RATING REPORT

Shahtaj Textile Limited

REPORT DATE:
November 13, 2024

RATING ANALYSTS:
Zunain Arif
zunain.arif@vis.com.pk

M. Amin Hamdani
amin.hamdani@vis.com.pk

RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A2	A-	A2
Rating Outlook/Rating Watch	Stable		Stable	
Rating Action	*Reaffirmed*		*Reaffirmed*	
Rating Date	*November 13, 2024*		*November 24, 2023*	

COMPANY INFORMATION	
Incorporated in 1990	**External Auditors:** Yousuf Adil, Chartered Accountants
Public Listed Company	**Board Chairman:** Mr. Muneer Nawaz
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. M. Naeem
Shahtaj Sugar Mills Limited ~11.90%	
Mrs. Amtul Bari Naeem ~8.65%	
Mr. M. Naeem ~6.82%	
Mr. Muneer Nawaz ~6.12%	
CDC-Trustee National Investment (Unit) Trust ~4.92%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial Corporates https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)
VIS Issue/Issuer Rating Scale: https://docs.vis.com.pk/docs/VISRatingScales.pdf

Shahtaj Textile Limited

OVERVIEW OF THE INSTITUTION

Shahtaj Textile Limited (STL) was incorporated in 1990 as a public limited company. The company was later listed on Pakistan Stock Exchange (PSX). Head office of the company is situated in Karachi while the factory is located in Kasur.

Profile of the Chairman:

The Board is chaired by Mr. Muneer Nawaz who possesses extensive experience in sugar and food industries. He has been associated with STL since 1990.

Profile of the CEO:

Mr Taqi Muhammad started his tenure as CEO on 19th March 2024 for a period of three years. He holds a B.S (Electrical) degree and also holds a M.S (Electrical) degree. He has a 32-year experience in the Electro-Mechanical Industry in various technical and managerial capacities and is a registered professional Engineer (P.E) from Pakistan Engineering Council.

RATING RATIONALE

Corporate Profile

Shahtaj Textile Limited ("STL" or "the Company") is a Shahnawaz Group Company. It was incorporated as a public limited company in January 1990, with the sole purpose of manufacturing and marketing of greige fabric (pronounced "grey" fabric). The mills started commercial production in January 1992 and is listed at Pakistan Stock Exchange.

STL's production facilities are located in the hub of Textile Industries near Lahore and are equipped with the most advanced high-speed Toyoda and Picanol Air Jet Looms of Japanese and Belgium origin. Starting with 72 looms now the number of installed looms has increased to 179 along with complete back up processes and captive power generation. While the registered and marketing office are located in Lahore, the Company head office is located in Karachi.

Group Profile

The Company is part of 'Shahnawaz Group', which has diverse investments in industries such as sugar, food, agriculture, and engineering. The group has over six decades of experience and a cumulative annual turnover of ~PKR30b according to management. Following are major group entities:

Table: Group Companies (*By Common Directorship*)

Name	Business Nature
Shezan International	Food & Beverage Processing
Shahtaj Sugar Mills	Sugar Processing
Nawazabad Farms	Agriculture-Fruit & Crop Farming, Organic Farming
Information Systems Associates Limited (Comstar)	Info Security, Network Infrastructure & softwares
Shahnawaz (Pvt) Ltd	Automotive & Engineering (only importer for genuine Mercedes parts in Pakistan)

Operational Performance

STL has consistently been operating at high operating efficiency with capacity utilization improved to 91.1% in FY24.

Table 1: Capacity & Production Data (Units in millions)

Capacity	FY21	FY22	FY23	FY24
Fabric Weaving Unit				
Number of looms installed	178	179	179	179
Number of looms worked	178	179	179	179
Plant capacity at 60 picks (sq. meters)	64.6	65.3	65.3	65.3
Production converted to 60 picks (sq. meters)	57.5	57.9	57.6	59.5
Capacity Utilization %	89.0%	88.7%	88.2%	91.1%

Sector Update

The business risk profile of the textile sector in Pakistan is characterized by a high level of exposure to economic cyclicality and intense competition. This sector's performance is significantly influenced by the broader economic conditions in the country, making it inherently vulnerable to fluctuations in demand driven by economic factors.

