RATING REPORT

Dairyland (Private) Limited (DPL)

REPORT DATE:
February 19, 2021

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook	Stable		Stable	
Rating Date	*February 19, 2021*		*October 15, 2019*	

COMPANY INFORMATION

Incorporated in February 2009	**External auditors:** Munaf Yusuf & Co. Chartered Accountants
Private Limited Company	**Chairman of the Board:** Mr. Javed Akhtar
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Sulaiman Monoo
Akhtar Textile (Pvt.) Limited – 45.9%	
Rainbow Textiles – 19.7%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (May 2019)
https://www.vis.com.pk/kc-meth.aspx

Dairyland (Private) Limited (DPL)

OVERVIEW OF THE INSTITUTION

Dairyland (Pvt.) Limited was incorporated in February 2009 as a Private Limited Company. The registered office of the company is located in Karachi. The company is a part of Akhtar Group of Companies

Akhtar Group of companies includes Dairyland Private Limited, ACT Wind Private Limited, Indigo Textile Private Limited, Akhtar & Sons and Rainbow Jordan

RATING RATIONALE

Dairyland (Private) Limited (DPL) is engaged in manufacturing and sales of dairy products, especially processed milk. The company is a part of Akhtar Group of Companies with majority shareholding vested with Akhtar Textile (Pvt.) Limited (45.9%) and Rainbow Textiles (19.7%). The company has developed a comprehensive value chain ranging from its own farm containing livestock for milk production to the final packaged products for the end-consumer. As per management, no human interaction is involved during the milk collection and processing. The company owns one farm which is located in Dhabeji, Karachi. Currently, the company has a herd of approximately 4,589 Australian cows for milk production. DPL deals under the brand name of 'Dayfresh' with a product portfolio encompassing Homogenized & Pasteurized milk, UHT Milk, Flavored Milk, Tea Whitener, Yogurt Raita, and Cheese & Eggs. DPL plans to launch six new products in FY21-FY22.

DPL has eight branded shops in Karachi, which offer the company's products via home delivery services to the customers. The company also has distribution arrangements with nine other major distributors through which its products are supplied to more than 4,000 shops in five major cities in the country. The third distribution channel encompasses B2B sales with the last channel being exports. The company exported a limited quantity to USA and Afghanistan in the outgoing year.

Capacity utilization

Details of Machinery	Function of Machinery	Production Capacity	Capacity Utilization				
			1H21	2020	2019	2018	2017
Milk Processing Plant	Milk Processing	5000 Liters per hour	59%	53%	50%	40%	35%
Bottle Filler (Filling & Capping Machine)	Milk Filling and Packing	1200 Bottles per hour	51%	38%	25%	19%	19%
Prepack click (Packing Machine)	Milk Filling and Packing	1800 Liters per hour	34%	34%	18%	14%	14%
Prepack Machine	Milk Filling and Packing	1800 Liters per hour	34%	37%	20%	14%	14%
Tetra Mik UHT Plant	Milk Processing	5000 Liters per hour	60%	60%	58%	25%	25%
Tetra Pack Filling Machine	Milk Filling and Packing	8000 Packs per hour	34%	33%	31%	16%	30%
Tetra Pack Filling Machine	Milk Filling and Packing	9000 Packs per hour	68%	68%	67%	44%	-
TBA19 - Filling line	Milk Filling and Packing	7500 Packs per hour	61%	61%	61%	-	-
Eggs	Birds	Per Year	77%	93%	64%	78%	0%
MilkyLab Cheese Plant	Processing & Packing	1800 KG Per Day	45.8%	45.8%	40.0%	-	-

As per management, capacity utilization is on the lower side because the processing and packaging capacity is higher than the milk production capacity. This was a deliberate decision on the part of management to invest in processing and packaging facilities keeping in view future demand. Management will gradually increase the milk production capacity in line with growth in demand.

Rating Drivers

Business risk is characterized by significant competition in the packaged milk industry, which comprises only one-tenth of the overall milk consumption in Pakistan. Loose milk constitutes around 91% of the total milk consumption in the country. Untapped loose milk market represents significant growth opportunity for the packaged milk industry players. Business risk profile of DPL is supported by strong brand equity and diversification into other dairy variants among which flavored milk has gained significant growth over the past few years

Milk industry in Pakistan can be broadly segregated into two segments: loose milk and processed milk. Loose milk constitutes around 91% of the overall market while penetration of processed milk is only 9%. Processed milk penetration in Pakistan is considered to be on the lower side compared to the regional peers such as India (14%), and Bangladesh (20%). Due to increase in awareness on importance of greater food quality, there is a huge potential for packaged milk in the industry. However, the main challenges faced by the packaged milk players include consumer's favorable perception towards loose milk and additional costs (transportation, processing and distributor margin) added to packaged milk operations.

