The Pakistan Credit Rating Agency Limited

Rating Report

Kangore Traders

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
31-May-2019	BB+	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Kangore's relative position in the country's rice export market. The sponsor is associated with the related business for long. Attributed to the commodity nature of 'non-basmati rice', business risk is low. Additionally, rupee devaluation is a benefit to the export industry as a whole. The key challenge, however, remains in the cyclical nature of the rice business. Kangore Traders bears the status of a sole proprietorship with the single owner being the man of the last mile. Corporate structure lacks on basic grounds. The same is depicted by the small size of the proprietorship. Given the industry dynamics, Company has maintained its profitability over the years. Management systems and controls also display a weak outlook, strictly necessitating the need for strengthening controls over financial reporting. Kangore's financial risk profile is reflected by a bottomline centric approach with a moderately leveraged capital structure; debt book majorly constitutes export related short term funding needs. With major focus of business towards African markets, working capital cycles have enlarged gradually, creating need for short term borrowing over a relatively longer horizon.

The ratings are dependent upon strengthening of corporate discipline, including enhancement of controls over financial reporting. Meanwhile, consistent profitability alongside growth in the business volumes is essential.

Disclosure

Name of Rated Entity	Kangore Traders
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Rice(Dec-18)
Rating Analysts	Raniya Tanawar | raniya.tanawar@pacra.com | +92-42-35869504

Profile

Legal Structure Kangore Traders, is a sole proprietorship established in 1996.

Background Mr. Nawal's family has been in the rice business since 1983, with three rice mills in the regions of Sindh; Golarchi and Badin. In 1996, Kangore Traders was established with a view of growing business prospects. Additionally, from 1996 Kangore was among the top 'pulses' exporters till a ban was imposed by GOP on the exports of pulses in 2006. At present, the company has vastly expanded its avenues in the African side, with branches in African countries; Benin, Niger, Madagascar and Nairobi.

Operations : Kangore's core business involves processing and trading of non-basmati rice locally and internationally, with main concentration in Afro based regions. The company has five (5) processing units, each with 30 M.Tons per hour capacity, located in Landhi, Karachi.

Ownership

Ownership Structure Kangore, being a sole proprietorship, is 100% owned by an individual, Mr Nawal.

Stability Dealing in 'non-basmati rice', that has prospective demand ensures company's long existence in the market, however, supplementing more competitive environment for the existing players.

Business Acumen Mr. Nawal is the man at the last mile, who spearheads the business alongside his family members.

Financial Strength Sponsor's support is the backbone of company since its establishment

Governance

Board Structure There exist no formal board structure since Kangore is a sole proprietorship.

Members' Profile Mr. Nawal, has more than two decades of experience and has been associated with the company since its inception. He belongs to an entrepreneurial background.

Board Effectiveness Absence of proper governance structure and lack of independent oversight instigate need for improvement.

Financial Transparency Amir Hussain Associates and Chartered Accountants are the auditors for the Kangore Traders (Pvt.) Ltd. Neither the audit firm doesn't satisfy the QCR ratings nor does it is classified in any of the categories defined by the State Bank of Pakistan. The auditors issued an unqualified opinion on the company's financial statements for the year ended June 30, 2018.

Management

Organizational Structure Kangore has a lean organization structure where all reporting resorts to Mr. Nawal.

Management Team The overall chores of operations are in the hands of family members. Mr. Nawal's elder son, Mr. Avinash and Mr. Sunil are directly involved in the business operations while Mr. Prem, Finance Manager, is his nephew.

Effectiveness There is no culture of conducing formal management committees since the sponsor himself is directly involved in the business.

MIS An in-house system based processes is in place at Kangore that is capable of systematic reporting, covering the following areas i) Purchase ii) Sale/Export iii) loan outstanding position and iv) pledge report.

Control Environment Non-existence of corporate governance framework, poses concerns over the internal controls of the company.

Business Risk

Industry Dynamics Pakistan's Rice industry continues to be instrumental for the Agriculture sector of the country. However, the total contribution to the GDP is meagre clocking in at 0.6%. There are around 150 silky plants and more than 1500 husking plants in the Sindh region. Only one company named MATCO is listed in the Pakistan Stock Exchange. The Rice cultivation area is 2.9 million hectors. Production of rice is ~7 M.Tons and the consumption is ~3M.Tons. The maximum contribution from the Rice sector in country's foreign exchequer is from non-basmati rice exports: marked USD 2bln in FY18.

Relative Position The Company's business mainly involves exporting non-basmati rice with a small market share of ~2%. The company has a major customer base in Afro-Asian countries, with the top consumers being from Africa, Kenya, U.A.E, China and Indonesia.

Revenues The Company's topline tend to witness an increasing trend since FY16. In line with the industry, the topline surged by ~43% in FY18 which however increased by only 1.3% in its corresponding period. This mainly attributed to the fact that West Africa is the newly discovered region and becoming the favorite for rice exporters including Kangore. Kenya has a major contribution towards the increase in company's topline that clocked in at PKR 5.8bln in FY18 and PKR 3bln in 1HFY19 (FY17: PKR 4bln).

Margins Margins of the company, with little or no deviation, stayed consistent over the years. Gross margins remained static at 32% since FY16 whereas net margin locked at 11% in 1HFY19 and FY18 (FY17: 10%) demonstrated operational efficiency.

