# RATING REPORT

## Siara Textile Mills (Pvt.) Limited (STML)

**REPORT DATE:**
February 27, 2024

**RATING ANALYSTS:**
M. Amin Hamdani
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| RATING DETAILS | | | | |
|---|---|---|---|---|
| Rating Category | Latest Rating | | Previous Rating | |
| | Long-term | Short-term | Long-term | Short-term |
| **Entity** | BBB | A-2 | BBB | A-2 |
| **Rating Outlook** | Stable | | Stable | |
| **Rating Action** | Reaffirmed | | Initial | |
| ***Rating Date*** | *February 27, 2024* | | *November 10, 2022* | |

| COMPANY INFORMATION | |
|---|---|
| **Incorporated in 2004** | **External Auditors:** Arshad Raheem & Co. Chartered Accountants |
| **Private Limited Company** | **Chairman of the Board:** Choudhry Mussarat Ali<br>**Chief Executive Officer:** Mr. Akhtar Ali Choudhry |
| **Key Shareholders (with stake 5% or more):** | |
| *Ch. Mussarat Ali – 44%* | |
| *Akhtar Ali Chaudhary – 19%* | |
| *Mr. Imran Akhtar – 10%* | |
| *Mr. Sufiyan Akhtar – 10%* | |
| *Mr. Wajid Ali – 10%* | |

## APPLICABLE METHODOLOGY(IES)

**VIS Entity Rating Criteria:** Industrial Corporates
*https://docs.vis.com.pk/docs/CorporateMethodology.pdf*

## APPLICABLE RATING SCALE(S)

***VIS Issue/Issuer Rating Scale:*** *https://docs.vis.com.pk/docs/VISRatingScales.pdf*

# Siara Textile Mills (Pvt.) Limited

## OVERVIEW OF THE INSTITUTION

*Siara Textile Mills (Pvt.) Limited (STML) was incorporated in 2004 and commenced commercial operations in 2007. The principal business activity of the company is manufacturing and sale of yarn in the local and international market. STML is ISO 9001 certified.*

***Profile of the Chairman:***
*Choudhry Mussarat Ali is the Chairman of Board of Director at STML. He is also Chairman of Lal Qila Group in Manchester, UK.*

***Profile of CEO:***
*Akhtar Ali Choudhry is the CEO of the company. He is a graduate and has over twenty-five years of experience in the textile sector. He has also served as Chairman Union Council from 1983-1991 and is an active member of Lahore, Gujrat and Sheikhupura Chamber of Commerce and Industry as well as the All-Pakistan Textile Mills Association.*

## RATING RATIONALE

**Corporate Profile**

Siara Textile Mills (Pvt.) Limited (STML) is a small sized spinning unit with an operational history of nearly 2 decades. Shareholding is completely vested with the sponsoring family that are also involved in running day to day operations. The company is principally involved in production and sale of yarn. The company operates through its head office at Faisal Town, Lahore and employees over 400 workers.

**Operational Performance**

STML's spinning mill is located at Warberton Road, Ferozewatwan, Sheikhupura. The company has the capacity to manufacture coarse yarn of counts ranging from 12/s to 30/s depending on market demand and product requirements. The company operates a single spinning unit with 23,232 spindles and on average can produce 700 bags of yarn per day translating into 70,000 kgs per day as each bag weighs nearly 100kg. In June 2023, it expanded this facility by adding an additional 8,400 spindles. These newly installed spindles became operational in July 2023. Post expansion the company has 31,632 installed spindles and the impact of this is expected to fully reflect in 2024.

During FY23, production figures have depicted a significant decrease compared to SPLY. The company's production model is based on pre-orders. Management has attributed the reduced production in FY23 to a decrease in demand orders. Going forward with additional spindles installed management anticipates improvement in production numbers.

**Table 1: Capacity & Production Data (Units in millions)**

| Capacity | FY22 | FY23 |
|---|---|---|
| No. of spindles installed | 23,232 | 23,232 |
| Installed Capacity (m. kgs) | 7.57 | 7.57 |
| Actual Production (m. kgs) | 7.41 | 5.81 |
| *Capacity Utilization %* | *97.9%* | 76.8% |

**Key Rating Drivers**

**Business risk profile elevated by cyclicality and high competition.**

The business risk profile of the spinning sector in Pakistan is characterized by high level of exposure to economic cyclicality and intense competition. This sector's performance is significantly influenced by the broader economic conditions in the country, making it inherently vulnerable to fluctuations in demand driven by economic factors.

