The Pakistan Credit Rating Agency Limited

Rating Report

Mount Fuji Textiles Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Apr-2023	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Mount Fuji Textile Limited ('Mount Fuji' or 'The Company') is a Public (unlisted) Limited Company, which is supported by its presence in the export-oriented value-added textile segment, significant control over quality maintenance, extensive sponsor experience, and three-decade operating track record in the textile business. The Company has sound internal control and IT framework; however, room for improvement exists in the governance structure given the private limited status of the company. The ratings of the Company incorporate the progressive growth over the years. While crossing the PKR 7bln mark in FY22, the topline registered a sizeable growth of 47% (FY21: 48%) primarily driven by an increase in fabric prices, while volumetric growth remained nominal. Sales mix represents a major contribution from the export market; FY22 majorly tilted towards exports at 86% of total revenue (FY21: 85%). The Company enjoys an established customer base with several export destinations in European Countries (56%), the United States of America (30%), and the United Kingdom (11%). The management is planning further penetration into the Australian market in the upcoming years. Overall client wise concentration risk in sales remains elevated. Profitability margins (on a both gross and net basis), following a decline in FY22, fell further in the ongoing year on the back of the current weak macroeconomic environment, all-time high inflation suppressing purchasing power of the masses, higher markup rates, unstable forex parity and depleting foreign exchange reserves will remain major challenges. The liquidity profile is underpinned by adequate cash flow coverages in relation to outstanding obligations. The ratings also incorporate a moderately leveraged capital structure supported by profit retention. During 7MFY23, the textile exports were valued at $10.08bln compared to $10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues.

The ratings are dependent on the management's ability to uphold the entity's growing performance trend. Meanwhile, maintaining strong margins and coverages to fulfill financial obligations will remain critical.

Disclosure

Name of Rated Entity	Mount Fuji Textiles Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Composite and Garments(Dec-22)
Rating Analysts	Iram Shahzadi | iram.shahzadi@pacra.com | +92-42-35869504

Profile

Legal Structure Mount Fuji Textile Limited ('Mount Fuji' or 'The Company') is a Public (unlisted) Limited Company. It was incorporated in Karachi, Pakistan on August 12, 1986.

Background Mount Fuji Textile Limited ('Mount Fuji' or 'The Company') was incorporated in Sindh, Pakistan as a Private Limited Company on August 12, 1986, under the Companies Ordinance, 1984 (Now the Companies Act, 2017) and was converted into a Public (unlisted) Limited Company with effect from May 07, 1992.

Operations The principal business of the Company is the manufacturing and export of garments and home textile products. The company has three units. The Company has five sectional warping machines of 1000 creels each with a warping capacity of approximately Two Million Meters a month. The Company has also a weaving facility of 138 Sulzer and 84 Airjet Looms with a weaving capacity of approximately 3.5mln Picks a day. The Company has 15 knitting machines, 2 raising machines, 846 computerized sewing machines & 19 cutting machines.

Ownership

Ownership Structure The ownership of the Company rests with the family of Mr. Ashraf including his sons. The major shareholding of the Company is owned by Mr. Ahmed Ashraf (28.57%), While the remaining is equally distributed between the sons of Mr. Ashraf.

Stability The Company was set up to engage and transfer over the technical and business skills of the first generation to the second generation of the Ashraf family. The Company encompasses the advice and expertise of first-generation the and leadership of the new generation. Although, no official succession plan has been announced to date.

Business Acumen The sponsors have vast experience and knowledge of various aspects of the textile value chain.

Financial Strength The sponsoring family has been involved in multiple businesses for more than 20 years. The family is involved in textile & garment manufacturing. This indicates sponsors' ability to provide support if the need arises.

Governance

Board Structure Mount Fuji's board comprises four members, including the Chairman - Mr. Ahmed Ashraf, and Chief Executive Officer (CEO) – Mr. Abdul Latif Ashraf. There are no independent directors on the board. The Company's board is dominated by sponsor-family members, raising concern about the lack of challenge posed to the management, thus hampering effective governance.

Members' Profile The members of the Board have relevant stature and extensive experience of around two decades in the textile industry. Currently, there are no independent directors on the board.

Board Effectiveness BoD meetings are held regularly in which discussion on various aspect is recorded in minutes and decision or action is referred to the CEO, Mr. Abdul Latif Ashraf.

