

## RATING REPORT

## Shadab Textile Mills Limited

**REPORT DATE:**

December 02, 2022

**RATING ANALYSTS:**

Arsal Ayub, CFA

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## RATING DETAILS

Rating Category	Latest Ratings		Previous Ratings	
	Long-term	Short-term	Long-term	Short-term
<b>Entity</b>	A-	A-2	A-	A-2
<b>Rating Action</b>	Maintained		Initial	
<b>Rating Outlook</b>	Negative		Stable	
<b>Rating Date</b>	02 <sup>nd</sup> Dec'2022		12 <sup>th</sup> Nov'2021	

## COMPANY INFORMATION

Incorporated in 1979	External Auditors: M/s. Fazal Mehmood & Company Chartered Accountants
Public Limited Company	Chairman: Mian Farrukh Naseem
<b>Key Shareholders (More than 5%):</b>	Chief Executive Officer: Mian Aamir Naseem
Mr. Aamir Naseem – 14.8%	
Mrs. Rukhasan Abdul Rasheed – 13.8%	
Mrs. Fatima Aamir – 11.1%	
Mr. Farrukh Naseem – 6.3%	
Mr. Saad Naseem – 5.8%	
Mr. Hamza Naseem – 5.8%	
Mr. Ahmed Naseem – 5.7%	

## APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (August 2021)

<https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf>

**Shadab Textile Mills Limited**
**OVERVIEW  
OF THE  
INSTITUTION**

Shadab Textile Mills Limited (STML) is engaged in the business of manufacturing, selling, buying and dealing in all types of yarn including different counts of blended yarn. The company was listed on the stock exchanges in 1985.

**Profile of the  
Chairman**

Mian Farrukh Naseem, Chairman/Director of the Company is a commerce graduate from Karachi University. He possesses over three decades of experience in the textile Business. He has been associated with the company since 1981.

**Profile of the CEO**

Mian Aamir Naseem, Chief Executive of the company has Masters in Business Administration from USA. He joined the Group in 1990 and looks after the operational, Technical, Marketing and Financial respects of the project.

**RATING RATIONALE**

Shadab Textile Mills Limited ('STML' or 'the Company') was incorporated in August 1979, as a public limited company and obtained certificate of commencement of business in November 1979. The Company is engaged in the business of manufacturing, selling, buying and dealing in all types of yarn including different counts of blended yarn. The Company was listed on the stock exchange in 1985. The manufacturing facilities are located at Faisalabad Road, Nasimabad, District Nankana Sahib (Unit-I) and 1-KM Chunian Road, Habibabad, District Kasur (Unit-II).

**Table 1: Capacity and Production**

	Spinning	FY21	FY22
<b>Total number of spindles installed</b>			
Unit-I (Ring)		33,600	33,600
Unit-II (MVS)		576	576
<b>Total number of spindles worked</b>			
Unit-I (Ring)		33,120	33,120
Unit-II (MVS)		576	576
Capacity (Kgs)		20,234,786	23,347,354
Actual production (Kgs)		20,016,747	22,998,125
Capacity Utilization on conversion (%)		<b>98.9%</b>	<b>98.5%</b>

**Sector Update**
**Table 2: Pakistan Export Statistics**

	FY20	FY21	FY22	1Q'FY22	1Q'FY23
<b>PAKISTAN EXPORTS (IN USD' MILLIONS)</b>	22,536	25,639	32,450	7,201	7,594
<b>TEXTILE (IN USD' MILLIONS)</b>	12,851	14,492	18,525	4,241	4,777
<b>PKR/USD RATE (AVERAGE)</b>	158.0	160.0	177.5	164.4	229.1

**SOURCE: SBP**

- Pakistan's export growth came in at 14% and 27% in FY21 and FY22 respectively. Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21), however, in FY22 exports finally broke the threshold, coming in at USD 32.4b.
- In FY22, textile exports were up 28%. Growth in textile exports played a significant role in this uptick in Pakistan's overall export base, contributing 59% of the growth in export base. Share of textile exports in total exports has oscillated in the range of 54-59%, coming in at 57% during the past 3-years (FY20-22).
- As illustrated in the table below, the composition of textile exports has depicted improvement in the, with contribution from higher value added segment increasing from 77.2% in FY20 to 80.8% in FY22 of aggregate textile exports