In FY23, the spinning sector faced challenges due to various economic and environmental circumstances. These included damage to the cotton crop resulting from flooding in 1HFY23, escalating inflation, and diminishing foreign exchange reserves.

The spinning sector in Pakistan comprises ~407 spinning mills, which include both composite units and spinning units. This industry exhibits a competitive market structure with a large number of players producing a relatively homogenous product.

During FY23, Pakistan's yarn production registered a substantial decline, primarily due to reduced availability of cotton, as a result of crop damage and import restrictions. The sector's profitability was constrained by factors such as higher production costs, increased raw material costs, and rising energy expenses, all of which constrained the sector's profit margin. The industry's performance is closely intertwined with the outlook of the cotton and textile industries, both of which were affected in FY23. Global economic slowdown and contractionary economic policies led to a decrease in demand for textile products and, consequently, cotton yarn.

While the global outlook for cotton production is expected to rebound, local challenges persist. These challenges include high interest rates, increasing energy costs, and difficulties with obtaining letters of credit (LCs). These factors are likely to result in continued sluggish performance for the spinning sector in FY24.

**Topline decreased during FY23, due to significant decline in volumes. Client concentration risk continues to remain high.**

After achieving a historic high of Rs.5.2b in sales revenue in FY22, the company experienced a decline of 20% in FY23, amounting to Rs. 4.2b in FY23. This decrease was mainly due to a reduction in demand. Consequently, sales volumes fell to 118,035 bags in FY23, down from 181,497 bags in FY22. However, the average selling price saw an increase of 23% during the year. Looking ahead, with the expected improvement in Pakistan's textile export volumes, management remains optimistic about achieving growth in net sales for FY24.

Almost all of the revenue is generated through local sale of yarn while a small portion is attained through sale of wastages. In FY23, proportion of total sales attained from the top 10 customers remained high at ~62% (FY22: 64%, FY21: 60%). However, in order to mitigate client concentration risk, the company has developed long-term relationship with customers over the years.

**Gross margins inched up slightly. Higher financial charges resulted in contraction of bottom-line.**

Gross margins improved modestly from 7.8% in FY22 to 8.8% in FY23. During this period, there was a notable shift in the company's cotton sourcing strategy, with a greater reliance on imported cotton. This shifted the ratio of imported to local cotton to 60:40 which historically stood at 40:60. On the cost front admin and other operating expenses remained intact. However, financial charges more than doubled due to greater utilization of short-term debt in a high-interest-rate environment within the country during FY23. As a consequence, bottom-line contracted significantly amounting to Rs. 7.2m in FY23 (FY22: 159.4m) and net margins shrank to 0.2% (FY22: 3.1%).

**Declining cash flows led to a weakening in debt coverage metrics; elevated cash conversion cycle indicate room for improvement in liquidity.**

Funds from operations (FFO) declined over the review period, aligning with the decrease in net profitability. FFO to total debt ratio dropped to 0.08x (FY22: 0.25x) and FFO to long-term debt decreased to 0.28x (FY22: 0.57x). Similarly, debt service coverage ratio (DSCR) declined to 0.88x (FY22: 2.94x).

Both the current ratio and coverage of short-term borrowings in relation to trade debts and inventory have also declined over time, yet both metrics remain satisfactory at above 1.1x. The cash conversion cycle (CCC) for FY23 increased to 63 days, largely due to a significant inventory pileup.

**Equity growth remained subdued, gearing and leverage ratios increased in FY23.**
Equity base (excluding revaluation surplus) experienced a nominal increase on a timeline basis amounting to Rs, 1.10b as at Jun'23 (Jun'22: 1.06b). A subordinated loan has been provided by the directors and associates of directors amounting to Rs. 159.6m against the facilities obtained from various financial institution. The rise in short-term borrowings during FY23 was due to higher working capital requirement. Consequently, gearing ratio inched up to 1.25x (Jun'22: 0.93x) and leverage ratio increased to 2.04x (Jun'22: 1.39x) as at Jun'23.

