

RATING REPORT

The Organic Meat Company Limited (TOMCL)

REPORT DATE:

December 07, 2021

RATING ANALYSTS:

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Rating Category	Initial Rating	
	Long-term	Short-term
Entity	A-	A-2
Rating Outlook	Stable	
Rating Date	December 07, 2021	

COMPANY INFORMATION

Incorporated in 2010

Private Limited Company

Key Shareholders (with stake 5% or more):

Mr. Faisal Hussain – 45.54%

Mr. Ali Hussain – 9.50%

External Auditors: Grant Thornton Anjum Rahman
Chartered Accountants

Chairman: Mr. Nihal Cassim

Chief Executive Officer: Mr. Faisal Hussain

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporate Rating Methodology (August 2021)

<https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf>

The Organic Meat Company Limited

OVERVIEW OF THE INSTITUTION

The Organic Meat Company Limited (TOMCL) began as a private limited company in 2010. The registered office of the company is situated at Plot No. 257, Sector 24, Korangi Industrial Area, Karachi.

Profile of Chairman

Mr. Nihal is an MBA from McGill University. He is currently a director on the Boards of International Steels Limited, The Organic Meat Company Limited, Uniquity Trading Limited, National Institutional Facilitation Technologies (Pvt) Limited (NIFT) and its subsidiary ISM (Pvt) Limited. He has served on the Board of Pakistan Oilfields Limited, Ferozsons Laboratories Limited and Mutual Funds Association of Pakistan (MUFAP).

Profile of CEO

Mr. Faisal Hussain is an MBA from IBA and also holds a Master of Finance Degree from Cardiff Business School, UK. He has over 21 years working experience in sheep casings (meat offal processing) industry and 11 years of experience in the meat processing industry.

RATING RATIONALE

The Organic Meat Company (‘TOMCL’ or ‘the Company’) was founded in 2010 as a private limited company in Karachi. The Company is Pakistan’s leading processor and exporter of Red Meat and Edible Offal. The major production facility of TOMCL is located at Gadap Town, Karachi and a separate offal processing facility been established in Korangi Industrial Area, Karachi. TOMCL is also in the process of setting up an animal fattening project adjacent to GADAP factory, expected to hold 3,000 cattle for fattening purposes. The Company was listed on Pakistan Stock Exchange (PSX) in July’2020.

Sector Brief:

Global Overview

- The market value of the global meat industry stands at USD 838b in 2020 which is expected to increase to USD 1t by 2025.
- Most of the world’s meat is produced in Asia, stands at around 41% of the global meat production.
- Out of the total worldwide production of meat, beef & veal and mutton/sheep consist 26% of the production.
- The global per capita meat consumption is around 35 Kg per annum, which is expected to remain stable; however, with the increase in global population, consumption of meat will rise steadily.
- In 2019, China was the top meat producer of the world with 88.15m MTs followed by Europe (63.84m MTs), USA (46.83m MTs), Brazil (29.34m MTs) and Russia (10.63m MTs).
- The top exporters of meat, in terms of value, are USA, Brazil and Europe while on the other hand top importers are Japan, USA and China.
- China, Mexico and Egypt are the top Edible Offal importing countries wherein China has the largest share of 42% in terms of volume followed by Mexico and Egypt with 6% each.

Pakistan’s Industry

- Pakistan produced roughly around 3.8m MT’s of meat in 2019, having an approximate market share of ~1.02% in the global meat production.
- Exports of Pakistan’s meat and edible offal stood, at USD 310m in FY20, rose from USD 216m in FY18. As per commodities export receipts data of State Bank of Pakistan (SBP) the number has increased to USD 353m in FY21.
- GoP has also taken initiative to promote export of Halal products to OIC countries. In this regard, meetings have been convened between Pakistan and KSA wherein six meat exporting companies inked contracts with the Saudi Food Drug Authority for export of meat to Saudi Arabia.
- In 2018 and 2019, sessions were held with Kuwait, Oman and Bahrain in order to enhance the cooperation in food and agriculture.
- As reported, Pakistan is aiming to boost meat exports to USD500m in FY22 after getting access to Jordanian and Egyptian halal meat markets.

Table 1: Pakistan’s Meat & Offal Export in USD Mn.

FY18	FY19	FY20	FY21
216	243	310	353

Key Rating Drivers

Ratings Incorporate TOMCL's Market Positioning & Access

TOMCL is a major player in the meat export market, having the largest capacity from slaughtering to packaging, highest halal meat exports receipts and the only offal processor in the formal meat sector. The Company also has the largest market access, given meat export approvals in 11 jurisdictions.

