RATING REPORT

Saakh Pharma (Private) Limited

REPORT DATE:
August 11, 2021

RATING ANALYST:
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RATING DETAILS

	Final Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	BBB+	A-2	BBB+	A-2
Rating Date	*August 11, 2021*		*February 25, 2020*	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION

Incorporated in 2014	**External auditors:** Grant Thornton Anjum Rahman Chartered Accountants
Private Limited Company	**Chairman & CEO:** Mrs. Syeda Sardar Bano
Key Shareholders (with stake 5% or more):	
Mrs. Syeda Sardar Bano – 100%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates (May 2019)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Saakh Pharma (Private) Limited (SPPL)

OVERVIEW OF THE INSTITUTION	RATING RATIONALE
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.*	Saakh Pharma (Private) Limited (SPPL) is the leading player amongst half a dozen prominent API (Active Pharmaceutical Ingredients) manufacturers in Pakistan. The company started its commercial operations in 2015 and is currently going through a growth phase. SPPL is a family-owned business and sponsors are well-experienced and dedicated professionals. Head office along with four manufacturing facilities are situated in Karachi and all production facilities have been operating at high capacity utilization levels. **Investment portfolio** SPPL holds 50% stake in CKD Pharma (a pharmaceutical formulation company) and Focus & Rulz Health Care Pvt. Limited (a joint venture engaged in herbal/nutraceutical business) respectively. Both companies are at nascent stage and are expected to post a healthy growth in the coming years. **Product portfolio** At present, 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. Moreover, the management has also enhanced focus towards process improvement, cost optimization and enriching product suite. Going forward, a new product **Ibuprofen** will be added over the rating horizon. **<u>Key Rating Drivers</u>** **Local industry dynamics** Pharmaceutical sector is highly dependent on imports to meet the demand of basic raw material – APIs (primary process in pharmaceutical manufacturing). As per estimates, Pakistan's API market stands at ~Rs 100b and 95% of it is being imported (mainly from China, Germany, UK, USA and France). Extended time frame for licensing, increasing working capital requirements, strict regulatory compliance and quality control standards act as entry barriers in API manufacturing industry to a certain extent. **Business risk profile is supported by stable & growing demand of pharmaceutical sector along with competitive advantages enjoyed by local API manufacturers' vis-à-vis imports.** Pakistan's pharmaceutical industry is estimated at Rs. 453b (in FY20), presently growing at 10% per annum. There are 733 registered Pharma companies including 16 MNCs while top 100 companies hold ~97% of total market share. Aging population, rising health issues (especially during the pandemic) and low average health expenditure per capita ($43 per capita compared with world's average of $100 per capita) translates into growing healthy demand of Pharmaceutical industry and in turn for APIs being manufactured by SPPL. Duty protection in form of custom duty, additional sales tax and advance income tax remains intact and continues to provide price advantage to local API manufacturers.

APIs	Custom Duty	Sales Tax	Income Tax	Additional Custom Duty
	11% - 20%	17%	11%	2% - 7%

Moreover, the pharmaceutical firms enjoy the convenience of lower lead time, limited exposure to exchange rate risk and facility of procuring desired quantity which in turn provides additional competitive advantage to local API industry.

Reputation and exchange rate risk are the key business risk factors. Low therapeutic area diversity and high product concentration is present across the sector.

The brand and reputation risk as a result of inferior product quality or a penalty by regulator due to compromise in manufacturing standards is the major risk for API supplier. However, as per SPPL's management, regular customers and regulatory audits ensure product quality. Moreover, given that major portion of raw material in API manufacturing is imported, any adverse movement in input prices (including currency devaluation) may impact margins and cash flows. In addition, heavy reliance on China for raw material procurement (against the backdrop of Covid-19 outbreak) has significantly increased the inherent risk of supply chain disruptions.

SPPL has managed to build a sizeable client base of over 250 pharmaceutical firms in a very short span of time; few major customers for each product. Client concentration in sales remains on the lower side yet therapeutic area diversity is low and product-wise concentration is high with revenues emanating almost entirely from three products.

Topline has witnessed a healthy recovery in the outgoing fiscal year. Going forward, sales revenue is targeted to cross Rs. 4b mark by FY23 and the growth will stem from new product additions and enhanced capacities.

Sales revenue doubled up and crossed the Rs. 2b mark during FY19 and while the same trend was expected to continue, non-production days due to pandemic-induced supply chain disruptions caused the sales growth to decline in FY20. However, following the ease in pandemic restrictions globally after the first wave and given subsequent economic recovery, topline witnessed a healthy recovery in the outgoing fiscal year, amounting to Rs. 3.1b (year-on-year uptick of ~35%). The organic growth in volumes from existing products and increase in average selling prices (of all products) were the key growth factors. In terms of product-wise sales, Cefixime, Amoxicillin and Paracetamol continue to contribute more than 95% of total revenue. Going forward, sales revenue is targeted to cross Rs. 4b by FY23 and the growth will stem from new product additions and enhanced capacities.