In FY23, the textile sector faced challenges due to various economic and environmental factors. These included damage to the cotton crop resulting from flooding in 1HFY23, escalating inflation, and import restrictions due to diminishing foreign exchange reserves.

During FY23, Pakistan's yarn production registered a substantial decline, primarily due to reduced availability of cotton, as a result of crop damage and import restrictions. The sector's profitability was constrained by factors such as higher production costs, increased raw material costs, and rising energy expenses, all of which constrained the sector's profit margin. The industry's performance is closely intertwined with the outlook of the cotton and textile industries, both of which were affected in FY23. Reduction in cotton supply, coupled with global economic slowdown and contractionary economic policies, led to a decrease in demand for textile products and, consequently, cotton yarn.

While the global outlook for cotton production is expected to rebound, local challenges persist. These challenges include high interest rates, increasing energy costs and inflationary pressures. Additionally, the sector's vulnerability to global market dynamics and the domestic economic landscape further contribute to its high business risk profile. The worrying trend has continued during the first quarter of FY25 as the cotton production has declined by 48% during the first 15 days of FY25. Several factors have contributed to this downturn. Climate change has altered weather patterns, resulting in irregular rainfall and increased temperatures that have negatively affected crop yields. Additionally, pest infestations, especially by the pink bollworm, have devastated cotton fields. Rising costs of inputs such as fertilizers, pesticides, electricity, and quality seeds have made cotton cultivation less profitable.

Addressing the decline in cotton production requires a multifaceted approach. Improved pest management practices, such as integrated pest management (IPM), can help control infestations more effectively. Education and training for farmers on IPM techniques are crucial. They need access to the latest research and pest-resistant cotton varieties. Investment in agricultural research and development is also essential. Developing drought-resistant and high-yield cotton varieties can mitigate the impacts of climate change.

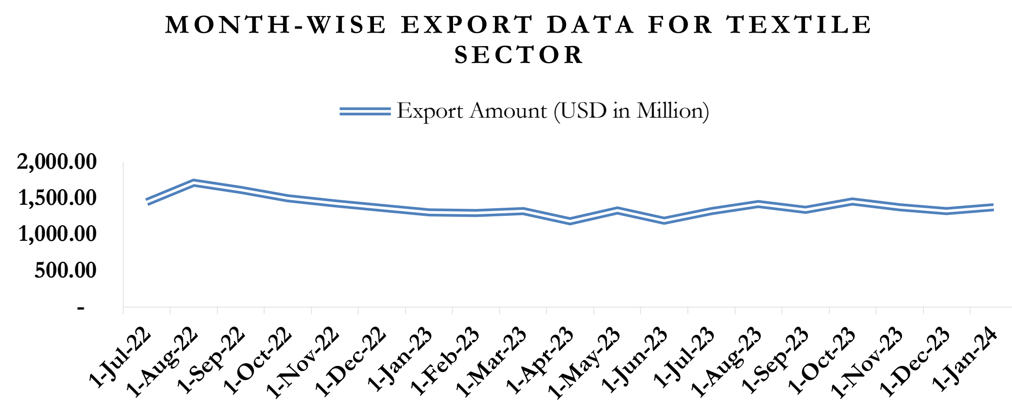

Figure 1: MoM Textile Exports (In USD' millions)
Source: SBP

<u>Key Rating Drivers</u>

Topline declined in FY24 owing to lower sales volumes. Margins have been impacted due to high energy and finance costs

