



The Pakistan Credit Rating Agency Limited

## Rating Report

### Zafa Pharmaceutical Laboratories (Pvt.) 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
13-Sep-2024	A-	A2	Stable	Maintain	-
13-Sep-2023	A-	A2	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

Zafa Pharmaceuticals (Pvt.) Limited (the “Company”) is a leading domestic player that holds a prominent position within the local market. The Company specializes in the formulation development, manufacturing, testing, and marketing of a diverse portfolio of quality, cost-effective medicines. Notably, its manufacturing facilities are among the few dedicated sites for producing Beta-Lactam and Cephalosporin products. The Board of Directors comprises experienced professionals, and its size is considered well-suited for effective governance and oversight. Zafa Pharmaceuticals (Pvt.) Limited’s top five products include Folic Acid tablets, Famila Injection, Zodip tablets, Xynosine Nasal Spray, and Ciprofloxacin HCL. The Company commands a good market share within the folic acid market. The Company is dedicated to its vision of delivering high-quality healthcare products to the public at competitive prices, offering a value proposition that is notably more affordable compared to its competitors. Pakistan’s pharmaceutical sector is a mix of local and multinational companies, with local firms holding a substantial share of the market. Global inflation, high logistics costs, and massive PKR depreciation have impacted the pharma sector negatively. On the other hand, Pakistan’s pharmaceutical industry experienced a significant increase driven by the government’s deregulation of drug prices for non-essential categories and a one-time price adjustment for 146 drugs in Feb 2024. In this context of industry-wide price adjustments, the Company’s revenue has increased by ~20% as compared with the previous period. The Company has grown and augmented its position and is seen fortifying its production capabilities and product range. In the coming years, some new products are also in the pipeline. Concurrently, the Company reported an enhancement in its profit margins, reflecting improved operational efficiency and financial performance. Additionally, the Company holds investments in its different subsidiaries. The Company’s capital structure is characterized by low leverage, with a debt-to-equity ratio of 30% during FY23 (FY22: 18%). The Company’s debt structure primarily consists majorly the short-term borrowings obtained for working capital management. Furthermore, the Company has outlined plans for future capital expenditures, which are expected to further impact its borrowing levels and coverage ratios.

The ratings are dependent on management’s ability to sustain its growth in revenues, margins and profitability. Prudent management of the working capital, and maintaining sufficient cash flows and coverages are imperative. Further improvement in governance structure remains important for the ratings.

#### Disclosure

<b>Name of Rated Entity</b>	Zafa Pharmaceutical Laboratories (Pvt.) Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology   Rating Modifiers(Apr-24),Methodology   Corporate Rating(Jul-23)
<b>Related Research</b>	Sector Study   Pharmaceuticals(May-24)
<b>Rating Analysts</b>	Muhammad Atif Chaudhry   Atif.Chaudhry@pacra.com   +92-42-35869504

## Profile

**Legal Structure** Zafa Pharmaceutical Laboratories (Private) Limited (the Company) was incorporated in Karachi, Pakistan as a private company limited by shares on 8 November 1974, previously under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The principal activity of the Company is to manufacture pharmaceutical products.

**Background** Zafa Pharmaceutical laboratories (Private) Limited has become one of the recognized pharmaceutical companies in Pakistan, Mr. Mohammad Amin Khan (late) Exemplified strong dedication and leadership prowess while serving as the Chairman and CEO at Zafa.

**Operations** The company specializes in the production of pharmaceuticals under multiple segments and is actively involved in the marketing and sales of licensed products approved by the Drug Regulatory Authority of Pakistan. Zafa boasts a comprehensive product portfolio of over 300 products, with an additional 30 products currently in development. Notably, 13 of their products have attained a leading market position within Pakistan. The company operates 10 manufacturing facilities, majorly situated in the industrial zone of Karachi.

## Ownership

**Ownership Structure** Zafa is majority owned by Mr. Jawad Amin Khan. (~91%); while other partners include Mr. Mohammad Amin Khan (late) (3.7%), Mrs. Zafar Amin (3.7%), Mrs. Maria Jawad Khan (0.11%), Mrs. Saba Ahmed (1.34%), and Mr. Mohammad Shah Mir Amin Khan (0.11%).

**Stability** Zafa Pharmaceutical is a prominent player in the pharmaceutical industry, conducting its operations in the country through its four affiliated companies. The strategic acquisition of a significant stake in BALSAM Pharmaceutical Company Limited will further strengthen its position in international market.

