

RATING REPORT

Everfresh Farms (Private) Limited

REPORT DATE:

August 02, 2024

RATING ANALYST:

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RATING DETAILS

Rating Category	Latest Ratings		Previous Ratings	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	BBB+	A-2
Rating Date	August 02, 2024		September 06, 2023	
Rating Action	Upgrade		Maintained	
Outlook/Rating Watch	Stable		Positive	

COMPANY INFORMATION

Incorporated in 2008

External auditors: Malik Haroon Shahid Safder & Co

Private Limited Company

Chairman: Mr. Muhammad Haleem

Key Shareholders (with stake 5% or more):

CEO: Mr. Muhammad Haleem

*Shafi Gluco-Chem (Pvt.) Limited – 55.7%**Mubammad Shafi Tanneries (Pvt.) Ltd – 11.4%**Mian Amjad Hafeez – 8.2%**Mian Naseem Shafi – 7.5 %**Other Shareholders – 17.2%*

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates

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

RATING SCALE(S)

VIS Issue/Issuer Rating Scale:

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

Everfresh Farms (Private) Limited

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

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 Limited (EFPL) was incorporated in 2008 under the repealed Companies Ordinance, 1984 (now Companies Act, 2017) as a private limited company.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.

Company Profile

EFPL was established as a private limited company, initiating its dairy farming activities in 2008. 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 discontinued selling and trading in 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 the formation of a formalized BoD with induction of external members in accordance with best practices.

However, there are two established board committees for 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

Production Capacity and Utilization

The Company operates a dairy farm engaged in milk production and pasteurization, dairy product manufacturing, and cold chain infrastructure management with a chiller capacity of 75 MT. The dairy farm and milk processing plant, situated on 120 acres in Bhera, District Sargodha, features a free stall layout with designated dirt lots for cows. Facilities include multiple cow sheds, a milking parlor, feed storage, staff residences, and allied facilities.

EFPL's equipment includes milking parlors accommodating 40 animals per batch, with a 12-minute cycle for thrice-daily milking sessions. Additional infrastructure comprises chillers, silos, and bunkers with capacities of 75 MT, 4,800 MT, and 10,000 MT respectively, along with two Keenan Wagons, tractors, harvesters, a stationary mixer, Lacto fans, and a cooling and showering system.

As of FY24, livestock numbered 4,052 Holstein cows, with equal milking and non-milking segments. The herd size is targeted to grow to 4,500 in FY25, through in-house breeding due to import costs and tax considerations.

Key Rating Drivers:

VIS considers the business risk profile of Pakistan's packaged milk industry medium characterized by non-cyclical, albeit seasonal demand, high competition with significant untapped growth potential. The recent increase in sales tax might be a challenge for further market penetration for the sector.

VIS considers the business risk profile of the packaged milk industry in Pakistan to be medium. The industry faces intense competition, albeit a significant growth opportunity exists in the untapped loose milk market.

The milk industry in Pakistan is divided into two primary segments: loose milk and processed milk. Loose milk constitutes about 90% of the market, while processed milk has a penetration rate of only 10%. Compared to neighboring countries like India (14%) and Bangladesh (20%), Pakistan's adoption of processed milk remains lower. However, a gradual shift towards packaged milk has been noted in recent years and indicates changing trends. The untapped loose milk market offers a significant growth opportunity for companies in the packaged milk sector, driven by increasing consumer awareness regarding food quality.

Challenges for packaged milk companies include consumer preference for loose milk and the additional costs associated with processing, transportation, and distributor margins. The recent imposition of an 18% sales tax on packaged milk may further exacerbate pricing challenges for the industry.

The demand for milk follows a seasonal pattern, with flush periods in the first half and lean periods in the second half of the year. Nevertheless, overall demand is considered non-cyclical with minimal effect of the economic cycle on the industry. As such, milk demand exhibits low elasticity and remains relatively stable. Factors such as urbanization and significant growth prospects in the untapped market contribute to the increasing demand for packaged milk.

Contractual agreement with Nestle provides support to the Company's business risk profile. However, this also poses a significant client concentration risk.

Amongst the contractual corporate clients, Nestlé holds the position of the largest customer for EFPL. Agreements 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 lowers business risk for EFPL, where the Company does not expect a drop in sales volume despite the imposition of 18% sales tax on packaged milk. In addition to Nestlé, the Company recently added Interloop to its corporate client base. However, with much of their sales dependent on two major clients, this poses a significant level of client concentration risk on the Company's business risk profile. Nevertheless, with a limited corporate client pool this is true for the entire industry.

Topline increased on the back of volumetric growth as well as price increases. Margins recover in 9MFY24, after significant contraction in FY23 on account of surge in fodder costs in 4QFY23.