Sustainability Sponsor support is a major catalyst for the company's sustainability. With an aim to diversify its exporting regions Company will be focusing on strengthening relationships with buyers in the Middle Eastern, African and as well as European countries, through their own brands.

Financial Risk

Working Capital : In anticipation to the future demand and sale prospects, the company's stock level have raised to 92days in 1HFY19, hence leading the working capital cycle to a higher end; ~166days (FY18: 149days, FY17: 170days, CY16: 172days). The entire working capital management is heavily supported by short term borrowings 1HFY19: ~1.5bln (FY18: PKR ~ 1.5bln, FY17: ~0.5bln), which also comprises export refinance facility.

Coverages Kangore enjoys good FCFO base over the years; PKR ~481mln in FY18 as against PKR ~397mln in FY17 (1HFY19: PKR ~400mln), on account of increased profitability. Keeping its coverages in comfortable position, the Interest repayment was at 14x in 1HFY19 (FY18: 11x).

Capitalization The company has not entered into any long term debt arrangement over the years. The financial profile is supported through mix of internally generated cashflows and short term borrowings. The company has maintained its capital structure at adequate level: 1HFY19 35% (FY18: ~39%, FY17: ~21%)

Rice
Financials (Summary) in PKR mln
The Pakistan Credit Rating Agency Limited

PKR mln

Kangore Traders
Proprietorship

BALANCE SHEET	Dec-18	Jun-18	Jun-17	Jun-16
	6M	12M	12M	12M
a Non-Current Assets	**36**	**35**	**36**	**37**
b Investments (Incl. Associates)	**-**	**-**	**-**	**-**
Equity Instruments	-	-	-	-
Debt Instruments	-	-	-	-
c Current Assets	**3,961**	**3,918**	**2,583**	**2,560**
Inventory	1,742	1,652	1,046	1,042
Trade Receivables	1,288	1,273	910	893
Others	931	993	628	625
d Total Assets	**3,997**	**3,953**	**2,619**	**2,597**
e Debt/Borrowings	**1,509**	**1,505**	**538**	**897**
Short-Term	1,509	1,505	538	897
Long-Term (Incl. Current Maturity of Long-Term Debt)	-	-	-	-
Other Short-Term Liabilities	72	66	56	39
Other Long-Term Liabilities	-	-	-	-
f Shareholder's Equity	**2,416**	**2,382**	**2,025**	**1,661**
g Total Liabilities & Equity	**3,997**	**3,953**	**2,619**	**2,597**
INCOME STATEMENT				
a Turnover	**3,360**	**5,844**	**4,084**	**4,031**
b Gross Profit	1,075	1,848	1,313	1,296
c Net Other Income	-	-	-	-
d Financial Charges	(28)	(45)	(36)	(116)
e Net Income	**367**	**621**	**423**	**413**
CASH FLOW STATEMENT				
a Free Cash Flow from Operations (FCFO)	396	481	400	377
b Total Cashflows (TCF)	396	481	400	377
c Net Cash changes in Working Capital	(44)	(1,111)	(1)	(597)
d Net Cash from Operating Activities	324	(675)	363	(335)
e Net Cash from InvestingActivities	(2)	-	-	-
f Net Cash from Financing Activities	(329)	682	(359)	338
g Net Cash generated during the period	(7)	7	4	3
RATIO ANALYSIS				
a Performance				
Turnover Growth	15%	43%	1%	#DIV/0!
Gross Margin	32%	32%	32%	32%
Net Margin	11%	11%	10%	10%
ROE	31%	28%	23%	25%
b Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	14.0	10.7	11.2	3.3
Interest Coverage (X) (FCFO/Gross Interest)	14.0	10.7	11.2	3.3
Debt Payback (Years) (Total Debt (excluding Covered Short Term Borrowings) / FCFO	0.0	0.0	0.0	0.0
c Capital Structure (Total Debt/Total Debt+Equity)				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	158	149	170	172
d Capital Structure (Total Debt/Total Debt+Equity)	38%	39%	21%	35%

Kangore Traders
May-19

Rating Scale

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.

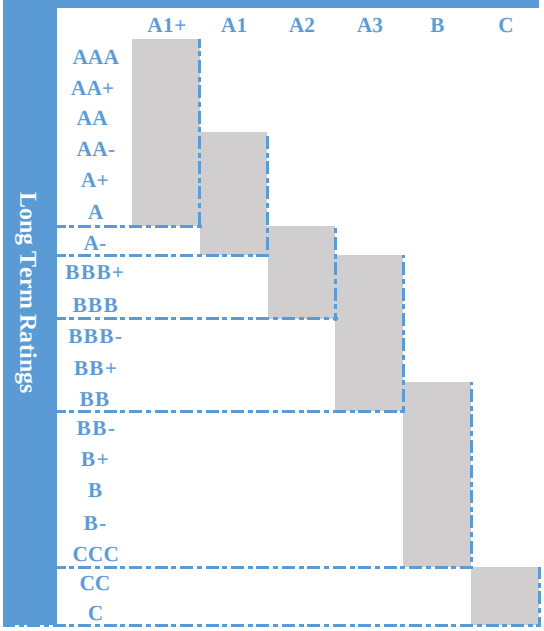
Long Term Ratings

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.

Short Term Ratings



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.

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