



The Pakistan Credit Rating Agency Limited

Rating Report

Saif Textile Mills Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
26-Jun-2020	A-	A2	Stable	Maintain	YES
27-Dec-2019	A-	A2	Stable	Maintain	-
28-Jun-2019	A-	A2	Stable	Maintain	-
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. Saif Textile has managed to increase its capacity and revenues in recent years, achieving economies of scale. The Company's margins remain in line with its peer though net margins deteriorate due to high finance cost, a facet of high leveraging and increasing interest rates. Due to Covid-19 and subsequent lockdown, demand for yarn has been impacted significantly, consequently squeezing margins of the Company. The financial profile of the Company remains constrained by debt driven BMR activities, resulting in highly leveraged capital structure with stretched coverages. However, SBP's initiative of reducing interest rates (525bps cut) and deferral of principal repayments for one year will provide relief. The assigned ratings incorporate an experienced management team, strong financial muscle of the Sponsors and their willingness to support the entity as demonstrated historically.

The Rating Watch signifies the prevailing uncertainty due to the outbreak of COVID-19 pandemic and tough economic conditions. This has impacted the entire textile chain as demand contracts due to shutdown in domestic and global markets. Recent SBP measures will provide some respite in this regard. The Company's production facilities were shut down but resumed after four days, though demand remains subdued. Demand has improved recently but will take time to reach pre-corona level. PACRA is closely monitoring the situation and will take rating action accordingly.

The ratings are dependent on the Company's ability to sustain its operations in prevailing conditions. Significant deterioration in business profile due to prolonged downturn leading to deterioration in coverages and/or margins will impact the ratings. Going forward, Saif group's support to the entity and prudent debt management would remain critical.

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-19),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria Rating Modifier(Jun-19)
Related Research	Sector Study Spinning(Sep-19)
Rating Analysts	Adil Kaleem adil.kaleem@pacra.com +92-42-35869504

Profile

Legal Structure Saif Textile Mills Limited (Saif Textile), was incorporated in 1989 as a Public Limited Company. It is Listed on Pakistan Stock Exchange.

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 is ~10MW which is wholly met through gas fired captive plant. Furthermore, the Company has NTDC connection as alternative source.

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 freefloat dispersed among general public.

Stability The Group has a holding company in place, with equal shareholding of all Saif brothers, portraying structured line of succession. However, the transfer of ownership to next generation is not documented yet

Business Acumen Saif Group is one of the oldest medium-sized business conglomerate in Pakistan with considerable interests in textile. The sponsors have a presence of five decades in local Spinning industry, eventually developing expertise. However, the Group's growth in textile sector was limited but it sustained through the volatility experienced by local textile industry.

Financial Strength Saif Group is one of the leading industrial and services conglomerates in Pakistan. The Group's interests lies in oil and gas exploration, power generation, textiles manufacturing, real estate development and health care services, through 7 subsidiaries and 4 associated companies across different sectors. The strong financial muscles of the Group portrays ability to support Saif Textile in time of need, as demonstrated in the past.

Governance

Board Structure Saif Textile's board comprises seven members, including the Chairman - Mr. Osman Saifullah. The board include four non-executive directors, while two directors are independent.

Members' Profile Mr. Osman Saifullah – Chairman – holds 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 members have vast knowledge and expertise of textile industry, though diversity in experiences exists as well, ensuring a requisite skill mix for strategic planning.

Board Effectiveness Two committees: Audit and Human Resource & Remuneration, are in place to assist the board in relevant matters and it ensures 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 meeting of Saif Group, whereas, operational matters 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 periods ended June 30, 2019 and December 31, 2019.

Management

Organizational Structure The management team is headed by Mr. Zaheen ud Din (CEO), with a defined reporting line to ensure smooth operations and efficiency. Meanwhile, the Company has 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 them have been associated with the Company for a reasonably long period of time.

Effectiveness There is no formal management committee, however the Company maintains an adequate IT infrastructure and related controls. Additionally, delegation of power by sponsors to management is considered positive for management 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; OEKA TEX 100, ISO 9001:2008, ISO 14001, Global Organic Textile Standards and Supima.

Business Risk

Industry Dynamics Textile exports of the country dropped by ~8% for 11MFY20 to stand at ~USD 11.6bln as compared to ~USD 12.6bln in 11MFY19 due to slowdown in demand for textile products internationally, instigated by Covid-19 led lock downs in major export destinations. Going forward, prevailing uncertainty in the dynamics of textile sector due to Covid-19 outbreak globally, lifting of lock downs in most countries, contraction in local and international demand is expected to affect the entire textile value chain. Locally, textile sector will find comfort in relief measures introduced by State Bank of Pakistan such as, deferment of loan payments for one year, low interest rates and salary refinance scheme.

Relative Position The Company's association with Saif Group strengthen its position in local spinning industry. However, on standalone basis the Company's share in local spinning industry is minimal.

Revenues During 9MFY20, the Company's revenue declined by 10% and stood at PKR 6,043mln (PKR 6,247mln) on the back of withdrawal of the zero-rating status of textile status and Covid-19 outbreak and subsequent lockdown in the country. Revenue remains dominated by local sales with 92.5% share in revenues. Revenue is expected to deteriorate further on the back of COVID-19 outbreak and lockdown.

