VIS
Credit Rating Company Limited

RATING REPORT

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MUHAMMAD SHAFI TANNERIES (PRIVATE) LIMITED

Chairman & Chief Executive: Mian M. Haleem & Mr. M. Naseem

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

RS. MILLION	FY23	FY24	9MFY25
Net Sales	1,713	2,697	1,707
LPBT	59	160	58
PAT	34	128	35
Paid up call	45	45	45
Equity (incl. surplus on PEE)	2,135	2,258	2,293
Total Debt	497	641	561
Debt Leverage	0.40	0.48	0.48
Gearing	0.23	0.28	0.24
FFO	54	118	(164)
FFO/Total Debt (x)*	0.11	0.18	(0.29)
NP Margin	2.0%	4.7%	2.1%

RATING DETAILS

RATINGS CATEGORY	LATEST RATING		PREVIOUS RATING	
	Long-term	Short-term	Long-term	Short-term
ENTITY	BBB+	A2	BBB+	A2
RATING OUTLOOK/ WATCH	Stable		Stable	
RATING ACTION	Reaffirmed		Reaffirmed	
RATING DATE	June 24, 2025		March 5, 2024	

RATING RATIONALE

The assigned ratings factor in the medium business risk profile of the leather industry in Pakistan, which is characterized by its export-oriented nature, cyclicality, and sensitivity to rising energy costs. Additionally, shift in consumer preference towards synthetic leather is also posing demand-side challenges for the sector.

The ratings are primarily based on the Company's conservative capital structure, with zero long-term debt as of 9MFY25 and minimal short-term borrowings. Sales has demonstrated strong growth, with a 3-year topline CAGR of 42% as of FY24 with historic high-capacity utilization in FY24 based on improved demand, although a loss of momentum was witnessed in 9MFY25. The lower topline along with cost pressures led to an operational loss and negative funds from operations (FFO) in 9MFY25, which is in line with the overall cyclicality of the sector. The insufficient debt service coverage from operational cash flow is a point of concern from the rating perspective. However, liquidity remained strong, supported by a high current ratio and satisfactory liquid assets available on the Company's balance sheet to meet its financial obligations.

Going forward, measures to mitigate cyclicality and recovery in operational cash flow, alongside maintaining of the conservative capital structure would remain crucial from ratings perspective.

COMPANY PROFILE

Muhmmad Shafi Tanneries (Private) Limited ('MSTL' or 'the Company') is a family-owned company with major shareholding vested with Mr. Amjad Hafeez (22%), Mr. Muhammad Naseem (20%), Mr. Tahir Hanif (13%) and Mr. Muhammad Haleem (12%).The Company is engaged in manufacture and export of finished leather made from goat and sheep hides, which is used in making of shoes, gloves and fashion articles. MSTL belongs to Shafi Group which has presence in the textile (Shafi Texcel Limited-STL), food (Everfresh Farms-EFPL, Shafi Foods - SFPL) and footwear sectors. The aggregate topline for the group (including MSTL) records at PKR 18 Bn for FY24 (FY23: PKR 14.2 Bn).

The Company was incorporated in 1972, as a partnership concern and later converted into a private limited company in 1988. The registered head office of the Company is located at Lalazar, Opposite Beach Luxury Hotel, Karachi and factory is located at Haroonabad, SITE, Karachi.

INDUSTRY PROFILE & BUSINESS RISK

The leather industry in Pakistan is characterized by a medium business risk profile, supported by its strong export-oriented nature. In FY24, the industry experienced a notable downturn due to global and domestic challenges. Exports of leather and leather products declined by 8.87%, falling to USD 808 Mn from USD 887 Mn in the previous year. This decline was primarily driven by demand side challenges as a result of global economic slowdown, political uncertainty and shift in consumer preference towards synthetic/artificial leather. Artificial leather is typically more cost-effective, offers a wider range of styles and patterns, and aligns with the growing global preference for animal-friendly products.

On the Supply side, challenges rose due to currency depreciation in 1HFY24, which increased the cost of imported raw materials. Additionally, the withdrawal of key government incentives, such as the Duty Drawback of Local Taxes and Levies (DLTL) scheme from July 2022 and concessional energy tariffs from May 2023, has further strained the sector.

To address these challenges, MSTL has adapted its product offerings by incorporating colors and patterns of artificial leather through the use of stamping foil, according to client needs (Foil article production for FY24: 9.5%, 9MFY25: 13.5%). This approach also provides the Company with a competitive edge in the regional market. However, it may not be sustainable in the long term, as the inherently higher cost of pure leather continues to be a disadvantage compared to synthetic leather. On the supply side, to mitigate rising energy costs, MSTL has installed a 250kW solar panel system during FY24, which has contributed to a reduction in its fuel and power expenses.

Product Profile & Capacity

The installed capacity has remained unchanged while utilization levels reflect a gradual increase since FY21, reaching 81% during FY24. However, in 9MFY25 the utilization rate lowered back to 61% due to demand-side constraints.

