

RATING REPORT

Syntronics Limited (SL)

REPORT DATE:

December 16, 2019

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Indicative Initial Ratings	
	Long-term	Short-term
Entity	BBB+	A-2
Rating Outlook	Stable	
Rating Date	10 Dec '19	

COMPANY INFORMATION

Incorporated in 1998	External auditors: M/S Shinewing Hameed Chaudhri & Co. Chartered Accountants
Public Limited Company (Unlisted)	Chairman of the Board: Mr. Abbas Sarfaraz Khan
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Abbas Sarfaraz Khan
M/S Gran Via Global Limited	34.27%
Mr. Iskander M. Khan	25.00%
Mr. Abbas Sarfaraz Khan	24.70%
M/S Premier Board Mills Limited	11.02%
Mr. Baber Ali Khan	5.00%

APPLICABLE METHODOLOGY

VIS Entity Rating Criteria: Corporates (May 2019)

<https://www.vis.com.pk/kc-meth.aspx>

Syntronics Limited (SL)

OVERVIEW OF THE INSTITUTION	RATING RATIONALE																																												
<p>Syntronics Limited is involved in the manufacturing of Ad*Star® Polypropylene Laminated Bottom Block Sacks mainly for cement packaging. The company commenced operations in 1998 as Public Limited Company (Unlisted). Registered office of the company is in Islamabad while manufacturing unit is located in Hattar, KPK.</p> <p>Profile of Chairman & Chief Executive Officer</p> <p>Mr. Abbas Sarfaraz Khan is the Chairman of board and Chief Executive Officer of Syntronics Limited. He is also the Chairman of Chashma Sugar Mills Limited and is also CEO of Premier Sugar Mills & Distillery Co. Limited and Arpak International Investment Limited. He also serves as director in other associated companies.</p>	<p>Syntronics Limited (SL) is primarily involved in the manufacturing of Ad*Star® Polypropylene Laminated Bottom Block Sacks which is used as packaging material mainly in cement industry. The company also manufactures polypropylene bags used in other industries like sugar, feed, flour, fertilizer etc. Presently, the company is operating four units with production capacity to produce 264 million bags per annum. Ad*Star® Polypropylene Sacks provide various benefits over traditional Kraft Paper Bags like better resistance against water, humidity & moisture, high tensile strength, zero bursting to withstand tough handling during transportation. Additionally, it provides more tear resistance due to its woven structure & lamination and is also more cost effective as compared to Kraft Paper bags.</p> <p>According to the management, the company has 25% share in the cement bags market and around 8% market share in the other sectors (sugar, feed, flour, fertilizer etc.). The other major competitors are Lahore Poly-Propylene Industries (Pvt.) Limited, Cherat Packaging Limited, Nova Synpac (Pvt.) Limited, Khyber Packaging Limited, etc. The company has installed machinery from various countries including Austria, USA, Japan, etc. Main raw material of the company is Polypropylene which is mainly procured from international market. The cumulative power requirement of the unit is 4.95 MW which is met primarily through WAPDA connection. The company also has backup arrangement in the form of 4.95 MW diesel generators.