Demand for milk is seasonal, with the flush and the lean period, which occur in the first and second half of the year, respectively. However, due to low elasticity demand for milk is non-cyclical. Increasing urbanization, under-penetrated milk market with great upside potential, favorable laws introduced by regulatory authorities and rising middle class contribute to the uprising aggregate demand for packaged milk. However, the key business risks include regulatory risk and the challenge of changing perceptions. VIS believes that benefits of marketing campaigns will be reflected in the medium to long term and there is no quick solution for changing perception in the short run unless significant regulatory changes such as minimum pasteurization law are enforced.

Sales revenue of DPL has depicted double-digit growth during FY20 on account of both price and volumetric increase along with geographical diversification and addition of new products in the product portfolio. Going forward, management plans to focus on premium products that contribute higher margin.

Net sales increased to Rs. 2.6b (FY19: Rs. 2.1b) on account of volumetric growth along with higher average prices. Introduction of the tea whitener product line coupled with diversification in the product portfolio through launch of lactose free milk have also contributed to growth in topline of the company. As per management, an increasing inclination of consumers to opt for healthier beverages has contributed to sizeable growth in the flavored milk sales. In FY20, DPL carried out geographical diversification by launching exports to USA & Afghanistan. Despite challenges faced due to the global pandemic disrupting supply chain operations whereby B2B segment and exports were hampered, DPL was still able to register growth in revenue since it is engaged in the supply of essential products. Going forward, management plans to focus on premium products that contribute higher margin. The following figure depicts the product mix of the company:

Sales Mix	FY19	FY20
Processed Milk	39.4%	30.7%
Raw Milk	4.7%	5.5%
Yoghurt	2.7%	1.9%
Flavored Milk	44.1%	36.0%
Cheese	3.9%	10.8%
Tea Whitener	0.0%	7.5%
Eggs	5.2%	6.4%
Export	0.0%	1.2%
Gross Sales	**2,200.14**	**2,670.34**

Gross Margins of the company have remained stable during the last three years as any increase in prices of raw materials was transferred in the form of higher product prices. Selling and distribution expenses have slightly increased (FY20: Rs. 394.7m; FY19: Rs.363.3m) primarily on account of higher promotion expenses and higher salaries and wages. Finance costs have registered an increase (FY20: Rs. 140.7m; FY19: Rs. 90.8m) during FY20 on account higher quantum of debt drawdown to fund capex requirements and to finance working capital needs. Despite increase in finance costs and operating costs, net margin remained stable at 4.0% (FY19: 4.0%) in FY20. Going forward, management expects topline to register sizeable growth due to increase in market penetration and focus towards value-added products. Management expects gross margins to remain at current levels since the company has carried out revaluation of assets, higher depreciation charge of which shall offset the impact of increase in sales revenue. Moreover, selling and distribution expenses are expected to grow but at a slower pace as the company has already incurred sizeable capex on developing the infrastructure.

Liquidity profile has witnessed improvement and is considered adequate

Liquidity profile of the company has improved during FY20 with adequate coverage of cash flows in relation to outstanding obligations, manageable ageing of trade debts and sound debt servicing ability. In line with increase in profitability, Funds from Operations (FFO) has also improved on a timeline basis. FFO amounted to Rs. 403.7m (FY19: Rs. 294.1m) in FY20. Cash flow coverages in relation to outstanding obligations is considered adequate as indicated by debt servicing coverage ratio of 1.5x (FY19: 1.0x) in FY20. FFO in relation to long term debt and FFO in relation to total debt were reported slightly lower at 47.8% (FY19: 49.6%) and 27.0% (FY19: 28.2%), respectively due to increase in quantum of debt drawdown. Stock in trade and trade debts provide adequate coverage for short term borrowings, while current ratio is also considered satisfactory as it remained at 1.0x at end FY20. Going forward, with projected growth in profitability of the company and planned cash flow management, liquidity indicators are also expected to improve.

