RATING REPORT

Shakarganj Food Products Limited

REPORT DATE:
July 03, 2024

RATING ANALYSTS:
Afifa Khalid
afifa.khalid@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	BBB-	A-3	BBB-	A-3
Outlook/Rating Watch	Stable		Negative	
Rating Action	Maintained		Downgraded	
Rating Date	*03 Jul'24*		*18 Aug'23*	
Sukuk	BBB-		BBB+	
Outlook/Rating Watch	Stable		Positive	
Rating Action	Downgraded		Maintained	
Rating Date	*03 Jul'24*		*02 Mar'23*	

COMPANY INFORMATION

Incorporated in 2001	**External auditors:** BDO Ebrahim & Co., Chartered Accountants
	Chairman of the Board: Mr. Anjum M. Saleem **Chief Executive Officer:** Mr. Anjum M. Saleem
Public Limited (Unlisted) Company	
Key Shareholders (with stake 5% or more):	
Shakarganj Limited – 52.4%	
Bank Islami Pakistan Limited – 36.4%	
Crescent Steel and Allied Products Limited – 8.4%	

APPLICABLE METHODOLOGIES

VIS Entity Rating Criteria: Corporates
https://docs.vis.com.pk/docs/CorporateMethodology.pdf
Rating the Issue
https://docs.vis.com.pk/docs/Rating-the-Issue-Aug-2023.pdf
VIS Rating Scale
https://docs.vis.com.pk/docs/ratingscale.pdf

Shakarganj Food Products Limited

OVERVIEW OF THE INSTITUTION

Shakarganj Food Products Limited (SFPL) is an unlisted public limited company setup by initially acquiring a fruit juice concentrate plant from A.M. Fruits in 2005 and later acquiring a dairy facility from Dairy Crest Limited in 2006. Principal activity of SFPL involves manufacturing, processing and sale of food products including dairy, fruit pulps, and concentrate juices.

Profile of Chairman/CEO

Mr. Anjum M. Saleem is the Chairman/CEO of SFPL and carries over 30 years of international and local corporate management experience. Mr. Anjum is a qualified Chartered Accountant from ICAEW (Institute of Chartered Accountants, England & Wales).

RATING RATIONALE

Shakarganj Food Products Limited ('SFPL' or 'the Company') is a subsidiary of Shakarganj Mills Limited (SML), with 52.4% shareholding, an associate of BankIslami Pakistan Limited and also has Crescent Steel & Allied Products Limited as a minority shareholder, forming an adequate sponsorship profile. The Company has a moderate business risk environment underpinned by in-elastic demand of milk and related products. However, competition has remained intense to grab market share amongst producers of packaged milk and related products. Moreover, the industry margins have remained sensitive to exchange rate risk and price risk pertaining to imported skimmed milk powder and edible oils. The Company has encountered low-capacity utilization in FY23 and onwards.

Rating Drivers

The packaged milk industry in Pakistan faces intense competition, even though it accounts for around 10% of the overall milk consumption. Untapped loose milk market represents significant growth opportunity for the packaged milk industry players.

The milk industry in Pakistan can be divided into two main segments: loose milk and processed milk. Loose milk accounts for approximately 90% of the market, while processed milk has a relatively low penetration rate of only 10%. In comparison to neighboring countries like India (14%) and Bangladesh (20%), the adoption of processed milk in Pakistan is relatively lower. However, there has been a gradual shift towards packaged milk in recent years, indicating a changing trend. The untapped market for loose milk presents a significant growth opportunity for companies operating in the packaged milk industry, driven by increasing consumer awareness regarding food quality. However, packaged milk companies face challenges, including consumer preference for loose milk and the additional costs associated with processing, transportation, and distributor margins. The demand for milk follows a seasonal pattern, with flush and lean periods occurring in the first and second halves of the year respectively. Despite this, the demand for milk shows low elasticity and remains relatively stable. Factors such as urbanization, an untapped market with significant growth prospects, favorable regulatory policies, and a rising middle class contribute to the increasing demand for packaged milk. Enforcing significant regulatory changes, such as implementing minimum pasteurization laws, could potentially address industry challenges more effectively. VIS is of the opinion that the advantages stemming from marketing initiatives will become evident over the medium to long duration.

