The Pakistan Credit Rating Agency Limited

Rating Report

Al-Khair Rice Mills (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
18-Jan-2022	BBB-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Rice is among the five major crops of Pakistan and is the second main staple food, after wheat. The segment contributes about 3.5% in agriculture value addition and 0.7% in GDP. Pakistan cultivates both basmati and non-basmati rice, most of which is exported. In Pakistan, rice is grown in most of the Sindh and Punjab Province. Sindh specializes in producing the long grains white rice IRRI-6 and IRRI-9, while Punjab produces world-class Basmati rice. Pakistan locally consumes Basmati Rice, which is a long, thin aromatic type of rice, considered premium and luxury category across the globe. Local consumption includes ~95% of basmati rice and ~5% non-basmati. The major players in rice exports include Pakistan, India, Thailand, and Vietnam. Pakistan is in direct competition with India, while Thailand and Vietnamese rice are considered premium. During FY21, rice cropped area increased to ~3.3mln hec (FY20: ~3mln hec), reflecting an increase of ~10%. This led to an increased rice production by ~13%, standing at ~8.4mln MT (FY20: ~7.4mln MT). Out of this, around 3.5mln MT of rice is consumed locally. While, ~3.7mln MT is exported to generate ~ PKR 325bln of export revenue. The maximum contribution is from non-basmati rice (72%) exports, as basmati rice is locally consumed and minimal quantity (28%) is exported. During FY21, rice exports deteriorated to ~USD 2bln (FY20: ~USD 2.2bln) owing to the Indian strategy of dumping the commodity in international market at cheaper rates. Going forward, the depreciating rupee is expected to supplement the export volumes for rice.
The ratings reflect Al-Khair Rice Mills association with well-established players in the oil marketing and distribution segments, namely Gas & Oil Petroleum and Sitara Petroleum. The Group also has presence in oil logistics, organic farming, and real estate segments of the economy. Being an establishing player in terms of volume, the Company mainly generates revenue from local basmati sales, along with sizeable contribution from exports. Moreover, the Sponsors are further pursuing export avenues in the Middle East and European regions. To cater this, they have lately enhanced the rice processing capacity to 25MT/hr from 15MT/hr. Governance and management are in their initial gestation phase, as the Group is in the process of integrating Al-Khair's systems and reporting alongside the other Group entities. Business risk profile portrays an improving topline, with modest margins due to low quantum of exports. Financial risk profile of the Company remains stable owing to moderately leveraged capital structure; consisting majorly of short-term debt, obtained to finance the working capital requirement. Coverage ratios are adequate.

The ratings are dependent on the management's ability to materialize the projected revenue stream, while maintaining business margins. Prudent management of expansion and investment-related debt in order to meet financial obligations will be important. Any significant decline in coverages and/or erosion of margins may adversely impact the ratings.

Disclosure

Name of Rated Entity	Al-Khair Rice Mills (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 | Rice(Oct-21)
Rating Analysts	Shayan Farooq | shayan.farooq@pacra.com | +92-42-35869504

Profile

Legal Structure Al-Khair Rice Mills (Pvt.) Limited ("Al-Khair" or "the Company") is a private limited company, incorporated in 2019.

Background Al-Khair is associated with well-established players in the oil marketing and distribution segments. The Group also has presence in oil logistics, organic farming, and real estate segments. The Group initially entered in the business arena by setting up an oil distribution. In 2009, Mr. Javed tapped in the rice trading business. In 2012, the oil distribution channel was formally incorporated as Sitara Petroleum. The Group then formed an OMC; Gas & Oil Petroleum. In 2019, rice trading channel was formally incorporated as Al-Khair Rice Mills. Initially, the Company was established as a partnership concern and was run and managed by the sponsoring family. In 2019, Al-Khair's legal status was changed to a private limited company. Today, the Company holds the membership of Rice Export Association of Pakistan (REAP).

Operations The Company's core operation includes processing and sale of basmati rice. The processing plant is located at Okara and spans across 25 acres. Initially, the Unit had a processing capacity of 15MT/hr. Lately, the Unit's capacity is enhanced to 25MT/hr. Al-Khair has latest imported machinery in place and the plant is a complete processing composite that is capable to perform all stages: Pre-cleaning, Drying, Color Sorting, De-stoning, Polishing, and Packing.

Ownership

Ownership Structure The shareholding of the Company resides between Mr. Javed Iqbal (90%) and his son, Mr. Siddique Javed (10%).

Stability Ownership stake with no expectation of change in the short horizon adhere to stability in the structure.

Business Acumen Before the formal establishment of Al-Khair, Mr. Javed Iqbal, was associated with the family business of rice farming and trading.

Financial Strength Financial strength of the Group is considered strong, as they are involved in oil marketing, oil logistics, organic farming, real estate. Total consolidated revenue of the Group stood at PKR 125bln as at FY21.

Governance

Board Structure The Company's BoD comprises two Executive Directors only.

