RATING REPORT

Shafi Lifestyle (Pvt.) Ltd

REPORT DATE:

31 January 2022

RATING ANALYSTS:

Sara Ahmed
sara.ahmed@vis.com.pk

Muzammil Noor Sultan
muzammil.noor@vis.com.pk

RATING DETAILS		
Rating Category	**Latest Rating**	**Previous Rating**
Entity	**BBB+/A-2**	**BBB+/A-2**
Rating Date	*January 31,'22*	*August 26,'20*
Rating Outlook	Positive	Stable

COMPANY INFORMATION	
Incorporated in 2009	**External auditors:** RSM Avais Hyder Liaquat Nauman
Private Limited Company	**Chairman of the Board:** Muhammad Haleem
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Muhammad Naseem
Shafi Glucochem Pvt Ltd – 45.4%	
Amjad Hafeez – 12.2%	
Muhammad Naseem – 11.1%	
Tahir Hanif – 7.2%	
Muhammad Haleem Sheikh – 6.5%	

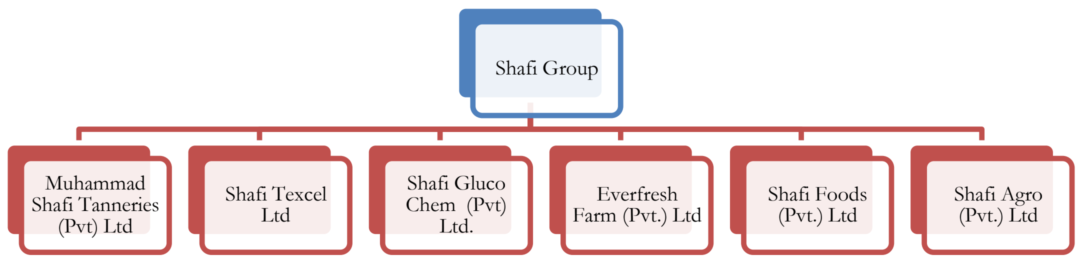
APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Corporates (August, 2021) https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Shafi Lifestyle (Private) Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

SLPL was incorporated in 2009, the company was previously known as 'Aisha Sons' partnership firm. The company was later on renamed and was converted into a private limited company.

Shafi Lifestyle (Pvt.) Limited (SLPL) is part of Shafi Group. The group has presence in textile, leather, food and footwear industries. The company is principally engaged in manufacturing and sale of leather footwear. The company's regional office is based in Karachi where as the factory is located in Lahore, Punjab. The Company relies on grid-based electricity for its power requirements.



Leather footwear exports exhibit growing trend

Export volumes of Pakistan's leather footwear exhibit steady growth, barring FY20 on account of COVID-19 led disruption. The growth has been led by higher demand and diversion of orders to Pakistan on account of slowdown in business operations within regional competitors like Bangladesh, Cambodia and Vietnam due to environmental concerns. Hence, the shifting of global customer base from competing nations to Pakistan provides an opportunity for this sector to grow further. The footwear industry of Pakistan comprises of 7 to 8 major players, one of them having exclusive dominance in terms of market share. For leather part, availability of required labor and raw materials on competitive rates from both local and foreign suppliers exhibits positive outlook for leather manufacturers in Pakistan. This is further supported by and HFY22 export figures which depict an increase in Pakistan footwear exports of 12.4%.

	FY19	FY20	FY21
Leather footwear(USD mn)	106.4	107.2	108.4
Quantity(000 Pairs)	7,008	6,587	8,034

Capacity expansion continues

SLPL's production capacity has more than doubled over last 5 years, as a result of capacity additions. Total production capacity increased to 660,000 pairs at end-FY21 (FY20: 525k pairs). Alongside capacity enhancement, the company undertook capex of Rs. 238m to build production hall facility to complement enhanced production as well as an office building. The company aims to increase the capacity up to 750,000 pairs by end-FY22. All the CAPEX financing to purchase imported machinery is being financed through an ILTFF facility.

		FY17	FY18	FY19	FY20	FY21
Installed Capacity	Pairs	300,000.0	456,000.0	456,000.0	525,000.0	660,000
Actual Production	Pairs	282,459.0	440,101.0	443,922.0	520,768.0	593,876
Capacity Utilization		94.2%	96.5%	97.4%	99.2%	90%

The company's product portfolio is focused towards high-end fashion segment and primarily consists of women's footwear (75%) coupled with a small range for men's shoes. Product portfolio includes women's ankle boots, ballerina shoes, coat shoes, long boot, saddle shoes and wedge shoes. Higher leather quantity and embellishments through accessories on ladies' shoes fetches higher prices from customers and therefore is expected to remain the main focus in the product mix, going forward. The raw material is procured from local as well as overseas suppliers on approximately 50/50 basis.

