The Pakistan Credit Rating Agency Limited

Rating Report

Mahmood Textile Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
21-Jun-2024	A-	A2	Stable	Maintain	-
23-Jun-2023	A-	A2	Stable	Maintain	-
25-Jun-2022	A-	A2	Stable	Maintain	-
25-Jun-2021	A-	A2	Stable	Maintain	-
26-Jun-2020	A-	A2	Stable	Maintain	Yes
27-Dec-2019	A-	A2	Stable	Maintain	-
28-Jun-2019	A-	A2	Stable	Maintain	-
28-Dec-2018	A-	A2	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect the presence of (“Mahmood Textile” or “the Company”) in the competitive textile landscape. This stems from its long history of operations as an export-based Company in the textile value chain along with a large strategic portfolio on a standalone basis. It is the flagship Company of the “Mahmood Group”. The Group enjoys multiple revenue streams with a large business profile optimally parked in diverse sectors of the economy. In segment-wise business contribution, the Spinning segment is the foremost segment followed by Weaving segment and Apparel segment. The product slate of the Company divests into Yarn, Grey Cloth, and Garments. The Company’s topline is dominated by export sales indicating a notable growth during the last three years. During 9MFY24, the Company secured a topline of PKR 52.4bln (FY23: PKR 54.6bln). The latest expansions in the Spinning and Apparel segment exacerbated the revenues in terms of volume. The Company enjoys a stable clientele around the globe. The prime export destinations of the Company are China, Bangladesh, Turkey, Hong Kong, Germany, and United States. The sales mix remained the same despite macroeconomic and industry-specific challenges. The Company’s margins dipped minutely due to expensive raw material procurement and elevated energy costs. The dividend income has created a buffer in the bottom line. The Company’s reliance on STBs has magnified the finance cost. This has largely diluted the profitability matrix of the Company (9MFY24: PKR 177mln; FY23: PKR 1.2bln). The improvement in the bottom line is significant to sustain the ratings. The management has commissioned the Solar project of 11 Mega Watt and has further planned the installation of a steam turbine to curtail risk associated with elevated energy costs. The Company's financial risk profile is considered adequate with stretched working capital management depicting the industry norm. The Company's working capital requirements are primarily met through short-term borrowings (STB). The cash flows and coverages of the Company are considered adequate. The Company has maintained a leveraged capital structure. The Company is in the process of debt reprofiling, to create a cushion in their cashflows. The size of the textile industry in Pakistan is estimated to be PKR 2.62Trn ~3.0% of the total GDP as of FY23. The composite & garment segment in the textile sector has a contribution of ~ PKR 1.6Trn mainly dominated by knitwear, readymade garments, bedwear, and towels followed by PKR 775bln from spinning and PKR 637bln from weaving. The escalation in energy tariffs & finance costs, PKR devaluation, and ensuring the availability of optimum quality raw materials are prime challenges specific to the industry to assess the international market and stay price-wise competitive.

The ratings are dependent upon the Company’s ability to sustain business growth while generating sufficient cashflows and maintaining the profitability matrix at an optimal level. The sustainability of margins and improvement in coverages while expanding business volumes remains critical.

Disclosure

Name of Rated Entity	Mahmood Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jul-23),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology | Rating Modifiers(Apr-24)
Related Research	Sector Study | Composite and Garments(Dec-23)
Rating Analysts	Muhammad Harris Ghaffar | harris.ghaffar@pacra.com | +92-42-35869504

Profile

Legal Structure Mahmood Textile Mills Limited ('Mahmood Textile' or 'The Company') is a public listed concern, incorporated in 1970. The company is listed on the Pakistan Stock Exchange.

Background The company is a part of Mahmood Group, which was originally established in 1935 by entering the tannery business. The group has now evolved into a diversified business empire with Mahmood Textile as the Group's flagship company.

Operations Mahmood Textile is engaged in the production and sale of yarn and greige fabric. Its production facilities are located in Muzaffargarh, DG Khan, and Multan. The company has 150,768 spindles and 228 looms facilitating its production processes. With a generation capacity of ~20.45MW, Mahmood Textile ensures uninterrupted operations, supplemented by a backup line from MEPCO. Notably, the company has recently invested in solar energy, installing an infrastructure capable of generating around ~11MW of power.

Ownership

Ownership Structure The majority of the company's shareholding (~92.85%) is vested with sponsors of the company. The remaining (~7.15%) stake rests with joint stock companies and the general public.

Stability Mahmood Group has no holding company. The third generation of the sponsoring family is actively involved in the operations of the company but no formal succession plan has been announced. Documentation or formation of a family office will bode well with stability and succession of ownership.

Business Acumen With more than eight decades of experience, the sponsors possess expertise across various sectors, spanning textile, tanneries, real estate, and food industries.

Financial Strength Mahmood Group maintains an adequate financial profile with a considerable equity base through Group companies and Stock market investments. Investments enhance the Group's financial profile through dividends and capital gains but also expose the Group to financial risk. The group has a strong financial strength to support the company, if needed.