During FY23, revenue surged by 8.4% to Rs 8.1b (FY22:7.5b) due to higher prices and increased volumes. However, increased energy and labour costs pushed the Gross Profit down to Rs 641m (FY22: 733m). Consequently, Gross Margin declined to 7.9% (FY22: 9.8%) in FY23. During FY24, revenues slightly declined by ~1% to Rs 8b (FY23: 8.1b) due to lower sales volumes. However, a decline in the yarn cost has contributed to an increase of 5% to the Gross Profit (FY24: Rs 673.3m: FY23: 640.9m). Consequently, Gross Margin has increased by 0.6% to 8.5% (FY23: 7.9%). Net Profit has declined during FY23 and FY24 owing to increased finance cost, higher administrative expenses and incidence of higher taxation (FY22:300m: FY23:153m: FY24: 27.2m). Consequently, Net Margin is on a downward trend from the last few years (FY22: 4%: FY23: 1.9%: FY24: 0.3%).

Direct and in-direct exports make up to ~44% of the total sales, while the remaining are destined for the local market. Major export destinations include Italy, Turkey, Belgium, Korea, Spain and USA. Top ten clients make up approximately 80% of the entire revenue while three local clients alone contribute 43% of the total sales, indicating some concentration risk.

FFO Coverage and liquidity indicators remain at adequate levels

During FY23, Funds from Operations (FFO) declined by 26.37% to Rs 363.6m (FY22: 493.8m) due to increased finance cost and an increase in the taxation. This trend continued during FY24 as the FFO further declined by 59.63% to Rs 146.8m due to a decline in profitability. Consequently, FFO To Total Debt dropped during FY23 and FY24 (FY22: 0.25x: FY23:0.21x: FY24: 0.09x) and FFO to Long Term Debt also dropped during FY23 and FY24 (FY22:0.47x: FY23: 0.38x: FY24: 0.17x), albeit remaining aligned with the assigned ratings.

The Company's short-term debt is sufficiently covered by trade receivables and inventory, providing coverage of 2.99x at the end of FY24 (FY23: 2.95x; FY22: 3.12x)

The current ratio though slightly declined in FY24 to 1.39x, due to drop in inventory and receivables levels, historically has remained adequate (FY22: 1.55x: FY23: 1.61x). Moreover, , the aging profile of trade debts reflects a healthy liquidity position, as ~77% of these debts are not yet due at the end of FY24.

The Company's cash conversion cycle remained relatively stable at around 87 days (FY22: 89 days; FY23: 91 days; FY24: 80 days) during the period FY22 to FY24, indicating effective management of the working capital.

The Debt Service Coverage Ratio (DSCR) has seen a decline during the period under review due to rising financial charges and lower FFO. DSCR was recorded at 1.16x at the end of FY24 (FY23: 1.93x; FY22: 3.67x). Going forward, improvement in debt service coverage will remain an important rating consideration.

Equity base experienced moderate growth, gearing and leverage ratios remain stable. Excluding revaluation surplus, equity base modestly increased by ~2.6% in the last 24 months, hitting PKR 1.59b at end-FY24, primarily driven by higher profit retention. The Company has a history of dividend payouts and paid a dividend of PKR57.92m in FY24 as well. The Company's Total Debt has declined by 18.3% in the last 24 months, to Rs 1.61b at end-FY24 (end-FY23: PKR 1.77bn. end-FY22: PKR 1.97bn) with timely debt redemptions. With the decline in debt, gearing and leverage indicators improved during the review period to stand at 1.01x at end-FY24 (end-FY23: 1.11x: end- FY22: 1.27x) and 1.68x at end-FY24 (end-FY23: 1.85x: end-FY22: 2.05x), respectively. Going forward, maintenance and improvement in capitalization indicators will remain important from the ratings perspective.

