RATING REPORT

Saakh Pharma (Private) Limited

REPORT DATE:
February 25, 2020

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	BBB+	A-2	BBB+	A-2
Rating Date	*February 25, 2020*		*October 25, 2018*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Initial	

COMPANY INFORMATION	
Incorporated in 2014	**External auditors:** Grant Thornton Anjum Rahman Chartered Accountants
Private Limited Company	**Chairman & Chief Executive Officer (CEO):** Mr. Syed Abrar Hussain Kazmi
Key Shareholders (with stake 5% or more):	
Mrs. Syeda Sardar Bano – 100%	

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

Saakh Pharma (Private) Limited (SPPL)

OVERVIEW OF THE INSTITUTION

Saakh Pharma (Private) Limited (SPPL) was incorporated as a private limited company in 2014 and subsequently commenced commercial operations in August'2015 with its head office based in Karachi, Pakistan. Manufacturing facilities of SPPL is situated in Port Qasim Karachi.

External auditors of the company are Grant Thornton Anjum Rahman Chartered Accountants. Auditors belong to category 'A' on the approved list of auditors published by the State Bank of Pakistan.

Financial Snapshot

Net Equity: June 2019: Rs. 458.1m, June 2018: Rs. 456.3m

Net Revenue: FY19: Rs. 2.06b, FY18: Rs. 1.04b

RATING RATIONALE

Saakh Pharma (Private) Limited (SPPL) is among few Active Pharmaceutical Ingredients (API) manufacturers in Pakistan. The company started its commercial operations in 2015 and is currently going through a growth phase. The management's long term vision is to be a one stop solution of all APIs for local pharmaceutical firms.

Investments & Business Plans

SPPL holds 50% stake in CKD Pharma, a pharmaceutical formulation company. Lately, the management has also made a long term investment in herbal/nutraceutical segment through a joint venture with 50/50 partnership. Both companies are at a relatively nascent stage but are expected to post healthy growth over the rating horizon.

Product Portfolio & Manufacturing Facilities

Presently, product portfolio comprises **Semi Synthetic Penicillin – SSP** (Amoxicillin, Ampicillin & Cloxacillin), **Semi Synthetic Cephalosporin – SSC** (Cefixime, Cephradine & Ciprofloxacin), **Corticosteroid**, **Paracetamol, Sitagliptin, and Esomeprazole** (22.5% & 8.5%). Alongside, **Taste masking** and **Pelletization** services are also being offered and capacities will be enhanced further. In line with product diversification strategy, management has planned to launch 'Pharma Sugar'; around one-half of total production will be sold by SPPL under an agency agreement with a local pharmaceutical company and sugar mill. Registered head office is situated in DHA Phase 6 while four production facilities are located in Port Qasim, Karachi. All production facilities are operating at high capacity utilization levels. The company has also recently set up an effluent treatment plant and obtained ISO certification for its manufacturing facilities.

Key Rating Drivers

Local industry dynamics

As per industry estimates, around 90% of the country's API requirement is fulfilled through imports. While capital requirements and entry barriers are considered low, extensive time for licensing requirements and increasing working capital requirements may act as entry barriers. SPPL is ranked at number two among half a dozen prominent API manufacturers in Pakistan.

Favorable business risk profile is supported by stable & growing demand of pharmaceutical sector and competitive advantages enjoyed by local API manufacturers' vis-à-vis imports.

Pharmaceutical products have historically witnessed relatively stable demand. This along with country's demographic profile translates into growing healthy demand for pharmaceutical products being manufactured by SPPL. Moreover, given that SPPL caters to less than 50% industry requirement of those above mentioned API products; product off-take risk is low.

Duty protection in the form of customs duty, additional sales tax and advance income tax provides price advantage to local API manufacturers. Moreover, convenience for pharmaceutical company due to lower lead time, limited exposure to exchange rate risk and facility of procuring desired quantity (vis-à-vis importers who have to buy in bulk) also provides competitive edge to local API manufacturers.

Regulatory & reputation risk along with rupee depreciation, low therapeutic area diversity and high product concentration are key business risk factors
Risk to reputation/brand as a result of inferior product quality or penalty by regulator due to manufacturing facilities not being up to the required standard is one of the major risks for API manufacturers. However, as per SPPL's management, regular customers and regulatory audits ensure product quality. Given that major portion of raw material is imported, any adverse movement in input prices, including on account of rupee devaluation, beyond levels that can be passed on to customers may impact margins and cash flows. Moreover, API manufacturers are reliant upon China for their raw material procurement, and in the backdrop of recent corona virus outbreak, maintaining procurement and supply chain efficiency will be important.

SPPL has managed to build a sizeable client base in a very short span of time with total number of clients comprising over 250 pharmaceutical companies. Client concentration in sales remains on the lower side. However, therapeutic area diversity is low and product-wise concentration is high with revenues emanating almost entirely from three products.

