of ~PKR 396bln. At the beginning of the COVID-19 pandemic, the closure of restaurants/marriage halls and export avenues led to a supply glut of poultry products in the local market. However, as business avenues became operational, demand for poultry products improved. Lately, a visible surge was also observed in feed and poultry product prices. This, along with SBP's interest rate cut along with deferment and/or restructuring option provided sufficient respite to the industry players.

Relative Position Hi-Tech Feeds' has secured prominent position in the market due to its high FCR, culminating in an increased demand for their product. The Company is ranked among the second-tier players of poultry feed industry.

Revenues The Company mainly generates revenue by manufacturing and selling variants of poultry feed. Around ~13% of the Company's revenue is generated by selling to associated Group company, Hi-Tech Farms. The Company mainly sells in the Central region (52%), and Northern region (31%), followed by Southern region (17%). In 3QFY21 the Company posted revenue of ~PKR 7.8bln (3QFY20: ~PKR 8.1bln), reflecting a decline of ~4% due to dip in prices of poultry products.

Margins In 3QFY21, the Company's gross margin dipped and stood at 8.2% (3QFY20: 10.1%) due to lower prices of poultry products and lower turnover compared to the same period prior year. Similarly, operational margin dipped to 5.8% (3QFY20: 7.7%). The Company posted net profit of PKR 270mln (3QFY20: PKR 60mln) and net profit margin increased to 3.5% (3QFY20: 0.7%) due to lower finance cost as a result of interest rate cut.

Sustainability High poultry feed prices and recovery of demand due to relaxation in lockdown tends to bode well for the Company. However, the Company is exposed to volatility and ensuing challenges in the feed and poultry sector.

Financial Risk

Working Capital The Company's working capital need originates from financing and storing maize and soybean meal in bulk. The inventory days stood at 176 days in 3QFY21 (3QFY20: 163 days). Receivable days witnessed slight increase and stood at 56 days (3QFY20: 49 days). Similarly, payable days stood at 82 days (3QFY20: 81 days) resulting in net working capital increasing to 150 days (3QFY20: 131 days). Furthermore, the Company's room to borrow against trade leverage remains stretched due to higher reliance on short-term borrowings for working capital needs.

Coverages During 3QFY21, the free cashflows from operations improved to ~PKR 641mln (3QFY20: ~PKR 565mln). Meanwhile, the finance cost decreased to ~PKR 376mln (3QFY20: ~PKR 499mln) on the back of lower interest rate. Resultantly, the interest cover witnessed improvement and stood at 1.8x (3QFY20: 1.2x). Similarly, core and total interest cover improved to 1.5x (3QFY20: 0.8x). Debt payback period stood at 1.5x (3QFY20: 2.9x).

Capitalization Hi-Tech Feeds has a moderately leveraged capital structure with a leveraging ratio of ~46% in FY20 (FY19: ~40%). Short-term borrowing constituted nearly 90% of total borrowings. In 3QFY21, the leveraging remained unchanged at ~46%.