**Business Acumen** Zafa Group, founded in 1973, is a prominent player in Pakistan's healthcare industry. It is renowned for its expertise in establishing international partnerships and strategic relations with reputable global firms. With a widespread presence across the country, Zafa has a team of skilled medical representatives and healthcare professionals.

**Financial Strength** Mr. Mohammad Amin Khan (late), the visionary behind Zafa Pharmaceutical and its primary sponsor, embarked on his career in the Pakistani pharmaceutical industry with a modest investment. Zafa Pharmaceutical Laboratories commenced its journey with a mere four products and a single factory, driven by a resolute mission to contribute to the betterment of the society. As at FY23, the Company has adequate asset and equity base.

## Governance

**Board Structure** The Board of Directors of Zafa Pharmaceutical consist of five members, all of whom are family representatives. Notably, there are currently no independent directors on the board. The composition of the board includes accomplished professionals with extensive background in the pharmaceutical and financial services sector. Lack of independent oversight and diversity indicates a room for improvement in the Company's governance structure.

**Members' Profile** Mr. Jawad Amin Khan, the Managing Director of the company, holds an MBA degree from Pakistan and possesses more than three decades of diverse professional experience within the country. With a remarkable tenure of 32 years in the pharmaceutical industry, he is deeply entrenched in the field. Additionally, Mr. Khan holds senior positions within other Group companies operating in the pharmaceutical and glass product industries

**Board Effectiveness** Zafa Pharmaceutical has no formal board committee in place at present.

**Financial Transparency** The auditors of the company are EY Ford Rhodes Chartered Accountants. There is an established Internal Audit function, that reports directly to the CEO/MD.

## Management

**Organizational Structure** Mr. Jawad Amin Khan, currently serving as the MD & CEO of Zafa, assumed the role of managing director within the company in 1991. With a wealth of experience spanning up to three decades, his expertise is predominantly focused on the pharmaceutical industry. Mr. Khan is backed by a seasoned core management team, comprising individuals with extensive tenure at Zafa and diverse professional backgrounds. Leading the financial operations of the company, Mr. Adnan (M.A Economics, LL.M, M.B.A, FCIS, CA) serves as the CFO of the Company.

**Management Team** Mr. Jawad Amin Khan is the CEO and is associated with the company for more than 30 years Mr. Khan has a Bachelor's degree in Science & Masters in Business Administration. Management team has long association with Zafa Pharmaceutical adding the required experience in Pharma industry and their respective fields. Whereas, Mr. Adnan holds the position of CFO in the Company.

**Effectiveness** The long association of the Company's senior management ensures consistency in overall policies and strengthens the management structure. Currently, the Company has no formal management committees in place, but company is in process of creating management committees in the near future.

**MIS** Zafa has successfully implemented and currently utilizes the complete suite of developed inhouse Oracle module as part of their enterprise resource planning (ERP) system. The ERP Applications include Finance, Procurement, Human Resources, Production, Sales, Laboratory Analysis, and Automation. These applications are updated from time to time as required and managed by the Development Team.

**Control Environment** To ensure operational efficiency, the Company has setup an internal audit function, which implements and monitors the policies and procedures of the Company. The internal audit department ensures compliance and efficiency by conducting quarterly evaluations. A quarterly presentation is sent to the MD by the CFO, detailing the company's financial performance for the quarter.

## Business Risk

**Industry Dynamics** Pakistan's pharmaceutical sector is a mix of local and multinational companies, with local firms holding a substantial share of the market. Pakistan's pharmaceutical industry achieved sales of Rs916 billion (USD 3.3 billion) in FY24, a 22% year-on-year (YoY) increase in PKR terms. The significant price hikes were largely driven by the government's approval of deregulating drug prices for non-essential categories and a one-time price increase for 146 drugs in February 2024.

**Relative Position** Zafa Pharmaceuticals stands as one of the leading pharmaceutical companies in Pakistan's evolving pharmaceutical landscape. Among the 26 multinational players in the country, Zafa has cemented its reputation not only domestically but also on the global stage, solidifying its strategic position in Pakistan's burgeoning pharmaceutical export market.

**Revenues** The company's revenue is sourced from both domestic and export markets. Local sales, which account for 86% of total revenue, have grown by 20%. Meanwhile, export sales, representing 14% has also surged. This notable increase in sales is primarily attributed to the price adjustments mandated by DRAP.