Healthy volumetric sales growth during FY19 and in the ongoing year While crossing the Rs. 2b mark in FY19, SPPL's topline has doubled as compared to last year. In HFY20, net sales were reported at Rs. 1.14b. Addition of new products (Paracetamol & Sitagliptin) and services (Taste masking & Pelletization), increase in average selling prices (of all products) and timely achievement of projected volumes were the key factors behind significant growth in sales during outgoing year FY19. In terms of product-wise sales, Cefixime, Amoxicillin and Paracetamol contribute more than 95% of total revenue. Going forward, management has budgeted sales target of around Rs. 3b for FY20. Growth in sales is expected to stem from the launch of 'Pharma Sugar' and increase in capacities of Taste masking and Pelletization services.

Profitability profile for FY19 impacted by exchange losses. Volumetric growth to be the key profitability driver for FY20.
Gross margins improved in FY19 and have sustained at above 10% in the ongoing year due to better absorption of fixed cost per unit. On the administrative cost front, overheads have increased on a timeline basis mainly due to increase in sales volume and new product being launched over time. Post FY18, finance cost has also increased considerably on the back of higher working capital requirements and increase in benchmark rates. Owing to significant rupee devaluation during FY19, the company posted an exchange loss of Rs. 65.2m. Excluding the impact of exchange loss, SPPL reported profit before tax of Rs. 83.1m (FY18: loss before tax of Rs. 21.1m) in FY19 while overall profit before was reported at Rs. 18.9m. Going forward, profitability growth will primarily be a function of volumetric sales growth.

Liquidity buffers to improve with profitability growth
Fund flow from operations (FFO) turned positive post FY17; however, one-off exchange loss during outgoing year significantly impacted the bottom-line and thus FFO. The same was reported at Rs. 17.9m (FY18: Rs. 83.7m) in FY19. SPPL's working capital cycle necessitates utilization of short-term debt with extended time to collect receivables and fund inventory levels. Current ratio was reported at 0.8(x) at end-FY19 while cushion of trade debts and stock in trade vis-à-vis short term borrowings is currently limited. In the medium term, management expects higher turnover and improved margins would translate in to

improvement in liquidity metrics.

Leverage indicators have trended upwards but comfort is drawn from conservative financial policy of undertaking capex through internal capital generation and equity injection

Equity base of the company has grown on timeline basis due to profit retention. Debt profile of the company is largely short term in nature with total interest bearing liabilities amounting to Rs. 552.1m (FY19: Rs. 545.1m; FY18: Rs. 183.1m) as at end-HFY20. Given that all capex planned is to be incurred through internal capital generation and fresh equity infusion, borrowings are only planned to be mobilized for working capital requirements. Leverage indicators on account of lower equity size and higher utilization of short term debt have elevated during outgoing year FY19. Ratings remain dependent on managing leverage indicators within prudent levels.

Corporate governance framework has room for improvement

Overall board structure and oversight has room for improvement through induction of additional directors (including independent directors), greater discussion on future strategy along with improvisation in internal control framework of the organization. The management has plans to set up a formalized internal audit department in the medium term.

Saakh Pharma (Private) Limited — Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**HFY20**
Fixed Assets	238.2	368.3	552.4	594.6
Stock-in-Trade	97.7	169.5	220.6	253.6
Trade Debts	112.9	226.9	394.0	414.5
Cash & Bank Balances	84.3	65.5	47.0	31.4
Total Assets	564.4	942.4	1,467.9	1,656.1
Trade and Other Payables	120.0	230.9	401.6	451.5
Short Term Debt	-	183.1	515.2	526.9
Paid-up Capital	569.5	569.5	625.2	625.2
Total Equity	433.2	456.3	458.1	589.6
INCOME STATEMENT	**FY17**	**FY18**	**FY19**	**HFY20**
Net Sales	510.7	1,044.3	2,062.9	1,139.2
Gross Profit	0.2	95.8	224.8	116.2
Operating Profit	(80.0)	5.7	109.1	46.8
Profit Before Tax	(76.9)	(21.1)	17.9	8.0
Profit After Tax	(93.2)	(32.7)	1.8	8.0
RATIO ANALYSIS	**FY17**	**FY18**	**FY19**	**HFY20**
Gross Margin (%)	0.05%	9.2%	10.9%	10.2%
Funds from operations (FFO)	(64.9)	83.7	17.9	NA
FFO to Total Debt (x)	-	0.46	0.03	NA
Current Ratio	2.72	1.15	0.75	0.90
Gearing (x)	-	0.40	1.19	0.94
Debt Leverage (x)	0.30	1.07	2.20	1.81
Debt Servicing Coverage Ratio (x)	-	25.02	1.86	NA
ROAA (%)	-19.1%	-4.3%	0..2%	1.0%
ROAE (%)	-24.5%	-7.3%	0.4%	3.0%

RATING SCALE & DEFINITION 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

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

(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

'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

Name of Rated Entity	Saakh Pharma (Private) Limited
Sector	Pharmaceutical
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see below
Instrument Structure	N/A
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.
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Due Diligence Meetings Conducted	see below

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
25 Feb, 2020	BBB+	A-2	Stable	Reaffirmed
25 Oct, 2018	BBB+	A-2	Stable	Initial

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Ayaz Wasay	Advisor	13-Feb-2020
2	Mr. Mujtaba	Management	13-Feb-2020