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Financial Summary
PKR mln

Hi-Tech Feeds (Pvt.) Limited	Mar-21	Sep-20	Jun-20	Mar-20	Sep-19	Jun-19	Jun-18
Poultry Feeds	9M	3M	12M	9M	3M	12M	12M
A BALANCE SHEET							
1 Non-Current Assets	5,564	5,643	5,702	5,233	5,214	5,267	932
2 Investments	-	-	-	-	-	-	85
3 Related Party Exposure	493	301	299	766	422	475	882
4 Current Assets	8,057	7,211	7,089	7,417	7,486	7,653	5,770
a Inventories	*5,448*	*4,862*	*4,570*	*4,798*	*5,065*	*4,743*	*3,488*
b Trade Receivables	*1,723*	*1,507*	*1,449*	*1,568*	*1,372*	*1,306*	*886*
5 Total Assets	14,113	13,155	13,090	13,417	13,121	13,396	7,669
6 Current Liabilities	2,985	2,028	2,550	1,865	2,682	3,906	2,664
a Trade Payables	*2,559*	*1,733*	*2,088*	*1,657*	*2,179*	*3,128*	*2,495*
7 Borrowings	4,936	5,249	4,700	5,886	4,733	3,789	3,556
8 Related Party Exposure	148	72	72	-	-	-	-
9 Non-Current Liabilities	140	137	134	83	77	75	75
10 Net Assets	5,905	5,670	5,635	5,582	5,629	5,626	1,374
11 Shareholders' Equity	5,905	5,670	5,635	5,582	5,629	5,626	1,374
B INCOME STATEMENT							
1 Sales	7,793	2,292	9,955	8,086	2,732	9,741	8,160
a Cost of Good Sold	*(7,157)*	*(2,012)*	*(8,797)*	*(7,272)*	*(2,487)*	*(8,953)*	*(7,460)*
2 Gross Profit	637	280	1,158	815	244	788	699
a Operating Expenses	(183)	(72)	(243)	(195)	(66)	(247)	(351)
3 Operating Profit	454	209	915	620	179	541	348
a Non Operating Income or (Expense)	*250*	*(3)*	*(2)*	*(0)*	*(3)*	*(1)*	*(36)*
4 Profit or (Loss) before Interest and Tax	704	205	912	620	175	539	313
a Total Finance Cost	*(376)*	*(144)*	*(786)*	*(499)*	*(124)*	*(364)*	*(185)*
b Taxation	*(58)*	*(27)*	*(93)*	*(61)*	*(15)*	*(34)*	*(19)*
6 Net Income Or (Loss)	270	35	33	60	37	141	108
C CASH FLOW STATEMENT							
a Free Cash Flows from Operations (FCFO)	*641*	*207*	*1,082*	*565*	*170*	*562*	*408*
b Net Cash from Operating Activities before Working Capital Changes	*261*	*15*	*358*	*49*	*26*	*310*	*238*
c Changes in Working Capital	*(739)*	*(594)*	*(1,211)*	*(1,950)*	*(1,642)*	*(588)*	*(1,083)*
1 Net Cash provided by Operating Activities	(477)	(579)	(853)	(1,901)	(1,616)	(277)	(845)
2 Net Cash (Used in) or Available From Investing Activities	240	1	390	(118)	593	(368)	(521)
3 Net Cash (Used in) or Available From Financing Activities	236	539	416	2,097	1,598	232	2,305
4 Net Cash generated or (Used) during the period	(2)	(39)	(47)	78	575	(413)	939
D RATIO ANALYSIS							
1 Performance							
a Sales Growth (for the period)	4.4%	-7.9%	2.2%	10.7%	12.2%	19.4%	-5.4%
b Gross Profit Margin	8.2%	12.2%	11.6%	10.1%	8.9%	8.1%	8.6%
c Net Profit Margin	3.5%	1.5%	0.3%	0.7%	1.3%	1.4%	1.3%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	-1.2%	-16.9%	-1.3%	-17.1%	-53.9%	-0.3%	-8.3%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	6.3%	2.4%	0.6%	1.4%	2.6%	3.2%	8.2%
2 Working Capital Management							
a Gross Working Capital (Average Days)	232	247	221	212	209	195	209
b Net Working Capital (Average Days)	150	171	126	131	120	90	73
c Current Ratio (Current Assets / Current Liabilities)	2.7	3.6	2.8	4.0	2.8	2.0	2.2
3 Coverages							
a EBITDA / Finance Cost	1.6	1.9	1.5	1.4	1.6	1.7	2.4
b FCFO / Finance Cost+CMLTB+Excess STB	1.7	1.5	1.3	0.8	1.4	1.4	0.6
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.5	1.8	1.7	2.9	0.0	0.2	2.0
4 Capital Structure							
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	46.3%	48.4%	45.9%	51.3%	45.7%	40.2%	72.1%
b Interest or Markup Payable (Days)	77.3	52.8	67.2	48.4	74.4	129.1	56.0
c Entity Average Borrowing Rate	9.2%	10.5%	16.3%	13.5%	10.8%	8.8%	6.9%

Credit Rating

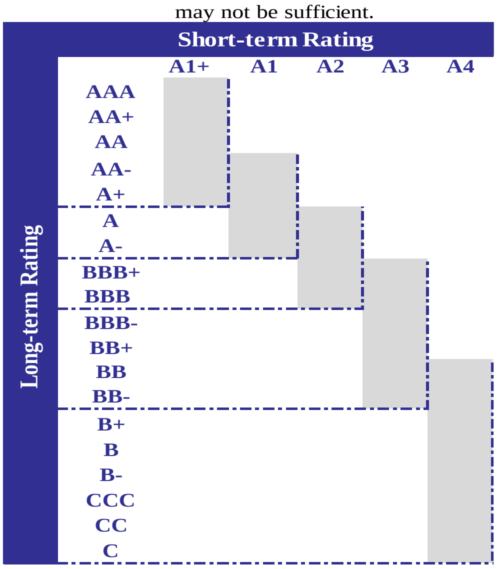
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 Rating

Scale	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
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 surveill 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):

Entities

a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

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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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(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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(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)
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