# RATING REPORT

# Soorty Enterprises (Private) Limited

**REPORT DATE:**
December 31, 2018

**RATING ANALYSTS:**

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## RATING DETAILS

| Rating Category | Latest Rating | | Previous Rating | |
|---|---|---|---|---|
| | Long-term | Short-term | Long-term | Short-term |
| **Entity** | AA- | A-1 | AA- | A-1 |
| ***Rating Date*** | *Dec 31, 2018* | | *March 22, 2018* | |
| **Rating Outlook** | Stable | | Stable | |
| ***Outlook Date*** | *Dec 31, 2018* | | *March 22, 2018* | |

## COMPANY INFORMATION

| | |
|---|---|
| **Incorporated in** 1984 | **External auditors:** Kreston Hyder Bhimji & Co. Chartered Accountants |
| **Private Limited Company** | **Managing Directors:**<br>- Mr. Shahid Rashid Soorty (CEO)<br>- Mrs. Nargis Shahid Soorty<br>- 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 has a significantly owned subsidiary in Bangladesh 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. 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 in Amsterdam, Netherlands and a Product Development Center in Turkey. The subsidiary in Bangladesh reported growth in revenues owing to increasing capacity utilization levels. The company has also diversified operations through investments in the power and industrial gases sectors.

**Key Rating Drivers**

**Satisfactory operating track record with consistently high capacity utilization in all three segments**
During FY18, the company enhanced its capacity in the spinning and weaving division by 18% and 20%, respectively. Consequently, the company is now able to meet around two-third of their fabric division's yarn requirement. Capacity utilization of all three segments- yarn, fabric and garments were reported on the higher side during FY18 and in the ongoing year. Moreover, during the ongoing year, the company is undergoing expansions in all three operating segments which are targeted to be completed in ongoing fiscal year. Post expansion which will increase the spinning segment capacity and additional spindles will be able to cater around four-fifth of the company's yarn requirement. In addition to capital expenditures pertaining to core operations, the company also has plans to incur investments for sustainability requirements and to remain compliant with best practices. In this regard, new certification was obtained during the ongoing year.

**Moderate business risk and low pricing power given sector dynamics**
Business risk profile is supported by stable and growing demand for denim products. However, local and international expansion by major players is expected to keep pricing power and hence margins under pressure. Despite diversification plans, the company's operations are currently concentrated with exposure 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. Given the focus of the government on enhancing exports, there is significant opportunity for Denim players to enhance exports. In this regard, SEL is well positioned to tap this opportunity given the ongoing and completed expansion in all three segments.

**Healthy sales growth with garment segment dominating sales mix**
Sales revenue of the company posted a growth of 14% in FY18 largely being a function of higher volumes sold. Increase in weaving division's production translated into a sizeable increase in fabric sales during the outgoing year. Growth in garments sales was a function of higher average selling prices due to currency devaluation. Moreover, with completion of expansion in the spinning and fabric division, product sales mix of the company changed during the outgoing year with proportion of denim fabric sales increasing to one-fourth of overall sales with remaining revenues emanating from garment sales. Going forward, management expects sales mix to remain at similar levels. Geographic sales mix demonstrates higher concentration of fabric sales directed to Bangladesh and garment sales directed to European market. The management is also looking to increasingly tap other markets. Increased focus on research and development and training and branding is being undertaken to sustain growth in revenues.

**Robust profitability profile which is expected to sustain over the rating horizon**
Gross Margins (GMs) of the company compare favorably to denim and non-denim textile operators and have been maintained at preceding year's levels. Higher volumetric sales, impact of rebate and currency devaluation have offset the impact of increase in raw material prices. Operating profit during FY18 was reported on the lower side due to decline in dividend income. Impact of increase in interest rates on profitability is expected to be limited due to low leveraged capital structure and primarily low cost export refinance borrowing mobilized. Going forward, JCR-VIS expects profitability profile to sustain on the back of volumetric growth in sales post increase in capacity. Full impact of enhanced capacity in all three segments will be visible from FY20 onwards.

**Strong liquidity profile with cash flows sufficient to fund planned capex**
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. Funds flow from operations increased by 32% and is expected to remain sufficient for funding all planned capex. With current assets being greater than current liabilities, current ratio of SEL was reported greater than 1(x) at end-FY18. 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.

**Low leveraged capital structure and conservative financial policy**
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. Equity base of the company have grown at a healthy pace over the last three years due to profit retention. Debt carried on the balance sheet comprises short-term debt to fund working capital requirements. Given the company's ability to finance its expansions through internal cash flows and no projected debt drawdown, leverage and gearing indicators are expected to remain commensurate with benchmarks for the assigned ratings. Impact of currency depreciation on overall cost of expansion is considered manageable.

**Adequate corporate governance infrastructure**
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.

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**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** | |

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| **RATING TYPE: ENTITY** | | | | |
| December 31, 2018 | AA- | A-1 | Stable | Reaffirmed |
| March 22, 2018 | AA- | A-1 | Stable | Initial |

| | |
|---|---|
| **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. |
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