



The Pakistan Credit Rating Agency Limited

Rating Report

Kangore Traders

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Rating History

| Dissemination Date | Long Term Rating | Short Term Rating | Outlook | Action | Rating Watch |
|--------------------|------------------|-------------------|---------|----------|--------------|
| 30-Nov-2019 | BB+ | A3 | Stable | Maintain | - |
| 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 agricultural nature of its product - non-basmati rice, business risk is low, yet bears a cyclicality. Over the years, Kangore has emerged as one of the prominent rice exporters of the country, therefore, strength is derived from its strong and growing topline. During FY19, the country's rice industry observed a subtle growth, whereas rupee devaluation favored the rice exporters to enhance their revenue base, including Kangore. Profitability margins, however, dwindled on the backdrop of higher operating costs, particularly risen selling expenses. Kangore bears the status of a sole proprietorship with a single owner being the man of the last mile therefore, the corporate structure is limited and lacks on basic grounds. Financial risk profile is reflected by a topline 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 sustained business growth and profitability margins. Meanwhile, improved governance practices, including financial veracity, remain imperative to the ratings.

Disclosure

| | |
|------------------------------|---|
| Name of Rated Entity | Kangore Traders |
| 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) |
| Related Research | Sector Study Rice(Nov-19) |
| 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, mainly exporting to; 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 37.5 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, alongside his brother Mr. Gangoomal and other family members, spearheads the business.

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. The firm is neither QCR rated 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 with defined departments and a thorough line of management.

Management Team The overall chores of operations are in the hands of family members who are well experienced in the field. 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 At present, there is no culture of conducting formal management committees since the sponsor is directly involved in the business activities.

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 On the side of corporate governance framework, improvement is required, though the internal controls are directly overseen by the directors.

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 and initiatives. During FY19, rice crop area decreased by ~3.1% to 2.8 million hectares 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 decrease in area cultivated, dry weather and shortage of water. 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 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 ~15% in FY19, where it increased by ~43% last year. This mainly attributed to the fact that West Africa became the new favourite region for rice exporters including Kangore. Kangore's topline clocked in at PKR 6.9bln as compared to PKR 5.8bln in FY18. Kangore was among the list of top 100 exporters with earnings of USD 49mln.

Margins Gross Margins of the company dropped to ~18% in FY19 after a period of consistency for three consecutive years; (FY18: ~32%, FY17: ~32%) mainly due to some one off export challenge, whereas net margins dropped to 1.1% in FY19 from ~11% in FY18 (FY17: 10%).

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 98days in FY19, hence leading the working capital cycle to a higher end; ~157days (FY18: 149days, FY17: 174days). The entire working capital management is heavily supported by short term borrowings FY19: ~1.7bln (FY18: PKR ~ 1.5bln, FY17: ~0.5bln), which also comprises export refinance facility.

Coverages Kangore FCFO base has shrunk to 178mln during FY19, after a strong trend over the years; FY18: PKR ~481mln, FY17: PKR ~397mln, on account of dwindled profitability. Keeping its coverages conservative at 1.8x in FY19 (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, though pacing towards higher end: FY19: ~48% (FY18: ~39%, FY17: ~21%)



The Pakistan Credit Rating Agency Limited

Financial Summary

| | PKR mln | | |
|-------------------------|---------------|---------------|---------------|
| Kangore Traders Rice | Jun-19 12M | Jun-18 12M | Jun-17 12M |

A BALANCE SHEET

| | | | |
|----------------------------|-------|-------|-------|
| 1 Non-Current Assets | 35 | 35 | 36 |
| 2 Investments | - | - | - |
| 3 Related Party Exposure | - | - | - |
| 4 Current Assets | 4,180 | 3,918 | 2,583 |
| <i>a Inventories</i> | 2,054 | 1,652 | 1,046 |
| <i>b Trade Receivables</i> | 1,138 | 1,273 | 910 |
| 5 Total Assets | 4,215 | 3,953 | 2,619 |
| 6 Current Liabilities | 84 | 66 | 56 |
| <i>a Trade Payables</i> | 84 | 65 | 53 |
| 7 Borrowings | 1,762 | 1,505 | 538 |
| 8 Related Party Exposure | - | - | - |
| 9 Non-Current Liabilities | - | - | - |
| 10 Net Assets | 2,369 | 2,382 | 2,025 |
| 11 Shareholders' Equity | 2,369 | 2,382 | 2,025 |