**Margins** Gross margins of the Company decreased and stood at 33% during FY23 (FY22: 37%) due to increase in the prices of raw material. Operating profit margin of the Company increased and stood at 9.6% during FY23 (FY22: 8.3%) due to increased prices by DRAP. Following this, net profit margins also increased and stood at 5% during FY23 (FY22: 4.2%)

**Sustainability** Going forward, the Company performance will largely depend on the pharmaceutical division, and its industry dynamics. Meanwhile, the Company is expected to continue its stable performance. Earning prospect is dependent on stability of the exchange rate, market share of top products, and profitability.

## Financial Risk

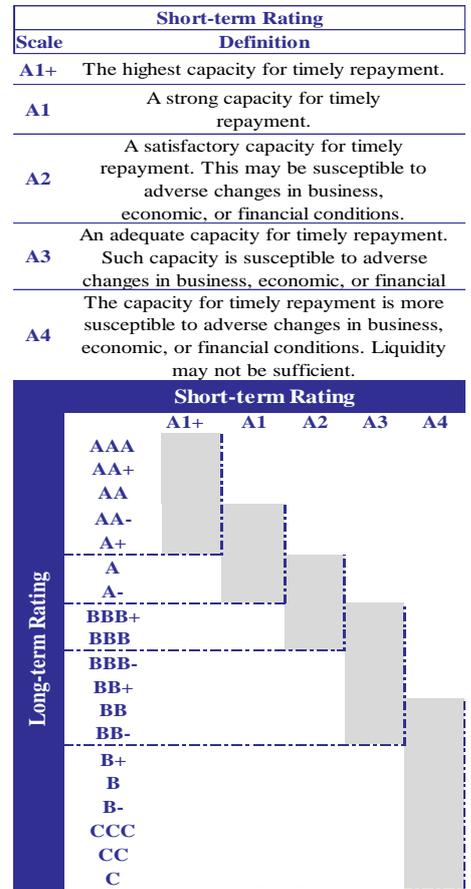
**Working Capital** The average inventory days of the Company deteriorated and stood at 108 days during FY23 (FY2: 90 days). Net working capital for the Company also deteriorated and stood at 116 days during FY23 (FY22: 99 days). Trade receivable days deteriorated and stood at 20 days during FY23 (FY22: 19 days).

**Coverages** The coverages of the Company stood at 4.3x during FY23 (FY22: 14x, 3QFY24: 2.2x) due hike in the finance cost (FY23: 134mln, FY22: 22mln, 3QFY23: PKR 107mln). EBITDA coverage ratio, which indicates the company's ability to cover its finance costs, deteriorated over the year and stood at 1.3x during FY23 (FY22: 3.5x).

**Capitalization** The Company's capital structure is characterized by moderate leverage, with a debt-to-equity ratio of 30% during FY23 (FY22: 18%). Company's debt structure consists of both short-term borrowings and long term borrowing. Furthermore, The Company is planning for CAPEX in future that will also be impacting on the borrowings and coverage of the Company.



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	Definition
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
<b>AA+</b>	<b>Very high credit quality.</b> 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.
<b>AA</b>	
<b>AA-</b>	
<b>A+</b>	<b>High credit quality.</b> 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.
<b>A</b>	
<b>A-</b>	
<b>BBB+</b>	<b>Good credit quality.</b> 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.
<b>BBB</b>	
<b>BBB-</b>	
<b>BB+</b>	<b>Moderate risk.</b> 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>BB</b>	
<b>BB-</b>	
<b>B+</b>	<b>High credit risk.</b> 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>B</b>	
<b>B-</b>	
<b>CCC</b>	<b>Very high credit risk.</b> 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.
<b>CC</b>	
<b>C</b>	
<b>D</b>	Obligations are currently in default.



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

<p><b>Outlook (Stable, Positive, Negative, Developing)</b> 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'.</p>	<p><b>Rating Watch</b> 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.</p>	<p><b>Suspension</b> 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.</p>	<p><b>Withdrawn</b> 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.</p>	<p><b>Harmonization</b> A change in rating due to revision in applicable methodology or underlying scale.</p>
---	---	--	---	---

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

**Disclaimer:** PACRA has used due care in preparation of this document. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information. Contents of PACRA documents may be used, with due care and in the right context, with credit to PACRA. Our reports and ratings constitute opinions, not recommendations to buy or to sell.

### **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 | Clause 11-(A)(p).
- (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)

### **Independence & Conflict of interest**

- (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 | 17-(a)
- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

### **Proprietary Information**

(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA's prior written consent