



The Pakistan Credit Rating Agency Limited

Rating Report

Sarena Textile Industries (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
29-Jul-2022	A	A2	Stable	Maintain	-
30-Jul-2021	A	A2	Stable	Upgrade	-
30-Jul-2020	A-	A2	Positive	Maintain	-
01-Aug-2019	A-	A2	Positive	Maintain	-
30-Jan-2019	A-	A2	Stable	Maintain	-
30-Jul-2018	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Sarena Textile Industries (Private) Limited specializes in weaving, dyeing, printing, finishing and stitching. The Company offers various finished products and has created a niche where it processes and produces specialized cloth for fire resistant and other uniforms. The company is also licensee for PROBAN® in Pakistan. The Company employs experienced professionals, aided by comprehensive reporting, who look after operations of the Company with complete autonomy. The Company has established its presence in the overseas market and also considered a strong player in local market as the revenue is balanced almost equally between the local and export market. Captive clientele in shape of group companies, provide an advantage in local sale. The Company's performance showed resistance, compared in the relative universe. In FY22, revenues depicted increase along with strengthened operating profit. Despite of increase in finance costs, bottom-line demonstrated a significant increase. The Company has a strong financial profile characterized by strong coverage and improving working capital management. Almost all of the borrowings of the Company are on SBP concessional rates, safeguarding it from volatility of interest rate. Working capital cycle reduced considerably driven by lower inventory days. During 9MFY22 (Jul21- Mar22), Pakistan textile exports surged to \$14.2bln (recording a growth of 25%) as compared to \$11.3bln in the same period last year. This is attributable to an increase in demand for textile products internationally and the channeling of export orders toward the Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth.

The ratings are dependent on the management's ability to improve its operations and margins amidst tough prevailing conditions in Pakistan and internationally. Maintaining good working capital management practices and strong coverages is important. Adverse movement in margins and/or coverages will impact the Strengthening of equity base will remain vital in rating upgrade.

Disclosure

Name of Rated Entity	Sarena Textile Industries (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),Mehtodology Rating Modifiers(Jun-22)
Related Research	Sector Study Composite and Garments(Dec-21)
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Profile

Legal Structure Sarena Textile Industries (Private) Limited (Sarena Textile) is a private limited company incorporated in 2001.

Background Sarena Textile is part of the Sefam and Ali Group of Industries, headquartered in Lahore, Pakistan. The Group is vertically integrated in the textile industry and has expanded its operations over the years. It owns many well-known retail brands including Bareezé, Leisure Club, Minnie Minors, Chinyere and Kayseria etc.

Operations The Company is engaged in the manufacture and sale of fabrics and garments used for fashion and work-wear with production operations divided into three main units: weaving, processing and stitching/apparel. The Company is self-sufficient in power generation with the capacity to produce 10.5 MW/H through own sources and an additional 4.7 MW/H through lines from LESCO while its power requirement adds up to an average of ~4 MW/H.

Ownership

Ownership Structure Shareholding of Sarena Textile lies with the children of late Mr. J.A Zaman, founder of Ali Embroidery Mills (Private) Limited. Ms. Seema Aziz and Mr. Hamid Zaman each hold 42% of the Company while Mr. Tariq Zaman and Ms. Ambreen Zaman hold the remaining 16%, equally.

Stability While no written agreement between the sponsors currently exists, the Group is moving towards consolidation and formalization of Group structure in line with the current management structure.

Business Acumen The sponsor Group holds extensive experience and expertise in the textile and retail industry. They are viewed as the pioneers of introducing the concept of brands in Pakistan. Apart from the textile industry, the Group has also diversified into corporate farming, energy etc, through small scale ventures.

Financial Strength The net worth of the Group is considered strong and the sponsors have shown willingness and ability to support the Company in the past.

Governance

Board Structure Sarena Textile's Board comprises six members, four from the sponsor family and two independent members. The Board operates in two parts: one is the 'family board' which comprises only sponsor family members and discusses matters pertaining to operations and future strategy, while the other is the 'extended board', which includes the independent members and oversees strategic planning.

Members' Profile Mr. Hamid and Ms. Seema both possess quality education from prestigious universities as well as significant experience in the textile industry. Ms. Seema also manages C.A.R.E foundation which she co-founded with Mr. Hamid. Other Board members are also well qualified and have been associated with the Company for a reasonable period of time.

