The Pakistan Credit Rating Agency Limited

NISHAT MILLS LIMITED

RATING REPORT

	NEW [JUN-17]	PREVIOUS [SEP-16]
Entity		
Long Term	AA	AA
Short Term	A1+	A1+
Outlook	Stable	Stable

REPORT CONTENTS

JUNE 2017

Profile & Ownership

- NML, established in 1951, is the largest textile composite unit and a leading exporter of textile products in the country.
- The company is majority (~52%) owned by Mansha family members and group companies; flagship company of Nishat Group (NG).
- NG – a leading conglomerate – maintains substantial presence in the country’s financial sector, and strong foothold in textile, cement, and power sectors.
- Lately, the group has expanded its presence in the hospitality sector with the start of operations of Nishat Emporium mall. Also, partnering with local and international entities, the group has announced to enter Pakistan’s automobile assembly industry.

Governance & Management

- NML has a seven-member board of directors; two, including the CEO, represent sponsoring family, four are working for NG companies (including one NML executive), and one is an independent member.
- CEO, Mr. Umer Mansha associated with NML since 1994, carries extensive experience in textile industry. He is supported by an experienced team.

Operational Risk

- Sound operational infrastructure; mainly European technology
- Oracle-based ERP solution; comprehensive MIS reporting
- Captive power generation (~114MW) to meet energy requirements

Business Risk

- Sizeable revenue base; predominantly export oriented
- Sales mix dominated by Processing & Home textile (P&HT) segment (~45%), followed by weaving (~26%), spinning (~17%) and garment (~12%) segments.
- Moderately low geographic and top ten customer revenue concentration.
- During 9MFY17, the company’s topline increased slightly by ~3% YoY to ~PKR 37bln. However, a higher than proportionate increase in cost of sales resulting in a reduction in business margins; gross margin fell to 11.3% vs 13.6% SPLY, and operating margin fell to 4.1% from 6.8% SPLY. Dip in margins is primarily due to higher labour and energy cost, which are industry-wide phenomenon.
- Dividend income, comprising ~80% of the company’s bottomline, remained largely constant during the period (~PKR 2.5bln).
- A reduction (~18%) in interest expense owing to better financial management helped reduce the final impact on net profit which decreased by ~13% to report at PKR 3,089mln during 9MFY17.
- NML maintains a hefty investment portfolio – ~74% of equity at end-Mar17 – mainly comprising strategic holdings. With presence in diversified sectors, the company has prudently managed its overall risk profile.
- A new garment plant (capacity: 7.2mln pieces p.a.) became operational in Apr’16, which incurred a loss of ~PKR 258mln during 9MFY17. Additionally, the company is shifting one spinning unit to a special economic zone within the city; the process is expected to complete in Aug’17.

Financial Risk

- Working capital requirements, a function of its receivables and inventory, are met through a mix of internal generation and short term borrowings.
- Net cash cycle remained largely constant YoY.
- NML borrows short-term loans to provide working capital finance to subsidiary companies thereby creating short-term liquidity pressure.
- Strong debt service coverages backed by regular dividend inflows continue to augment the company’s financial risk profile.
- Low-leveraged capital structure (end-Mar17; ~19%); expected to remain range bound.

RATING RATIONALE

The ratings reflect the diversity of Nishat Mills' (NML) underlying businesses, along with a conservative capital structure. This emanates from its implicit holdco structure within Nishat Group (NG). This helps in managing the impact of adversities in any industry, particularly textile business, on the overall profile of NML. NML's significant as well as diverse strategic investment portfolio is generating a regular and growing dividend stream in addition to a potential of capital appreciation.

NML has an established business profile in textile industry. The company continues to maintain its position as a sizeable, export-oriented composite unit in the country's textile sector. NML has adequate diversification levels, in terms of both geography and customer base. The ongoing year has seen relatively subdued operational performance relative to last year on the back of industry-wide margin squeeze. The management intends to focus on enhancing existing facilities in order to achieve overall cost efficiencies.