Members' Profile Mr. Javed Iqbal chairs the BoD and has an overall experience of over 25 years in rice farming and manufacturing.

Board Effectiveness The Directors are directly engaged in the management of the Company. Moreover, there are no committees in place to assist the Board. Pertinent matters are discussed informally and documented as per requirement. Thus, there is room for improvement in the governance framework.

Financial Transparency Crowe Hussain Chaudhury & Co. Chartered Accountants have been appointed as the auditors for the Company. The firm satisfies QCR ratings, and are classified in 'A' category of SBP panel of auditors. In the year ended August 31, 2021, the auditors have issued an unqualified opinion.

Management

Organizational Structure The Company has an experienced team. All managerial staff at the head office and factory report directly to the Directors.

Management Team Mr. Javed, the CEO and Board's Chairman, has been in the business for more than 25 years. Before the formal establishment of Al-Khair, Mr. Javed Iqbal, was associated with the family business of rice farming and trading.

Effectiveness Keeping in view the size and operations of the Company, management lacks effectiveness as there are no management committees in place. Thus, indicating a room for improvement.

MIS The Company has deployed ERP software from Oracle for internal disseminations. It plans to shift to SAP in the near future.

Control Environment Internal audit function is placed at Group level. Going forward, the Group plans to enhance its control environment through induction of additional individuals for Al-Khair primarily.

Business Risk

Industry Dynamics Rice is among the five major crops of Pakistan and is the second main staple food, after wheat. The segment contributes about 3.5% in agriculture value addition and 0.7% in GDP. Pakistan cultivates both basmati and non-basmati rice, most of which is exported. In Pakistan, rice is grown in most of the Sindh and Punjab Province. Sindh specializes in producing the long grains white rice IRRI-6 and IRRI-9, while Punjab produces world-class Basmati rice. Pakistan locally consumes Basmati Rice, which is a long, thin aromatic type of rice, considered premium and luxury category across the globe. Local consumption includes ~95% of basmati rice and ~5% non-basmati. The major players in rice exports include Pakistan, India, Thailand, and Vietnam. Pakistan is in direct competition with India, while Thailand and Vietnamese rice are considered premium. Thailand's 'Jasmine' rice has emerged lately as high-price premium rice. During FY21, rice cropped area increased to ~3.3mln hec (FY20: ~3mln hec), reflecting an increase of ~10%. This lead to an increased rice production by ~13% and stood at ~8.4mln MT (FY20: ~7.4mln MT). Out of this, around 3.5mln MT of rice is consumed locally. While, ~3.7mln MT is exported to generate ~ PKR 325bln of export revenue. The maximum contribution is from non-basmati rice (72%) exports, as basmati rice is locally consumed and minimal quantity (28%) is exported. During FY21, rice exports deteriorated to ~USD 2bln (FY20: ~USD 2.2bln) owing to the Indian strategy of dumping the commodity in international market at cheaper rates.

Relative Position Al-Khair's revenue is driven from sale of basmati rice.

Revenues The Company generates ~38% of revenue from rice exports and ~62% through local sales. Over the years, the Company's revenue stream remained stable, mainly being focused on local market for basmati rice. The Company makes sales through a well-defined distribution channel across Punjab. During Aug-21, revenue surged by 4x and clocked in at ~ PKR 2,305mln (Aug-20: ~ PKR 416mln) mainly supported by price. During Aug-20, the Company booked sales for three months only - May, Jun and Jul-20 - post incorporating as a private limited concern.

Margins Al-Khair has sanguine profitability margins; Gross profit margin is stable at 8% in Aug-21 (Aug-20: 9%), as high input costs were passed on to the consumers. Gross profit rose to PKR 181mln (Aug-20: PKR 36mln) as full year's profitability was reported during Aug-21, unlike during Aug-20. Operating margins reduced to 7% in Aug-21, from 8% in Aug-20, due to an increase in operating expenses (Aug-21: PKR 20mln, Aug-20: PKR 4mln), mostly freight expense. Net income rose to ~PKR 60mln in Aug-21 (Aug-20: ~ PKR 5mln) due to trickle down effect of gross profits. Similarly, net profit margin posted a surge (Aug-21: 3%, Aug-20: 1%).

Sustainability The Company has recently increased the production capacity of its existing operations to 25MT/hr. Materialization of projected revenue growth is essential considering the competitiveness of rice market. Going forward, the Company plans to expand its footings in the export market. Thus, working capital management remains pivotal.

Financial Risk

Working Capital Working capital needs are derived from receivables and inventory days while the cash conversion cycle is linked to rice seasonality. The Company procures paddy on cash and has a receivable cycle of 40 to 45 days. Net working capital days improved in Aug-21 to 136 days (Aug-20: 570 days) supported by lower inventory days (Aug-21: 109 days, Aug-20: 540 days) owing to better rice offtake. Early receipts also constituted short receivable days (Aug-21: 44 days, Aug-20: 76 days). The Company has a limited borrowing cushion. Going forward, the Company plans to expand its footings in the export market. thus, working capital cycle is expected to inflate.