**Table 3: Segment-wise textile Exports (All Figures in USD' Millions, except for percentages)**

	FY20	FY21	FY22	1Q'FY22	1Q'FY23	FY20	FY21	FY22	1Q'FY22	1Q'FY23
<b>High Value-Added Segment</b>	<b>9,669</b>	<b>12,427</b>	<b>15,605</b>	<b>3,561</b>	<b>3,749</b>	<b>77.2%</b>	<b>80.7%</b>	<b>80.7%</b>	<b>80.6%</b>	<b>81.8%</b>
- Knitwear	2,794	3,815	5,121	1,145	1,321	22.3%	24.8%	26.5%	25.9%	28.8%
- Readymade Garments	2,552	3,033	3,905	861	912	20.4%	19.7%	20.2%	19.5%	19.9%
- Bed wear	2,151	2,772	3,293	803	780	17.2%	18.0%	17.0%	18.2%	17.0%
- Towels	711	938	1,111	241	237	5.7%	6.1%	5.8%	5.5%	5.2%
- Made-up Articles (Excl. towels & bed wear)	591	756	849	197	180	4.7%	4.9%	4.4%	4.5%	3.9%

- Art, Silk & Synthetic Textile	315	370	460	108	108	2.5%	2.4%	2.4%	2.4%	2.4%
- Others	555	743	866	206	211	4.4%	4.8%	4.5%	4.7%	4.6%
<b>Low to Medium Value-added Segment</b>	<b>2,858</b>	<b>2,972</b>	<b>3,717</b>	<b>860</b>	<b>835</b>	<b>22.8%</b>	<b>19.3%</b>	<b>19.2%</b>	<b>19.4%</b>	<b>18.2%</b>
- Cotton Cloth	1,830	1,921	2,438	557	581	14.6%	12.5%	12.6%	12.6%	12.7%
- Cotton Yarn	984	1,017	1,207	289	236	7.9%	6.6%	6.2%	6.5%	5.2%
- Others	43	34	72	14	18	0.3%	0.2%	0.4%	0.3%	0.4%
<b>Total</b>	<b>12,527</b>	<b>15,399</b>	<b>19,332</b>	<b>4,421</b>	<b>4,584</b>					

Source: PBS

- Cotton production in Pakistan, was at its lowest level in decades for FY21, albeit the same posted 18% uptick in FY22. Actual production at 8.33m bales still missed the targeted production of 10.5m bales. Cotton prices rose to a new 12-year high of ~Rs. 21,600/maund as of March'22, as a result of the shortage and higher input costs of fertilizer and energy. Cotton imports were also up 19.8%, in USD terms, for FY22 vis-à-vis preceding year.
- According to United States Department of Agriculture (USDA), the 2022/23 harvested area has declined notably following devastation caused by recent flood in Sindh and Southern Punjab. Hence, the projected production has been brought down to 5m bales. To counter the shortage, import of 5.8m bales is expected during FY23, which is 29% higher than preceding year.

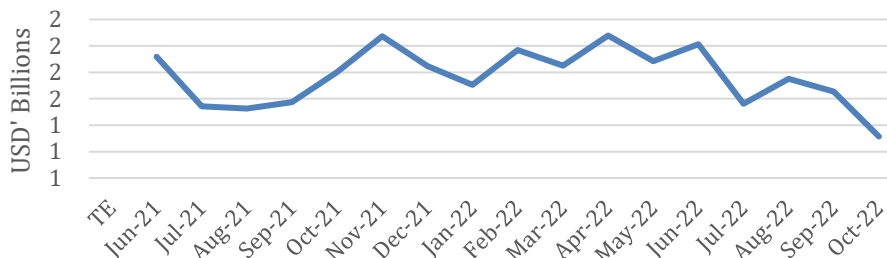
Table 4: Cotton Prices

	FY19	FY20	FY21	FY22
Per Maund (Rs.)	8,770	8,860	13,000	17,380
% Change	26%	1%	32%	34%

### Future Outlook – Textile Industry

- After posting windfall margins in FY21 and H1'FY22, margins of textile operators, particularly spinners, weavers and dying units, have come under pressure during the period Jan-Sep'2022, mainly on account of higher input costs and recessionary trend in export markets.
- The recessionary trend in Pakistan's major export textile export markets, mainly North America and EU, has started to materialize in Pakistan's MoM export proceeds, with receipts for October 2022 (at USD 1.36b) being lower by 11% and 15% vis-à-vis preceding month and corresponding period last year respectively, as also illustrated in the table below.