Capacity & Utilization					
In Million Sq.ft	**FY21**	**FY22**	**FY23**	**FY24**	**9MFY25**
Installed Capacity	12	12	12	12	9
Actual Production	5.5	6.8	7.3	9.7	5.5
Utilization	**46%**	**57%**	**61%**	**81%**	**61%**

FINANCIAL RISK

Capital Structure

The Company maintains a conservative capitalization profile wherein both gearing and leverage remained historically lower than 0.3x and 0.5x, respectively. Long-term debt stood at negligible levels at end-9MFY25, consisting only lease liabilities, while short-term borrowings are also relatively low. During FY24, the Company had also taken interest-free loan of PKR 75 Mn from a related party, Shafi Gluco Chem (Pvt) Limited, which has been repaid during the on-going year.

Gearing and leverage ratio stood at 0.24x and 0.48x at end-9MFY25 (FY24: 0.25x, 0.48x), which were marginally up from FY23 levels.

Looking ahead, the Company plans to further expand its solar power capacity by installing an additional 500 kW panels at an estimated cost of PKR 60 Mn. The project will be financed through internal cash reserves with an expected completion timeline of two years. As per the management, the Company expects to save ~ PKR 20 Mn annually.

Profitability

The Company's topline reports a 3-year CAGR of 42% with FY24 sales reaching PKR 2.7 Bn (FY23: PKR 1.7 Bn, FY21: PKR 936 Mn). On a YoY basis, sales grew by 57%, largely driven by higher volumetric export sales (70% of total volume), predominantly to China and Germany. Additionally, the Company's client diversification improved with its top ten client concentration decreasing to 61% (FY23: 87%).

Gross margin edged down to 19.1% (FY23: 20.7%) in FY24 primarily due to an increase in average cost of hides, although some of this impact was mitigated by higher pricing.

Meanwhile, finance cost rose by 67% amidst elevated interest rates, however, other income gain of PKR 56 Mn (FY23 Other Loss: PKR 28 Mn) from MSTL's short term investment in mutual funds and PKR 36 Mn share of profit from associates (FVTPL adjustment therefore no cash impact), supported Company's bottom line. As a result, MSTL reported a net income of PKR 128 Mn (FY23: PKR 34 Mn), with a net margin of 4.7% (FY23: 2.0%).

During 9MFY25 amid slowdown in demand, topline reported at PKR 1.7 Bn with export contribution rising to 78% (FY24: 70%). Gross margins fell to 13.3% due to increase in salaries, wages and factory overheads. Subsequently, Company reported an operational loss of PKR 68 Mn and a negative operating margin of 4.0%. Finance costs were relatively low at PKR 33 Mn while other income of PKR 45 Mn and a higher share of profit from associates (9MFY25: PKR 113 Mn. FY24: PKR 39 Mn), once again aided in preventing net margin erosion. Consequently, net margin turned positive at 2.1% with a net income of PKR 35 Mn.

Table 1: Product-wise sales

Product Wise	FY23		FY24		9MFY25	
	Volume	Value	Volume	Value	Volume	Value
Goat	59.6%	58.4%	53.3%	50.5%	54.0%	54.6%
Sheep	36.2%	32.6%	40.0%	34.7%	35.8%	30.5%
Cow	1.0%	1.2%	1.7%	2.4%	4.2%	5.2%
Deer	3.2%	7.8%	5.0%	12.5%	6.0%	9.7%

Debt Coverage & Liquidity

At end-FY24, liquidity profile remained strong with a high current ratio of 2.09x (FY23: 2.35x). Further, the Company's cash conversion cycle improved from 254 days to 194 days driven by a higher inventory turnover.

Attributed by higher net profit, Funds from Operations (FFO) rose to PKR 118 Mn (FY23: PKR 54 Mn). Consequently, coverage ratios improved with FFO to short term and total debt recording at 0.19x and 0.18x (FY23: 0.11x), respectively. Meanwhile, Debt Service Coverage Ratio (DSCR) strengthened to 2.45x (FY23: 1.79x).

During 9MFY25, current ratio reported at 1.99x reflecting reduction in cash balance and receivables. Cash conversion cycle remained stable at 193 days, while FFO reported negative as a result of operational loss. However, coverage profile draws comfort from satisfactory liquid assets available on the Company's balance sheet in order to meet its financial obligations. Going forward, improvement in cash-generation will remain an important rating trigger.

GOVERNANCE

As of FY24, the Company has changed its auditor to BDO Ebrahim & Co. Chartered Accountants (Previously was 'RSM Avais Hyder Liaquat Nauman Chartered Accountants'). Some concerns regarding governance are raised following current auditor's significant corrections to errors in Company's financial statements for the year FY23 and FY22. These mainly pertain to incorrect recording of 'share of profits from associates' which had been based on management accounts up to June 2023. Moreover, carrying value of investments in associate was also inaccurately reported.