Coverages Despite an increase in finance cost (Aug-21: PKR 72mln, Aug-20: PKR 25mln), interest coverage turned strong (Aug-21: 2.5x, Aug-20: 1.2x) as the Company managed to earn good profits. FCFO rose to PKR 169mln during Aug-21 (Aug-20: PKR 30mln) therefore reflecting strong coverages. Total and core coverage stood at 2.2x as at Aug-21 (Aug-20: 0.9x).

Capitalization The Company's business model is designed around securing short term borrowings to fuel working capital needs. Leveraging improved during Aug-21, moving to 49% (Aug-20: 78%). Total debt clocked in at PKR 835mln as at Aug-21 (Aug-20: PKR 634mln). Out of this, PKR 804mln (Aug-20: PKR 595mln) is short term, while PKR 31mln (Aug-20: PKR 41mln) is of long term nature.

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Financial Summary
PKR mln

Al-Khair Rice Mills Pvt. Limited	Nov-21	Aug-21	Aug-20
Rice	3M	12M	12M
A BALANCE SHEET			
1 Non-Current Assets	1,103	647	202
2 Investments	-	-	-
3 Related Party Exposure	-	-	-
4 Current Assets	1,544	1,211	782
a Inventories	*1,037*	*668*	*704*
b Trade Receivables	*494*	*508*	*52*
5 Total Assets	2,647	1,858	984
6 Current Liabilities	153	153	104
a Trade Payables	*110*	*116*	*94*
7 Borrowings	1,621	835	634
8 Related Party Exposure	-	-	41
9 Non-Current Liabilities	3	3	-
10 Net Assets	870	867	205
11 Shareholders' Equity	870	867	205
B INCOME STATEMENT			
1 Sales	667	2,305	416
a Cost of Good Sold	*(615)*	*(2,125)*	*(380)*
2 Gross Profit	52	181	36
a Operating Expenses	(5)	(20)	(4)
3 Operating Profit	47	160	32
a Non Operating Income or (Expense)	*(1)*	*(6)*	-
4 Profit or (Loss) before Interest and Tax	46	154	32
a Total Finance Cost	*(38)*	*(72)*	*(25)*
b Taxation	*(5)*	*(23)*	*(2)*
6 Net Income Or (Loss)	3	60	5
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	*67*	*169*	*30*
b Net Cash from Operating Activities before Working Capital	*34*	*97*	*6*
c Changes in Working Capital	*(355)*	*(386)*	*(655)*
1 Net Cash provided by Operating Activities	(320)	(289)	(649)
2 Net Cash (Used in) or Available From Investing Activities	(487)	(180)	(202)
3 Net Cash (Used in) or Available From Financing Activities	786	473	875
4 Net Cash generated or (Used) during the period	(22)	4	24
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	15.7%	454.8%	-74.2%
b Gross Profit Margin	7.7%	7.8%	8.6%
c Net Profit Margin	0.4%	2.6%	1.2%
d Cash Conversion Efficiency (FCFO adjusted for Working C	-43.1%	-9.4%	-150.3%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Te*	1.2%	11.2%	1.7%
2 Working Capital Management			
a Gross Working Capital (Average Days)	185	153	615
b Net Working Capital (Average Days)	170	136	570
c Current Ratio (Current Assets / Current Liabilities)	10.1	7.9	7.5
3 Coverages			
a EBITDA / Finance Cost	1.9	2.6	1.3
b FCFO / Finance Cost+CMLTB+Excess STB	1.7	2.2	0.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fi	4.0	0.3	13.3
4 Capital Structure			
a Total Borrowings / (Total Borrowings+Shareholders' Equit	65.1%	49.1%	76.7%
b Interest or Markup Payable (Days)	0.0	91.8	92.8
c Entity Average Borrowing Rate	12.0%	9.1%	4.2%

Credit Rating

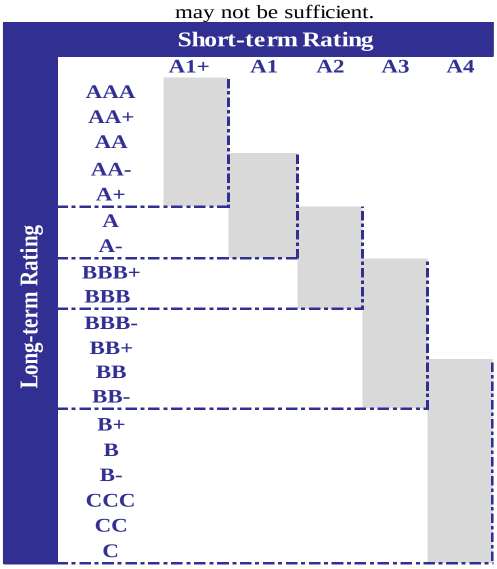
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**

i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)

Proprietary Information