RATING REPORT

Everfresh Farms (Pvt.) Limited

REPORT DATE:
September 6, 2023

RATING ANALYSTS:
Abdul Kadir
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RATING DETAILS		
Rating Category	**Latest Rating**	**Previous Rating**
Entity	BBB+/A-2	BBB+/A-2
Rating Date (Entity)	Sep 6, 2023	July 15, 2022
Rating Outlook	Positive	Stable

COMPANY INFORMATION	
Incorporated in 2008	**External auditors:** Malik Haroon Shahid Safder & Co
Private Limited Company	**Chairman and Chief Executive Officer:** Mr. Muhammad Haleem
Key Shareholders (with stake 5% or more):	
Shafi Gluco-Chem (Pvt.) Limited - 55.7%	
Muhammad Shafi Tanneries (Pvt.) Ltd - 11.4%	
Mian Amjad Hafeez - 8.2%	
Mian Naseem Shafi - 7.5%	

APPLICABLE METHODOLOGY

VIS Entity Rating Criteria: *Corporates (MAY 2023)*
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

VIS Rating Scale
https://docs.vis.com.pk/docs/ratingscale.pdf

Everfresh Farms (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Everfresh Farms (Pvt.) Limited (EFPL) was incorporated in 2008 under the repealed Companies Ordinance, 1984 (now Companies Act, 2017) as a private limited company. The principal business activity of the company is to run the business of farming, dairies, cultivation of food grains, seeds, foods and manufacturing of products associated with the farming interest.

RATING RATIONALE

Company Overview

Everfresh Farms (Pvt.) Limited (EFPL) initiated its dairy farming activities in 2008 and was established as a privately held enterprise according to the former Companies Ordinance of 1984 (now recognized as the Companies Act of 2017). The primary operational focus of the company involves managing a dairy farm dedicated to the production of milk and agricultural goods. EFPL is affiliated with the Shafi Group of Companies, a conglomerate that operates in various sectors including textiles (Shafi Texcel Limited-STL), food (Everfresh Farms-EFPL, Shafi Foods - SFPL, Shafi Gluco Chem Private Limited), leather (Shafi Tanneries Private Limited), and footwear. EFPL operates as a family-owned entity and is headquartered along with its dairy farm in Lahore, Pakistan. The company has discontinued selling and trading of various products including cheese, raw vegetables, and frozen fries during FY23. The company's products now include raw milk, seeds and food grains.

As the company is owned by family members, there is no established formal Board structure. However, discussions with the senior management are convened when required. Room for improvement exists in formation of a formalized BoD with induction of external members in accordance to best practices.

The Board of Directors has established two committees to ensure efficient quarterly supervision: the Executive Committee and the Farm-level Committee. The company has enlisted the services of Malik Haroon Shahid Safder & Co. to conduct the necessary external audit as per their categorization under group C in the SBP Panel of Auditors.

The company has also obtained the following ISO certifications:

- Food Authority Certificate for raw milk
- HACCEP Certificate 2017
- EPA certificate for Operation and Construction

Business Model

EFPL's core business model centers on the operation of a dairy farm engaged in milk production, and the oversight of a cold chain infrastructure with a chiller capacity of 55MT. The expansive dairy farm, spanning 120 acres of land situated in Bhera, Sargodha, is organized in a free stall layout with designated dirt lots. The farm encompasses various structures, including multiple sheds for milking cows, a separate shed for dry cows, another for young animals, a fully automated milking parlor, storage sheds for cow feed, residential areas for staff, and other related facilities.

EFPL's roster of Plant & Machinery features milking parlors designed to accommodate 40 animals per batch, with a batch cycle of 12 minutes for three daily cow milking sessions. The company also utilizes chillers, silos, and bunkers with capacities of 55 tons, 4,800 tons, and 10,000 tons respectively. In addition to these items, EFPL possesses two Keenan Wagons, tractors, harvesters, a stationary mixer for food preparation, Lacto fans, and a cooling & showering system. These assets collectively support the operational activities of the business.

By end-FY23, the company's livestock count reached a total of 4,068 animals with equal number of milking and non-milking Holstein cows. The management's objective is to gradually enhance the herd size to 5,500 over the medium-term with natural growth process. Given high cost for imports and significant tax framework, the company has recently relied entirely on in-house breeding initiative. Given higher yields and the expanding herd size, the company enhanced its milk production storage chiller capacity to 65MT/day (FY22: 53MT/day; FY21: 45MT/day) in FY23.

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. There is considerable potential for growth 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. EFPL's exposure to business risk is relatively limited, given its secure contractual agreements with significant corporate clients.

