



The Pakistan Credit Rating Agency Limited

## Rating Report

### Sarena Textile Industries (Pvt.) Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Jul-2023	A	A2	Stable	Maintain	-
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, incorporated in 2001. The Company has established expertise in weaving, dyeing, printing, finishing, and stitching. The business manufactures a variety of completed goods and has carved out a market for itself by processing and manufacturing specialized materials for uniforms and fire protection. The company is also a licensee for PROBAN® in Pakistan. With the use of thorough reporting and the expertise of its staff, the company manages its operations independently. The Company has carved out a place for itself in the international market and is also regarded as a prominent name in the domestic industry, with revenue mainly inclined towards exports in 9MFY23. In the relative world, the Company's performance displayed resistance. Revenues during FY22, recorded good growth (PKR 25.4bln, FY21: PKR 15.5bln). The momentum continued in 9MFY23 (revenues: PKR 23.2bln) where the operating profit reflected good boast. The bottom line witnessed considerable growth to reach PKR 2.7bln in 9MFY23, despite an increase in finance costs. The Company has a solid financial standing with sufficient coverage. The Company's previous moderate leveraging further declined recently attributable to an enhanced equity base. The Company utilized an export-related credit facility from SBP to obtain short-term borrowings totaling PKR 6.7bln. The remaining amount was availed by FIs through running finance. Going forward, the strategy is to further increase its penetration in Europe and North America where new customers may also be taken on board. With high-capacity utilization levels and volumes, the management is seeing growth momentum to continue. A keen focus on further dilution in leveraging is also a priority.

The management's capacity to continuously improve the operating profitability along with effective management of finance costs remains vital. Further, range bound leveraging with cushion in coverage is essential, going forward.

#### Disclosure

<b>Name of Rated Entity</b>	Sarena Textile Industries (Pvt.) Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Rating(Jun-22),Methodology   Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology   Rating Modifiers(Jun-22)
<b>Related Research</b>	Sector Study   Composite and Garments(Dec-22)
<b>Rating Analysts</b>	Sehar Fatima   sehar.fatima@pacra.com   +92-42-35869504

## Profile

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

**Background** Sarena Textile belongs to the same group as Sefam Pvt. Limited, headquartered in Lahore, Pakistan. The Group is vertically integrated into the textile industry and has expanded its operations over the years.

**Operations** The Company is engaged in the manufacture and sale of fabrics and garments used for fashion and workwear 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 has its own grid of 12MW from LESCO while its power requirement adds up to an average of ~7 MW/H.

## Ownership

**Ownership Structure** Shareholding of Sarena Textile lies with the children of the 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. The shareholding is expected to change in FY24 where majority shareholding shall be transferred to Mr. Hamid Zaman.

**Stability** The Group has recently formalized the 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 in 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 Industries Board operates in two parts: one is the 'Business Board', which comprises six members, four from the sponsor family (majority Hamid Zaman family) and two independent members that oversee the strategic planning, while the other is the 'Ownership Board' which comprises only the sponsor's family members and discusses matters pertaining to operations and future strategy. Textile Board is reportable to Business Board.

**Members' Profile** Mr. Hamid Zaman possesses a quality education from a prestigious university as well as significant experience in the textile industry. The engagement of the second generation in the business's strategic affairs bodes well for the Company. Other Board members are also well-qualified and have been associated with the Company for a reasonable period of time.

**Board Effectiveness** The frequency of board meetings varies across both Boards. The business board meets quarterly; however, additional meetings can be held as and when required basis during the year. Minutes of meetings are well documented.

**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 is segregated into different departments, which are headed by their respective heads resulting in effective control and management.

**Management Team** The position of Group CEO lies with Mr. Mustafa Ahmad Zaman. The CEO of Sarena Textile- Mr. Asif Masood looks after all the day-to-day operations of the Company. All the department heads report to the CEO, who in turn reports to Mr. Mustafa Ahmad Zaman (Group CEO), engaged 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 have a formal management committee/board in place. Meetings among management are held only monthly and attended by the relevant engagement personnel. Formal meeting minutes are well 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 PROBAN®, a quality-controlled technological process that gives cotton and cotton-rich woven and knitted textiles flame retardant properties.

## Business Risk

**Industry Dynamics** During 9MFY23, the textile exports were valued at \$12.47bln compared to \$14.24bln, reflecting a 12% decline YoY - the declining trend has been recorded in the last two quarters. The Country's textile exports for the month of March clocked in at US\$1.26bln, up 7% MoM. The decline in the previous overall exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand in international markets is also a challenge. During the month of March, value-added textile exports increased by 6% MoM to US\$863mln mainly due to Readymade Garments and Knitwear increasing by 8% and 12% MoM respectively while towels decreased by 6% MoM. Basic textiles witnessed an increase of 8% MoM to US\$230mln in Mar-23. In volume terms, Knitwear, Readymade Garments, Bedwear, and Towels increased by 18%, 13%, 5%, and 2% MoM respectively. The demand pattern is expected to improve in the upcoming quarters.

**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 workwear, leading to a higher value-added product mix.

**Revenues** The Company has a mix of both domestic and export sales. An increase in exports was recorded in the latest quarter. During FY22, the top line significantly improved to PKR 25.4bln (FY21: PKR 15.5bln), contributed equally by domestic and exports. Whereas, during 9MFY23, the Company's top-line continued the momentum to PKR 23.2bln which was mainly dominated by exports.

