RATING REPORT

Kausar Ghee Mills (Pvt.) Limited (KGML)

REPORT DATE:
July 04, 2022

RATING ANALYSTS:
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RATING DETAILS				
	Latest Ratings		Previous Ratings Before Suspension	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2	A-	A-2
Rating Date	*July 04, 2022*		*September 09, 2020*	
Rating Action	Reaffirmed		Initial	
Rating Outlook	*Stable*		*Stable*	

COMPANY INFORMATION	
Incorporated in 1992	External auditors: A. Aziz Chaudary & Co. Chartered Accountants
Private Limited Company	CEO: Mr. Zahid Ali Malik
Key Shareholders (with stake 5% or more):	
Sajid Ali Malik – 20.7%	
Zahid Ali Malik – 19.9%	
Malik Attique Ahmad – 18.8%	
Hamid Ali Malik – 16.5%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (August 2021) **https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf**

Kausar Ghee Mills (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Kausar Ghee Mills (Pvt.) Limited (KGML) was established in 1992. The company is involved in the manufacturing of Vegetable Ghee, Cooking Oil, and allied products.

Profile of the Chairman/CEO

Mr. Zahid Ali Malik serves as the Chairman and CEO, he is an engineer by profession and has been involved with the company for over 5 decades.

RATING RATIONALE

The ratings assigned to Kausar Ghee Mills (pvt.) Limited (KGML) take into account its association with Kausar Group of Companies, having business stake in various sectors involving edible oils, poultry, poultry feed, and rice processing. The assigned ratings reflect stable business model, growing equity base and sound liquidity profile. The ratings incorporate growth in revenues in the last three years, ongoing capex to enhance efficiency in the operations, projected improvement in financial profile post efficiency enhancement initiatives and stable demand prospects for edible oil in the domestic market.

Furthermore, ratings draw comfort from integrated production facility, well established distribution network, brand recognition in the local market and vertical integration with group owned feed mill. KGML's conservative capital structure as evident from minimal reliance on credit financing coupled with sound coverages is a key rating driver. However, the ratings remain sensitive to highly price sensitive import market of raw material.

Impact of COVID-19 pandemic has remained minimal on the financial risk profile of the company given its presence in relatively inelastic consumer goods sector catering to day to day food based requirements of the population. Nevertheless, ratings will remain dependent on the company's ability to improve margins, maintain scale of operations and leverage indicators at current levels.

Integrated manufacturing facility

The company was established by late Malik Mubarak Ali with its first production unit of vegetable ghee and edible oils processing in Gujranwala in 1992. Later in line with growth objectives, the company added a solvent plant in Karachi at Port Bin Qasim. The commercial production of edible oils including canola, soya, sunflower and blended cooking oil was started in 2014. At end-June'21, installed capacity and relevant utilization levels are elaborated in the table below:

Capacity in MT	FY20			FY21		
	Installed Capacity	Actual Production	Utilization	Installed Capacity	Actual Production	Utilization
Ghee Plant, Gujranwala						
Ghee	57,600	30,103	52%	57,600	35,069	61%
Cooking Oil	24,900	3,355	13%	24,900	2,301	9%
	82,500	**33,458**	**41%**	**82,500**	**37,370**	**45%**
Solvent and Physical Refinery Plant, Karachi						
Seed Crushing	120,000	109,059	91%	120,000	107,110	89%
Cooking Oil	75,000	17,732	24%	75,000	21,510	29%
	195,000	**126,791**	**65%**	**195,000**	**128,620**	**66%**
Ghee Plant Karachi						
Ghee	75,000	12,887	17%	75,000	10,560	14%

The company is marketing its products nationwide through around 200 distributors and dealers covering 3 provinces and 400 towns. The company also possesses an in-house sales team of 50 people. KGML is a family owned business concern, the Board of Directors comprise eight directors all being members of the sponsoring family. Mr. Zahid Ali Malik serves as the CEO, he is an engineer by profession and has been involved with the company for over 5 decades. Other group companies include Kausar Feed Mills (pvt.) Limited (KFML), Kausar Rice and General Mills (KRGML) and Kausar Farms.

Business model and power mix

Given the presence of the company in the edible oil industry, the business model is highly import dependent. The raw material for vegetable ghee including crude palm oil, palm olein and RBD palm oil is imported from Malaysia and Indonesia. On the other hand, for processing of edible oil, soy, canola and sunflower seeds are imported from USA, Brazil, Canada, Eastern Europe and Australia. The raw material is imported under sight letter of credit; the same operates as a mitigant against exchange rate risk.

