



The Pakistan Credit Rating Agency Limited

Rating Report

Pearl Petro Industry (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
12-Jun-2023	BBB-	A2	Positive	Initial	-

Rating Rationale and Key Rating Drivers

Pearl Petro Industry (Pvt.) Limited is major producer and seller of Polypropylene bags, Polyethylene Bags (liner bags), farm house PT sheets and other plastic sheets. Further, The Company has also set up a flexible packaging line where they print and provide packaging products to large-scale corporate clientele. The assigned ratings factor in the established and long track record of operations of the Company with extensive experience of sponsors in the plastic packaging industry. The Company relies heavily on imports, as the raw materials for its finished products are entirely sourced from the world's leading suppliers in countries such as KSA, USA, UAE, Kuwait, Singapore, and Qatar. Raw materials are petrochemical derivatives and its prices remain highly volatile, thus Pearl Petro is exposed to the risk of volatility in the prices of crude oil. Pearl Petro is currently operating at the capacity of 17,500 MT for the Polypropylene (PP) department, with a utilization rate of ~85%. The Polyethylene (PE) department has a capacity of 45,000 metric tons with a utilization rate of ~70%. It is noteworthy that these capacities tend to vary depending on the season. The assigned ratings also support the favorable demand prospects of the industry in the domestic market. The Company generated a topline of PKR~ 7,985mln in 9MFY23 (FY22: PKR 8,689mln, FY21: PKR 5,698mln). Additionally, the Company's high product concentration increases its vulnerability to competitive, pricing and innovation risks. The ratings also factor in Pearl Petro's working capital-intensive operations with moderately high inventory holding requirements and the vulnerability of its profitability to fluctuations in raw material prices.

The Company is actively progressing with its expansion plans, including installing a three-layer printing unit. This expansion initiative is anticipated to bolster the company's revenue streams and unlock potential growth opportunities. Moreover, Company exhibits a proactive stance in effectively managing its leverage exposure in order to reduce reliance on bank borrowing. The Company is moderately leveraged with sound financial indicators as of end-Mar'23.

The ratings are dependent upon sustainable revenue growth, along with improvement in profitability and coverage indicators and product diversification. An improved working capital cycle leading to improvement in liquidity could also trigger the ratings.

Disclosure

Name of Rated Entity	Pearl Petro Industry (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology Rating Modifiers(Jun-22)
Related Research	Sector Study Paper and Packaging(Nov-22)
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Profile

Legal Structure Pearl Petro Industry (Pvt.) Limited ("Pearl Petro" or "the Company") is a private limited company.

Background Pearl Petro, previously known as MH Plastic, was founded in 1979 by Mr. Munawar Hussain Malik. The Company was engaged in the sales and marketing business of plastic bags. Later on, it was converted to a private limited company in 2014, under the companies' ordinance 1984 (Companies Act 2017).

Operations Pearl Petro is among major producers of plastic products, including manufacturing and sale of Polypropylene bags, Polyethylene Bags (liner bags), farm house PT sheets and other plastic sheets. Further, Company has also set up a flexible packaging line where they print and provide packaging products to large-scale corporate clientele. The registered office and manufacturing facility are located in Lahore.

Ownership

Ownership Structure Pearl Petro is a family-owned business. Major shareholding (72.73%) of the Company holds by the founder - Mr. Munawar Hussain Malik while remaining shareholding of the Company lies with his daughter Ms. Bushara Fatima Malik (27.72%). Moreover, Mr. Malik intends to engage his offspring in the day-to-day affairs of the business, while also endowing him with a proportion of the Company's ownership.

Stability Being a family-owned business, over the years the management control of the Company remains unchanged and is expected to remain stable in near future.

Business Acumen The sponsors of the Company have a solid understanding of the Company's potential and value. The extensive experience of Mr. Malik has helped him in strong understanding of the market dynamics and develop relationships with the customers & suppliers, which will continue to support the business risk profile.

Financial Strength Owners of the Company have significant resources to finance the Company if the need arises.

Governance

Board Structure The Company has a two-member owner-dominated board, comprises of executive directors.

Members' Profile Mr. Munawar Hussain Malik is the Founder & Chief Executive Officer (CEO) of the Company. He has over three decades of professional experience. He is fully involved in day-to-day operations and also looks after all the strategic matters of the Company. His daughter, Ms. Bushara Fatima Malik is Executive Director. She participates in strategic decision-making and is also the part of Company's operations.

Board Effectiveness Both of the board members meet frequently to discuss all the strategic issues. Minutes of the meetings are formally documented.