Margins Despite lower revenue, the Company was able to improve its gross margins in 9MFY20 to 13% (9MFY19: 11.45) on the back of better yarn prices. Similarly operating margins also improved and stood at 8.3% (9MFY20: 7%). However due to higher finance cost (9MFY20: PKR 645mln; 9MFY19: PKR 411mln) the Company's Net margin further dropped (9MFY20: -3.9% : 9MFY19: -1.2%) and the Company posted higher loss Net loss (9MFY20: PKR -235mln, 9MFY19: PKR -75mln). Profitability is expected to further decrease as margins have deteriorated since COVID-19 outbreak.

Sustainability Due to COVID-19 outbreak and subsequent lockdown, Saif Textile has to shut down all of its operations as per government directive. However, after getting approval the Company resumed its operations though production remained low. Since the government has eased the lockdown from 11th May demand has improved with production capacity hovering around 65%-80% in May and over 80% in June. However, full resumption of operations and recovery in sales of the Company remains unclear. The Company's performance is expected to deteriorate further by end FY20

Financial Risk

Working Capital Saif Textile meets its working capital requirement through short term borrowing. During 9MFY20, the Company's inventory cycle increased (9MFY20: 111 days; 9MFY19: 88 days) on the back of higher inventory procurement and lower revenue. Consequently, networking capital days also increased (9MFY20: 151 days; 9MFY19: 132 days). The Company's room to borrow at trade asset level further deteriorated and stood at -15% showing an asset-liability mismatch.

Coverages In 9MFY20, the Company's FCFO improved slightly (9MFY20: PKR 603mln; 9MFY19: PKR 569mln) on the back of better margins. however, due to higher short term borrowing and higher interest rates, finance cost increased which led to further deterioration of the coverages (Interest coverage : 9MFY20: 1x; 9MFY19: 1.5x; Debt coverage: 9MFY20: 0.6x, 9MFY19: 0.9x). However, the Company has opted to defer principal repayment of debt for one year under SBP COVID-19 relief initiative which will provide a much-needed breather to the coverages.

Capitalization Despite an increase in short term borrowings (9MFY20: PKR 2,571mln, 9MFY19: PKR 2,191mln), Saif Textile has slightly reduced its leverage to 69.2% in 9MFY20 (9MFY19: 72.9%), owing to the waiving off of subordinated loan. 66% of the borrowing is of short term and ~10% borrowing is from SBP at concessionary rates. The Company has recently availed SBP loan for salaries introduced by SBP under COVID-19 relief initiative.



Saif Textile Mills Limited Textile	Mar-20 9M	Jun-19 12M	Jun-18 12M	Jun-17 12M
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A BALANCE SHEET

1 Non-Current Assets	5,622	5,439	5,023	4,525
2 Investments	40	6	5	6
3 Related Party Exposure	10	11	10	4
4 Current Assets	4,886	4,547	3,967	4,104
<i>a Inventories</i>	2,571	2,340	1,836	2,029
<i>b Trade Receivables</i>	1,519	1,211	1,268	1,018
5 Total Assets	10,558	10,003	9,005	8,639
6 Current Liabilities	805	911	903	786
<i>a Trade Payables</i>	428	542	445	409
7 Borrowings	6,594	5,664	5,472	5,319
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	223	229	227	261
10 Net Assets	2,937	3,198	2,402	2,273
11 Shareholders' Equity	2,937	3,198	2,402	2,273

B INCOME STATEMENT

1 Sales	6,043	8,976	7,852	7,586
<i>a Cost of Good Sold</i>	(5,250)	(7,938)	(6,997)	(6,823)
2 Gross Profit	793	1,038	855	763
<i>a Operating Expenses</i>	(315)	(356)	(342)	(370)
3 Operating Profit	478	682	513	393
<i>a Non Operating Income</i>	4	833	(78)	28
4 Profit or (Loss) before Interest and Tax	482	1,515	435	421
<i>a Total Finance Cost</i>	(645)	(595)	(385)	(315)
<i>b Taxation</i>	(73)	(89)	(4)	(84)
6 Net Income Or (Loss)	(235)	830	46	23

C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	603	796	668	641
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	8	313	346	379
<i>c Changes in Working Capital</i>	(521)	(407)	204	(814)
1 Net Cash provided by Operating Activities	(513)	(94)	550	(435)
2 Net Cash (Used in) or Available From Investing Activities	(402)	(676)	(602)	(214)
3 Net Cash (Used in) or Available From Financing Activities	908	781	44	639
4 Net Cash generated or (Used) during the period	(8)	11	(8)	(10)

D RATIO ANALYSIS

1 Performance				
<i>a Sales Growth (for the period)</i>	-10.2%	14.3%	3.5%	--
<i>b Gross Profit Margin</i>	13.1%	11.6%	10.9%	10.1%
<i>c Net Profit Margin</i>	-3.9%	9.3%	0.6%	0.3%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	11.2%	10.2%	9.1%	9.2%
<i>e Return on Equity (ROE)</i>	-10.2%	29.7%	2.0%	1.0%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	173	135	143	113
<i>b Net Working Capital (Average Days)</i>	151	115	123	93
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	6.1	5.0	4.4	5.2
3 Coverages				
<i>a EBITDA / Finance Cost</i>	1.1	1.6	2.0	2.4
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	0.5	0.7	0.7	0.7
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	-214.4	8.7	8.0	5.8
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	69.2%	63.9%	69.5%	70.1%
<i>b Short-Term Borrowings / Total Borrowings</i>	0.7	0.7	0.6	0.6
<i>c Average Borrowing Rate</i>	13.3%	10.1%	6.8%	5.5%

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

Restrictions

- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (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.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (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)
- (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)

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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