Financial Transparency BDO Ebrahim & Co, Chartered Accountants, is the external auditor of the Company. The auditor has expressed an unqualified opinion on the financial reports for the year ending 30th June 2022. The auditors fall under category' A' of SBP's panel of auditors.

Management

Organizational Structure The organizational structure of the Company is divided into three main departments namely, i) Procurement, ii) Administration and IT, iii) Marketing and iv) Technical. All department reports to the executive director.

Management Team Mr. Abdul Latif Ashraf – CEO – holds a Master's degree and is in the Textile business for the last two decades. He is the Director of the Company since its incorporation in 1999. Hence, Mr. Muhammad Ashraf – the managing director – holds a Master's Degree from Karachi. He is in Textile Business for the last one and a half decades. He is Looking after all types of Procurement & Marketing. While Mr. Shehzad Ashraf – the executive director – holds a Master's Degree from the U.K. He is looking the Finance and Admin department. He is in Textile Business for the last five years.

Effectiveness The Company has no management committees. Sponsor's close involvement in day to day affairs of the business bodes well with the effectiveness of the Company.

MIS The Company has built an in-house ERP to cater to its business needs. The senior management monitors the business performance through certain Key MIS reports.

Control Environment Production is completely order driven, there is a rigorous quality check done on the end product by the QC department. The Company has obtained ISO 9001, ISO 14001, GSV, BICI, OEKO-TEX, WCA, Sedex, & & SQP certifications.

Business Risk

Industry Dynamics During 7MFY23, the textile exports were valued at $10.08bln compared to $10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand for yarn in international markets is also a challenge. The analysis of 5MFY23 reveals that among value-added items, bedwear has witnessed the largest decline of 19% (on an MoM basis), down to $217 million. Knitwear remained on the downward path in October 2022 and declined by 10% to $392 million. Among non-value-added items, cotton yarn has shown the largest decline of 35%. Moreover, a slowdown is prevailing in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. The demand pattern is expected to improve post-Jun-23.

Relative Position With 222 operational looms, Mount Fuji Textile Limited's standalone position in Pakistan's looms capacity is considered moderate.

Revenues During FY22, the Company's revenue grew by 47% to stand at PKR 7.1bln (FY21: PKR 4.8bln) primarily driven by an increase in fabric prices. The major portion of the revenue base is derived from exports. The cost of sales of the company is inclined due to the increase in the prices of fuel and energy. Same with the case for the Company's operating expenses, as they also inclined by 76% and stood at PKR 886mln (FY21: PKR 504mln). This scenario ultimately translated into an operating profit of PKR 245mln (FY21: PKR 385mln). Finance costs also increased driven by the incline in the key policy rate. After the incorporation of finance costs, the net profit for FY22 stood at PKR 198mln (FY21: 218mln). Furthermore, in 1HFY23, the topline stood at PKR 3.5bln. While the profitability was recorded at PKR 24mln.

Margins During FY22, the Company's cost of goods sold increased by 52% to PKR 5.9bln (FY21: PKR 3.9bln). Consequently, the gross profit margin reflected declined to 15.9% (FY21: 18.4%) and the operating profit margin to 3.4% (FY21: 8%). The management closely monitors overheads, translating into an improvement in 1HFY23. Gross margin stood at 17.5% and operating profit margin of 6.2%. Hence, the net profit margin clocked at 0.4%.

Sustainability Going forward, with better efficiency and a specialized product profile, the management expects the Company's margins to improve.

Financial Risk

Working Capital During FY22, the Company's net working capital days increased to 83 days (FY21: 78 days) due to an increase in inventory days (FY22: PKR 88 days, FY21: PKR 76 days) and receivables days (FY22: PKR 48 days, FY21: PKR 40 days). On the other hand, the Company's short-term trade leverage increased and stood at 6.7% in FY22 (FY21: -1.7%). In FY22, the current ratio of the Company is 2.5x (FY21: 3.8x).

Coverages FCFO of the Company during FY22 decreased to PKR 311mln (FY21: PKR 453mln) due to a decrease in EBITDA. Higher finance costs declined the interest coverage ratio to 2.8x in FY22 (FY21: 7.9x).

Capitalization During FY22, the Company's leveraging recorded an uptick to 51.9% (FY21: 49.3%). Short-term borrowings makeup up 67% of the total borrowings, increased to PKR 2,054mln in FY22 (FY21: 1,704mln) and the overall borrowings of the Company also reflected an upward trend and closed at PKR 3,063mln at the end of FY22 (FY21: PKR 2,514mln).