Figure 1: MoM Textile Exports (TE) (In USD' Billions)



- Given expected industrial gas load shedding during the period Dec-Feb'22, and prevailing recession in major export markets and peak inventory levels, export proceeds are expected to fall by ~10% in FY23. Furthermore, profitability margins of textile operators, particularly spinners, weavers and dying companies, are expected to remain under pressure given higher input and financial costs.

**Business Update – STML**

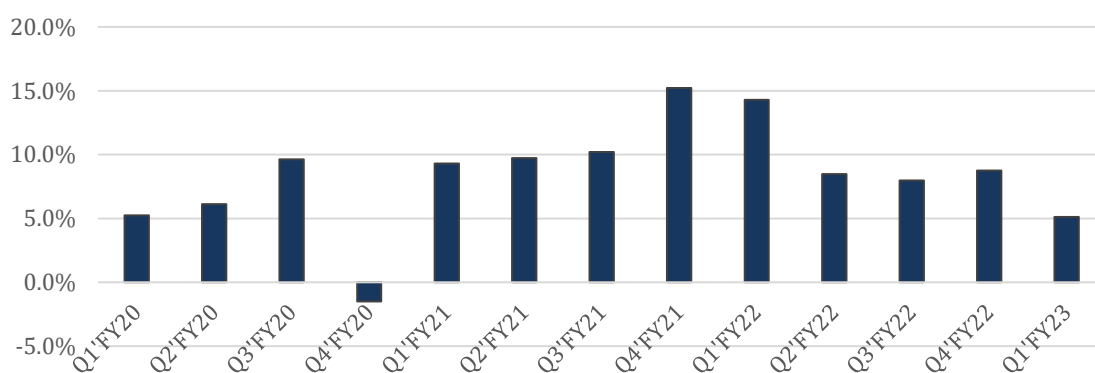
**Sales & Operations**

*Table 5: P&L (Extract)*

	FY21	FY22	Q1'FY22	Q1'FY23
<b>NET SALES (PKR MILLION)</b>	3,305	5,297	1,145	1,373
<b>GROSS MARGIN (%)</b>	11.6%	9.7%	14.3%	5.1%
<b>OPERATING MARGIN (%)</b>	7.9%	6.7%	11.0%	2.4%
<b>NET MARGIN (%)</b>	5.2%	3.7%	8.5%	(1.1)%

- The topline of the Company soared in FY22 with an increase of 60%, mainly being driven by higher pricing. In Q1'FY23, topline was up 20% vis-à-vis SPLY.
- STML's gross margin, which had risen during FY21-22, has notably dropped in Q1'FY23. As illustrated in the table below, the gross margin started tapering off from Q3'FY22, contracting notably in Q1'FY23.

*Figure 2 – QoQ Gross Margin - STML*



- The decline in gross margin is attributable to higher raw material and fuel costs. STML's imported raw material (Polyester, Cotton, Viscose and Acrylic) constitutes roughly a third of the total raw material costs (average for FY21-22), hence devaluation of PKR had a direct impact on the cost of raw material. Going forward, the Company's topline is expected to remain range-bound at ~Rs. 5b during FY23, while gross margin is anticipated to remain depressed for the period.
- The Top 10 client concentration of the Company remains on the higher side depicting an elevated risk profile.
- After decline in bottom-line in FY22, it dropped to negative in 1Q'FY23 owing to the high finance cost during the period. Overall, the Company's margins have fallen below that of peers.

