



The Pakistan Credit Rating Agency Limited

Rating Report

Ahmed Fine Textile Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
29-Aug-2018	A-	A2	Stable	Upgrade	-
28-Feb-2018	BBB+	A2	Stable	Maintain	-
26-Jan-2017	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Ahmed Fine Textile Mills (Ahmed Fine) association with renowned business groups of Pakistan - jointly owned by Fazal Group and Hussain Group. The company, is engaged primarily in spinning business and also has presence in weaving segment through a wholly owned subsidiary – Fazal Rehman Fabrics Limited. The ratings incorporate improved business performance of the company - topline increased by ~23% - a factor of better pricing and increase in exports sale as proportion of total sales. Recent devaluation of currency and exports rebate packages announced by the government also supplemented growth in revenue. The company's margins improved, a factor of operational efficiencies. However, re-imposition of custom duty and sale tax on cotton imports in FY19 budget, coupled with exclusion of tax rebate on yarn and greige fabric may put pressure on industry margins. Ahmed Fine's financial profile is strong reflected by (i) relatively efficient working capital cycle, (ii) strong coverages, and (iii) moderately leveraged capital structure. Going forward, the company intends to enhance its capacity if market conditions remain favorable. The expansion will be primarily financed through debt. The ratings also incorporate the experienced management team.

The ratings are dependent on sustaining business margins while maintaining a sound financial profile with strong coverages and manageable leveraging. The company's ability to generate ensuing cash flows to fulfill its financial obligations, in case of debt driven expansion, remains critical for the ratings.

Disclosure

Name of Rated Entity	Ahmed Fine Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Criteria Rating Modifier(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale Jun18(Jun-18)
Related Research	Sector Study Textile(Oct-17)
Rating Analysts	Muhammad Hassan muhammad.hassan@pacra.com +92-42-35869504

Profile

Legal Structure Ahmed Fine Textile, a public unlisted company, is engaged in the manufacturing and marketing of yarn and fabric.
Background Ahmed Fine Textile incorporated in 1966 is associated with Fazal Group (FG) since its inception.
Operations Ahmed Fine operates with a single spinning unit having a capacity of 45,888 spindles - manufacturing coarser count yarn. The company caters its power needs via in-house production (6MW), as well as MEPCO's connection.

Ownership

Ownership Structure The company is jointly owned by Fazal Group and Hussain Group (~50% each). Both groups belong to the same family descending from Mr. Fazal-ur-Rehman.
Stability The representation of Fazal and Hussain Group's textile ventures in Pakistan's textile industry remains critical. Going forward, succession plan of transfer of ownership is yet to be seen.
Business Acumen Fazal Group has interests in textile, Fertilizer and Power whereas, Hussains Group's interests lies only in textile. The sponsors expertise in textile remains important in case of any textile industry driven crisis.
Financial Strength Fazal and Hussain Groups maintain dominant position in Multan's textile industry. Fazal Group in particular is one of the wealthiest group with strong financial health. Strategic investment in fertilizers and textile provide ample room of financial support to Ahmed Fine when needed.

Governance

Board Structure The company's seven member Board is dominated by Fazal Group representatives, including the Chairman and CEO. The remaining three members are representatives of Hussain Group.
Members' Profile Board comprises experienced professionals and have reasonably long association with the company. Mr. Sheikh Naseem is a Chairman of board. Mr. Naseem has over 5 decades of experience.
Board Effectiveness Despite the presence of two sponsoring groups on the board, lack of challenge weakens the governance structure of the company. Moreover, Board Audit Committee has been formed to assist the board.
Financial Transparency M/s Deloitte Yousuf Adil & Co., Chartered Accountants is the external auditor of the company. The auditors have expressed unqualified opinion on the financial reports for the year ended 30th June, 2017. Audit of financial statements for the period FY18 is under process.

Management

Organizational Structure Management control of the company vests with Fazal Group. Mr. Rehman Naseem – the CEO – primarily manages the company's affairs.
Management Team Management team comprises long associated and experienced individuals, including Mr. Naveed Amer in the capacity of CFO, carrying three decades of experience.
Effectiveness The management meetings are held on a quarterly basis with formal recording of meeting minutes, followed by need based meetings to resolve bottlenecks and ensure smooth operations.
MIS Ahmed Fine deploys Oracle based Enterprise Resource Planning (ERP) system that provides comprehensive MIS reporting.
Control Environment Ahmed Fine's plant is connected with head office through VPN, thereby reporting on real time basis. Furthermore, Fazal rehman has received International certifications such as ISO 9001, Lycra assured and Fair Trade.