**Margins** Margins reflected an improvement in FY22. Gross and operating profit margins inched-up to 15.7% and 11.2% respectively (FY21: 13.4%, 8.2%). Whereas, the net profit margin improved significantly to 8.0% from 3.3% in FY21, due to a prominent increase recorded in the bottom line. During 9MFY23, the Company's net profit margin further escalated to 11.7%. The Company's finance cost displayed an increase and was recorded at PKR 1.01bln due to a rise in the SBP Policy rate and SBP concessionary Rate i.e. for ERF during the period.

**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. In the upcoming year, capacity utilization levels are expected to increase further to support the growth momentum planned by the management.

## Financial Risk

**Working Capital** The net cash cycle increased during the period (9MFY23: 119 days, FY22: 99 days) where Inventory days largely remained the same. The short-term borrowings / total borrowings remained largely the same around 80% in FY22 and 9MFY23. The short-term trade leverage improved massively, in 9MFY23, clocked in at 25.3% (FY22: 8.2%) while the cushion against total current assets amounted to 20% (FY22: 8%), which is considered healthy.

**Coverages** During FY22, the company managed to record a sizable improvement in its free cashflows. Free cash flows from operations clocked in at PKR 3.7bln, compared to PKR 1.58bln in FY21. The interest coverage for the period was enhanced to 5.1x (end-Jun21: 4.7x) while core debt coverage amounted to 2.8x (FY21: 1.5x). The Company's debt payback stood at 0.7 years in 9MFY23 (FY22: 0.8 years).

**Capitalization** In 9MFY23, the Company's debt-to-equity ratio stood at 55.7% (FY22: 60%). Short-term borrowings witnessed a rise due to an increase in working capital needs. Similarly, long-term borrowing displayed a YoY increase. The equity base of the company was enhanced to PKR 9.3bln (end-Jun22: PKR 6.6bln) attributable to accumulated profits. Going forward, the leveraging is planned to remain range bound.



The Pakistan Credit Rating Agency Limited

Financial Summary

Sarena Textile Industries Textile		PKR mln			
		Mar-23 9M	Jun-22 12M	Jun-21 12M	Jun-20 12M
<b>A BALANCE SHEET</b>					
1 Non-Current Assets	7,970	7,478	5,768	4,654	
2 Investments	20	112	-	-	
3 Related Party Exposure	254	41	124	95	
4 Current Assets	17,821	15,278	8,550	7,862	
<i>a Inventories</i>	5,678	4,336	2,751	2,406	
<i>b Trade Receivables</i>	8,590	7,616	3,515	2,958	
5 Total Assets	26,065	22,908	14,442	12,611	
6 Current Liabilities	4,919	6,067	3,212	2,255	
<i>a Trade Payables</i>	3,363	2,648	1,705	1,150	
7 Borrowings	11,764	9,922	6,419	6,112	
8 Related Party Exposure	-	251	193	212	
9 Non-Current Liabilities	41	41	21	50	
10 Net Assets	9,340	6,627	4,596	3,982	
11 Shareholders' Equity	9,341	6,627	4,596	3,982	
<b>B INCOME STATEMENT</b>					
1 Sales	23,283	25,456	15,529	12,677	
<i>a Cost of Good Sold</i>	(19,176)	(21,459)	(13,455)	(10,907)	
2 Gross Profit	4,108	3,996	2,074	1,770	
<i>a Operating Expenses</i>	(1,207)	(1,133)	(806)	(767)	
3 Operating Profit	2,901	2,863	1,268	1,003	
<i>a Non Operating Income or (Expense)</i>	1,183	307	(275)	45	
4 Profit or (Loss) before Interest and Tax	4,083	3,170	993	1,048	
<i>a Total Finance Cost</i>	(1,013)	(729)	(333)	(291)	
<i>b Taxation</i>	(356)	(411)	(148)	(142)	
6 Net Income Or (Loss)	2,714	2,030	512	615	
<b>C CASH FLOW STATEMENT</b>					
<i>a Free Cash Flows from Operations (FCFO)</i>	3,395	3,251	1,314	1,268	
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	2,477	2,693	1,011	988	
<i>c Changes in Working Capital</i>	(3,076)	(3,842)	(218)	(758)	
1 Net Cash provided by Operating Activities	(599)	(1,149)	793	230	
2 Net Cash (Used in) or Available From Investing Activities	(861)	(1,655)	(1,237)	(807)	
3 Net Cash (Used in) or Available From Financing Activities	1,195	3,112	521	734	
4 Net Cash generated or (Used) during the period	(265)	308	78	157	
<b>D RATIO ANALYSIS</b>					
1 Performance					
<i>a Sales Growth (for the period)</i>	22.0%	63.9%	22.5%	--	
<i>b Gross Profit Margin</i>	17.6%	15.7%	13.4%	14.0%	
<i>c Net Profit Margin</i>	11.7%	8.0%	3.3%	4.8%	
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	1.4%	-2.3%	7.1%	4.0%	
<i>e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity) ]</i>	45.3%	36.2%	11.9%	15.4%	
2 Working Capital Management					
<i>a Gross Working Capital (Average Days)</i>	154	131	137	154	
<i>b Net Working Capital (Average Days)</i>	119	99	103	121	
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	3.6	2.5	2.7	3.5	
3 Coverages					
<i>a EBITDA / Finance Cost</i>	4.2	5.9	5.6	6.7	
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	2.0	2.8	1.5	2.3	
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	0.7	0.8	1.7	1.5	
4 Capital Structure					
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	55.7%	60.6%	59.0%	61.4%	
<i>b Interest or Markup Payable (Days)</i>	99.0	135.3	133.0	111.7	
<i>c Entity Average Borrowing Rate</i>	11.1%	7.3%	4.2%	3.8%	

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

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



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

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

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

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

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

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

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

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

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

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

### **2) Conflict of Interest**

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

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

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

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(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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(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)

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(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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