RATING REPORT

Soorty Enterprises (Private) Limited

REPORT DATE:
April 05, 2018

RATING ANALYSTS:

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RATING DETAILS		
	Latest Rating	
Rating Category	Long-term	Short-term
Entity	AA-	A-1
Rating Date	*March 22, 2018*	
Rating Outlook	Stable	
Outlook Date	*March 22, 2018*	

COMPANY INFORMATION	
Incorporated in 1984	**External auditors:** Kreston Hyder Bhimji & Co. Chartered Accountants
Private Limited Company	**Managing Directors:** - Mr. Shahid Rashid Soorty (CEO) - Mrs. Nargis Shahid Soorty - Mr. Asad Shahid Soorty

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (May, 2016) http://www.jcrvis.com.pk/kc-meth.aspx

Soorty Enterprises (Private) Limited

OVERVIEW OF THE INSTITUTION

Soorty Enterprises (Private) Limited (SEL) was incorporated as a Private Limited Company on March 12, 1984.

SEL is a family owned business with major shareholding resting with Mr. Shahid Rashid Soorty and Mr. Abdul Rashid. Mr. Shahid Soorty has been associated with SEL since the past three decades and is currently the CEO of the company.

SEL is compliant with International Social and Environmental & Quality standards. SEL owns 99.99% shareholding in Soorty Textiles (BD) Limited which is involved in the manufacturing of denim garments. The company also has a wholly owned subsidiary in UAE involved in investment in securities and providing textile related services. The company has a Marketing and Display Center in Amsterdam and a Product Development Center in Turkey. The company also has a marketing office in Dubai to facilitate its sponsors and staff visa and business meetings.

RATING RATIONALE

Soorty Enterprises (Private) Limited (SEL) is one of the leading denim fabric and garment manufacturers in the country with vertically integrated operations. The company commenced its operations in 1984 as a denim garment manufacturer and backward integrated operations through diversifying in the spinning and weaving segment. SEL operates through various units at different locations in Landhi and Korangi, Karachi and Nooriabad, Pakistan, comprising spinning, denim weaving, garments and washing units. The Company also has international presence through a subsidiary in Bangladesh, a marketing company in United Arab Emirates, a Research, Development and Design Office, Amsterdam, Netherlands and a Product Development Center in Turkey. SEL's operations encompass the following three divisions:

Spinning: This division deals in production of yarn which is utilized in-house for production of fabric. Current spinning capacity of SEL can cater to around half of fabric division's yarn requirement. The company is in the process of installing additional spindles subsequent to which the company will be able to cater to over three-fourth of fabric division's yarn requirement.

Denim Fabric: In volumetric terms, around three fifth of the total fabric produced is utilized in-house to manufacture garments whereas the remaining is exported and sold in the local market to garment manufacturers. Fabric sales comprise around one-fifth to the company's total revenues. In order to cater to higher demand of the garment division (In Pakistan and Bangladesh), the company is in the process of enhancing production through induction of efficient looms which is targeted to be completed by the end of the ongoing year.

Denim Garments: Garments sales contribute around four fifth to the total sales revenue of SEL. Utilization of denim garments has improved on a timeline basis due to enhanced production efficiency. Utilization levels are reported lower as compared to peers due to a cushion maintained by the management to cater orders that require lesser lead times. To furnish rising demand, SEL plans to increase garments manufacturing capacity which is anticipated to complete by the end of the ongoing fiscal year. SEL's garments exports are largely concentrated in the European region which is a function of the management's focus to foster direct client relationships rather than following the agency model. The management also has future plans of tapping the US market post expansion.

Diversification: Diversification initiatives include 10% shareholding in a furnace oil based IPP. Also, recently, the company has invested in the industrial gases segment while diversification in the power sector is in the pipeline. Moreover, liquid investments held on balance sheet support income streams. SEL through its planned investment in NASDA Wind Power project is expected to diversify in the renewable energy sector.

Key Rating Drivers

Sector Dynamics and Business risks

Business risk profile is supported by stable and growing demand for denim fabric and garments. However, local and international expansion by major players is expected to keep pricing power and hence margins under pressure. Moreover, significant investment required by customers as part of sustainability initiative is expected to add to cost pressures for denim manufacturers. Despite diversification plans, SEL's operations are currently concentrated with exposure entirely to the denim industry which might significantly impact business risk profile in case of change in demand patterns or any other industry specific factors. Therefore keeping pace with rapid changes in fashion trends is considered important. JCR-VIS expects demand for denim products to remain stable over the medium term. Other key business risk factors include efficient procurement of cotton and weakening in law and order situation.

Profitability
Revenues of the company have grown at a CAGR of 7% over the past three years. Growth in sales is primarily attributable to volumetric increase while average prices have witnessed a declining trend. Export sales represent the major portion of company's revenues with garment segment contributing around four-fifth of the company's topline. In volumetric terms, around three fifth of the fabric produced is utilized in-house to further manufacture garments. The remaining is exported and sold locally to garment manufacturers. Gross margins of the company compare favorably to non-denim textile operators but have witnessed a declining trend on a timeline basis on account of declining average selling prices, higher average cotton procurement prices and rising cost of doing business. Despite rupee depreciation during the ongoing year, JCR-VIS expects gross margins to remain under pressure on account of increasing competition. Quantum of future profits will depend on volumetric growth in sales post capacity expansion.

Liquidity
Liquidity profile of the company is considered strong in view of adequate cash flows in relation to outstanding obligations and ageing profile of trade debts which remain within manageable levels. During FY18, cash flows will also be supported by receipt of rebates announced by the government under the textile policy. With current assets being greater than current liabilities, current ratio of SEL was reported greater than 1 at end-FY17. With majority payment of cotton being made upfront (local cotton is procured on cash and imported cotton is obtained on site LC), and higher time to collect receivables and inventory days, SEL's working capital cycle necessitates utilization of short term borrowing.

Funding and Capitalization
The company's historical stance of maintaining very low dividend payouts and funding its expansions through limited debt is reflective of a conservative financial policy. Capitalization levels of the company have grown at a healthy pace over the last three years due to profit retention. Debt carried on the balance sheet largely comprises short-term debt to fund working capital requirements. With increase in equity base being higher than growth in debt, gearing and leverage indicators have improved on a timeline basis. Given the company's expansion plans, leverage indictors will increase slightly but are projected to remain commensurate with benchmarks for the assigned ratings.

Corporate Governance
Overall scope and functioning of internal audit and IT function are considered adequate. Given the company's nature as a private limited company, there is significant room for improvement in board composition and oversight.

ISSUE/ISSUER RATING SCALE & DEFINITION — Appendix I

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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 II

Name of Rated Entity	Soorty Enterprises (Private) Limited
Sector	Textile Industry
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	(see table below)
Instrument Structure	N/A
Statement by the Rating Team	JCR-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	JCR-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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
March 22, 2018	AA-	A-1	Stable	Initial