Net revenue increased by an annualized growth rate of ~14% in 9MFY24. This growth is attributed to both higher volumetric sales as well as the increase in prices of milk during the period, as per the management. During 4QFY23, the Company halted all ancillary operations and is now focused on selling only raw milk. The management is confident that it will achieve its target net revenue of 10 billion by 2030.

Gross margins were impacted by a surge in fodder costs in 4QFY23, contracting to 5.6% (FY22: 14.0%) in FY23. However, as fodder costs normalized, while prices of milk increased, margins recovered to 12.4% in 9MFY23, albeit slightly lower than the historic average.

Historically healthy coverage profile reported weakening in FY23 before recovering in 9MFY24. While the liquidity profile reported significant improvement.

In FY23, the funds from operations were constrained by significant contraction in the gross margins, resulting in the debt service coverage ratio (DSCR) to be stressed to 0.88x (FY22: 2.32x) in FY23. However, with the recovery of margins in 9MFY24, the DSCR improved to 3.43x in 9MFY24. Meanwhile, EFPL's short-term debt coverage improved to 2.57x (FY22: 1.70x) in FY23 and then further to 6.52x in 9MFY24. Additionally, the current ratio rose sharply, to 1.71x (FY23: 1.10x; FY22: 1.15x) and remained well above the benchmark of 1.00x.

Sound capitalization profile with low debt levels.

The Company maintains a low debt profile, reflecting a sound capitalization profile with a 5-year historic gearing ratio of 0.37x and leverage ratio of 0.87x. Following a minor increase in the gearing ratio in FY22, due to higher short-term debt utilization, the ratio has since declined to 0.11x in 9MFY24 (FY23: 0.24x, FY22: 0.38x). This decline is attributed to ongoing payments of long-term debt and an increase in the equity base from retained profits.

Considerations for Future Reviews

Going forward, key business and financial risk indicators include the industry's ability to manage competition, consumer preferences, and the effects of recent tax increases on pricing. The commitment of major clients like Nestlé supports the stability of sales volumes, but ongoing management efforts are necessary to address challenges and maintain financial ratios. The dependency on continued client relationships and improvement in certain financial metrics will impact future ratings.

Everfresh Farms (Private) Limited
Annexure I

FINANCIAL SUMMARY				
BALANCE SHEET (PKR millions)	FY21A	FY22A	FY23A	9MFY24M
Property Plant and Equipment	974	1,136	1,225	1,320
Stock-in-Trade	259	359	457	376
Trade Debts	22	50	49	58
Biological assets	561	544	655	567
Cash & Bank Balances	60	37	40	100
Other Assets	149	364	642	631
Total Assets	2,025	2,490	3,067	3,051
Trade and Other Payables	473	306	709	477
Short Term Debt	-	241	197	67
Long Term Debt	284	304	220	166
Total Debt	284	545	417	233
Other Liabilities	201	192	207	258
Total Liabilities	958	1,043	1,333	968
Total Equity (including loan from related parties)	1,066	1,447	1,734	2,083
Paid-up Capital	959	1,215	1,215	1,215

INCOME STATEMENT (PKR millions)	FY21A	FY22A	FY23A	9MFY24M
Net Sales	1,338	1,694	2,675	2,336
Gross Profit (excl. gain on. reval)	189	237	150	289
Operating Expenses	50	71	66	49
Finance Costs	19	25	69	48
Profit After Tax	113	174	154	249
Gain on revaluation of biological assets	74	46	202	87

RATIO ANALYSIS	FY21A	FY22A	FY23A	9MFY24M
Gross Margin (%) (excl. gain on. reval)	14.1	14.0	5.6	12.4
Net Margin (%)	8.5	10.2	5.7	10.7
Net Working Capital (PKR millions)	(95)	96	98	446
Trade debts/Sales (%)	1.6	2.9	1.8	1.9
FFO (PKR millions)	154	191	47	344
FFO to Total Debt (x)	0.54	0.35	0.11	1.97
FFO to Long Term Debt (x)	0.54	0.63	0.21	2.76
Current Ratio (x)	0.84	1.15	1.10	1.71
Debt Servicing Coverage Ratio (x)	2.79	2.32	0.88	3.43
Gearing (x)	0.27	0.38	0.24	0.11
Leverage (x)	0.90	0.72	0.77	0.46
Short-Term Borrowing Coverage (x)	0.00	1.70	2.57	6.52
ROAA (%)	6.0	7.7	5.5	10.8
ROAE (%)	11.0	13.8	9.7	17.4
Cash Conversion Cycle(days)	(66)	(12)	(8)	(24)

A – Audited Accounts

M – Management Accounts

P – Projected Accounts

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	Outlook/ Rating Watch	Rating Action
	RATING TYPE: ENTITY				
	02-08-2024	A-	A-2	Stable	Upgrade
	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.				
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 Meeting Conducted	Name	Designation	Date		
	Mr. Zahid Haleem	Director	21 July, 2024		
	Mr. Mubeen Iqbal	Manager Accounts			