Governance

Board Structure Mahmood Textile has a seven-member board including two independent directors. The board is dominated by the Sponsoring family. The board is chaired by Mr. Khawaja Muhammad Ilyas.

Members' Profile Mr. Khawaja Muhammad Ilyas has more than five decades of textile experience. He has been a key position holder in various local corporate bodies of Pakistan. Overall, the board members possess diversified knowledge and experience which leads to a good skill mix of their competencies.

Board Effectiveness In line with best corporate governance practices, there are two sub-committees in place to assist the board on relevant matters: Audit and Human Resources. Attendance of directors in meetings remains high, boding well for the board's effectiveness. Meanwhile, minutes have room for improvement. The company has an internal audit function in place to ensure effective oversight, with the Head of Internal Audit reporting directly to the Board Audit Committee.

Financial Transparency M/s Shinewing Hameed Chaudhri & Co. Chartered Accountants are the external auditors of the company, listed in Category "B" of the State Bank's panel of auditors. The auditor expressed an unqualified opinion on the financial statements of the company for the period ending June 30th, 2023.

Management

Organizational Structure The organizational structure of Mahmood Textile is divided into various departments reporting to the CEO and CFO. The departments are as follows: (i) Audit (ii) Taxation (iii) HR and Admin (iv) IT and ERP (v) Export and (vi) Finance.

Management Team The CEO – Mr. Khawaja M. Younus – has been associated with the company for over four decades. He is supported by a team of seasoned professionals, most of whom have been associated with the company for a long period of time.

Effectiveness Adequate IT infrastructure and related controls are maintained. There is the preparation of regular reports regarding the company's receivables and payables position, purchases and procurement, audit report, etc., to be submitted to higher management.

MIS The company has deployed Oracle-based ERP with daily and monthly MIS to ensure the timely availability of information for effective decision-making.

Control Environment Mahmood Textile is accredited with international certifications for compliance including ISO 9001. The company adheres to the latest quality assurance standards for fabric production and trade in addition to the employment of quality control procedures.

Business Risk

Industry Dynamics During FY23, the size of the textile industry stood at PKR 2.9trn mainly supplemented by PKR 1,584bln from composite and garments, PKR 775bln from spinning, and PKR 637bln from weaving. The spinning industry has ~13.4mln spindles installed moving down the chain, the weaving industry has 9,000 looms working with an export cotton cloth volume of 2,012mln Sq. Meter and amount of PKR 499bln. The composite & garments segment has ~59 players major players operating in this specific industry and its export segment is mainly dominated by knitwear (PKR 1,089bln), Readymade garments (PKR 861bln), Bedwear (PKR 664bln) & Towels (PKR 248bln). The availability of raw materials like cotton yarn, inflated finance costs, and energy tariffs are prime challenges specific to the industry.

Relative Position With 150,768 spindles and 228 looms, Mahmood Textile is one of the large players with an adequate market share in the respective industry.

Revenues During FY23, the company's top line rose by 33.4% YoY to stand at PKR 54.6bln (FY22: PKR 40.9bln) driven by a 33.3% YoY increase in export sales, which constituted 73.8% of total revenue. The company has established a stable customer base in the global market. Local sales also grew significantly to PKR 15.6bln (FY22: PKR 12.6bln), up by 24.1%. During 9MFY24, the company sustained its growth trajectory, with revenue reaching PKR 52.4bln (9MFY23: PKR 37.8bln) primarily due to increase in exports. Yarn dominated sales at 59%, followed by Cloth at 30%, and Apparel at 5%.

Margins During FY23, the company's gross profit inched down to 14.1% (FY22: 15.1%) on the back of expensive raw material procurement and elevated energy costs. However, income from financial assets bolstered the bottom line (FY23: PKR 598mln; FY22: PKR 965mln). The company got a major hit on finance cost at PKR 3.9bln (FY22: PKR 1.7bln) indicating a substantial increase of 121.5%, aligning with the industry trend. The company's net profitability diluted (FY23: PKR 1.2bln; FY22: PKR 1.9bln). Hence, the net profit margin witnessed a minute dip (FY23: 2.2%; FY22: 4.7%). During 9MFY24, the company's gross margin clocked at 12.5% (9MFY23: 12.7%) whereas the operating margin inched up to 8.8% (9MFY23: 8.1%).

Sustainability To mitigate the adverse impact of elevated energy cost, the management has installed a ~3MW steam turbine. Additionally, the company plans to invest in a Biomass project for ~10MW, further enhancing its sustainability profile.

Financial Risk

Working Capital The company's working capital requirements are a function of inventory and receivables for which the company relies on internally generated cash and short-term borrowings. The company's net working capital cycle was stretched (end-Jun23: 128 days; end-Jun22: 120 days) to maintain the optimum inventory levels (end-Jun23: 98 days; end-Jun22: 87 days). As of end-Mar24, the company's net working cycle improved to 115 days whereas the inventory days remained largely the same at 99 days.

Coverages As of end-Jun23, the free cash flows from operations clocked at PKR 5.7bln (end-Jun22: PKR 5.2bln). The company's interest coverage and core operating coverage declined to 1.5x (end-Jun22: 3.2x) and 1.0x (end-Jun22: 1.9x). This dip is driven by the surge in policy rate which ultimately triggered the finance cost. As of end-Mar24, the free cash flows from operations clocked at PKR 5.5bln.