Financial Performance

Despite higher prices, revenue decreased on account of lower volumetric sales. However, margins and profitability increased in FY23

Net sales decreased in FY23 and 1HFY24 owing to lower demand for products. Gross margins increased to 17.0% (FY22: 13.6%) in FY23, due to focus on high margin products. With decrease in sales promotion and advertisement expense, operating profit increased considerably in FY23. PBT stood significantly higher at Rs. 733m (FY22: Rs. 72m). However, with higher tax incidence mainly due to the impact of deferred taxation, net profit increased to Rs. 167m (FY22: Rs. 123m) in FY23. Net sales decreased to Rs. 7.3b (1HFY23: Rs. 9.1b) in 1HFY24. Gross margins stood lower at 13.7% which resulted in decrease in net profit to Rs. 118m (1HFY23: Rs. 278m) despite reduced operating expenses.

Coverages improved though liquidity in terms of current ratio is still inadequate

In FY23, FFO improved to Rs. 885m (FY22: Rs. 193m). With higher FFO, the DSCR improved to 1.78 x (FY22: 0.75x) in FY23. FFO to total debt and long-term debt also improved. The current ratio, though improved to 0.8x (FY22: 0.5x), still remained below the minimum threshold. Based on sensitized projections, coverages are projected to remain adequate and current ratio is projected to improve gradually. Additionally, SFPL has generated cash flows, through sale of assets held for sale and other operating assets, amounting to Rs. 506m in FY23. Further assets amounting Rs. 268m were sold in 1HFY24, and others assets worth Rs. 644m were specifically held for sale, projected to be sold within the ongoing year.

Improving trend in capital structure.
The equity base (excluding surplus on revaluation) stood at Rs. 2.9b (FY23: Rs. 2.7b; FY22: Rs. 2.4b) at end-1HFY24 on the back of profit retention. The company's debt structure is a mix of both long and short-term borrowings. With effective management of working capital, short-term debt has remained range bound. The long-term debt has been decreasing on a timeline basis. Debt leverage improved, though remain high at 2.5x (FY23: 2.6x; FY22: 3x) at end-1HFY24 mainly due to high trade payables. However, with lower total amount of outstanding borrowings, gearing has improved further while remaining low at 0.39x (FY23: 0.48; FY22: 0.71x) at end-1HFY24.

Sukuk Restructuring and Payments
Rated, secured, privately placed, shariah compliant sukuk certificates of PKR 725m were issued in July 2018 for a tenor of 6 year, with quarterly principal buy-out & rental payments, inclusive of 1 year grace period for buy-out payments. The Investment Agent acted as a trustee to the beneficiaries/sukuk certificate holders. The Company had requested a one-year deferral during Covid-19, on the basis of relaxations given by the SBP & SECP to give businesses relief after unprecedented damage caused to the economy. SFPL continued its obligations after the deferral and had been repaying its quarterly obligations since 10th July, 2021.

SFPL, due to volatile macro-economic conditions and its implications, has been facing liquidity challenges. Due to these issues, SFPL entered into a restructuring /re-profiling of the outstanding Sukuk. The Trustee, Pak Oman has informed VIS in writing that initially in March 2023, the Company submitted a restructuring request to the lenders. The request involved the deferral of principal payments for a duration of one year, beginning from the 19th redemption i.e., April 10, 2023, and an extension in the tenor of the Sukuk for a corresponding period. After the request was circulated to investors, a meeting was held on April 5, 2023, wherein investors recommended that SFPL settle its principal payment for the 19th redemption i.e. Rs. 36.25m, and agreed to consider the restructuring request for a one-year deferment starting from the 20th redemption i.e., July 10, 2023, onwards, for the remaining buy-out payments amounting to Rs. 326.25m

SFPL settled the principal payments to all investors with delay for the 19th redemption, and submitted a revised restructuring request for the deferral of principal payments for one year beginning from the 20th redemption. The profit component for the 20th redemption had been settled by the Company, while principal had been part of the restructuring request as in principally agreed by the lenders. All investors confirmed their approvals for the principal deferment for one year, namely Al Meezan Investments, Faysal Funds, Dawood Family Takaful Limited, Pak Libya Holding Company, NBP Funds and PAIR Investment Company Limited. Following the agreement, SFPL has been repaying the profit amount every quarter while the sukuk redemptions were deferred till 10th July. 2024. FFO for FY25 is projected at Rs. 427m while its Rs. 546m for FY26; the annual repayment of sukuk due in FY25 & FY26 is Rs. 145m & Rs. 108.75m per annum, respectively. The *(sensitized)* projections of the company have depicted sufficient cash flows to cover the remaining sukuk repayments in a timely manner.