</p> <p>Ownership of the company is mainly vested with the sponsoring family</p> <p>The ownership of SL is vested with the sponsoring family which holds virtually 100% shares in the company. There are seven directors in the company, details of shareholding is given below:</p> <table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="text-align: center;">Shareholders Name</th> <th style="text-align: center;">Relationship</th> <th style="text-align: center;">No of Share Held</th> <th style="text-align: center;">Shareholding %</th> </tr> </thead> <tbody> <tr> <td>Mr. Abdul Qadar Khattak (Employee)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">500</td> <td style="text-align: center;">0.00%</td> </tr> <tr> <td>M/S. Gran Via Global Limited</td> <td style="text-align: center;">Group Company</td> <td style="text-align: center;">10,801,250</td> <td style="text-align: center;">34.27%</td> </tr> <tr> <td>Mr. Abbas Sarfaraz Khan (Self)</td> <td style="text-align: center;">CEO</td> <td style="text-align: center;">7,787,246</td> <td style="text-align: center;">24.70%</td> </tr> <tr> <td>Mr. Babar Ali Khan (Cousin)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">1,576,000</td> <td style="text-align: center;">5.00%</td> </tr> <tr> <td>Mr. Iskander M. Khan (Cousin)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">7,879,874</td> <td style="text-align: center;">25.00%</td> </tr> <tr> <td>Mr. Aziz Sarfaraz Khan (Father)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">500</td> <td style="text-align: center;">0.00%</td> </tr> <tr> <td>Begm Laila Sarfaraz (Mother)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">500</td> <td style="text-align: center;">0.00%</td> </tr> <tr> <td>M/S Premier Board Mills Limited</td> <td style="text-align: center;">Group Company</td> <td style="text-align: center;">3,474,880</td> <td style="text-align: center;">11.02%</td> </tr> <tr> <td>Ms. Najda Sarfaraz (Sister)</td> <td style="text-align: center;">Director</td> <td style="text-align: center;">500</td> <td style="text-align: center;">0.00%</td> </tr> <tr> <td>Total</td> <td style="text-align: center;">-</td> <td style="text-align: center;">31,521,250</td> <td style="text-align: center;">100%</td> </tr> </tbody> </table> <p>M/S. Gran via Global Limited is wholly owned by Mr. Abbas Sarfaraz Khan while he, along with with his father, M. Aziz Sarfaraz Khan, holds 57% share of Premier Board Mills Limited. Companies of Premier Group are as follows:</p> <ol style="list-style-type: none"> i. M/S. Arpak International Investment Limited ii. M/S. The Premier Sugar Mills & Distillery Co. Limited iii. M/S. Azlak Enerprises (Pvt.) Limited iv. M/S. The Frontier Sugar Mills & Distillery Co. Limited v. M/S. Chashma Sugar Mills Limited vi. M/S. Premier Board Mills Limited vii. M/S. Premier Construction & Housing Limited viii. M/S. Philipson & Co. (Pvt.) Limited ix. M/S. Syntron Limited x. M/S. Gran Via Global Limited 	Shareholders Name	Relationship	No of Share Held	Shareholding %	Mr. Abdul Qadar Khattak (Employee)	Director	500	0.00%	M/S. Gran Via Global Limited	Group Company	10,801,250	34.27%	Mr. Abbas Sarfaraz Khan (Self)	CEO	7,787,246	24.70%	Mr. Babar Ali Khan (Cousin)	Director	1,576,000	5.00%	Mr. Iskander M. Khan (Cousin)	Director	7,879,874	25.00%	Mr. Aziz Sarfaraz Khan (Father)	Director	500	0.00%	Begm Laila Sarfaraz (Mother)	Director	500	0.00%	M/S Premier Board Mills Limited	Group Company	3,474,880	11.02%	Ms. Najda Sarfaraz (Sister)	Director	500	0.00%	Total	-	31,521,250	100%
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Product Portfolio – Primarily focused on Polypropylene Laminated Bottom Block Sacks for Cement Industry