KGML's total power requirement is around 2MW comprising 1.2MW for Karachi unit and 0.75Mw for Gujranwala unit. For Gujranwala unit Water and Power Development Authority (WAPDA) supply is available; meanwhile the solvent unit is totally dependent on alternate sources including 2.5MW gas generator as primarily source along with other secondary sources based on diesel. The power supply from WAPDA is currently relatively cheap; therefore alternate sources of 1.1MW for Gujranwala unit are hardly utilized. To improve the power mix as the working of gas generators is affected during winters in line with load-shedding, the management has installed a 1MW diesel generator during FY21*. The capex on the same was completely funded from company's own sources.

Business and Industry Risk Factors

Edible oil market is highly competitive on account of highly fragmented structure with no dominant player and low barriers to entry resulting in limited pricing power and thin profitability margins. KGML's market share has remained at around 3.85% in FY21*. The domestic production of oilseeds is low, which exposes the industry to risks associated with the import of raw material, including excessive inventory lead-time, government duties, exchange rate risk, and price volatility. Pakistan is amongst the leading consumers of edible oil with the same comprising 2.8% of the GDP. Current per capita consumption stands at around 22kg in 2020 compared to global average of 24kg. Going forward, overall demand is likely to expand on the back of growing demand of frying and processed food, increasing number of restaurants, urbanization and growing disposable incomes along with ongoing shift from unpackaged to packaged products.

The demand risk in the oil meal segment being a by-product of solvent extraction is mitigated through sales to group feed mill while price risk is mitigated due to high demand in the poultry sector. KGML mitigates inventory risk by synchronizing procurement orders with sales forecast. The company mitigates exchange rate risk by taking exposure in futures contracts while keeping close watch for price fluctuation in the international market.

Steady Growth in topline noted on a timeline basis. While Gross margins improved marginally in the outgoing year, the same has remained range-bound over the past three years.

Net sales of the company increased to Rs. 18.9b (FY20: Rs. 15.1b) during FY21 largely being a function of higher average retail price along with capturing of market share of another player in the industry. Limited growth in terms of quantity indicates intense competition faced by the company with entry of new market players making market capitalization difficult. Banspati Ghee *(under the flagship brand of Kausar Banaspati Ghee)* has remained the major revenue driver over the years, representing around 65-70% of the total sales, followed by cooking oil. KGML sells around 30% of meal produce to its associate concern while the remaining is sold in the open market.

Gross margins of the company largely remained range bound in the last three years, with slight increase to 10.0% (FY20: 8.5%) during FY21 as an outcome of higher average sales price per unit of all products. Gross margins were at similar level in 3Q22. The raw material mix of the company primarily comprises imported seed constituting more than 90% of total purchases. The capacity utilization of ghee plant (Karachi & Gujranwala) and oil refinery (Karachi and Gujranwala) were reported at 34% (FY20: 32%) and 24% (FY20: 21%) respectively. As per the management, the production units are operational throughout the year while the ghee and solvent plants are shut down for one week and four weeks respectively for annual maintenance. Overall the underutilization is attributable to strong competition within the packaged oil market. Utilization levels of the ghee plant at Karachi were recorded at 14%.

The selling and distribution cost has increased in line with increase in company's scale of operations; meanwhile, the administration expenses were largely rationalized in terms of sales growth with increase manifested in compensation benefits. KGML follows a conservative long-term debt free structure since inception, therefore the interest expenses are on the lower side. With improvement in margins and lower finance costs, the bottom line was recorded higher at Rs. 896.2m (FY20: Rs. 499.9m) during FY21. Maintenance of margins amidst declining international palm oil prices post lifting of ban on Indonesian exports which classifies as the largest exporter of palm oil in the world. PAT was reported higher at Rs. 896.5m during 9MFY22 largely attributable to increase in average selling prices.

Adequate liquidity supported by sufficient cash flows in relation to outstanding obligations

In line with improving profitability, funds from operations (FFO) improved to Rs. 1084.4mm (FY20: Rs. 551.4m) during FY21. Given extended working capital cycle in the outgoing year, quantum of short-term borrowings increased to Rs. 1.3b at end-FY21.

However, liquidity profile of the company is supported with zero reliance on long-term borrowing and reduced utilization of short-term credit given by the sponsors to meet working capital requirements. FFO to total debt was reported at 85.4% (FY20: NA, FY19: 3,486.3 %) during FY21. Further, debt service coverage ratio is considered strong.

Stock in trade doubled at end-FY21 due to increased prices as compared to previous year comprising mainly of imported raw material; the company is strategizing to meet its inventory demand through continuous production, in order to lower the cost associated with holding higher inventory levels and perishable nature of certain products. Trade debts were recorded lower relative to quantum of sales during the period under review with satisfactory profile of receivables. At quarter-end March'22, trade debts were reported higher at Rs. 2.3b.