FINANCIAL SUMMARY *(amounts in PKR millions)*				*Appendix I*	
BALANCE SHEET	**FY21**	**FY22**	**FY23**	**FY24**	**9MFY25**
Property, plant and equipment	341.7	361.9	393.0	437.3	458.0
Right-of-use Assets	8.6	8.4	5.2	4.4	4.4
Intangible Assets	0.4	0.3	0.3	0.3	0.3
Long-term Investments	826.7	751.2	780.5	819.5	932.8
Stock-in-trade	840.1	734.5	1,027.3	1,184.0	1,280.1
Trade debts	120.7	174.7	222.3	388.0	198.7
Short-term Investments	368.3	594.9	173.6	46.2	161.4
Cash & Bank Balances	72.5	73.9	75.1	112.5	31.0
Total Assets	**2,878.2**	**2,983.8**	**2,987.3**	**3,343.4**	**3,386.6**
Creditors	122.5	234.5	256.9	336.4	409.3
Long-term Debt (incl. current portion)	84.3	65.3	22.8	17.5	8.5
Short-Term Borrowings	400.0	499.1	474.8	623.2	552.2
Total Debt	484.3	564.4	497.5	640.7	560.7
Total Liabilities	**685.6**	**867.3**	**851.9**	**1,085.8**	**1,093.9**
Paid up Capital	44.6	44.6	44.6	44.6	44.6
Revenue Reserve	1,995.2	1,919.3	1,938.0	2,060.2	2,095.3
Total Equity	**2,192.6**	**2,116.7**	**2,135.4**	**2,257.6**	**2,292.7**
INCOME STATEMENT	**FY21**	**FY22**	**FY23**	**FY24**	**9MFY25**
Net Sales	936	1,298	1,713	2,697	1,707
Gross Profit	117	253	355	515	227
Operating Profit	(77)	36	107	145	(68)
Finance Costs	(24)	(19)	(42)	(71)	(33)
Profit Before Tax	(45)	75	59	160	58
Profit After Tax	(62)	57	34	128	35
RATIO ANALYSIS	**FY21**	**FY22**	**FY23**	**FY24**	**9MFY25**
Gross Margin (%)	12.6%	19.5%	20.7%	19.1%	13.3%
Operating Margin (%)	-8.2%	2.8%	6.2%	5.4%	-4.0%
Net Margin (%)	-6.6%	4.4%	2.0%	4.7%	2.1%
Funds from Operation (FFO) (PKR Millions)	(65.23)	58.51	53.80	118.21	(163.96)
FFO to Total Debt* (%)	-13.5%	10.4%	10.8%	18.4%	-29.2%
FFO to Long Term Debt* (%)	-77.4%	89.6%	236.5%	674.4%	-1935.4%
Gearing (x)	0.22	0.27	0.23	0.28	0.24
Leverage (x)	0.31	0.41	0.40	0.48	0.48
Debt Servicing Coverage Ratio* (x)	(0.58)	1.28	1.79	2.45	(2.69)
Current Ratio (x)	2.88	2.37	2.35	2.09	1.99
(Stock in trade + trade debts) / STD (x)	2.40	1.82	2.63	2.52	2.68
Return on Average Assets* (%)	-2.1%	1.9%	1.1%	4.0%	1.4%
Return on Average Equity* (%)	-2.8%	2.6%	1.6%	5.8%	2.1%
Cash Conversion Cycle (days)	367	224	254	194	193
* Annualized Figures					

REGULATORY DISCLOSURES					Appendix II
Name of Rated Entity	Muhammad Shafi Tanneries (Private) Limited				
Sector	Tanneries and Leather Products				
Type of Relationship	Solicited				
Purpose of Rating	Entity Ratings				
Rating History	Rating Date	Medium to Long Term	Short Term	Outlook / Rating Watch	Rating Action
	RATING TYPE: ENTITY				
	06/24/2025	BBB+	A2	Stable	Reaffirmed
	03/05/2024	BBB+	A2	Stable	Reaffirmed
	05/09/2023	BBB+	A2	Stable	Reaffirmed
	05/19/2022	BBB+	A2	Stable	Downgrade
	07/26/2021	A-	A2	Negative	Maintained
	06/30/2020	A-	A2	Rating Watch - Developing	Maintained
	05/02/2019	A-	A2	Negative	Maintained
	01/26/2018	A-	A2	Stable	Reaffirmed
	06/17/2015	A-	A2	Stable	Reaffirmed
	05/20/2014	A-	A2	Stable	Upgrade
	03/18/2013	BBB+	A3	Stable	Reaffirmed
	02/01/2012	BBB+	A3	Stable	Initial
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.				
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Due Diligence Meetings Conducted	S.No.	Name	Designation	Date	
	1.	Mr. Shahid Ahmed	CFO	29-May, 2025	