The Pakistan Credit Rating Agency Limited

Rating Report

Nishat Mills Limited

Report Contents

Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Apr-2018	AA	A1+	Stable	Maintain	-
30-Jun-2017	AA	A1+	Stable	Maintain	-
27-Sep-2016	AA	A1+	Stable	Maintain	-
28-Oct-2015	AA	A1+	Stable	Maintain	-
10-Jan-2015	AA	A1+	Stable	Upgrade	-

Rating Rationale and Key Rating Drivers

The ratings reflect diversity of Nishat Mills underlying businesses, along with a conservative capital structure. This emanates from its implicit holdco structure within Nishat Group (NG), providing resilience to adversities in underlying sectors, particularly textile, while upholding the overall profile of Nishat Mills. Significant as well as diverse strategic investment portfolio of the company generates a regular and growing dividend stream in addition to a potential of capital appreciation. Nishat Mills is one of the market leaders in textile industry, maintaining a sizeable, export-oriented composite unit in the country's textile sector. Superior profile is characterized by requisite diversification, in terms of both geography and customer base. Despite key challenges being faced by the textile industry, it has maintained its performance indicators. The management is focusing on capitalizing enhanced facilities in order to achieve overall cost efficiencies.

The ratings are dependent on the company's ability to sustained business margins and, hence, support profitability. Low leveraged capital structure provides room for expansion; should be managed prudently. Moreover, induction of independent members on board for better governance is considered important.

Disclosure	
Name of Rated Entity	Nishat Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating Methodology(Jul-17),Methodology | Correlation between long-term and short-term rating scale(Jun-17),Methodology | Criteria Modifiers(Jun-17)
Related Research	Sector Study | Textile(Oct-17)
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NISHAT MILLS LIMITED	
Incorporated	1951
Major business lines	Single largest textile composite unit of Pakistan – spinning combing, weaving, bleaching dyeing, printing and stitching
Capacity	236,496 Spindles, 795 looms, 4 Rotary Printing Machines, 7 Digital Printing Machine, 5Thermosole Dyeing and 3,757 stitching machines
Location	32 manufacturing units: located at Faisalabad, Sheikhupura, Feroze Watwan and Lahore
Legal status	Listed Company

INDUSTRY SNAPSHOT

- During FY17, total textile exports stood at USD ~ 12,453mln.
- Cotton yarn contributes (10%), cotton cloth (17%), home textile (29%), while garments contributes (38%).
- Pakistan's weaving sector continues to witness suppressed margins.
- High cost of doing business as compared to other countries like Bangladesh, India and Vietnam.

OWNERSHIP

- Nishat Mills is the flagship company of Nishat Group. Mansha family collectively to own majority (~53%) shares of the company directly through individuals (~45%) and group companies (~8%). Remaining (~47%) stake is well spread among financial institutions, companies, and the general public
- NG - a leading conglomerate - maintains substantial presence in the country's financial sector, and strong foothold in textile, cement, power sectors, and hospitality sector. Also, the group has entered in Pakistan's automobile assembly industry.

GOVERNANCE

- Seven member board including the Chairman – Mr. Hassan Mansha, and Chief Executive Officer (CEO) – Mr. Umer Mansha.
- The board comprises two directors from sponsoring family – CEO and Chairman, one independent member, one Nishat Mill's executive, while all other members are non-executive directors working with NG entities. A high proportion of Nishat Group executives on the board, though enhances quality, undermines independence of the board.

MANAGEMENT

- The CEO is supported by a by a team of qualified and experienced professionals. Most of the senior management has been associated with Nishat Mills for a reasonably long time.
- A large number (ten) of senior executives, including heads for different production processes and units report directly to the CEO.
- Given the large scale of Nishat Mill's operations spread at various locations and divided into various segments and processes, the need for quality information systems is paramount to control and maintain the efficiency of operations.