Sales of cement sacks are demand driven as company manufactures sacks based on orders from cement manufacturers. Since demand of cement sector in north region decreased during FY19 due to downturn in real estate sector and development projects, the company has enhanced its focus on other sectors especially flour, while capacity utilization has decreased on a timeline basis. Find below details of capacity utilization during the last three years:

	FY17	FY18	FY19
Installed Capacity (million bags)	264.0	264.0	264.0
Actual Production (million bags)	144.3	143.5	131.0
Capacity Utilization %	54.6%	54.3%	49.6%

Sales growth emanating from price increase

During FY19, the company reported net sales of Rs. 2.55b (FY18: Rs. 2.32b; FY17: Rs. 2.27b) driven largely by favorable average selling prices of sacks & stitched bags in the local market. The average selling price of sacks increased to Rs. 26.5 per bag (FY18: Rs. 19.5 per bag) during FY19 while average price of stitched bags increased to Rs. 16.2 per bag (FY18: Rs. 14.9 per bag). The price of sacks/bags are also dependent on weight of sacks/bags, higher the weight higher the price. The company was able to sell 69.0 million cement sacks during FY19 (FY18: 93.1 million) while stitched bags quantity increased to 45.9 million (FY18: 34.6 million). The company is contemplating sales increase to cement sector going forward as there is a possibility of ban on kraft paper bags in cement sector. The price of kraft paper bags is higher (around Rs. 8/bag) than PP bags. The company has also started production of biodegradable bags for shopping due to ban on plastic shopping bags which may also provide additional revenue, going forward. Top 10 customers generated sales of 60.4% (FY18: 63.4%, FY17: 67.8%) during FY19 which is high, though decreasing on timeline basis. Find below the percentage sales of each sector during the last three years:

Sector	2017	2018	2019
Cement	82%	79%	72%
Flour	3%	9%	25%
Fertilizer	1%	1%	-
Sugar	4%	6%	-
Misc.	8%	4%	3%
Total	100%	100%	100%

The gross margins of the company improved to 14.8% (FY18: 7.6%; FY17: 9.5%) during FY19 mainly on account of price increase during the year. Operating expenses of the company increased to Rs. 142m (FY18: Rs. 106m; FY17: Rs. 117m) mainly on account of higher exchange loss of Rs. 28.6m (FY18: Rs. 6.8m). The company books dollar rate on LC opening and when LC is retried, the difference between these rates is either exchange gain or loss. As dollar was appreciating against Pak rupees during FY19, hence company recorded higher exchange loss. The finance cost of the company increased to Rs. 157m (FY18: Rs. 111m, FY17: Rs. 77m) mainly on account of higher interest rates during FY19. The company was able to generate net profit of Rs. 100m (FY18: Rs. 54m loss) during FY19 while net profit margin improved to 3.9% (FY18: -2.3%; FY17: 2.8%).

Trade debts increased owing to relatively relaxed payment terms

Given no major capex, the non-current assets of the company decreased to Rs. 1.23b (FY18: Rs. 1.35b, FY17: Rs. 1.43b) by end-FY19. Long term investment in associated company “Chashma Sugar Mills Limited” increased to Rs. 769m (FY18: Rs. 526m, FY17: Rs. 521m) by end-FY19 on account of post-acquisition profit and other comprehensive income brought forward, share of profit, and share of revaluation reserve on PPE while equity investment remained at 12.51% (3.59 million shares). At end-FY19, SL held total inventory worth Rs. 536m (FY18: Rs. 574m; FY17: Rs. 461m)

which mainly comprises raw material and work in process of Rs. 331m (FY18: Rs. 369m) and Rs. 155m (FY18: Rs. 163m), respectively. Trade receivables increased to Rs. 592m (FY18: Rs. 502m, FY17: Rs. 343m) by end-FY19 with higher receivable days of 85 days (FY18: 79 days, FY17: 55 days). The company has relaxed payment terms to major cement manufacturers due to slowdown in cement sector of the northern region. Around 87% of these receivables are not due yet or 1-3 months overdue. Amount due over one year amounted to Rs. 5.4m. Tax refunds from government stood at Rs. 644m (FY18: Rs. 671m, FY17: Rs. 630m) at end-FY19 which includes income tax refundable / tax deducted at source of Rs. 557m (FY18: Rs. 527m, FY17: Rs. 428m). Cash & bank balances stood at Rs. 84m at FY19-end (FY18: 79m, FY17: Rs. 223m).

Improving coverages and liquidity indicators

Funds from operations (FFO) improved to Rs. 172m (FY18: Rs. 48m; FY17: Rs. -2m) in line with positive bottom line during FY19. In order to meet working capital requirements, the company mobilized short term borrowings amounting Rs. 1.05b at end-FY19 (FY18: Rs. 1.18b; FY17: Rs. 912m). FFO to total debt improved to 14.6% (FY18: 3.2%; FY17: -0.19%) while FFO to long-term debt stood higher at 145.9% (FY18: 16.2%; FY17: -0.91%). The debt service coverage ratio, remained below 1, though somewhat improved to 0.97x (FY18: 0.38x; FY17: 0.26x) during FY19. The current ratio remained stable at 1.21x (FY18: 1.14x; FY17: 1.14x). Additionally, inventory plus trade receivables to short-term borrowings improved to 1.07x (FY18: 0.91x; FY17: 0.88x) by end-FY19.