Financial Transparency The External Auditors of the Company M/s. Amin Mudassir and Co., Chartered Accountants - a QCR rated firm - expressed an unqualified opinion on financial statements for the period ended Jun'22. An internal audit function is also present in the Company. Each transaction is thoroughly examined by the internal auditors on a regular basis.

Management

Organizational Structure The Company has a lean organizational structure to control personnel costs while efficiently managing its operations. The functions reporting to the CEO are: 1) Accounting & Finance, 2) Marketing & Sales, 3) HRM, 4) Quality Assurance 5) Supply Chain and 6) Production. Management committee does not exist.

Management Team Mr. Malik is also the Chief Executive Officer of the Company. He is assisted by a team of seasoned professionals. Company's Secretary and Finance Manager - Mr. Mushitaq is associated with the Company since its inception, possessing all relevant expertise, knowledge and experience. General Manager of the Company, Mr. Muhammad Akram is associated with the Company for more than 24 years.

Effectiveness The head of departments meet as and when required. Senior management gives input in the decision-making while Mr. Malik is the final authority for all decision-making processes.

MIS Pearl Petro deployed "SoftTech" accounting software, having all the required modules like inventory, sales & marketing, finance, procurement, HR and others. It generates reports on a daily, weekly and monthly basis. Further Company also installed a database on-site, and stores data on servers on a daily basis.

Control Environment : The Company has acquired ISO-9001, ISO-22000, ISO-14001 and PS-3733 certifications to enhance and maintain the highest levels of quality standards. Additionally, the Company has developed an effective mechanism for the identification, assessment, and reporting of all types of risk arising out of the business operations. Management of the Company ensures operational efficiency under the direct supervision of CEO.

Business Risk

Industry Dynamics A major challenge faced by the sector is prices and availability of raw materials specifically polymers such as polypropylene, & polyethylene. Polymers' prices are largely a function of global crude oil prices, demand-supply dynamics, and exchange rate volatility. The recent market dynamics of the cost base of raw materials represented a rising trend. This coupled with the significant depreciation of the currency would be expected to lead to higher raw material prices and thus create pressure on margins going forward. If the cost of raw materials with predictable exchange rates sustain, it will produce better profitability and margins for the industry in the future.

Relative Position The Company has built a strong market position in the industry with its long operations resulting in healthy relationships with suppliers, distributors, and customers. Additionally, with sponsors' strong understanding of the market, the Company was able to expand its capacities since its inception.

Revenues Pearl Petro has been constantly developing new products based on customer needs. During FY22, revenue of the Company showed substantial growth of 52.5% YoY to PKR 8.6bln (FY21: PKR 5.6bln). This significant increase in revenue is backed by the increased demand for PP bags. Top-3 products (i.e., PT Poly Bags (48.9%), Polypropylene Bags (21.3%), HD poly bags (11.3%)) constitute 81.5% of the total sales; reflecting high concentration. Pearl Petro makes all its sales directly to its customers. The Company's customers include well-established brands such as Punjab Foods, Engro Fertilizers, etc. The Company's top ten customers contributed 9.9% to total revenue signifying a low level of concentration. During 9MFY23, revenue of the Company stood at PKR~ 7,985mln.

Margins The major (raw material) Polyethylene is a petrochemical derivative and its prices remain highly volatile, thus Pearl Petro is exposed to the risk of volatility in the prices of crude oil. Despite a sharp fluctuation in the price of raw materials, Company managed to sustain its gross margin at 8.4% (FY21: 7.6%, 9MFY23: 8.7%) in FY22. Operating profit margin of the Company was recorded at 7.3% in FY22 (FY21: 6.1%, 9MFY23: 7.0%). Although the Company's bottom line remained robust at PKR 199mln for FY22 (compared to PKR 182mln in FY21), with a net profit margin of 3.2% (compared to 2.6% in FY21), the Company was negatively impacted by a significant foreign exchange loss and high finance costs, which had an adverse effect on its profitability. During 9MFY23, net profit of the Company was reported at PKR~ 251mln, and net profit margin reported to 3.1%

Sustainability Management will continue to work on preserving its cost leadership and performance uptrend. Furthermore, management intends to add a three-layer printing unit that will expand the Company's income base and provide new prospects.

Financial Risk

Working Capital The Company's operations remain working capital-intensive by nature due to high raw material inventory holding, which can be attributed to its growing scale of operations. In addition, rising prices resulted in high inventory levels. In FY22, the Company's utilisation of borrowing limits remained high as well as stretched through payables. As at end-Jun22, Pearl Petro reported 39 average inventory days (end-Jun21: 26 days). It maintains 2 - 3 months of raw materials inventory on account of the import of raw materials. However, the finished goods inventory is order backed. The credit period allowed to customers is around 20-25 days. During 9MFY23, Pearl's net working capital days surged to 46 days.