Rating is constrained by business risk of 'Food & Allied' segment and Client/Geographic Concentration inherent in TOMCL's revenue stream

The rating incorporates business risk of 'Food & Allied' segment and TOMCL-specific risk factors, which are as follows:

- Factors such as price variations due to seasonal impacts in the local market posit business challenges to the Company. With the addition of the animal fattening plant, this business risk will be partly addressed as the Company will be able to cater for 25% of its requirements.
- Business risk emanating from high geographic concentration as 74% of the revenue comes from UAE. Client concentration is also high with 70% of the revenue being generated from top 5 clients. However, cognizant of this, the management is working on improving the same by addition of new export destinations. TOMCL is one of the three meat exporters from Pakistan which recently got the permission to export halal meat to Jordan and Egypt. Furthermore, the Company has received USA FDA clearance for export of pet food raw material to USA.

Rating incorporates consistent topline growth, stable & adequate profitability margins and strong cash flow coverage indicators

- The Company's business risk profile is supported by the consistent growth in Company's topline and moderately stable gross margins, which have averaged 17% during the past 5-year period (FY17-FY21).
- The Company's business model is relatively leaner than peers, with all of the sales being export-oriented and quantum of fixed overheads being low. Despite having lower gross margin, the Company is able to post higher operating margin than peers, mainly on the back of this limited expense base.
- Given strong growth in revenue base, the Company's cash flow coverage indicators have remained comfortably high during the past 5-year period. In addition, coverage of short term borrowings by stock of inventory and trade debts has been improving and stands comfortably high as at 1.9x, as of Sep'21.

Ratings incorporate a conservative capital structure

- The Company's capital structure is tilted towards equity, standing at 26:74 (Debt: Equity) as of Sep'21. The loan from related party has been taken as debt, as it's classified in current liabilities and is repayable on lender's demand. However, it is pertinent to mention that this borrowing is interest-free and has remained with the Company for more than 2 years. Accordingly, if the same is incorporated as equity, the capital structure further improves to 22:78.
- The Company's gearing and leverage indicators have improved on a timeline and as of Sep'21, stood comfortably low. In case, short term (interest-free) borrowing from related party is considered as equity, gearing falls further to 0.28x.

Corporate Governance Framework is reflective of Company's operational status as a Listed Entity

- Experienced and qualified management team with the function wise organizational hierarchy in place.
- Board committees include Audit committee, HR & Remuneration committee and IT committee.
- Board members consist of Chairman, three executive and four independent directors with a female representation.
- The company has a manual ERP for finance department only. Management is exploring the options for a fully integrated ERP for better management of operations to build in further efficiency.

The Organic Meat Company Limited
Appendix I

Key Financial Indicators					
<i>(Amount in Millions)</i>					
<u>BALANCE SHEET</u>	Jun'18	Jun'19	Jun'20	Jun'21	Sep'21
Property, Plant & Equipment	1,257	1,245	1,420	1,827	1,845
Stock in Trade	131	201	239	188	138
Trade Debts	849	824	702	912	1,235
Cash & Bank Balances	16	5	7	125	164
Total Assets	2,333	2,569	2,731	3,643	3,913
Trade and Other Payables	207	139	76	89	238
Short Term Borrowings	573	719	659	702	724
Long-Term Borrowings <i>(Inc. current matur)</i>	100	52	12	38	103
Total Liabilities	919	947	843	900	1,086
Issued, Subs, and Paid Up Capital	100	718	718	1,118	1,118
Equity (net of revaluation surplus)	777	1,028	1,349	2,270	2,369
<u>INCOME STATEMENT</u>	FY18	FY19	FY20	FY21	Q1'FY22
Net Sales	2,053	2,578	3,384	3,928	1,070
Gross Profit	354	408	622	650	180
Operating Profit	214	336	374	430	108
Profit Before Tax	157	265	283	340	91
Profit After Tax	143	218	266	303	84
FFO	271	455	431	437	131
<u>RATIO ANALYSIS</u>	FY18	FY19	FY20	FY21	Q1'FY22
Gross Margin (%)	17.24%	15.82%	18.38%	16.54%	16.83%
Net Margin (%)	6.98%	8.46%	7.87%	7.73%	7.84%
FFO to Long-Term Debt	2.72	8.84	34.75	11.46	5.08*
FFO to Total Debt	40.3%	59.1%	64.2%	59.0%	63.5%*
Debt Servicing Coverage Ratio (x)	4.19	4.08	3.79	5.17	7.73*
ROAA (%)	7.8%	8.9%	10.1%	9.5%	8.6%*
ROAE (%)	20.8%	24.2%	22.4%	16.8%	14.1%*
Gearing (x)	0.87	0.75	0.50	0.33	0.35
Debt Leverage (x)	1.18	0.92	0.63	0.40	0.46
Current Ratio (x)	1.25	1.42	1.55	2.09	2.07
Inventory + Receivables/Short-term Borrowings (x)	1.71	1.43	1.43	1.57	1.90
* Annualized					

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

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	The Organic Meat Company Limited				
Sector	Food				
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				
	12-07-2021	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 Conducted	Name	Designation	Date		
	Mr. Faisal Hussain	CEO	November 10, 2021		