PACRA

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Mount Fuji Textiles Limited	Dec-22	Jun-22	Jun-21	Jun-20
Composite & Garments	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	4,120	3,993	3,204	2,805
2 Investments	339	112	150	324
3 Related Party Exposure	-	-	-	-
4 Current Assets	3,191	4,040	3,367	1,685
a Inventories	*1,534*	*2,118*	*1,318*	*684*
b Trade Receivables	*1,028*	*1,175*	*690*	*369*
5 Total Assets	7,650	8,145	6,721	4,814
6 Current Liabilities	932	1,609	895	365
a Trade Payables	*797*	*1,359*	*721*	*264*
7 Borrowings	3,044	3,063	2,514	1,514
8 Related Party Exposure	68	224	265	324
9 Non-Current Liabilities	-	207	194	68
10 Net Assets	3,606	3,041	2,853	2,543
11 Shareholders' Equity	3,606	3,041	2,853	2,543
B INCOME STATEMENT				
1 Sales	3,524	7,119	4,832	3,253
a Cost of Good Sold	*(2,909)*	*(5,987)*	*(3,944)*	*(2,711)*
2 Gross Profit	615	1,132	888	542
a Operating Expenses	(398)	(886)	(504)	(332)
3 Operating Profit	217	245	385	209
a Non Operating Income or (Expense)	*(61)*	*178*	*(42)*	*2*
4 Profit or (Loss) before Interest and Tax	156	424	343	211
a Total Finance Cost	*(91)*	*(130)*	*(71)*	*(55)*
b Taxation	*(41)*	*(96)*	*(54)*	*(35)*
6 Net Income Or (Loss)	24	198	218	121
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*190*	*311*	*453*	*309*
b Net Cash from Operating Activities before Working Capital Changes	*100*	*468*	*386*	*253*
c Changes in Working Capital	*72*	*43*	*(1,083)*	*(155)*
1 Net Cash provided by Operating Activities	171	511	(697)	99
2 Net Cash (Used in) or Available From Investing Activities	(137)	(995)	(281)	(532)
3 Net Cash (Used in) or Available From Financing Activities	(196)	522	2,248	1,290
4 Net Cash generated or (Used) during the period	(161)	38	1,270	856
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	-1.0%	47.3%	48.5%	0.0%
b Gross Profit Margin	17.5%	15.9%	18.4%	16.7%
c Net Profit Margin	0.7%	2.8%	4.5%	3.7%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	7.4%	5.0%	-13.0%	4.7%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	1.5%	6.7%	8.1%	4.8%
2 Working Capital Management				
a Gross Working Capital (Average Days)	152	136	116	118
b Net Working Capital (Average Days)	96	83	78	89
c Current Ratio (Current Assets / Current Liabilities)	3.4	2.5	3.8	4.6
3 Coverages				
a EBITDA / Finance Cost	3.5	3.4	8.5	7.6
b FCFO / Finance Cost+CMLTB+Excess STB	2.5	1.1	3.2	3.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	5.1	6.1	2.7	2.5
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	46.3%	51.9%	49.3%	42.0%
b Interest or Markup Payable (Days)	0.0	70.5	106.0	82.0
c Entity Average Borrowing Rate	4.8%	3.6%	2.5%	2.4%

Credit Rating

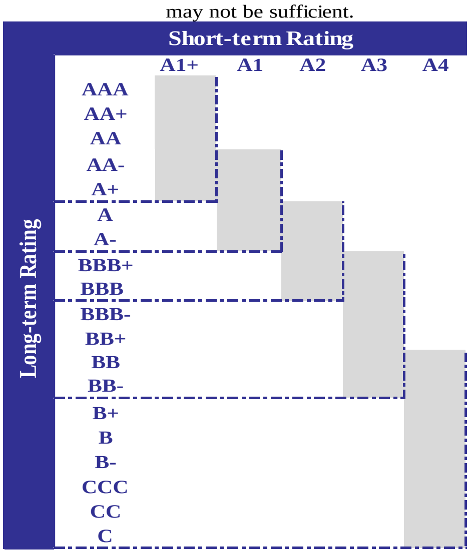
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**

i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)

ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)

iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)

(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)

(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)

(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).

(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)

(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)

(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity

(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers’ associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)

(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)

(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)

(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst’s area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)

(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)

(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)

Proprietary Information