



The Pakistan Credit Rating Agency Limited

Rating Report

Saif Textile Mills Limited

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Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Dec-2018	A-	A2	Stable	Maintain	-
27-Jun-2018	A-	A2	Stable	Maintain	-
29-Dec-2017	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Saif textile mills limited (Saif Textile), a prominent textile venture of Saif Group, is involved in manufacturing and marketing of various varieties of cotton yarn including, melange yarn, dyed yarn, man-made yarn and raw white yarn. Despite challenging textile industry dynamics, Saif Textile managed to maintain its optimal capacity while upgrading its machinery in order to ensure operational efficiencies and eventually higher production volumes. Meanwhile, rupee devaluation has provided a breather to the Company’s margins; even though its export share is relatively small. Re-imposition of custom duties and sales tax on cotton & yarn imports, coupled with increasing interest rates has made it challenging for the local textile industry. The company's margins have consequently been volatile. Going forward, with better efficiency, the management expects the margins to improve and come comparable with peers. The financial profile of the company remains constrained by debt driven BMR thus keeping pressure on coverages and highly leveraged capital structure. The ratings incorporate the experienced management team and the entity’s association with Saif Group, as the Group has demonstrated support in the past.

The ratings are dependent on managing financial obligations while improving business margins. Any further accumulation of debt and/or shift from current business strategy, impacting the risk profile of the entity, may negatively affect the ratings. Going forward, Saif group's support to the entity would remain important.

Disclosure	
Name of Rated Entity	Saif Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Textile(Oct-18)
Rating Analysts	Muhammad Hassan muhammad.hassan@pacra.com +92-42-35869504

Profile

Legal Structure Saif Textile Mills Limited (Saif Textile), was incorporated in 1989 as a public limited company.

Background Saif Textile is associated with Saif Group since its inception. The group has presence in spinning sector through Kohat textile and Maditerranean Textile. The company's production facilities are located in Gadoon Industrial Estate, KPK.

Operations The company's current operational capacity comprises 100,968 Spindles. The total energy requirement of the company clocks in at ~10MW which is wholly met through gas fired captive plant. Furthermore, the company has NTDC connection as alternative sources.

Ownership

Ownership Structure Saif Group holds majority of the shareholding of Saif Textile's through its holding company – Saif Holdings. It exercises its control over the company's board by virtue of its ~50% shareholding in the company, followed by NIT and State life with 7% and 4% stake respectively. The company has a large free float dispersed among general public.

Stability The group has a holding company in place, portraying a structured line of succession. The holding company constitutes equal stakes of all Saif brothers; structuring succession going forward.

Business Acumen Saif Group – one of the oldest medium-sized business conglomerate in Pakistan with considerable interests in textile. The sponsors have developed expertise in textile spinning sector. However, the Group's growth in textile sector was limited but it sustained through the volatility of textile industry.

Financial Strength Saif Group is one of the leading industrial and services conglomerates in Pakistan. The Group has interest's in oil and gas exploration, power generation, textiles manufacturing, real estate development and health care services. The Group have 7 subsidiaries and 4 associated companies across different sectors. The Group financial strength is considered strong, portraying ability to support its Group entities in time of need, as they have demonstrated in the past.

Governance

Board Structure Saif Textile's board comprises seven members, including the Chairman - Mr. Osman Saifullah. The board include six non-executive directors, while one director is independent. In recent elections the board have been down sized to seven directors, for the purpose one director was removed. Additionally, Mr. Faisal Saifullah Khan has joined the board, replacing an existing director.

Members' Profile Mr. Osman Saifullah – Chairman, has a post graduate degree in engineering from University of Oxford and post graduate degree in business administration from University of Stanford. Mr. Osman has overall experience of over two decades and he is also a senator. The board comprises vast knowledge and experience of textile, though diversity in experiences exists as well, ensuring a requisite skill mix for decision making.

Board Effectiveness Two committees: Audit and Human Resource & Remuneration, are in place to assist the board in relevant matters and ensure proper oversight. Attendance of board members in meetings remains adequate and meeting minutes were formally documented. Meanwhile, overall strategy of the company is discussed in bi-annual group meeting of Saif Group, whereas, day to day operations are discussed in board meetings.

Financial Transparency M/s Shinewing Hameed Chaudhri & Co., Chartered Accountants are the external auditors of the company. They have expressed unqualified opinion on the financial statements of the company for the year ended June 30, 2018.

Management

Organizational Structure The management team is headed by Mr. Zaheen ud Din (CEO), with defined reporting line to ensure smooth operations and efficiency. Moreover, the company have nine functional departments, while all HOD's reports directly to CEO.

Management Team Mr. Zaheen ud Din, a Chartered Accountant, has been serving as the CEO for four years. He is supported by a team of seasoned professionals, most of whom have been associated with the company for a reasonably long period of time.

Effectiveness There is no formal management committee, however the company maintains adequate IT infrastructure and related controls. Moreover, delegation of power by sponsors to management bodes well with management's effectiveness.

MIS Saif Textile has in place Microsoft Dynamics based ERP system that provides comprehensive MIS reporting.

Control Environment The company is compliant with following quality assurance standards for yarn production, which include OEKA TEX 100, ISO 9001:2008, ISO 14001, Global Organic Textile Standards and Supima.

Business Risk

Industry Dynamics During FY18, total textile exports of Pakistan stood at USD ~ 13.53bln, a 9% YoY growth. Re-imposition of custom duty and sales tax on cotton imports in FY19 budget, coupled with exclusion of tax rebate on yarn and greige fabric has further stretched the industry margins. However, rupee devaluation in recent times provide breather to textile ventures with net exports.