## Siara Textile Mills (Pvt.) Limited — Appendix I

| BALANCE SHEET (PKR Millions) | Jun'22 | Jun'23 | Dec'23 |
|---|---|---|---|
| Property, Plant & Equipment | 1,560.8 | 1553.4 | 1,516.4 |
| Store, Spares and Loose Tools | 33.2 | 40.4 | 37.6 |
| Stock-in-Trade | 550.2 | 1008.9 | 1,845.3 |
| Trade Debts | 236.1 | 280.8 | 532.4 |
| Advances, Deposits & Prepayments | 204.8 | 293.1 | 22.1 |
| Balances with Statutory Authorities | 117.6 | 294.4 | 513.0 |
| Cash & Bank Balances | 50.6 | 46.2 | 185.0 |
| Long Term Deposits | 34.0 | 40.7 | 41.5 |
| **Total Assets** | **2,787.2** | **3557.8** | **4,693.2** |
| Trade and Other Payables | 224.7 | 560.1 | 1,144.0 |
| Deferred Liabilities | 157.5 | 139.3 | 142.2 |
| Long Term Debt *(including current maturity)* | 434.5 | 379.0 | 341.13 |
| Short Term Debt | 559.4 | 1000.2 | 1,570.3 |
| **Total Debt** | **993.9** | **1,379.2** | **1,911.4** |
| **Total Liabilities** | **1,486.6** | **2,240.9** | **3,368.8** |
| **Tier-1 Equity** | **1,067.2** | **1,100.2** | **1,115.3** |
| Total Equity *(including revaluation surplus)* | 1,300.6 | 1,316.9 | 1,324.4 |
| Paid-up Capital | 300.0 | 300.0 | 300.0 |
| | | | |
| **INCOME STATEMENT** | **FY22** | **FY23** | **1HFY24** |
| Net Sales | 5,169.9 | 4155.1 | 3,398 |
| Gross Profit | 402.7 | 364.5 | 247.5 |
| Profit Before Tax | 228.4 | 59.6 | 50.1 |
| Profit After Tax | 159.4 | 7.2 | 7.5 |
| Funds from Operations | 246.5 | 107.5 | 83.6 |
| | | | |
| **RATIO ANALYSIS** | **FY22** | **FY23** | **1HFY24** |
| Gross Margin (%) | 7.8 | 8.8 | 7.3 |
| Net Margins (%) | 3.1 | 0.2 | 0.2 |
| Current Ratio (x) | 1.34 | 1.14 | 1.07 |
| FFO to Total Debt (x) | 0.25 | 0.08 | 0.04 |
| FFO to Long Term Debt (x) | 0.57 | 0.28 | 0.25 |
| Debt Leverage (x) | 1.39 | 2.04 | 3.02 |
| Gearing (x) | 0.93 | 1.25 | 1.71 |
| DSCR (x) | 2.94 | 0.88 | 0.96 |
| ROAA (%) | 6.6 | 0.2 | 0.2 |
| ROAE (%) | 16.4 | 0.7 | 0.7 |
| (Stock in Trade+ Trade Debt) to Short-Term Borrowing Ratio (x) | 1.41 | 1.29 | 1.51 |

## REGULATORY DISCLOSURES — Appendix II

| | |
|---|---|
| **Name of Rated Entity** | Siara Textile Mills (Pvt.) Limited |
| **Sector** | Textile |
| **Type of Relationship** | Solicited |
| **Purpose of Rating** | Entity Ratings |

**Rating History**

| Rating Date | Medium to Long Term | Short Term | Rating Outlook | Rating Action |
|---|---|---|---|---|
| 27/02/2024 | BBB | A-2 | Stable | Reaffirmed |
| 10/11/2022 | 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. |
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**Due Diligence Meeting Conducted**

| Name | Designation | Date |
|---|---|---|
| **Mr. Muhammad Anwar** | Finance Manager | December 21, 2023 |
| **Mr. Saleem Akhtar** | Director | |