Board Effectiveness Frequency of board meetings vary across both Boards. The family board meets more frequently; however, there is no fixed number of meetings that are to be held in a year. Meetings are conducted when deemed fit while minutes are not documented formally.

Financial Transparency The Company has appointed EY Ford Rhodes & Co. as its external auditor, listed in the "A" category on the State Bank of Pakistan's panel of auditors. The quality of the auditor reflects well on the governance framework of the Company.

Management

Organizational Structure A simplified organizational structure exists in the Company. The business profile segregated into different departments, which are headed by their respective heads resulting in effective control and management.

Management Team The CEO - Mr. Asif Masood looks after all day to day operations of the Company. All the department heads report to CEO, who in turn reports to Mr. Hamid Zaman, who is the Managing Director of the Company, involved in key strategic decision making. The management of the Company comprises qualified and experienced professionals with a wide range of skills and relevant experience.

Effectiveness The Company does not have any formal management committees in place. Meetings among management are held only on a need-basis and attended by the relevant engagement personnel. Formal meeting minutes are not documented.

MIS Sarena Textile deploys SAP ECC6 as their primary ERP solution, in addition to having Oracle (modified in-house) and S-Track, which is an in-house developed software. The Company has a comprehensive MIS in place with regular generation of reports to aid informed and timely decision making.

Control Environment Sarena Textile has an ISO17025 accredited Quality Assurance Lab and is the only Licensee in Pakistan for PROBANO, a quality controlled technological process that gives cotton and cotton rich woven and knitted textiles flame retardant properties.

Business Risk

Industry Dynamics During 9MFY22 (Jul21-Mar22), Pakistan's textile exports surged to \$14.2bln (recording a growth of 25%) as compared to \$11.3bln in the same period last year. This is attributable to an increase in demand for textile products internationally and the channeling of export orders toward the Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth. However, month on month basis, textile exports have declined by 3.5%. Going forward, the textile sector's outlook is expected to stay good in the medium term where demand for textile products is expected to sustain.

Relative Position Sarena Textile is an established name in Pakistan's textile industry. The Company enjoys higher margins in comparison to local competitors mainly due to its penetration into the niche of work-wear, leading to a higher value-added product mix.

Revenues The Company has a fairly balanced sales mix, increase in exports is recorded in line with enhanced exports of the country. Exports constituted ~54% of the Company's topline in 9MFY22 (~41% in FY21). During 9MFY22, the Company's topline witnessed an increase of 59% to PKR 18,523mln (9MFY21: PKR 11,339mln).

Margins For 9MFY22, the Company's gross margin increased marginally (9MFY22: 15.8%; 9MFY21: 13.9%). The operating margin also enhanced to 11.4% (end-Jun21: 8.2%) while the net margin clocked in at 8.2% (end-Jun21: 3.3%). The Company's finance cost displayed an increase and was recorded at PKR 520mln due to a rise in short-term borrowings to finance higher working capital needs during the period. Despite higher financing costs, Net profitability showed significant growth (9MFY22: ~PKR 1522mln; 9MFY21: ~480mln).

Sustainability In recent years, the Company has regularly performed CAPEX in the form of BMR and expansionary activities which included the installation of machines and some replacements in the processing and weaving segments. In line with its plans of increasing its presence in the international market, the Company has expanded its stitching capacity to cater to more work-wear orders as well as fashion customers in Europe.

Financial Risk

Working Capital The net cash cycle declined during the period (9MFY22: 90 days, FY21: 103 days), mainly on account of the decrease in inventory days. The short-term trade leverage improved, in 9MFY22, clocked in at ~11% (FY21: -1%) while the cushion against total current assets amounts to 10% (FY21: 5%), which is considered adequate.

Coverages During 9MFY22, the Company managed to record a sizable improvement in its free cashflows. Free cash flows from operations clocked in at PKR 2,269mln, compared to PKR 890mln in 9MFY21. The interest coverage for the period was enhanced to 5x (end-Jun21: 4.7x) while core debt coverage amounted to 2.4x (FY21: 1.5x). The Company's debt payback improved and stood at 0.8 years in 9MFY22 (FY21: 1.7 years).