B INCOME STATEMENT

| | | | |
|--|---------|---------|---------|
| 1 Sales | 6,936 | 5,844 | 4,084 |
| <i>a Cost of Good Sold</i> | (5,625) | (3,996) | (2,771) |
| 2 Gross Profit | 1,311 | 1,848 | 1,313 |
| <i>a Operating Expenses</i> | (1,125) | (1,126) | (820) |
| 3 Operating Profit | 186 | 722 | 493 |
| <i>a Non Operating Income or (Expense)</i> | - | - | - |
| 4 Profit or (Loss) before Interest and Tax | 186 | 722 | 493 |
| <i>a Total Finance Cost</i> | (99) | (45) | (36) |
| <i>b Taxation</i> | (9) | (56) | (34) |
| 6 Net Income Or (Loss) | 78 | 621 | 423 |

C CASH FLOW STATEMENT

| | | | |
|--|-------|---------|-------|
| <i>a Free Cash Flows from Operations (FCFO)</i> | 86 | 481 | 400 |
| <i>b Net Cash from Operating Activities before Working Capital Changes</i> | (13) | 436 | 365 |
| <i>c Changes in Working Capital</i> | (236) | (1,111) | (1) |
| 1 Net Cash provided by Operating Activities | (249) | (675) | 363 |
| 2 Net Cash (Used in) or Available From Investing Activities | - | - | - |
| 3 Net Cash (Used in) or Available From Financing Activities | 258 | 682 | (359) |
| 4 Net Cash generated or (Used) during the period | 8 | 7 | 4 |

D RATIO ANALYSIS

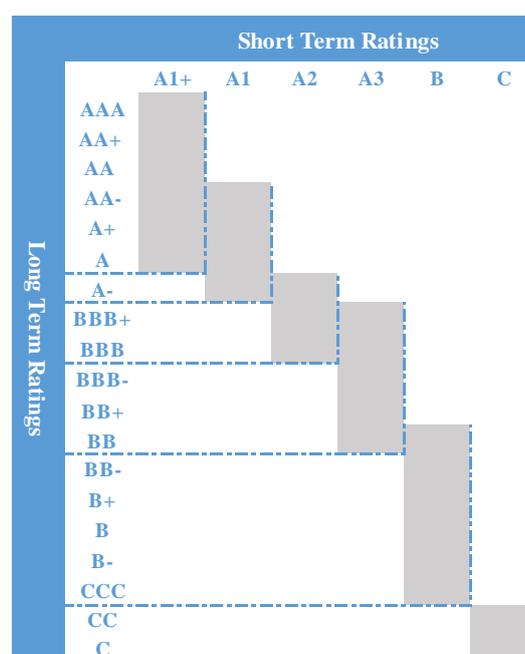
| | | | |
|---|-------|-------|-------|
| 1 Performance | | | |
| <i>a Sales Growth (for the period)</i> | 18.7% | 43.1% | 1.3% |
| <i>b Gross Profit Margin</i> | 18.9% | 31.6% | 32.1% |
| <i>c Net Profit Margin</i> | 1.1% | 10.6% | 10.3% |
| <i>d Cash Conversion Efficiency (EBITDA/Sales)</i> | 2.7% | 12.4% | 12.1% |
| <i>e Return on Equity (ROE)</i> | 3.3% | 28.2% | 22.9% |
| 2 Working Capital Management | | | |
| <i>a Gross Working Capital (Average Days)</i> | 161 | 152 | 174 |
| <i>b Net Working Capital (Average Days)</i> | 157 | 149 | 170 |
| <i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i> | 50.0 | 59.4 | 45.8 |
| 3 Coverages | | | |
| <i>a EBITDA / Finance Cost</i> | 1.9 | 16.0 | 13.8 |
| <i>b FCFO / Finance Cost+CMLTB+Excess STB</i> | 0.9 | 10.7 | 11.2 |
| <i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i> | 0.0 | 0.0 | 0.0 |
| 4 Capital Structure (Total Debt/Total Debt+Equity) | | | |
| <i>a Total Borrowings / Total Borrowings+Equity</i> | 42.7% | 38.7% | 21.0% |
| <i>b Interest or Markup Payable (Days)</i> | 0.0 | 0.0 | 0.0 |
| <i>c Average Borrowing Rate</i> | 6.1% | 4.4% | 5.0% |

| # | Notes |
|----|---|
| D5 | The line includes Advances from Customers, amounting to PKR 2.5bln [FY17: PKR 2.2bln] |
| - | - |
| - | - |
| - | - |
| - | - |

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+ 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. | A1 | A strong capacity for timely repayment. |
| 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. | A2 | A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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. | A3 | An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions. |
| 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 | The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. |
| 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. | C | An inadequate capacity to ensure timely repayment. |
| 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. | | |



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)

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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- (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)
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- (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)

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- (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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