Relative Position Saif Textile's association with Saif Group strengthen the company's position at group level. However, on standalone basis the company's share in local spinning industry is minimal.

Revenues During FY18, the company's top-line clocked in at ~PKR 7,852mln, a ~3.5% YoY increase. This is due to better pricing in local market, favoring the domestic-oriented nature of the company. The company's sales remained tilted toward local market ~92%. Moreover, Top ten customers' revenue concentration in local markets is considered high; though declining over the years. Whereas, during 1QFY19 Saif Textile's revenues amounted to ~PKR 1,888mln, posting a growth of 8% QoQ.

Margins The company's gross margins improved (FY18: 10.9%, FY17: 10.1%), a factor of lower than proportionate increase in cost of sales (~2.5%). This is attributable to prudent inventory procurement and constant BMR activities in previous years, followed by better operating margins (FY18: 6.5%, FY17: 5.2%). The finance costs increased by ~82%, as a result of higher long term borrowing, coupled with increased interest rates. While, on account of taxation the company's net profit increased to ~PKR 46mln (FY17: ~PKR 23mln). In 1QFY19, the company's margins picked up (gross -1QFY19: 13.4%, net - 1QFY19: 8.9%), owing to better local industry dynamics.

Sustainability The company has incurred BMR of almost PKR 1,3bln in recent years, comprising induction of energy efficient machinery and partial replacement of old spindles with energy efficient spindles. This will ensure market capitalization of wider range of products with better efficiency, eventually strengthening company's margins.

Financial Risk

Working Capital Though the company's reliance on STB has declined during the year, portraying prudent management of cash flows. At the same time, STB is equal to net trade assets, limiting further room to borrow. Meanwhile, increase in receivable days (FY18: 53days, FY17, 43days), lead to higher working capital days (gross - FY18: 143days, FY17, 134days, net - FY18: 131days, FY17 122days); though at par with peers. The trend of increasing working capital cycle continued in 1QFY19, reflected from higher working capital days (gross - 1QFY19: 158days, net - 1QFY19: 144days), on account of higher receivables.

Coverages During FY18, the company's operating cash flows (FCFO) posted a minimal growth. However, higher then proportionate increase in finance cost has resulted in deteriorated interest coverage (FY18: 1.7x, FY17: 2.0x), while the debt coverage remained stagnant at ~0.7x. Whereas, coverages marginally improved in 1QFY19 to stand at (interest: 2.1x, debt: 1.0x), owing to increased profitability. Going forward, rise in interest rate may stretch the company's coverages.

Capitalization Saif textile has a highly leveraged capital structure (~69.5%) at end-June 18 (end-June 17: 70.1%). Total debt stood at PKR 5,472mln, mainly comprising current debt ~ 66.2%. During 1QFY19 the company's leveraging remained the same.



Saif Textile Mills Limited

BALANCE SHEET	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	1QFY19	FY	FY	FY
Non-Current Assets	5,164	5,023	4,521	4,630
Investments (Incl. Associates)	6	5	6	6
Equity	6	5	6	6
Loans to Associates/Debt Securities	-	-	-	-
Investment Property	-	-	-	-
Current Assets	4,212	3,977	4,112	3,393
Inventory	2,176	1,836	2,029	1,766
Trade Receivables	1,251	1,268	1,018	1,759
Others	785	872	1,065	869
Total Assets	9,381	9,005	8,639	8,029
Debt/Borrowings	5,778	5,472	5,319	4,679
Short-term	3,362	3,299	3,430	2,768
Long-term (Incl. Current Maturity of Long-Term Debt)	2,416	2,173	1,889	1,912
Other short-term liabilities	920	903	786	848
Other long-term liabilities	232	227	261	261
Shareholders' Equity	2,451	2,402	2,273	2,241
Total Liabilities & Equity	9,381	9,005	8,639	8,029

INCOME STATEMENT

Turnover	1,888	7,852	7,586	6,698
Gross Profit	253	855	763	622
Net Other Income	(13)	(78)	28	3
Financial Charges	(104)	(385)	(315)	(324)
Net Income	49	46	23	(49)

Cashflow Statement

Free Cash Flow from Operations (FCFO)	215	668	641	449
Net Cash changes in Working Capital	(205)	204	(814)	(257)
Net Cash from Operating Activities	(83)	550	(435)	(68)
Net Cash from Investing Activities	(203)	(602)	(214)	(469)
Net Cash from Financing Activities	293	44	639	539

Ratio Analysis

Performance				
Turnover Growth (vs. SPLY)	8%	4%	13%	-16%
Gross Margin	13%	11%	10%	9%
Net Margin	3%	1%	0%	-1%
Coverages				
Interest Coverage (FCFO/Gross Interest)	2.1	1.7	2.0	1.4
Core: (FCFO) / (Gross Interest+CMLTD+Uncovered Total STB)	1.0	0.7	0.7	0.5
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	1.0	0.7	0.7	0.5
Debt Payback (Total LT Debt Including Uncovered Total STBs) / (FCFO- Gross Inter	22.5	8.5	6.2	17.4
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	143.7	131.5	122.0	118.7
Capital Structure (Total Debt/Total Debt+Equity)	70%	69%	91%	89%

Saif Textile Mills Limited

December 2018

Credit Rating Scale & Definitions

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.

Long Term Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
AA+ 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.	A1	A strong capacity for timely repayment.
A+ 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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
BBB+ BBB 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
BB+ BB 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.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
B+ 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.	C	An inadequate capacity to ensure timely repayment.
CCC CC C	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.		
D	Obligations are currently in default.		



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) 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.

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

Rating Team Statements

(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)

Conduct of Business

- (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.
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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)
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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)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
- (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)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

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- (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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