Capitalization In 9MFY22, the Company's debt-to-equity ratio stood at 62.3% (FY21: 59%). Short-term borrowings witnessed a YoY rise of 65%, due to an increase in working capital needs. However, a sizable quantum lies in borrowing from SBP. Similarly, long-term borrowing displayed a YoY increase of 30% to stand at ~PKR 1,224mln. The equity base of the company was enhanced to PKR 6,118mln (end-Jun21: PKR 4,596mln) attributable to accumulated profits.



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Financial Summary

PKR mln

Sarena Textile Industries (Private) Limited Composite	Mar-22 9M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	6,899	5,768	4,654	4,104
2 Investments	1	-	-	69
3 Related Party Exposure	(72)	124	95	133
4 Current Assets	13,534	8,550	7,862	7,302
<i>a Inventories</i>	3,802	2,751	2,406	2,060
<i>b Trade Receivables</i>	6,496	3,515	2,958	3,573
5 Total Assets	20,362	14,442	12,611	11,609
6 Current Liabilities	4,092	3,212	2,255	2,691
<i>a Trade Payables</i>	2,646	1,705	1,150	1,046
7 Borrowings	9,958	6,419	6,112	5,264
8 Related Party Exposure	172	193	212	164
9 Non-Current Liabilities	21	21	50	70
10 Net Assets	6,118	4,596	3,982	3,421
11 Shareholders' Equity	6,118	4,596	3,982	3,421
B INCOME STATEMENT				
1 Sales	18,523	15,529	12,677	13,068
<i>a Cost of Good Sold</i>	(15,603)	(13,455)	(10,907)	(11,346)
2 Gross Profit	2,920	2,074	1,770	1,722
<i>a Operating Expenses</i>	(813)	(806)	(767)	(815)
3 Operating Profit	2,107	1,268	1,003	907
<i>a Non Operating Income or (Expense)</i>	150	(275)	45	315
4 Profit or (Loss) before Interest and Tax	2,257	993	1,048	1,222
<i>a Total Finance Cost</i>	(520)	(333)	(291)	(256)
<i>b Taxation</i>	(215)	(148)	(142)	(92)
6 Net Income Or (Loss)	1,522	512	615	873
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	2,269	1,314	1,268	1,224
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	1,820	1,011	988	977
<i>c Changes in Working Capital</i>	(4,641)	(218)	(758)	(1,800)
1 Net Cash provided by Operating Activities	(2,820)	793	230	(822)
2 Net Cash (Used in) or Available From Investing Activities	(1,184)	(1,237)	(807)	(821)
3 Net Cash (Used in) or Available From Financing Activities	3,561	521	734	783
4 Net Cash generated or (Used) during the period	(443)	78	157	(860)
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	59.0%	22.5%	-3.0%	38.8%
<i>b Gross Profit Margin</i>	15.8%	13.4%	14.0%	13.2%
<i>c Net Profit Margin</i>	8.2%	3.3%	4.8%	6.7%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-12.8%	7.1%	4.0%	-4.4%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	37.9%	11.9%	16.6%	28.7%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	122	137	158	126
<i>b Net Working Capital (Average Days)</i>	90	103	127	101
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	3.3	2.7	3.5	2.7
3 Coverages				
<i>a EBITDA / Finance Cost</i>	5.6	5.6	6.7	7.2
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	2.4	1.5	2.3	1.9
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	0.8	1.7	1.5	1.2
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	62.3%	59.0%	61.4%	61.3%
<i>b Interest or Markup Payable (Days)</i>	104.7	133.0	111.7	111.7
<i>c Entity Average Borrowing Rate</i>	7.6%	4.2%	4.1%	4.1%

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+	
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-	
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	
CC	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.
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):

<p>Entities</p> <ul style="list-style-type: none"> a) Broker Entity Rating b) Corporate Rating c) Financial Institution Rating d) Holding Company Rating e) Independent Power Producer Rating f) Microfinance Institution Rating g) Non-Banking Finance Companies (NBFCs) Rating 	<p>Instruments</p> <ul style="list-style-type: none"> a) Basel III Compliant Debt Instrument Rating b) Debt Instrument Rating c) Sukuk 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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(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

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(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)

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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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