Capitalization The company has a highly leveraged capital structure. As of end-Jun23, the company's total borrowings exhibited a sizeable increase to stand at PKR 28.5bln (end-Jun22: PKR 21.3bln) as evidenced by an incline in the Gearing ratio (end-Jun23: 67.5%; end-Jun22: 62.8%). As of end-Mar24, the company's total borrowings remained largely the same recorded at PKR 28.7bln.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Mahmood Textile Mills Limited	Mar-24	Jun-23	Jun-22	Jun-21
Composite & Garments	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	18,195	17,713	13,999	9,722
2 Investments	185	187	325	311
3 Related Party Exposure	5,681	5,539	5,114	4,610
4 Current Assets	28,473	27,931	20,355	12,181
a Inventories	*20,243*	*17,736*	*11,638*	*7,820*
b Trade Receivables	*5,147*	*6,145*	*6,281*	*2,650*
5 Total Assets	52,533	51,371	39,793	26,825
6 Current Liabilities	9,232	8,470	5,146	2,313
a Trade Payables	*2,707*	*2,370*	*975*	*400*
7 Borrowings	28,789	28,560	21,377	14,131
8 Related Party Exposure	0	0	62	56
9 Non-Current Liabilities	579	586	558	388
10 Net Assets	13,932	13,755	12,651	9,938
11 Shareholders' Equity	13,932	13,755	12,651	9,938
B INCOME STATEMENT				
1 Sales	52,453	54,627	40,969	27,934
a Cost of Good Sold	*(45,895)*	*(46,919)*	*(34,774)*	*(24,121)*
2 Gross Profit	6,558	7,708	6,195	3,813
a Operating Expenses	(1,918)	(2,422)	(2,471)	(1,312)
3 Operating Profit	4,640	5,287	3,724	2,502
a Non Operating Income or (Expense)	*404*	*591*	*786*	*632*
4 Profit or (Loss) before Interest and Tax	5,044	5,878	4,510	3,133
a Total Finance Cost	*(4,342)*	*(3,953)*	*(1,784)*	*(1,258)*
b Taxation	*(525)*	*(723)*	*(784)*	*(535)*
6 Net Income Or (Loss)	177	1,202	1,942	1,341
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*5,592*	*5,762*	*5,285*	*3,159*
b Net Cash from Operating Activities before Working Capital	*1,163*	*2,612*	*3,710*	*1,456*
c Changes in Working Capital	*119*	*(5,120)*	*(5,799)*	*13*
1 Net Cash provided by Operating Activities	1,282	(2,508)	(2,089)	1,469
2 Net Cash (Used in) or Available From Investing Activities	(1,539)	(4,471)	(5,054)	(1,133)
3 Net Cash (Used in) or Available From Financing Activities	273	6,902	7,092	(283)
4 Net Cash generated or (Used) during the period	16	(78)	(51)	53
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	28.0%	33.3%	46.7%	14.2%
b Gross Profit Margin	12.5%	14.1%	15.1%	13.6%
c Net Profit Margin	0.3%	2.2%	4.7%	4.8%
d Cash Conversion Efficiency (FCFO adjusted for Working C	10.9%	1.2%	-1.3%	11.4%
*e Return on Equity [Net Profit Margin * Asset Turnover * (T*	1.7%	9.1%	17.2%	14.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	129	140	126	135
b Net Working Capital (Average Days)	115	128	120	130
c Current Ratio (Current Assets / Current Liabilities)	3.1	3.3	4.0	5.3
3 Coverages				
a EBITDA / Finance Cost	1.4	1.7	3.5	3.1
b FCFO / Finance Cost+CMLTB+Excess STB	1.1	1.0	1.9	1.5
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fi	5.6	5.5	2.5	3.4
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equit	67.4%	67.5%	62.8%	58.7%
b Interest or Markup Payable (Days)	74.8	118.0	108.5	86.4
c Entity Average Borrowing Rate	18.5%	15.6%	9.4%	7.6%

Credit Rating

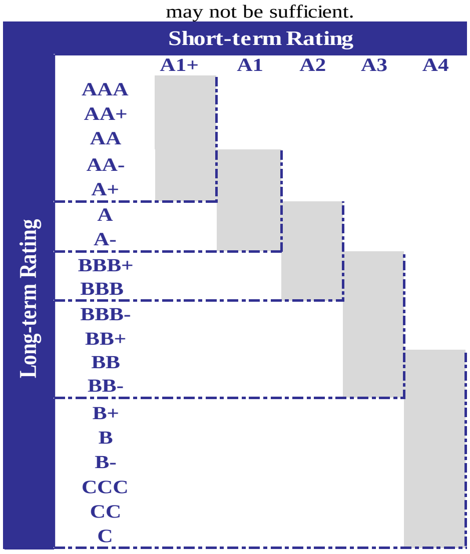
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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 | 17-(a)
(19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)
Proprietary Information