Growing asset base

By end-March'23, the company's total assets stood at Rs. 2.5b (FY22: Rs. 2.5b; FY21: Rs. 2.0b), with non-current assets constituting 73% of the asset composition. The valuation of property, plant, and equipment exhibited continuous growth over the years (9MFY23: Rs. 1.2b; FY22: Rs.

1.1b; FY21: Rs. 1.0b; FY20: Rs. 0.8b). The increase corresponds to EFPL's strategic investment in land, driven by its intent to venture into the agricultural sector within the short to medium term. The value of biological assets has maintained a consistent level at Rs. 554.1m (FY22: Rs. 543.7m; FY21: Rs. 561.4m), despite the progressive expansion of the herd size. The stagnancy is due to the revaluation cycle for biological assets taking place every three years, scheduled for completion at the conclusion of FY23.

Given the inherent characteristics of its business model, the company maintains relatively moderate working capital requirements. While these requirements have increased in tandem with the expanding business operations, the proportion of trade receivables in relation to sales remains low at 2.8% (FY22: 2.9%; FY21: 1.6%) in 9MFY23. EFPL extends an average credit period of 10 – 15 days to its primary institutional clients, which contributes over 95% of the company's sales revenue.

EFPL experienced a 16% rise in net revenue during the first 9 months of FY23, driven by increased volumetric sales supported by the expansion of the milking herd size. Margins have demonstrated a positive trend over recent years, attributed to both organic growth and favorable adjustments in price agreements with key purchasers.

Net revenue increased to Rs. 2.0b (FY22: Rs. 1.7b; FY21: Rs. 1.3b) in 9MFY23. The growth was primarily driven by heightened volumetric sales, which were propelled by the continual expansion of the milking herd size. The sales composition continued to be dominated by milk, contributing over 96% of the total revenue, while smaller contributions emanated from the sales of cheese, mushrooms, olives, jalapenos, frozen fries, and crops. During the 4QFY23, the company halted all ancillary operations and is now focused on selling raw milk only.

Amongst the corporate clients that the Company is under contract with, Nestlé holds the position of the largest customer for EFPL. Contractual arrangements have been established for the sale of raw milk, with a daily supply of around 45-60 MTs. The financial stability and market presence of Nestlé provide a sense of reassurance. In addition to Nestlé, the company's corporate client base includes Olpers, Haleeb, Fauji Foods, and Adams.

Sales (PKR mlns)	2020	%	2021	%	2022	%
Raw Milk	868.1	95.6%	1,268.1	94.8%	1,639.9	96.7%
Cheese	31.8	3.5%	56.0	4.2%	29.3	1.7%
Mushroom, olives & jalapenos	1.3	0.1%	5.8	0.4%	5.1	0.3%
Frozen Fries	0.9	0.1%	0.0	0.0%	7.6	0.4%
Crops	6.0	0.7%	7.6	0.6%	14.1	0.8%
Gross Sales	**908.0**		**1,337.6**		**1,696.0**	

Gross margins increased to 15.4% (FY22: 14.0%; FY21: 14.1%; FY20: 6.1%) in 9MFY23. The improvement was attributed to both the organic growth in revenue and the revision of rates with Nestlé, in addition to the acquisition of fresh corporate contracts.

The increase in operating expenses primarily stemmed from higher salaries, wages, and rent. The finance costs incurred amounted to Rs. 41.1m (FY22: Rs. 25.0m; FY21: Rs. 18.8m) higher average borrowings and interest rates. The overall profile of profitability was further supported by rental income generated from agricultural land and the resolution of certain liabilities. Consequently, the company's net profit stood higher at Rs. 205.4m (FY22: Rs. 173.6m; FY21: Rs. 113.4m) in 9MFY23. Looking ahead, the management anticipates a gradual rise in profitability driven by economies of scale. However, escalating interest costs might exert pressure on the overall profit levels.

Improvement in overall liquidity profile on a timeline basis

Aligned with the increased profitability, the company exhibited enhanced funds from operations (FFO) during 9MFY23, amounting to Rs. 316.2m (annualized) (FY22: Rs. 190.6m; FY21: Rs. 154.5m). FFO-to-total debt and debt service coverage ratios improved to 0.7x (FY22: 0.4x; FY21: 0.5x) and 3.6x (FY22: 2.3x; FY21: 2.8x) respectively. The inventory and trade debt adequately cover short-term borrowings while the current ratio improved to 1.4x (FY22: 1.2x; FY21: 0.8x) by end-9MFY23.

