



The Pakistan Credit Rating Agency Limited

Rating Report

Basfa Textile (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
30-Apr-2019	BBB-	A3	Stable	Maintain	-
28-Dec-2018	BBB-	A3	Stable	Maintain	-
30-Jun-2018	BBB-	A3	Stable	Maintain	-
29-Dec-2017	BBB-	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect adequate business profile of Basfa Textile (Pvt) Ltd. The Company is engaged in the manufacturing and sale of Viscose Yarn and different varieties of cotton yarn. Sponsor's primary business interest is in car paint and chemical raisins. However, lately they diversified into textile sector i.e. through Basfa Textile. Recent devaluation of Pakistan currency is expected to bode well with textile industry. However, on standalone basis, the Company being an importer of raw material suffered from devalued currency, which in turn decreased margins. The Company has over the years successfully created its niche market in viscose yarn, which is expected to provide stability to its margins in future. Building on these benefits, the management has fully shifted to viscose yarn in FY19. The Company has minimal long-term debt which keeps the financial risk profile at low level. Short-term borrowings are used to finance its working capital needs.

The ratings are dependent on sustaining business margins while maintaining financial risk at low level. Governance framework and financial transparency needs improvement. At the same time, prudent management of short-term liquidity is considered important.

Disclosure

Name of Rated Entity	Basfa Textile (Pvt.) 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(Jun-18)
Related Research	Sector Study Textile(Oct-18)
Rating Analysts	Ateeb Riaz ateeb.riaz@pacra.com +92-42-35869504

Profile

Legal Structure Basfa Textile (Pvt.) Ltd (Basfa) was incorporated in 2006. However, the commercial operations started in 2008. The corporate office of the Company is located in Lahore.

Background The Company was established by Mr Jahangir Saleem. He was involved in the business of car paints and chemical raisins under the name of 'Basfa Industries Pvt Ltd' and 'Crown Chemicals & Motor Co' prior to textile business. The name "BASFA" is titled as per the name of his four sons. Mr. Babar Jahangir, Mr. Sajid Jahangir, Mr. Fahad Jahangir and Mr. Ahmad Jahangir. Basfa Textile started its commercial operations with the initial cost of the investment of PKR ~637mln which was financed with 100% equity.

Operations The Company is engaged in the manufacturing and sale of Viscos Yarn (Capacity: 34,632 spindles). Viscos yarn is sold under the brand name of "Super-Diamond" and Cotton yarn – under the brand name of "Super-Gold", whereas, vicinity of the plant is at 36-KM Ferozepur Road, Lahore.

Ownership

Ownership Structure The controlling stake of the Company is held by Jahangir Saleem Family. Mr Jahangir Saleem (Chairman/CEO) holds 55.51% shares in the Company, while Mr. Babar Saleem, son of Mr. Jahangir, holds 44.44% shares.

Stability Although there is no formal succession plan, but the ownership of shares and business roles are equally divided between all the four brothers. Formation of a group holding company or documented succession plan would do well to secure the future of the Company.

Business Acumen Mr. Jahangir Saleem has an overall working experience of ~40 years. His diverse experience in the field of textile sector and chemical raisins brings specialized and comprehensive knowledge to the board.

Financial Strength Other than textile business, sponsors are also involved in the business of car paints and chemical raisins that are used in fibre glass industry and steel putty (a product of auto industry). Sponsors can provide support to the entity in time of need.

Governance

Board Structure Board comprises of two members including CEO/Chairman and Managing director. The CEO and Chairman of the Company is Mr. Jahangir Saleem. Whereas, Mr. Babar Jahangir – holds the position of Managing director of the Company.

Members' Profile Mr. Jahangir Saleem, is the chairman and founder of the Company. He did his graduation in commerce and started business with his father in Karachi at a young age. Mr. Babar Jahangir holds graduation degree from United Kingdom. He has got an overall experience of ~15 years in his portfolio out of which ~10 years of experience is in Basfa Textile Pvt Ltd.

Board Effectiveness The board is currently heading two committees (i) Audit Committee – who is primarily responsible for supervision of all matters related to audit and finalization of financial accounts. (ii) corporate performance and evaluation committee – who is primarily responsible for recommending HR policies, succession planning of key management roles, monitoring key performance metrics.

Financial Transparency A. Aziz Chaudhury are the external auditors of the Company – not listed on panel of auditors maintained by State Bank of Pakistan but have satisfactory QCR rating. They expressed an unqualified opinion on the Company's annual financial statements for the year ended June 30, 2018.

Management

Organizational Structure The organizational structure of the Company is divided into various functional departments: (i) Marketing, (ii) Finance, (iii) Accounts, (iv) Procurement, (v) Technical operations. The management hierarchy including various levels, enables the Company to carry out smooth operations.

Management Team The Company's managing director - Mr. Babar Jahangir – is one of the sons of Mr. Jahangir Saleem. He has completed his graduation from United Kingdom. Mr. Abdul Basit is the CFO of the Company – a fellow public accountant and Fellow Cost and Management Accountant with overall experience of ~22 years in his portfolio. Marketing team is led by the General Manger Marketing, who is also a textile engineer with more than 20 years of experience in the yarn sales.

Effectiveness Basfa Textile maintains adequate IT infrastructure and related controls. The Company deploys Quick Books – Accounting edition - since 2016 with the license of ~10 corporate user. The operational modules including (i) Payable, (ii) Receivable, (iii) Inventory, (iv) Procurement, (v) Order Management, (vi) General Ledger, (vii) Fixed Assets, and (viii) Cash Management.

