RATING REPORT

Tahir Omer Industries Limited (TOIL)

REPORT DATE:
December 11, 2018

RATING ANALYSTS:
Maimoon Rasheed
maimoon@jcrvis.com.pk

Syed Fahim Haider Shah
fahim.haider@jcrvis.com.pk

RATING DETAILS		
	Initial Rating	
Rating Category	**Long-term**	**Short-term**
Entity	A-	A-2
Rating Outlook	*Stable*	
Rating Action	Initial	
Rating Date	*December 11th.'18*	

COMPANY INFORMATION	
Incorporated in 1992	External auditors: Kamran & Co. Chartered Accountants
Public Limited Company – Unquoted	Chairman of the Board/CEO: Rana Iqbal Hussain
Key Shareholders (with stake 5% or more):	
Rana Iqbal Hussain – 33.33%	
Rana Tahir Iqbal – 33.33%	
Rana Omer Iqbal – 33.33%	

APPLICABLE METHODOLOGY(IES)
JCR-VIS Entity Rating Criteria: Industrial Corporates (May 2016)
http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf

Tahir Omer Industries Limited

OVERVIEW OF THE INSTITUTION

Tahir Omer Industries Limited (TOIL) was incorporated in July 1992 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). TOIL is the flagship company of Khalis Group which is considered as one of the major players in the edible oils industry of Pakistan. TOIL is mainly involved in the manufacturing and sale of vegetable ghee, cooking oil and meal products.

Profile of the Chairman/CEO

Rana Iqbal Hussain is the founder of Khalis Group and serves as the Chairman of BoD and Chief Executive Officer of the company. He has over 26 years of experience in edible oils sector.

Financial Snapshot

Total Equity: end-FY18: Rs. 5.4b; end-FY17: Rs. 4.6b; end-FY16: Rs. 3.5b

Assets: end-FY18: Rs. 20.2b; end-FY17: Rs. 14.5b; end-FY16: Rs. 10.7b

Profit After Tax: FY18: Rs. 677m; FY17: Rs. 1.0b; FY16: Rs. 524m

RATING RATIONALE

Tahir Omer Industry Limited (TOIL) is one of the largest players in the edible oil industry of Pakistan and is a part of Khalis Group. Shareholding holding of the company is vested with Mr. Rana Iqbal Hussain & family, who have over 26 years of industry experience. The assigned ratings take into account sizeable oilseed crushing, extraction & refining operations and established business relations with the large institutional clients operating in the edible oil and poultry feed industries. The business risk profile of TOIL is underpinned by positive demand dynamics of the said industries, a diverse range of products, and expansion of oilseed crushing operations in the recent years, resulting in sustained growth in sales and largely stable profit margins. The ratings also factor in relatively sound liquidity position and adequate debt service coverage ratios, albeit recent increase in leverage indicators. However, the ratings are constrained by strong competition and inherently low margins, regulatory duties, and increased susceptibility to risk of disease outbreaks in the poultry industry, a major buyer. The corporate governance framework has room for improvement.

<u>Key Rating Drivers:</u>

Industry dynamics
The edible oil industry of Pakistan is highly fragmented and competitive due to low barriers to entry, leading to limited pricing power and inherently low profit margins. The industry is prone to many risk factors that emanate from price volatility, regulatory uncertainties, and timely availability of raw material. Domestic consumption of edible oils is largely dependent on import of raw materials, and hence exposes the industry to global demand-supply dynamics. However, the demand dynamics remain positive as consumption of edible oils has increased at a 3-year CAGR of around 3% and reached 4.52m tons in FY18. Supported by positive demographic factors, the demand is expected to increase in line with the GDP over medium to long-term period.

Making a strategic shift to attain higher growth
TOIL mainly follows a business to business model (B2B) model with sales emanating from three strategic business units; branded vanaspati ghee and cooking oil, bulk crude edible oil, and oilseed meal. With the augmentation of solvent extraction capabilities, TOIL has shifted its focus from highly competitive branded ghee & cooking oil segment to oilseed meal and bulk crude edible oil over the past few years. This strategic shift has helped TOIL attain 26% compounded annual growth in sales as the demand for oilseed cakes and meals from poultry feed mills has been increasing by 10% – 12% per annum. During FY18, sales contribution of oilseed meal and bulk crude edible oil segments increased on the back of higher capacity utilization of solvent extraction unit. However, branded ghee and oil business fetched slightly higher margins despite lower sales contribution of 30%. Going forward, sales mix is expected to remain largely dependent on the business dynamics of poultry industry.