Business Risk

Industry Dynamics During FY18, total textile exports of Pakistan stood at USD ~ 13.53bln, a 9% YoY growth. Re-imposition of custom duty and sales tax on cotton imports in FY19 budget, coupled with exclusion of tax rebate on yarn and greige fabric may put pressure on the industry margins.
Relative Position Ahmed Fine is associated with Fazal Group, which maintains a prominent position in Pakistan's spinning sector, consequently strengthening Ahmed Fine's market position. However, on standalone basis, Ahmed Fine's share in spinning industry is minimal.
Revenues Sales mix (local: export) is shifting from local to exports in recent years, posting a rise of 50% YoY. Since FY15, Ahmed Fine's revenues are on growing trajectory. During FY18, the company's revenues registered ~23.6% YoY growth, which is mainly attributable to increase in export volume, supplemented with rupee devaluation.
Margins The gross margins marginally improved (FY18: 10.8%, FY17: 9.8%), followed by improved operating margin (FY18: 8.0%, FY17: 6.8%) due to cost controls. Despite the increase in finance cost by ~25%, the company posted net profit with an increase of ~48% (FY18: PKR 129mln, FY17: PKR 87mln).
Sustainability Ahmed Fine has invested in a wholly owned subsidiary, Fazal Rehman Fabrics Limited (Fazal Rehman). Despite positing profits, Fazal Rehman has yet not paid dividends. In future, dividends from Fazal Rehman will be helpful in meeting future cash needs. Furthermore, the company is planning expansion by installing 50,000 spindles. However, materialization of expansion is yet to be seen.

Financial Risk

Working Capital During FY18, the company reduced its reliance on STB and met its needs from internal cash flows. Overall company's working capital needs remained at the same level, though due to higher trade debtor days (FY18: 87days, FY17: 74days), net cash cycle increased (FY18: 145days, FY17: 137days).
Coverages Operating cash flows significantly increased (~33%) on YoY basis on the back of higher pre-tax profitability, as a result of improved profitability. Consequently, interest coverages improved (FY18: 4.0x, FY17: 3.8x) and debt coverage slightly deteriorated (FY18: 1.4x, FY17: 1.7x), on account of higher CMLTD.
Capitalization Ahmed Fine has moderately leveraged capital structure ~46.3% at FY18 (FY17: 50.4%), constituting wholly of long-term borrowing. Furthermore, company is looking towards debt driven expansion (constituting PKR 4.4bln in debt to equity of 80:20), with ten years debt payback period.

Ahmed Fine Textile Mills Limited

BALANCE SHEET	30-Jun-18	30-Jun-17	30-Jun-16
	Annual*	Annual	Annual
Non-Current Assets	1,506	1,604	1,442
Investments (Incl. associates)	355	355	355
Equity	355	355	355
Mutual funds	-	-	-
Current Assets	1,796	1,625	972
Inventory	469	563	345
Trade Receivables	826	767	331
Others	501	295	295
Total Assets	3,657	3,585	2,768
Debt	1,392	1,508	783
Short-term	-	416	275
Long-term (Incl. Current Maturity of long-term debt)	1,392	1,091	508
Other shortterm liabilities	543	483	509
Other Longterm Liabilities	109	112	80
Shareholder's Equity	1,612	1,483	1,396
Total Liabilities & Equity	3,657	3,585	2,768

INCOME STATEMENT

Turnover	3,965	3,209	3,038
Gross Profit	429	315	297
Other Income	(37)	(15)	(15)
Financial Charges	(104)	(83)	(67)
Net Income	129	87	112

Cashflow Statement

Free Cashflow from Operations (FCFO)	419	316	262
Net Cash changes in Working Capital	(2)	(656)	310
Net Cash from Operating Activities	311	(410)	495
Net Cash from Investing Activities	(69)	(309)	(131)
Net Cash from Financing Activities	(116)	724	(357)
Net Cash generated during the period	126	6	6

Ratio Analysis

Performance			
Gross Margin	10.8%	9.8%	9.8%
Net Margin	3.3%	2.7%	3.7%
ROE	7.5%	5.7%	8.0%
Coverages			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.4	1.7	1.7
Interest Coverage (x) (FCFO/Gross Interest)	4.0	3.8	3.9
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest)	4.4	4.7	2.6
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	145	137	87
Capital Structure (Total Debt/Total Debt+Equity)	46.3%	50.4%	35.9%

**un audited financials*

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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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 surveil the opinion due to lack of requisite information.

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

Disclaimer: PACRA's ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA's opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security's market price or suitability for a particular investor.

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

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- (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.
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- (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)
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- (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)

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- (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)

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