Liquidity profile of the company is also supported by short-term investments on the books to the tune of Rs. 31m (FY22: Rs. 17m, FY21: Rs. 25m) comprising exposure in mutual funds and cash deposits mainly in savings account amounting Rs. 48m (FY22: 37m; FY21: 60m). Working capital cycle of the company is on the lower side given receipt from customers realized earlier and longer payment terms. Maintenance of liquidity coverages is considered important from a ratings perspective.

Leverage indicators have depicted improvement on a timeline basis on account of profit retention, interest-free loan from associates and share deposit money by the parent company

The paid-up capital remained at Rs. 1.2b at end-9MFY23. The capital increased to Rs. 1.2b (FY21: 0.96b) by end-FY22 on account of issuance of shares. The overall equity base, encompassing related-party loans, share deposit funds, and profit retention increased to Rs. 1.7b (FY22: Rs. 1.4b; FY21: Rs. 1.1b) by end-9MFY23. The total liabilities decreased to Rs. 835.6m (FY22: Rs. 1,042.8m; FY21: Rs. 958.5m) primarily due to lower payables and debt levels.

Gearing has remained manageable at 0.3x (FY22: 0.4x; FY21: 0.3x) while debt leverage exhibited improvement on a timeline basis to 0.5x (FY22: 0.7x; FY21: 0.9x) by end-9MFY23. Given no major capex going forward, leverage indicators are expected to remain manageable. Maintaining gearing within manageable levels is considered important for the assigned ratings.

Everfresh Farms (Pvt.) Limited — Annexure I

FINANCIAL SUMMARY				(Amounts in PKR millions)
BALANCE SHEET	**FY20**	**FY21**	**FY22**	**9MFY23**
Property Plant and Equipment	783.6	973.6	1,136.0	1,201.1
Stock-in-Trade	166.0	259.1	358.9	192.7
Trade Debts	27.7	21.6	49.7	72.9
Biological assets	572.6	561.4	543.7	554.1
Cash & Bank Balances	43.2	59.7	37.1	48.4
Other Assets	185.6	149.5	364.5	435.4
Total Assets	1,778.7	2,024.9	2,489.9	2,504.7
Trade and Other Payables	409.9	472.9	306.0	192.5
Short Term Debt	-	-	240.8	207.9
Long Term Debt	223.1	284.2	304.4	241.0
Total Debt	223.1	284.2	545.2	449.0
Other Liabilities	155.8	201.3	191.6	194.2
Total Liabilities	788.8	958.5	1,042.8	835.6
Total Equity (including loan from related parties)	989.9	1,066.4	1,447.1	1,669.1
Paid-up Capital	958.6	958.6	1,215.5	1,215.5
INCOME STATEMENT	**FY20**	**FY21**	**FY22**	**9MFY23**
Net Sales	904.0	1,337.6	1,694.3	1,959.4
Gross Profit	55.1	188.7	237.0	301.7
Operating Expenses	(59.5)	(49.9)	(71.1)	(36.0)
Profit After Tax	20.7	113.4	173.6	205.4
Gain on revaluation of biological assets	88.2	74.2	45.5	10.4
RATIO ANALYSIS	**FY20**	**FY21**	**FY22**	**9MFY23**
Gross Margin (%) (excl. gain on revaluation)	6.1%	14.1%	14.0%	15.4%
Net Margin (%)	2.3%	8.5%	10.2%	10.5%
Net Working Capital	(64.3)	(95.0)	96.1	201.3
Trade debts/Sales (%)	3.1%	1.6%	2.9%	2.8%
FFO	22.4	154.5	190.6	316.2*
FFO to Total Debt (x)	0.10	0.54	0.35	0.70*
FFO to Long Term Debt (x)	0.10	0.54	0.63	1.31*
Current Ratio (x)	0.87	0.84	1.15	1.41
Debt Servicing Coverage Ratio (x)	2.23	2.79	2.32	3.63
Gearing (x)	0.23	0.27	0.38	0.27
Leverage (x)	0.80	0.90	0.72	0.50
Short-term Borrowing Coverage (x)	-	-	1.70	1.28
ROAA (%)	1.3%	6.0%	7.7%	11.0%*
ROAE (%)	2.5%	11.0%	13.8%	17.6%*
Cash Conversion Cycle	(62)	(66)	(12)	13

- *Annualized*

REGULATORY DISCLOSURES	Annexure II
Name of Rated Entity	Everfresh Farms (Pvt.) Limited
Sector	Consumer Goods
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
06-09-2023	BBB+	A-2	Positive	Maintained
15-07-2022	BBB+	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.
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Due Diligence Meeting Conducted	Name	Designation	Date
	Mr. Zahid Haleem	CFO	21 August, 2023
	Mr. Mubeen Iqbal	Senior Deputy Manager	21 August, 2023