Shahtaj Textile Limited — Appendix I

Financial Summary (PKRin milllions)						
<u>Balance Sheet</u>	FY19	FY20	FY21	FY22	FY23	FY24
Plant, Property and Equipment	1,080.8	1,152.2	1,409.4	1,760.7	1,632.2	1,862.1
Stock-in-Trade	529.3	690.7	1,016.6	1,801.6	1,253.2	1,112.3
Trade Debts	948.9	590.6	647.6	997.3	1,082.0	1,067.3
Cash & Bank Balances	32.2	49.2	50.4	17.2	42.6	34.4
Total Assets	2,899.0	2,824.1	3,360.7	4,943.1	4,730.5	4,450.7
Trade and Other Payables	357.1	544.5	628.2	955.8	916.2	859.0
Long Term Debt	386.4	540.7	658.0	1,053.0	952.0	855.6
Short Term Debt	791.2	390.5	298.2	913.0	819.8	749.9
Total Debt	1,177.6	931.2	956.3	1,966.0	1,771.9	1,605.5
Paid Up Capital	96.6	96.6	96.6	96.6	96.6	96.6
Total Equity (Excluding Surplus)	1,141.8	1,133.9	1,325.0	1,546.3	1,590.4	1,586.4
<u>Income Statement</u>	FY19	FY20	FY21	FY22	FY23	FY24
Net Sales	4,787.6	4,365.8	4,937.5	7,455.5	8,085.2	7,953.4
Gross Profit	448.8	421.3	550.3	733.0	640.9	673.3
Operating Profit	251.6	193.0	334.6	464.4	375.8	371.3
Finance Cost	87.3	80.2	47.4	86.5	214.3	318.0
Profit Before Tax	251.4	113.1	287.5	401.7	137.1	(7.1)
Taxation	63.3	40.5	70.6	101.7	15.9	34.3
Profit after Tax	188.0	72.6	217.0	300.0	153.0	27.2
<u>Ratio Analysis</u>	FY19	FY20	FY21	FY22	FY23	FY24
Gross Margin	9.4%	9.6%	11.1%	9.8%	7.9%	8.5%
Net Margin	3.9%	1.7%	4.4%	4.0%	1.9%	0.3%
Net Working Capital	536.2	636.0	868.9	1,117.6	1,160.2	712.8
Current Ratio	1.4	1.6	1.8	1.6	1.6	1.4
<u>FFO</u>	259.0	199.3	376.8	493.8	363.6	146.8
FFO to Total Debt	22%	21%	39%	25%	21%	9%
FFO to Long Term Debt	67%	37%	57%	47%	38%	17%
Debt Servicing Coverage Ratio	2.7	2.1	5.5	3.7	1.9	1.2
(Trade Debts + Inventory)/Short term Borrowings	1.9	3.4	5.7	3.1	2.9	2.99
Adjusted Gearing	1.0	0.8	0.7	1.3	1.1	1.0
Adjusted Leverage	1.5	1.4	1.3	2.1	1.8	1.7
ROAA	6.74%	2.54%	7.02%	7.23%	3.16%	0.59%
ROAE	17.09%	6.38%	17.65%	20.90%	9.76%	1.71%
Days Sales Outstanding	60	64	46	40	47	49
Days Inventory Outstanding	44	56	71	77	75	59
Days Payables Outstanding	20	25	29	28	31	28
Cash Conversion Cycle (Days)	84	95	88	89	91	80

REGULATORY DISCLOSURES — Appendix II

Name of Rated Entity	Shahtaj Textile Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Instrument Structure	N/A

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
11/13/2024	A-	A2	Stable	Reaffirmed
11/24/2023	A-	A2	Stable	Reaffirmed
11/23/2022	A-	A2	Stable	Reaffirmed
01/14/2022	A-	A2	Stable	Reaffirmed
12/29/2020	A-	A2	Stable	Reaffirmed
4/23/2020	A-	A2	Rating Watch Developing	Maintained
12/26/2019	A-	A2	Stable	Reaffirmed
01/18/2019	A-	A2	Stable	Reaffirmed

Statement by the Rating Team

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.

Probability of Default

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.

Disclaimer

Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Contents may be used by news media with credit to VIS.

Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Amir Ahmed	Chief Financial Officer	October 17, 2024
Mr. Wasim	Manager Accounts and Finance	