Gross margins have remained under pressure; however, exchange gain supported the bottom-line profitability. Going forward, profitability growth will primarily be a function of projected increase in sales volumes.

Gross margins witnessed a considerable decline in FY20 and remained at similar level in the outgoing fiscal year. The decrease was mainly attributable to higher fixed cost incurred (supply chain remained affected as main API's raw material supplier was from Wuhan) and increasing input prices. On the other hand, overall operating expenses witnessed an increasing trend primarily due to growth in sales volume and new product being launched over time while rising debt levels led to a significant increase in financial charges. However, higher other income and exchange gain of Rs. 52.0m supported the bottom-line profitability during 9M'FY21. Profit after tax was reported at Rs. 81.6 (FY20: loss after tax of Rs. 133.5m) in 9M'FY21. Going forward, profitability growth will primarily be a function of projected increase in sales volumes.

Liquidity buffers remain adequate

Fund flow from operations (FFO) turned positive post FY17 and stood at Rs. 50.6m (FY19: Rs. 17.9m; FY18: Rs. 83.7m) at end-FY20. SPPL's working capital cycle necessitates utilization of short-term debt with extended time to collect receivables and fund inventory levels. Nonetheless, cash conversion cycle has witnessed an improving trend over the years. Current ratio was reported at 0.9(x) at end-9M'FY21 while cushion of trade debts and stock in trade vis-à-vis short term borrowings is satisfactory. Trade debts have increased consistently over the years on the back of increase in sales. However, aging profile of the same remain within manageable levels.

Leverage indicators have trended upwards on a timeline basis.

SPPL's equity base though has increased on a timeline basis but remains limited in terms of size. Debt profile is largely short term in nature with total interest bearing liabilities amounting to Rs. 930.2m at end-FY21; one-fifth is long-term debt. In recent years, higher working capital requirements has necessitated increase in utilization of short-term debt. Consequently, leverage and gearing ratios have witnessed a considerable increase. Moreover, loan support from directors on short-term basis is also undertaken to meet the working capital needs. Going forward, ratings remain dependent on managing leverage indicators within prudent levels.

Room for improvement exists in terms of corporate governance framework.

During the period under review, Mrs. Syeda Sardar Bano was appointed at the position of Chairman & CEO, replacing her late husband Mr. Syed Abrar Hussain Kazmi. Overall corporate governance framework may be improved through induction of additional directors (including independent directors), development of board level committees and greater discussion on future strategy. An experienced management team with relevant industry expertise is in place. There are 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**	**FY20**	**9M'FY21**
Fixed Assets	238.2	368.3	552.4	623.2	636.6
Stock-in-Trade	97.7	169.5	220.6	461.9	608.5
Trade Debts	112.9	226.9	394.0	353.1	688.6
Cash & Bank Balances	84.3	65.5	47.0	32.7	23.5
Total Assets	564.4	942.4	1,467.9	1,777.8	2,428.5
Trade and Other Payables	120.0	230.9	395.2	668.3	861.2
Payable to related parties *(Directors' loan)*					
Short Term Debt	-	183.1	515.2	561.0	827.2
Paid-up Capital	569.5	569.5	625.2	625.2	625.2
Total Equity	433.2	456.3	458.1	501.6	591.8
INCOME STATEMENT					
Net Sales	510.7	1,044.3	2,062.9	2,332.4	2,497.8
Gross Profit	0.2	95.8	224.8	166.7	180.7
Operating Profit	(80.0)	5.7	109.1	27.5	59.2
Profit Before Tax	(76.9)	(21.1)	17.9	(98.5)	81.6
Profit After Tax	(93.2)	(32.7)	1.8	(133.5)	81.6
RATIO ANALYSIS					
Gross Margin (%)	0.05%	9.2%	10.9%	7.1%	7.2%
Funds from operations (FFO)	(64.9)	83.7	17.9	50.6	NA
FFO to Total Debt (x)	-	0.46	0.03	0.08	0.20
Current Ratio	2.72	1.15	0.75	0.86	0.91
Gearing (x)	-	0.40	1.19	1.20	1.48
Debt Leverage (x)	0.30	1.07	2.20	2.54	3.10
Debt Servicing Coverage Ratio (x)	-	25.02	1.86	1.38	7.96
ROAA (%)	-19.1%	-4.3%	0.2%	-8.2%	3.4%
ROAE (%)	-24.5%	-7.3%	0.4%	-27.8%	13.8%

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	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action	
	RATING TYPE: ENTITY					
	11 Aug, 2021	BBB+	A-2	Stable	Reaffirmed	
	25 Feb, 2020	BBB+	A-2	Stable	Reaffirmed	
	25 Oct, 2018	BBB+	A-2	Stable	Initial	
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		Name	Designation	Date		
	1	Mr. Saad Madani	Advisor	15-July-2021		
	2	Mr. Muhammad Masood Ibrahim	GM Finance			