MIS Various MIS reports are prepared for the management to keep track of all operating activities. Daily reports are generated for the senior management which help them in day-to-day decision making. Apart from daily reporting, the management also receives a more detailed MIS on a monthly basis. This report is used in the monthly review meeting of the management.

Control Environment Intra-networking is being used within the Company so that all the departments are connected through a common network. User-based controls are in place. Servers are installed where data management and back-up policies are in place to make the functions smooth and sound.

Business Risk

Industry Dynamics Textile exports of the country grew by ~9% in FY18, backed by devaluation of the rupee, bailout package from the government and GSP Plus Scheme of the EU. During 9MFY19, however, exports stagnated. Even though major segments including cotton cloth, knitwear, garments and bedwear displayed strong quantitative growth, industry players needed to share the benefit of the currency depreciation with their buyers which resulted in a unit price dip across all major categories, curbing overall growth. This, coupled with cotton yarn displaying double-digit quantitative decline on account of the US-China trade war as well as strong domestic demand for yarn, resulted in overall increase in exports of only ~0.1% YoY. Going forward, the devalued currency, recently announced relief in electricity tariffs for textile players as well as expected payment of tax refunds is expected to boost exports.

Relative Position Basfa Textile has Brand-Based clientele. Final product is sold through intermediary with no direct sales mechanism – following the industry norms. Traders are given the commission between 0.5% and 1% of the sales amount. Ninety percent (90%) of the customer base of Basfa Textile is in Faisalabad, Punjab. Going forward, the Company is planning to expand its customer base in other parts of the country as well.

Revenues Over the years, the Company's revenue growth has improved significantly. During 1HFY19, the Company's revenues grew by ~17.3% (1HFY18: ~15.3%). The increase in total revenue is primarily seen because the Company is now focusing more on production of Viscose Yarn – a premium quality yarn – which caused significant increase in production capacity, leading to higher selling volumes. In addition, the prices of the finished products also increased due to higher input costs, triggering the growth further.

Margins During 1HFY19, the gross margin remained at ~6.5% (1HFY18: 7%). The gross margin declined due to higher cost of sales compared to previous year, triggered by increase in cost of raw materials due to devaluation of Pak rupee.

Sustainability The Company has shifted its focus on viscose yarn completely and discontinued production of other types of yarns. Due to this shift the Company might have to face increased international prices of raw materials due to rupee depreciation. Going forward, the Company is planning to install more spindles to increase the production of viscose yarn.

Financial Risk

Working Capital For 1HFY19, the Company's net working capital days stood at 76 days (1HFY18: 71 days). The management increased stock levels during 1HFY19 in anticipation of increased cost due to expected rupee devaluation, which led to higher net working capital days.

Coverages For 1HFY19, FCFO stood at ~PKR 112mln (1HFY18: ~PKR 76mln), the increase is mainly caused by higher top line. The interest coverage stood at 5.5x in 1HFY19 (1HFY18: 3.8x). The debt coverage ratio remained at 4.1x (1HFY18: 2.6x). The ratios improved due to higher FCFO.

Capitalization Basfa has moderately leveraged capital structure (1HFY19: ~39%, 1HFY18: ~31%). Out of the total debt ~2% of the debt comprises of long-term borrowings. Going forward, in absence of any major capacity expansion, and with the gradual payments of long-term loans, the leveraging is expected to reduce over time.



**Basfa Textile (Private) Limited
Private Limited**

BALANCE SHEET	Dec-18 6M	Jun-18 12M	Jun-17 12M	Jun-16 12M
a Non-Current Assets	678	665	617	589
b Investments (Incl. Associates)	-	-	-	-
Equity Instruments	-	-	-	-
Debt Instruments	-	-	-	-
c Current Assets	930	745	778	562
Trade Receivables	45	55	51	47
Others	885	689	727	514
d Total Assets	1,608	1,410	1,395	1,150
e Debt/Borrowings	583	446	451	315
Short-Term	570	410	417	264
Long-Term (Incl. Current Maturity of Long-Term Debt)	13	36	34	51
Other Short-Term Liabilities	80	61	76	44
Other Long-Term Liabilities	21	7	18	1
f Shareholder's Equity	924	896	850	790
g Total Liabilities & Equity	1,608	1,410	1,395	1,150

CASH FLOW STATEMENT

a Free Cash Flow from Operations (FCFO)	112	208	185	125
b Total Cashflows (TCF)	112	208	185	125
c Net Cash changes in Working Capital	(169)	(1)	(178)	(200)
d Net Cash from Operating Activities	(74)	169	(18)	(100)
e Net Cash from Investing Activities	(59)	(144)	(121)	(69)
f Net Cash from Financing Activities	136	(4)	136	163
g Net Cash generated during the period	3	21	(4)	(5)

RATIO ANALYSIS

a Performance				
Turnover Growth	17%	6%	62%	-10%
Gross Margin	6%	6%	7%	8%
Net Margin	2%	2%	2%	3%
ROE	6%	5%	7%	5%
b Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	4.1	2.7	4.5	2.2
Interest Coverage (X) (FCFO/Gross Interest)	5.5	5.1	7.2	5.0
Debt Payback (Years) (Total Debt (excluding Covered Short Term Borrowings) / FCFO)	0.1	0.2	0.2	0.5
c Capital Structure (Total Debt/Total Debt+Equity)				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	75	79	72	84
d Capital Structure (Total Debt/Total Debt+Equity)	39%	33%	35%	29%

Basfa Textile (Private) Limited

Apr-19

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

- (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)

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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)

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)

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