Coverages The Company's liquidity position is adequate, driven by the healthy annual cash accrual and supported by the recent equity infusion through share capital. The interest coverage ratio (EBITDA/Finance cost) stood at 5.4x (Jun'21: 13.1x). The Company's liquidity situation is well bolstered by FCFO of PKR 384mln (FY21: PKR 253mln). Also, management intends to limit their exposure to leverage and focus more on equity. During 9MFY23, interest coverage ratio stands at 5.1x.

Capitalization Pearl has leveraged capital structure, gearing ratio of the Company stood at 66.9% at end of Jun-22 (Jun-21: 62.3%). Increase in gearing ratio owing to the utilization of funded lines from FIs. STB of the Company stood at PKR 1,539mln in FY22 (FY21: PKR 1,155mln) whereas, LTB of the Company surged to PKR~ 460mln (FY21: PKR~ 94mln). Equity of the Company stood at PKR~1,048mln (FY21: PKR~ 894mln). During 9MFY23, Company's equity stands at PKR~ 1,299mln.



The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Pearl Petro Industry (Pvt) Ltd. ##	Mar-23 9M	Jun-22 12M	Jun-21 12M	Jun-20 12M
A BALANCE SHEET				
1 Non-Current Assets	1,883	2,113	1,369	341
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	3,046	2,404	1,028	862
a Inventories	1,200	1,426	360	375
b Trade Receivables	1,296	416	313	256
5 Total Assets	4,929	4,517	2,397	1,203
6 Current Liabilities	1,540	951	112	43
a Trade Payables	839	793	55	1
7 Borrowings	1,699	2,118	1,282	467
8 Related Party Exposure	-	-	120	-
9 Non-Current Liabilities	390	400	34	25
10 Net Assets	1,300	1,048	849	668
11 Shareholders' Equity	1,299	1,048	849	668
B INCOME STATEMENT				
1 Sales	7,985	8,689	5,698	3,643
a Cost of Good Sold	(7,290)	(7,963)	(5,267)	(3,372)
2 Gross Profit	695	726	430	271
a Operating Expenses	(137)	(91)	(83)	(65)
3 Operating Profit	558	634	347	206
a Non Operating Income or (Expense)	(86)	(160)	(60)	(33)
4 Profit or (Loss) before Interest and Tax	472	475	287	173
a Total Finance Cost	(118)	(109)	(27)	(10)
b Taxation	(103)	(167)	(79)	(67)
6 Net Income Or (Loss)	251	199	182	96
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	457	384	253	116
b Net Cash from Operating Activities before Working Capital Changes	349	318	233	107
c Changes in Working Capital	100	57	(25)	122
1 Net Cash provided by Operating Activities	449	374	207	229
2 Net Cash (Used in) or Available From Investing Activities	78	(906)	(1,042)	(184)
3 Net Cash (Used in) or Available From Financing Activities	3	678	251	(4)
4 Net Cash generated or (Used) during the period	529	146	(584)	40
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	22.5%	52.5%	56.4%	10.2%
b Gross Profit Margin	8.7%	8.4%	7.6%	7.4%
c Net Profit Margin	3.1%	2.3%	3.2%	2.6%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	7.0%	5.1%	4.0%	6.5%
e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh	28.5%	21.0%	23.9%	15.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	74	53	42	67
b Net Working Capital (Average Days)	46	35	40	67
c Current Ratio (Current Assets / Current Liabilities)	2.0	2.5	9.2	19.9
3 Coverages				
a EBITDA / Finance Cost	5.1	5.4	13.1	20.7
b FCFO / Finance Cost+CMLTB+Excess STB	0.4	0.3	0.5	0.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.7	6.0	3.3	4.4
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	56.7%	66.9%	62.3%	41.1%
b Interest or Markup Payable (Days)	0.0	0.0	0.0	0.0
c Entity Average Borrowing Rate	8.2%	6.1%	2.8%	2.0%

Credit Rating

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	Very high credit quality. Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
AA-	
A+	
A	High credit quality. Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
A-	
BBB+	Good credit quality. Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BBB	
BBB-	
BB+	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
BB	
BB-	
B+	
B	High credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
B-	
CCC	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
CC	
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*The correlation shown is indicative and, in certain cases, may not hold.

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults, or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

- a) Broker Entity Rating
- b) Corporate Rating
- c) Debt Instrument Rating
- d) Financial Institution Rating
- e) Holding Company Rating
- f) Independent Power Producer Rating
- g) Microfinance Institution Rating
- h) Non-Banking Finance Companies Rating

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(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)

ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)

iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)

(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

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(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)

(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).

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(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)

(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity

(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)

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(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

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Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)

(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)

(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(F-VII)

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