Manageable leverage indicators amid relatively small equity base

Equity base increased to Rs. 1.62b (FY18: Rs. 1.49b; FY17: Rs. 1.53b) by end-FY19 on the back of profit retention. During FY19, the company did not carry out any major capital expenditure while company repaid long term loan of Rs. 180m (FY18: Rs. 281m, FY17: Rs. 222m) due to which long term finance facility decreased to Rs. 118m (FY18: Rs. 296m, FY17: Rs. 237m). Given the decrease in total borrowings to Rs. 1.17b (FY18: Rs. 1.48b, FY17: Rs. 1.15b) by end-FY19, debt leverage stood lower at 1.18x (FY18: 1.39x, FY17: 1.26x) while gearing also decreased to 0.73x (FY18: 0.99x, FY17: 1.26x). Given low capacity utilization, no major capex projected in the foreseeable future. Leverage indicators are, therefore, expected to remain within manageable levels.

Governance & Audit

The Board of Directors comprises seven members, out of which six members are from sponsoring family whereas board meetings were held three times during FY19. The company has deputed "Shinewing Hameed Chaudhri & Co. Chartered Accountants" as external auditors of the company which is QCR rated company and have "B" rating on SBP Auditors panel. The company is utilizing "Cosmosoft SARP Enterprise Suite (version 6.2)" system for integrating different departments of the company.

Syntronics Limited
Appendix I

FINANCIAL SUMMARY		<i>(Amounts in PKR millions)</i>		
BALANCE SHEET	30-Jun-17	30-Jun-18	30-Jun-19	
Non-Current Assets	1,430	1,356	1,234	
Long Term Investment	521	526	769	
Stock in Trade	461	574	536	
Trade Debts	343	502	592	
Tax Refund from Government	630	671	644	
Other Assets	164	167	150	
Cash & Bank Balances	223	79	84	
Total Assets	3,772	3,875	4,009	
Trade and Other Payables	522	323	459	
Short Term Borrowings	912	1,185	1,057	
Long Term Loan	237	296	118	
Total Interest Bearing Debt	1,149	1,481	1,175	
Other Liabilities	244	271	280	
Total Liabilities	1,916	2,075	1,914	
Tier 1 Equity	1,525	1,490	1,620	
Total Equity	1,857	1,800	2,096	
Paid Up Capital	315	315	315	
INCOME STATEMENT	30-Jun-17	30-Jun-18	30-Jun-19	
Net Sales	2,271	2,322	2,556	
Gross Profit	215	176	379	
Operating Profit	133	87	289	
Finance Cost	77	111	157	
Profit before Tax	56	(24)	131	
Profit after Tax	64	(54)	100	
RATIO ANALYSIS	30-Jun-17	30-Jun-18	30-Jun-19	
Gross Margin (%)	9.5	7.6	14.8	
Net Margin (%)	2.8	(2.3)	3.9	
Current Ratio (x)	1.14	1.14	1.21	
Net Working Capital	225	240	347	
Debt Leverage (x)	1.26	1.39	1.18	
Gearing (x)	0.75	0.99	0.73	
FFO	(2)	48	172	
FFO to Total Debt (%)	(0.19)	3.2	14.6	
FFO to Long Term Debt (%)	(0.91)	16.2	145.9	
Debt Servicing Coverage Ratio (x)	0.26	0.38	0.97	
Inventory + Receivables/Short-term Borrowings (x)	0.88	0.91	1.07	
ROAA (%)	0.9	(0.7)	3.8	
ROAE (%)	2.1	(1.8)	7.7	

ISSUE/ISSUER RATING SCALE & DEFINITIONS

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	Syntronics Limited				
Sector	Paper & Packaging				
Type of Relationship	Initial				
Purpose of Rating	Entity Ratings				
Rating History	Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
	RATING TYPE: ENTITY				
	10/12/2019	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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