Sales growth being driven by higher volumes
The company has been able to achieve continuous growth in sales during last few year. During FY18, TOIL recorded 12% increase in net sales on the back of a sizeable growth in volumetric sales of oilseed meal and bulk crude edible oil. In line with the industry practice, TOIL has increased the selling price to mitigate devaluation of rupee. Gross margins improved slightly on the back of higher selling prices of ghee and cooking oil in the branded and bulk markets, whilst prices of oilseed meal decreased marginally as the poultry industry remained under pressure during the year. The positive impact of notable growth in sales and gross profits was offset by considerably higher charity & donation, finance cost, and tax expense during the year, resulting in lower profit after tax for FY18. Going forward, sales growth momentum may slow down as the company has already attained 90% capacity utilization at its solvent extraction unit.

Relatively sound liquidity and adequate capacity to meet financial obligations
Funds from operations (FFO) were recorded notably higher on the back of slightly improved cash flows before working capital changes and a net tax benefit. The net tax benefit ensued from a higher refund received/adjusted against income tax recoverable during the year. With minimal burden of long-term financing and significantly higher cash flows, FFO to total debt improved to 0.13x (FY17: 0.08x; FY16: 0.10x) despite considerably higher utilization of short-term borrowings during the year. The debt service

coverage also improved to 3.2x (FY17: 2.3x; FY16: 2.6x) during FY18. This along with consistently sufficient current ratio, overall liquidity and cash flows position of TOIL is considered relatively stronger than peers.

Increased gearing due to elevated working capital requirements

The core equity base of TOIL augmented to Rs. 5.4b with continued retention of profits, while long-term debt decreased to Rs. 24m by end-FY18 on account of scheduled repayments. However, the outstanding balance of short-term borrowings increased to Rs. 12.6b (FY17: Rs. 8.5b; FY16: Rs. 5.8b) on account of higher working capital requirements, stemming from recent devaluation of rupee and clustered shipments of raw material inventory received; as per management volatile sea conditions resulted in some changes in shipment timings. Consequently, gearing and debt leverage indicators stood higher at 2.36x and 2.57x, respectively, (FY17: 1.86x and 2.0x; FY16: 1.68x and 1.83x) by end-FY18. Given no major expansion plan in sight, the company doesn't plan to raise a new long-term debt or inject fresh equity. However, gearing may improve with the accumulation of profits and settlement of outstanding L/Cs.

Corporate governance framework needs improvements

The Board of Directors of the company comprises three members; all are the members of sponsoring family. The senior management team is well-equipped with the industry knowledge and experience and has depicted stability. Microsoft Dynamics-based ERP platform with integrated modules is considered adequate for the management reporting.

Tahir Omer Industries Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	June 30, 2016	June 30, 2017	June 30, 2018
Non-Current Assets	1,912	2,151	2,929
Stores, Spares. And Loose Tools	56	114	151
Stock-in-Trade	2,380	2,485	6,363
Trade Debts	4,122	6,524	7,974
Tax Refund Due From The Government	1,605	2,485	1,953
Cash & Bank Balances	540	619	607
Other Assets	37	78	266
Total Assets	**10,652**	**14,456**	**20,243**
Trade and Other Payables	158	272	417
Short-Term Borrowings	5,806	8,476	12,616
Long-Term Borrowings *(Inc. current matur)*	99	74	24
Deferred Taxation	299	276	554
Other Liabilities	65	97	140
Total Liabilities	6,427	9,195	13,751
Tier-1 Equity	**3,518**	**4,587**	**5,355**
Total Equity	4,226	5,261	6,492
INCOME STATEMENT	June 30, 2016	June 30, 2017	June 30, 2018
Net Sales	27,553	38,783	43,505
Gross Profit	1,716	2,321	2,689
Operating Expenses	402	516	766
Finance Cost	377	504	709
Profit Before Tax	938	1,304	1,223
Profit After Tax	524	1,031	677
FFO	566	682	1,626
RATIO ANALYSIS	June 30, 2016	June 30, 2017	June 30, 2018
Gross Margin (%)	6.2%	6.0%	6.2%
Net Margin (%)	1.9%	2.7%	1.6%
Net Working Capital	2,696	3,447	4,158
FFO to Long-Term Debt	5.7	9.3	67.1
FFO to Total Debt	0.10	0.08	0.13
Debt Servicing Coverage Ratio (x)	2.6	2.3	3.2
ROAA (%)	-	8.2%	3.9%
ROAE (%)	-	21.7%	11.5%
Gearing (x)	1.68	1.86	2.36
Debt Leverage (x)	1.83	2.00	2.57
Current Ratio	1.45	1.39	1.32

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix II

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: JCR-VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.jcrvis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. www.jcrvis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES	**Appendix III**
Name of Rated Entity	Tahir Omer Industries Limited
Sector	Consumer Goods
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	
Instrument Structure	N/A
Statement by the Rating Team	JCR-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	JCR-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, JCR-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. JCR-VIS is not an NRSRO and its ratings are not NRSRO credit ratings. Copyright 2018 JCR-VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to JCR-VIS.

Rating History:

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
11/12/2018	A-	A-2	Stable	Initial