As per management, the company has purchased 10 acre land near the solvent unit in Karachi to install three silos entailing a capacity of 5000MT each to be used for storage of all kinds of imported seeds. The processes involving human handling like loading and unloading of seeds in the production cycle will be eliminated; hence with automation, efficiency enhancement and cost saving will be achieved. The project has been completed in the outgoing year, the financing for the same was arranged from company's own sources. Given projected increase in profitability led by favorable demand dynamics, liquidity position is projected to improve further, going forward.

Going forward, to avail the benefit of price fluctuations in plastic resin, KGML plans to install pet bottle making machines by end-FY23. The expected capital expenditure on the same is projected around Rs. 38.0m and is to be arranged from company's own sources. With the investment diversification in revenue streams is expected to be achieved. This project put on hold last year due to COVID-19.

Conservative capital structure

Equity base of the company has strengthened in line with internal capital generation. Debt profile of the company in the past majorly comprised short-term borrowings with zero reliance on long-term financing. During FY21, short-term commercial borrowings increased to Rs. 1.2b (FY20: Nil) on account of extended working capital cycle due to increasing raw material prices. The company also has short-term interest free short-term sponsor loan on the books. The loan is payable on demand depending on availability of funds with the company. As per management strategy, the company is not expected to obtain any commercial funding either for capital expenditure or for short-term requirements. With minimum dependence on credit financing along with strengthening of equity base, gearing and leverage indicators are considered to be on the lower side in comparison to peers and were reported at 0.42x (FY20: 0.01x) and 1.01x (FY20: 1.32x); respectively, by end-FY21. Gearing and leverage indicators are projected to remain within manageable levels given limited reliance on credit financings. Equity base was reported higher at Rs. 3.9b at end-March'22.

Kausar Ghee Mills (Pvt.) Limited Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY19**	**FY20**	**FY21**	**9M22**
Fixed Assets	910.3	943.4	962.3	978.0
Stock-in-Trade	1,665.2	1,064.9	2,226.2	1,974.3
Trade Debts	681.1	877.9	1,684.5	2,299.2
Cash & Bank Balances	56.4	997.5	137.2	220.2
Total Assets	4,521.8	4,889.7	6,044.4	6,573.6
Trade and Other Payables	948.9	1,080.2	633.3	1,764.1
Long Term Debt	-	15.8	22.8	-
Short Term Debt	1,303.6	-	1,247.4	-
Total Debt	1,303.6	15.8	1,270.2	-
Total Equity	1,957.6	2,107.1	3,003.2	3,899.8
Total Liabilities	2,564.2	2,782.6	3,041.2	2,673.8
Paid Up Capital	500.0	500.0	500.0	500.0
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**9M22**
Net Sales	11,426.2	15,116.7	18,891.9	18,258.6
Gross Profit	950.9	1,291.1	1,885.7	1,833.2
Operating Profit	535.7	748.1	1,273.6	1,270.7
Profit Before Tax	469.4	748.2	1,283.9	1,262.7
Profit After Tax	157.0	499.9	896.2	896.5
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**9M22**
Gross Margin (%)	8.3%	8.5%	10.0%	10.0%
Net Margin (%)	1.4%	3.3%	4.7%	4.9%
Net Working Capital	1084.1	1216.1	2101.9	2968.2
Trade debts/Sales	6.0%	5.8%	8.9%	9.4%
FFO	267.3	551.4	1084.4	957.6
FFO to Total Debt (%)	20.5%	3486.3%	85.4%	NA
FFO to Long Term Debt (%)	NA	3486.3%	4755.5%	NA
Debt Servicing Coverage Ratio (x)	5.3	17.1	85.1	36.1
Current Ratio (x)	1.4	1.4	1.7	2.1
Stock+Trade Debts/STD	180.0%	NA	313.5%	NA
Gearing (x)	0.7	0.0	0.4	0.0
K Leverage (x)	1.3	1.3	1.0	0.7

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

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	Kausar Ghee Mills (Pvt.) Ltd				
Sector	Consumer Goods				
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				
	July 04, 2022	A-	A-2	Stable	Reaffirmed
	Sep 09, 2020	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.				
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. Copyright 2022 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS				
Due Diligence Meetings Conducted		**Name**	**Designation**	**Date**	
	1	Mr. Shujaat Butt	Senior Manager	Nov 23, 2021	
	2	Mr. Bilal	Director	Nov 23, 2021	