KEY RATING DRIVERS

The ratings continue to depend on the management's ability to maintain its business profile while sustaining its market position. Sustenance of business margins at a reasonable level remains important. Moreover, a formal holding company structure to monitor a large investment portfolio would bring structural efficiencies with focused decision making.

Textile

The Pakistan Credit Rating Agency Limited — Financials (Summary)

PKR mln

Nishat Mills Limited

BALANCE SHEET	31-Mar-17	30-Jun-16	30-Jun-15	30-Jun-14
	9M	FY	FY	FY
Non-Current Assets	**26,226**	**24,877**	**24,510**	**23,115**
Investments (Incl. associates)	**74,374**	**61,661**	**58,400**	**50,943**
Equity	69,181	57,464	54,150	47,999
Debt	4,725	3,724	3,771	2,557
Investment property	468	473	479	387
Current Assets	**24,112**	**20,061**	**18,230**	**22,991**
Inventory	14,199	9,934	10,350	12,752
Trade Receivables	2,453	2,253	3,014	2,929
Others	7,460	7,874	4,865	7,309
Total Assets	**124,712**	**106,599**	**101,140**	**97,049**
Debt/Borrowings	**21,954**	**17,086**	**18,890**	**22,495**
Short-term	15,375	10,476	11,524	14,468
Long-term (Incl. Current Maturity of Long-Term Debt)	6,579	6,610	7,365	8,027
Other short-term liabilities	7,525	7,097	5,860	5,489
Other long-term liabilities	1,256	262	247	475
Shareholder's Equity	**93,978**	**82,155**	**76,143**	**68,589**
Total Liabilities & Equity	**124,712**	**106,599**	**101,140**	**97,049**
INCOME STATEMENT				
Turnover	**37,287**	**47,999**	**51,178**	**54,444**
Gross Profit	4,198	6,264	6,024	7,864
Net Other Income	2,734	3,762	3,639	3,309
Financial Charges	(670)	(1,046)	(1,745)	(1,610)
Net Income	**3,089**	**4,923**	**3,912**	**5,513**
Cashflow Statement				
Free Cashflow from Operations (FCFO)	2,698	4,163	4,373	4,942
Net Cash changes in Working Capital	(4,379)	1,696	2,744	1,561
Net Cash from Operating Activities	204	8,517	8,470	8,003
Net Cash from InvestingActivities	(5,357)	(3,077)	(6,215)	(11,024)
Net Cash from Financing Activities	3,119	(3,378)	(5,006)	4,695
Ratio Analysis				
Performance				
Turnover Growth (vs. SPLY)	3%	-6%	-6%	4%
Gross Margin	11%	13%	12%	14%
Net Margin	8%	10%	8%	10%
Coverages				
Interest Coverage (FCFO/Gross Interest)	4.0	4.0	2.5	3.1
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	1.2	1.4	1.2	1.5
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	2.3	2.6	2.1	2.5
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest	2.4	2.1	2.8	2.4
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	76.9	74.0	88.9	97.4
Capital Structure (Total Debt/Total Debt+Equity)	19%	17%	20%	25%

The Pakistan Credit Rating Agency Limited

STANDARD RATING SCALE & DEFINITIONS

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 Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
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-	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**Highly speculative.** Significant 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	**High default 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 Ratings

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 conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved with in foreseeable future, but may continue if underlying circumstances are not settled.

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'.

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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.

Regulatory and Supplementary Disclosure

Name of Issuer	Nishat Mills Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Dissemination Date	Long Term	Short Term	Outlook	Action
30-Jun-17	AA	A1+	Stable	Maintain
27-Sep-16	AA	A1+	Stable	Maintain
27-Oct-15	AA	A1+	Stable	Maintain
10-Jan-15	AA	A1+	Stable	Upgrade
10-Jan-14	AA-	A1+	Stable	Stable

Related Criteria and Research

Rating Methodology	Corporate Rating Methodology
Sector Research	Textile Sector Overview - 2016

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Rating Team Statement

Rating Procedure
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