Profitability underpinned by higher sales and increasing margins

During FY21 sales revenue exhibited an increase of 33.5%, primarily contributed by export sales. Growth in topline was largely a function of higher volumetric sales in the international market with 12-13% increase in average selling prices due to currency devaluation. The share of local sales in total revenue has fallen from 55% in FY17 to 0.2% in FY21. The company aims to maintain its focus on exports, owing to higher margins and stable demand. Germany and Holland remain top export markets while the company initiated tapping the USA market in FY21. The Company looks forward to diversify its clientele further. As per management, Australia is considered a high-potential market but stringent lockdowns has been an impediment. Client concentration of SLPL is on the higher side, although it has improved over the years.

Improvement in gross margins from 31.4% in FY20 to 34.4% in FY21 was brought about by enhanced cost control and economies of scale obtained with higher production. The Company has also reaped benefit from local currency devaluation. Shipment costs have increased globally; however, since most of SLPL's business is based on FOB, the impact has been muted for the Company.

Higher volume sales and improved margins led to higher profitability Rs. 349.2m in FY21 (FY20: Rs. 231.6m). Going forward, management expects enhanced capacity to be full y utilized on account of adequate orders in pipeline while gross margins are projected to sustain around existing levels.

Liquidity profile remains satisfactory due to healthy cash flow generation and strong debt servicing ability.

Higher profitability in FY21 translated into increased Funds From Operations (FFO) (FY21: Rs. 414.8m, FY20: Rs: 265.5m). Consequently, debt servicing coverage stood strong at 17.15x (FY20: 12.81x) in FY21 coupled with small quantum of long term debt on the balance sheet. Aging of receivables is satisfactory. The current ratio remains adequate. Inventory and trade debt provide adequate coverage for short term borrowing.

Sound capitalization indicators

Total equity, excluding the revaluation surplus, increased to Rs. 924m (FY20: Rs. 578.2m), as a result of retained profits. Debt levels increased in FY21, primarily manifested in short term borrowings (FY21: Rs. 425m; FY20: Rs. 8m) to meet working capital requirements. Previously, the Company has been funding working capital through Rs 340m associate loan which was paid off in FY21. The Company subsequently mobilized concessionary financing facilities for working capital and acquisition of plant and machinery. Increased debt levels as a result pushed up the gearing level to 0.6x (FY20: 0.1x), albeit remaining low. Given the healthy internal capital generation along with moderate capex plans, leverage indicators are expected to remain on the lower side over the rating horizon.

Corporate governance and control framework is considered adequate

The Company has a formal board structure which primarily includes family members. The Company has established an in-house internal audit function. A fully integrated ERP platform is in implementation phase and will be completed by Jun'22. The Company has two backup sites, one on-site and the other at the Head office in Karachi.

Financial Summary (Rs. in m)				
Balance Sheet	**FY18**	**FY19**	**FY20**	**FY21**
PPE	277.9	289.6	395.4	739.2
Stock-in-Trade	175.2	219.6	276.0	351.9
Trade Debts	143.3	281.2	372.3	603.1
Total Assets	814.5	1,034.7	1,463.8	2,227.9
Trade and Other Payables	174.0	202.6	350.6	465.5
Long Term Debt	22.0	13.6	72.8	128.7
Short Term Debt	-	-	8.0	425.0
Total Debt	22.0	13.6	80.8	553.7
Paid Up Capital	374.3	374.3	597.5	597.5
Equity-(excl surplus reval)	101.4	346.2	578.2	924.0
Income Statement				
Net Revenue	717.1	1,094.9	1,531.0	2,043.7
Gross Profit	112.0	285.9	481.5	703.4
Profit Before Tax	(4.3)	101.2	246.9	373.6
Profit After Tax	(13.0)	92.3	231.7	349.2
Ratio Analysis				
Gross Margin (%)	15.6%	26.1%	31.4%	34.4%
Net Margin (%)	-1.8%	8.4%	15.1%	17.1%
FFO	15.4	96.5	265.5	414.8
FFO to Total Debt (%)	69.7%	707.9%	328.6%	74.9%
Debt Servicing Coverage Ratio (%)	1.75	6.63	12.81	17.15
Gearing (x)	0.22	0.04	0.14	0.60
Leverage (x)	6.10	1.72	1.37	1.14
Current Ratio (x)	0.88	1.23	1.42	1.51
STD Coverage (%)	-	-	8104.3%	224.7%
ROAA (%)	-2.0%	10.0%	18.5%	18.9%
ROAE (%)	-12.0%	41.2%	50.1%	46.5%

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

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	Shafi Lifestyle (Private) Limited				
Sector	Leather Footwear				
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				
	31/01/22	BBB+	A-2	Positive	Maintained
	26/08/20	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.				
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Copyright 2022 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.				
Due Diligence Meetings Conducted		Name	Designation	Date	
	1	Mr. Mustafa Hafeez	Executive Director – Finance	13/01/22	
	2	Mr. Mazhar Iqbal	Manager Accounts	13/01/22	