PERFORMANCE

- Sizeable revenue base; leading exporter of country (FY17: 3% export share)
- During FY17, sales mix of Nishat Mills continued to be dominated by Processing & Home textile (P&HT) segment as the key revenue contributor (~40%), followed by weaving (~24%) and spinning (~22%), and garment (~11%) segments. Top ten customer concentration in export sales remained moderate (FY17: ~30%).
- Topline rose by ~3% on YoY basis on account of improved export performance – despite highly competitive international market. Core business expenses increased by ~5% on due to higher input and energy costs. Consequently, margins weakened (gross: FY17: ~11%, FY16: ~13%; operating: FY17: ~4%, FY16: ~6%) on YoY basis.
- A reduction (~13%) in interest expense owing to better financial management helped reduce the final impact on pre-tax profit which decreased by ~12% to report at PKR 5,020mln during FY17.
- During 1HFY18 performance indicators improved; 6% growth in topline, the company reported pre-tax profit of PKR 3,039mln (1H17: PKR 2,935mln)
- Nishat Mills maintains a hefty investment portfolio (PKR 59,278mln) – ~75% of equity at end-Dec17, mainly comprising strategic holdings (PKR 56,383mln). With presence in diversified sectors, the company has prudently managed its overall risk profile.

FINANCIAL RISK

- Working capital requirements, a function of its receivables and inventory, are met through a mix of internal generation and short term borrowings.
- Though payables were stretched to an extent, inventory and receivable days increased, resulting in higher net cash cycle (1H18: 80 days, FY17: 78days, FY16: 74days).
- Sizeable FCFO (PKR 3,684mln), topped up with strong cashflows from investment (PKR3, 535mln) provides 2.4 times coverage to debt servicing (PKR3,008) reflecting well on financial risk profile of the company.
- Low-leveraged capital structure (end-Jun17; ~20%); expected to remain range bound.

Nishat Mills Limited

BALANCE SHEET	30-Dec-17	30-Jun-17	30-Jun-16	30-Jun-15
	6M	FY17	FY16	FY15
Non-Current Assets	**28,491**	**28,057**	**24,877**	**24,510**
Investments (Incl. Associates)	**59,278**	**68,354**	**61,661**	**58,400**
Equity	51,980	62,544	57,464	54,150
Loans to Associates/Debt Securities	6,834	5,343	3,724	3,771
Investment Property	464	467	473	479
Current Assets	**22,675**	**22,315**	**20,061**	**18,230**
Inventory	13,332	12,723	9,934	10,350
Trade Receivables	2,502	2,246	2,253	3,014
Others	6,842	7,346	7,874	4,865
Total Assets	**110,445**	**118,726**	**106,599**	**101,140**
Debt/Borrowings	**23,319**	**22,036**	**17,086**	**18,890**
Short-term	15,621	14,697	10,476	11,524
Long-term (Incl. Current Maturity of Long-Term Debt)	7,697	7,339	6,610	7,365
Other short-term liabilities	7,508	7,144	7,097	5,860
Other long-term liabilities	707	783	262	247
Shareholders' Equity	**78,910**	**88,763**	**82,155**	**76,143**
Total Liabilities & Equity	**110,444**	**118,726**	**106,599**	**101,140**
INCOME STATEMENT				
Turnover	**25,520**	**49,248**	**47,999**	**51,178**
Gross Profit	2,577	5,380	6,264	6,024
Net Other Income	2,607	4,068	3,762	3,639
Financial Charges	(451)	(915)	(1,046)	(1,745)
Net Income	**2,666**	**4,278**	**4,923**	**3,912**
Cashflow Statement				
Free Cash Flow from Operations (FCFO)	1,754	3,684	4,163	4,373
Net Cash changes in Working Capital	(5)	(4,129)	1,696	2,744
Net Cash from Operating Activities	3,845	2,172	8,517	8,470
Net Cash from Investing Activities	(3,361)	(7,428)	(3,077)	(6,215)
Net Cash from Financing Activities	(462)	3,201	(3,378)	(5,006)
Ratio Analysis				
Performance				
Turnover Growth (vs. SPLY)	6%	3%	-6%	-6%
Gross Margin	10%	11%	13%	12%
Net Margin	11%	9%	10%	8%
Coverages				
Interest Coverage (FCFO/Gross Interest)	3.9	4.0	4.0	2.5
Core: (FCFO) / (Gross Interest+CMLTD+Uncovered Total STB)	1.0	1.2	1.4	1.2
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	2.4	2.4	2.6	2.1
Debt Payback (Total LT Debt Including Uncovered Total STBs) / (FCFO- Gross Interes	3.1	2.7	2.1	2.8
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	80.1	78.1	74.0	88.9
Capital Structure (Total Debt/Total Debt+Equity)	23%	20%	17%	20%

CREDIT 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.
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 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.

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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) PACRA finds it impractical to surveill the opinion due to lack of requisite information

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.
(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)
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