RATING REPORT

Al-Razzaq Fibres (Private) Limited

REPORT DATE:
June 21, 2022

RATING ANALYST:

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RATING DETAILS		
	Initial Rating	
Rating Category	Long-term	Short-term
Entity	A-	A-2
Rating Date	*June 21, 2022*	
Rating Action	Initial	
Rating Outlook	Stable	

COMPANY INFORMATION	
Incorporated in 2013	**External auditors:** M. Saleem Associates
Private Limited Company	**Chief Executive Officer (CEO):** Mr. Mustafa Saya
	Chairperson: Mr. Muhammad Yasin Saya

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria *Industrial Corporates (August 2021)*
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Al-Razzaq Fibres (Private) Limited

OVERVIEW OF THE INSTITUTION

Al-Razzaq Fibres (Private) Limited was incorporated in 2013 as a private limited company and registered under the repealed Companies Ordinance, 1984 (Companies Act, 2017). The Company's manufacturing facility is located in Nooriabad Industrial Area, Sindh, and the registered office is situated in P.E.C.H.S., Karachi.

RATING RATIONALE

Corporate Profile: Incorporated in 2013 as a private limited concern; Al-Razzaq Fibres (Private) Limited was established as a weaving company producing griege fabric. The Company launched its own retail brand later in 2017 with the name of "SAYA". Weaving capacity is sufficient to cater the requirements of retail brand. Furthermore, dyeing, finishing, and embroidery functions are outsourced from third parties, and cut-to-pack services are performed in-house. Therefore, sales are primarily local (including indirect exports) while a minor proportion is exported depending on market opportunities.

The first retail shop of Saya was opened in 2018 at Lucky One Mall, Karachi, and the Company has twenty-eight retail shops till date.

Rating Drivers

Healthy growth in sales which continues in the ongoing year

Sales revenue of the Company depict strong year on year growth, recording a 34% growth led by surge in volumetric fabric sales as well as unit prices. Sales mix is focused on local fabric sales, although management has plans to increase exports going forward. Client concentration is relatively on the higher side with top ten clients constituting 46% (FY20: 54%) of the total sales in FY21. Procurement strategy of the Company depicts dependence on imported yarn relative to local on a timeline basis due to better rates and availability issues. In the ongoing year, sales growth momentum continues.

Margins depict a declining trend on a timeline basis

Gross margins of the Company depict a declining trend on a timeline basis. In FY21, the same declined to 9.3% (FY20: 11.6%) owing to increase in yarn prices. While gross margins have shown recovery in H1'FY22, and stands at 15.7%, we expect margins to streamline by year end to existing levels, which remain relatively lower than the peers. Selling and administrative expenses witnessed ~6% increase. Consequently, operating margins were recorded lower at 5.1% (FY20: 6.3%) during the outgoing year. Finance costs surged significantly due to adoption of IFRS 16 which impacted the net margins reducing them to 3.0% (FY21: 4.4%). Going forward, the Company expects to maintain margins at similar levels with sales growth in tandem with industry growth.

Focus remains on increasing backward integration, efficiency and capacity

The Company is undergoing capacity addition initiatives on a timeline basis, whereby capacity was increased by 2.5m meters per annum (FY20: 1.02m meters) in FY21 financed through a combination of internal cash generation and director's loan. Furthermore, the Company is planning to establish a spinning unit incorporating 50,000 spindles which is expected to come online in FY23. As per management, spinning unit will be funded through a mix of internal cash generation and sponsor support, if needed.

Liquidity profile is supported by adequate cash flows and sound debt servicing ability.

Funds from Operations (FFO) increased by 57.93% (FY20: 42.51%) in FY21 on account of higher profitability. Cash flow coverage indicators of the Company are strong with FFO to Total Debt and FFO to Long term debt standing at 68% (FY20: 105%) and 119% (FY20: NA) respectively in FY21. Debt servicing is also sound.

Liquidity profile is adequate with current ratio standing at 1.15x (FY20: 1.32x) in FY21. Working capital management strategy of the Company primarily entails alterations in receivable days and payable days outstanding with minimal dependence on short term borrowings; and depicts improvement in FY21 with cash conversion cycle decreasing to 96 days (FY20: 107 days) on account of increase in days payable outstanding. Ageing of trade debts remains manageable during the outgoing year with 2% of the credit sales outstanding since more than 180 days.

Sound capitalization indicators

Post adjustment of surplus on revaluation, equity base of the Company increased by 9% (FY20: 11%) in FY21 on the back of profit retention. Debt profile encapsulates lease undertaken for rented retail outlets in accordance with implementation of IFRS 16, related party loans, and minimal short-term borrowings for working capital management. However, the Company has exposure to non-funded lines to finance Letter of Credits (LCs) opened for raw material, machinery and spinning project. With no interest bearing obligations, capitalization indicators are low with gearing and leverage levels standing at 0.46x (FY20: 0.21x) and 1.61x (FY20: 1.14x) respectively in FY21. Adjusted gearing after excluding related party loans stands at 0.2x. Going forward, while management envisages internal cash flows to be sufficient to meet the capex requirements, we expect that over the rating horizon, there may be some pressure on gearing. Moreover, with the spinning capacity coming online, working capital requirements will also increase. Ratings, however, remain dependent upon maintenance of low capitalization indicators going forward.

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix I

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 II
Name of Rated Entity	Al-Razzaq Fibres (Private) Limited				
Sector	Textiles				
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				
	June 21, 2022	A-	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 Meetings Conducted		**Name**	**Designation**	**Date**	
	1	Mr. Faheem Anwar	Chief Accountant	2nd -Feb-2022	