*Table 6 - Cash Conversion Cycle*

	FY20	FY21	FY22	1Q'FY23
<b>CASH CONVERSION CYCLE</b>	<b>11.5</b>	<b>30.6</b>	<b>45.7</b>	<b>59.0</b>
- DIO	30.1	39.3	44.0	51.8
- DSO	18.4	18.9	19.3	24.9
- DPO	37.1	27.6	17.6	17.6

- The Company's cash conversion cycle has elongated on a timeline owing to consistent increase in inventory and receivable days.
- STML's credit sales accounts for 70.0% of the total sales by volume in FY22. As of Sep'22, the Company's trade debt to sales (annualized) stood at 7.5%; a review of aging profile of trade debts is indicative of low sound credit risk with no trade debt outstanding for more than 60 days as of October 2022.

## Cash Flow Coverages

Table 7: Cash flow Analysis

	FY20	FY21	FY22	1Q'FY23
<b>FFO (MN.) (PKR MILLION)</b>	63	293	403	32
<b>FFO TO TOTAL DEBT (X)</b>	0.31	0.47	0.43	0.13*
<b>FFO TO LONG TERM DEBT (X)</b>	9.99	0.72	0.96	0.31*
<b>DEBT SERVICING COVERAGE RATIO (X)</b>	4.58	11.61	3.29	1.27*
<b>CURRENT RATIO</b>	2.02	1.54	1.54	1.45
<b>(STOCK IN TRADE+ TRADE DEBTS)/STD</b>	1.72	2.89	2.10	1.95
<i>*ANNUALIZED</i>				

- The Company's cashflow coverage indicators remained strong through the past 3-year period (FY20-22), albeit given slowdown in offtake and contraction in margins, the Company's DSCR (annualized) has notably fallen in Q1'FY23. The Company's DSCR is expected to remain stressed through the rating horizon, at ~1x, while FFO to Debt is expected to fall below 10%.
- Given the contraction in profitability and sales offtake, cash flow coverage indicators have fallen below threshold for the assigned rating.

## Capitalization

Table 8: Balance Sheet (Extract) (all figures stated in PKR' Millions, unless stated otherwise)

	JUN'20	JUN'21	JUN'22	SEPT'23
<b>TOTAL ASSETS</b>	1,376	2,443	2,970	3,051
<b>TOTAL LIABILITIES</b>	522	1,040	1,398	1,494
<b>TOTAL EQUITY</b>	855	1,403	1,571	1,556
<b>TOTAL DEBT</b>	204	624	937	992
- <b>LONG TERM DEBT</b>	6	406	422	405
- <b>SHORT TERM DEBT</b>	198	218	516	588
<b>LEVERAGE (X)</b>	0.61	0.74	0.89	0.96
<b>GEARING (X)</b>	0.24	0.45	0.60	0.64

- Despite the sizable uptick in debt, the Company's gearing remains on the lower side, mainly as the Company opted to retain full profitability for FY22.
- The uptick in gearing has been noted. As per our projections, the impact of lower margins would be netted off by lower working capital requirements for the period in a way that total debt is likely to remain at similar level. Given potential for posting slight accounting loss for the period, there might be a slight uptick in gearing, albeit this uptick is likely to remain measured with gearing envisaged to remain below 1x through the rating horizon.