Shakarganj Food Products Limited — Annexure I

Financial Statements *(Amount in Million)*

BALANCE SHEET	FY21	FY22	FY23	1HFY24
Non Current Assets	7,774	7,572	5,932	5,754
Store and Spare Parts	194	220	248	278
Stock in Trade	1,608	1,028	707	892
Trade Debts	137	158	78	94
Loans and Advances	80	49	64	73
Tax refunds due from Government	384	1,434	2,425	2,904
Cash & Bank Balances	282	47	70	56
Other Assets	27	197	810	666
Total Assets	**10,485**	**10,705**	**10,335**	**10,717**
Trade and Other Payables	4,089	4,000	3,624	4,056
Short Term Borrowings	349	450	352	333
Long-Term Borrowings *(Inc. current matur)*	1,648	1,244	929	775
Total Borrowings	1,998	1,694	1,281	1,108
Retirement Benefit	336	392	392	412
Contract Liabilities	844	1,017	938	926
Other Liabilities	57	95	548	500
Total Liabilities	**7,324**	**7,197**	**6,783**	**7,002**
Tier-1 Equity	2,227	2,376	2,656	2,857
Total Equity	**3,161**	**3,508**	**3,553**	**3,715**
Paid-Up Capital	1,676	1,676	1,676	1,676

INCOME STATEMENT	FY21	FY22	FY23	1HFY24
Net Sales	18,024	18,027	15,069	7,267
Gross Profit	2,353	2,448	2,566	999
Operating Expenses	1,763	2,019	1,524	716
Profit from Operations	619	470	1,140	386
Finance Charges	319	398	407	201
Profit/(Loss) Before Tax	300	72	733	185
Profit/(Loss) After Tax	124	123	167	118
FFO	562	193	885	165

RATIO ANALYSIS	FY21	FY22	FY23	1HFY24
Gross Margin (%)	13.1	13.6	17.0	13.7

Net Margin (%)	0.7	0.7	1.1	1.6
FFO to Long-Term Debt	0.34	0.16	0.95	0.21
FFO to Total Debt	0.28	0.11	0.69	0.15
Debt Servicing Coverage Ratio (x)	1.38	0.75	1.78	1.10
Interest Coverage	1.94	1.18	2.80	1.92
Gearing (x)	0.90	0.71	0.48	0.39
Debt Leverage (x)	3.3	3.0	2.6	2.5
Current Ratio	0.5	0.5	0.8	0.8
Cash Conversion Cycle	(60)	(61)	(83)	(86)

REGULATORY DISCLOSURES Annexure II

Name of Rated Entity	Shakarganj Food Products Limited
Sector	Consumer Goods
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Outlook / Rating Watch	Rating Action
		RATING TYPE: ENTITY		
Jul 03, 24	**BBB-**	**A-3**	**Stable**	**Maintained**
Aug 18, 23	BBB-	A-3	Negative	Downgrade
Mar 02, '23	BBB+	A-2	Positive	Upgrade
Jan 04, '22	BBB+	A-3	Stable	Maintained
Nov 23, '20	BBB+	A-3	Negative	Downgrade
July 18, '19	A-	A-2	Stable	Reaffirmed
Mar 20, '18	A-	A-2	Stable	Initial
		RATING: SUKUK		
Jul 03, 24	**BBB-**		**Stable**	**Downgraded**
Aug 18, 23		Suspended		
Mar 02, '23	BBB+		Positive	Maintained
Jan 04, '22	BBB+		Stable	Maintained
Nov 23, '20	BBB+		Negative	Downgrade
July 18, '19	A		Stable	Final
Mar 20,'18	A		Stable	Preliminary

Instrument Structure	The Sukuk certificates amounted to Rs. 725m at the time of issue, with a tenor of 6 years including 1-year grace period, repayable in 20 quarterly installments of principal and respective quarterly rental payments till the end of tenor. The facility has been secured by first pari passu charge over moveable & immovable fixed assets of the company with 25% profit rate plus margins or other security mutually agreed on pr as advised by the legal counsel. A deferral of one year was granted in line with SBP & SECP's relaxations for businesses during Covid-19. A second deferral of one year was granted after the 19th redemption. At present, a principal buy-out of Rs. 398.75m has taken place and 9 quarterly installments of Rs. 36.25m each are remaining, amounting to Rs. 326.25m.
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

Name	Designation	Date
n/a		