Leverage indicators have depicted a slight increase during FY20 primarily on account of capex requirement and working capital needs; however the same are expected to remain within manageable levels due to projected growth in profitability and sponsor support.

Equity base of the company has increased over the last three years primarily on account of injection of interest free loan coupled with profit retention. Sponsor has continued to inject interest free loan (FY20: Rs. 4.8b; FY19: Rs. 4.4b) which is convertible into ordinary shares of the company at the discretion of the management. As total debt escalated more in relation to the improvement in equity, both leverage (FY20:0.52; FY19:0.40) and gearing levels (FY20: 0.26; FY19: 0.20) have slightly increased. Debt levels increased to finance working capital requirements and capital expenditures. Although leverage indicators have depicted a slight increase in FY20 primarily on account of capex requirement but are expected to remain within manageable levels due to projected growth in profitability and sponsor support.

Corporate governance framework is adequate but depicts room for further improvement

Board and management's oversight of operations is considered thorough with detailed discussion conducted on every aspect of the business during the meetings. Management team comprises of seasoned professionals and a management committee has been established which meets on a monthly basis. However, formalization of board and management committee meeting minutes may be undertaken to ensure greater transparency. In line with best practices, management may consider inclusion of independent directors on the board. Furthermore, establishment of a separate and independent internal audit in line with management plans is also considered important from governance perspective.

Dairyland (Pvt.) Limited

Appendix I

FINANCIAL SUMMARY (Amounts in PKR millions)			
BALANCE SHEET	**FY18**	**FY19**	**FY20**
Non-Current Assets	5,379.0	6,519.1	8,636.3
Stock-in-Trade	680.8	878.1	885.2
Trade Debts	78.6	128.6	143.7
Biological assets held for sale	28.0	33.7	40.5
Cash & Bank Balances	4.4	4.6	8.2
Total Assets	6,523.0	8,038.4	10,349.5
Trade and Other Payables	371.6	691.7	597.2
Short Term Debt	400.7	449.3	648.8
Long Term Debt	810.7	592.4	844.5
Total Debt	1,211.4	1,041.7	1,493.3
Total Liabilities	1,759.9	2,060.9	2,962.1
Total Equity (excluding revaluation surplus)	3,889.5	5,197.0	5,730.9
Total Equity (including revaluation surplus)	4,763.1	5,977.5	7,387.3
Paid-up Capital	436.0	436.0	436.0
INCOME STATEMENT			
Net Sales	1,517.4	2,106.4	2,558.4
Cost of Sales	1,075.4	1,491.3	1,837.5
Gross Profit	442.1	615.1	720.9
Selling and Distribution Expenses	(223.2)	(363.3)	(394.7)
Administrative Expenses	(75.8)	(74.2)	(79.6)
Operating Profit	143.1	177.6	246.6
Finance Cost	(78.4)	(90.8)	(140.7)
Profit before Tax	29.6	57.5	83.7
Profit After Tax	29.6	36.1	63.4
Gain on revaluation of biological assets	43.5	47.3	38.0
Net Profit	73.1	83.4	101.4
RATIO ANALYSIS			
Gross Margin (%)	29.1%	29.2%	28.2%
Net Margin	4.8%	4.0%	4.0%
Net Working Capital	44.4	124.4	0.4
Trade debts/Sales	5.2%	6.1%	5.6%
FFO	259.0	294.1	403.7
FFO to Total Debt (%)	21.4%	28.2%	27.0%
FFO to Long Term Debt (%)	32.0%	49.6%	47.8%
Current Ratio (x)	1.04	1.09	1.00
Debt Servicing Coverage Ratio (x)	1.18	0.96	1.46
Gearing (x)	0.31	0.20	0.26
Leverage (x)	0.45	0.40	0.52
(Stock in Trade+Trade Debts)/STD	190%	224%	159%
ROAA (%)	1.2%	1.1%	1.1%
ROAE (%)	2.2%	1.8%	1.9%

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: 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.vis.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.vis.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.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'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.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when 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	Dairyland (Private) Limited
Sector	Dairy
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
Feb-19-2021	A-	A-2	Stable	Reaffirmed
Oct-15-2019	A-	A-2	Stable	Initial

Instrument Structure	N/A
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.
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Due Diligence Meetings	

Name	Designation	Date
Muhammad Siraj	Manager Finance	21-Jan-2021
Shoaib-ur-Rehman	Deputy Manager	21-Jan-2021