**Shadab Textile Mills Limited (Rs. in million)**  
**Annexure I**

<b>BALANCE SHEET</b>	<b>June'20</b>	<b>June'21</b>	<b>June'22</b>	<b>Sept'22</b>	
Non-Current Assets	391	1,512	1,522	1,512	
Short-term Investments	236	-	-	-	
Stock-in-Trade	225	405	748	730	
Stores & Spares	64	72	100	115	
Trade Debts	117	226	333	415	
Loans & Advances	11	37	47	43	
Trade deposits & prepayments	12	34	128	122	
Other Receivables	69	133	75	98	
Cash & Bank Balances	252	23	16	16	
<b>Total Assets</b>	<b>1,376</b>	<b>2,443</b>	<b>2,970</b>	<b>3,051</b>	
Trade and Other Payables	249	252	258	271	
Short Term Borrowings	37	218	516	588	
Long Term Borrowings	6	406	422	405	
Sponsor Loan	161	-	-	-	
<b>Total Liabilities</b>	<b>522</b>	<b>1,040</b>	<b>1,398</b>	<b>1,494</b>	
Paid Up Capital	166	166	166	166	
<b>Core Equity/Total Equity</b>	<b>855</b>	<b>1,403</b>	<b>1,571</b>	<b>1,556</b>	
<b>INCOME STATEMENT</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>1Q'FY22</b>	<b>1Q'FY23</b>
Net Sales	2,291	3,305	5,297	1,145	1,373
Gross Profit	130	383	513	164	70
Operating Profit	46	260	357	126	33
Profit Before Tax	63	239	292	113	2
Profit After Tax	41	171	195	98	(15)
FFO	63	293	403	157	32
<b>RATIO ANALYSIS</b>	<b>FY20</b>	<b>FY21</b>	<b>FY22</b>	<b>1Q'FY23</b>	
Gross Margin (%)	5.7	11.6	9.7	5.1	
Net Margin (%)	1.8	5.2	3.7	(1.1)	
Current Ratio (x)	2.02	1.54	1.54	1.45	
FFO to Total Debt (x)	0.31	0.47	0.43	0.13*	
FFO to Long Term Debt (x)	9.99	0.72	0.96	0.31*	
Debt Service Coverage Ratio (x)	4.58	11.61	3.29	1.27*	
ROAA (%)	3.8	8.9	7.2	(2.0)*	
ROAE (%)	6.1	15.1	13.1	(3.8)	
Gearing (x)	0.24	0.45	0.60	0.64	
Debt Leverage (x)	0.61	0.74	0.89	0.96	
Stock+ Trade debts/ Short-term Borrowings (x)	1.72	2.89	2.10	1.95	
<i>*Annualized</i>					

**ISSUE/ISSUER RATING SCALE & DEFINITIONS**

**Appendix II**

**VIS** Credit Rating Company Limited

**RATING SCALE & DEFINITIONS: ISSUES / ISSUERS**

**Medium to Long-Term**

**AAA**

Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

**AA+, AA, AA-**

High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

**A+, A, A-**

Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

**BBB+, BBB, BBB-**

Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

**BB+, BB, BB-**

Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

**B+, B, B-**

Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

**CCC**

Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

**CC**

A high default risk

**C**

A very high default risk

**D**

Defaulted obligations

**Short-Term**

**A-1+**

Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

**A-1**

High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

**A-2**

Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

**A-3**

Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

**B**

Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

**C**

Capacity for timely payment of obligations is doubtful.

**Rating Watch:** VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. [www.vis.com.pk/images/criteria\\_watch.pdf](http://www.vis.com.pk/images/criteria_watch.pdf)

**Rating Outlooks:** The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details. [www.vis.com.pk/images/criteria\\_outlook.pdf](http://www.vis.com.pk/images/criteria_outlook.pdf)

**(SO) Rating:** A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

**(blr) Rating:** A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

**'p' Rating:** A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. [www.vis.com.pk/images/policy\\_ratings.pdf](http://www.vis.com.pk/images/policy_ratings.pdf)

**'SD' Rating:** An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES		Appendix III			
<b>Name of Rated Entity</b>	Shadab Textile Mills Limited				
<b>Sector</b>	Textile				
<b>Type of Relationship</b>	Solicited				
<b>Purpose of Rating</b>	Entity Rating				
<b>Rating History</b>	<b>Rating Date</b>	<b>Medium to Long Term</b>	<b>Short Term</b>	<b>Rating Outlook</b>	<b>Rating Action</b>
	<b>RATING TYPE: ENTITY</b>				
	02-12-2022	A-	A-2	Negative	Maintained
	22-11-2021	A-	A-2	Stable	Initial
<b>Instrument Structure</b>	N/A				
<b>Statement by the Rating Team</b>	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
<b>Probability of Default</b>	VIS ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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<b>Due Diligence Meetings Conducted</b>	<b>Name</b>		<b>Designation</b>	<b>Date</b>	
	1	Mr. Mohammad Aslam	CFO	17-November-2022	