



The Pakistan Credit Rating Agency Limited

Rating Report

Rustam Towel (Pvt.) Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
29-Apr-2022	BBB	A2	Stable	Maintain	-
29-Apr-2021	BBB	A2	Stable	Upgrade	-
29-Apr-2020	BBB-	A3	Stable	Maintain	Yes
30-Oct-2019	BBB-	A3	Stable	Maintain	-
30-Apr-2019	BBB-	A3	Stable	Upgrade	-
30-Oct-2018	BB+	A3	Stable	Maintain	-
29-Mar-2018	BB+	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Rustam Towel (Pvt.) Limited ('Rustam Towel' or 'the business', a conventional family-owned business concern, is operating for over two decades in the towel industry as an export-oriented towel manufacturer. It holds a stable position and is classified among the top ten towel exporters of the country, with a strong customer foothold based in Europe and America. The Country's textile exports have witnessed a growth of ~ 25% in 1HFY22 and stood at \$9.4bln as compared to \$7.4bln in 1HFY21, whereas towel exports contribute ~ 6% (value-wise) of it. The exports of towels increased by 22% in 1HFY22 as compared to the same period last year which is a positive sign. The rating incorporates the operational strength of the business as it is well integrated vertically. The revenues are expected to witness an uptick as there has been a worldwide surge in demand for towels on account of improved hygiene practices. To capitalize this opportunity a capacity expansion of total 48 looms is underway, currently, 24 looms have been installed out of 48 looms and production capacity is now increased by ~33%, the expansion is funded by internal cash. Towel industry enjoys relatively better margins that are reflected in Rustam Towel's profitability as well. On standalone basis, the business concentration levels – both customer and geographical – are well managed with having a policy of capping revenue through an intermediary. The business was able to achieve growth in revenue of ~14% during 1HFY22 due to volumetric and price increases in sales and enjoys reasonable margins and profitability. Finance Risk profile appears adequate, with comfortable coverages, stretched working capital cycle, and leveraged capital structure; encompassed short-term borrowings for working capital management. The ratings also draw comfort from strong financial strength of sponsors. Rustam Towel is a private limited hence, room for improvement in its governance structure continues to be essential.

The ratings are dependent upon the business's ability to improve its revenues, margins, and profitability. Meanwhile, the ideology to dilute borrowing levels and adherence to sound financial discipline gives comfort to the ratings. Strengthening of governance structure and financial transparency will lend support to the ratings.

Disclosure

Name of Rated Entity	Rustam Towel (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-21),Criteria Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria Rating Modifiers(Jun-21)
Related Research	Sector Study Towel(Jan-22)
Rating Analysts	Sohail Ahmed Qureshi sohail.ahmed@pacra.com +92-42-35869504

Profile

Legal Structure Rustam Towel (Pvt.) Limited (Rustam Towel) was incorporated in 1998 as a Private Limited Company.

Background Rustam Towel is a small-scale towel manufacturing concern. Primary business of the Company is to manufacture and export various types of towels. The Company started its business two decades ago and experienced consistent double-digit growth since 1998 by providing quality commercial textiles with competitive pricing. Mr. Arif Dogar – Father of Mr. Sana Ullah Dogar - in 1970s started textile business by setting up a textile mill, Rustam Weaving (Pvt.) Limited in Gujranwala. Mr. Sana Ullah started to work with his father. In 1998, along with his four brothers he formed a towel manufacturing company – Rustam Towel.

Operations Rustam Towel is classified among top 10 exporters of terry towels in Pakistan. It exports bath products to leading retailers, hospitality, and healthcare industries across the world. European countries like United Kingdom, France, Germany, and Spain are the main areas of concentration for the Company. Rustam Towel has weaving, dyeing, and finishing solutions, all under one roof. The production facility of the Company has been set up near Lahore on 22-acre land with 10,000 spindles and 78 looms. Further, the Company has also diversified its portfolio by adding a denim production facility. Operations at the facility have officially started from August 2019 with an installed capacity of 120,000 pieces per month.

Ownership

Ownership Structure Majority of the shareholding lies with Mr. Sana Ullah (35%) and his son Mr. Sohaib Ali (20%). Mr. Wasim Arif, Mr. Zaka Ullah and Mr. Zia Arif are brothers of Mr. Sana Ullah and hold 20%, 10% and 15% shareholding, respectively.

Stability There is no formal succession plan, the ownership and family businesses are clearly divided mutually among brothers. Formation of documented succession plan would further strengthen stability of the Company.

Business Acumen Dogar family is in textile industry for more than four decades. Mr. Sana Ullah Dogar has been associated with the family business since inception. He has vast experience and knowledge of the towel industry.

Financial Strength The Dogar family owns another towel manufacturing company namely Saif Tex. Apart from textile business, the family has a property business in Gujranwala. The sponsors has invested and got franchises of international food chains in Lahore and Gujranwala.

Governance

Board Structure The overall governance matters are overseen by Sponsors. There is room for improvement as the governance structure lacks independent oversight.

Members' Profile Mr. Sana Ullah Dogar is the Chairman and brings ~40 years of experience to the Board. All other members have sufficient experience of the industry.

Board Effectiveness There is no independent director on the board. The board has not formed any board committees. All board members are also the shareholders of the Company. The board meetings are not conducted formally but family members meet regularly to discuss business developments and challenges.

Financial Transparency Akhter Mahmood Mian, Chartered Accountants are the external auditors of the Company. The auditors are not QCR rated by ICAP nor falls in the list of SBP's panel of auditors. Auditors, have given unqualified audit opinion on Company's financial statements for the year ending 30th June 2021.

Management

Organizational Structure Mr. Sana Ullah Dogar, heads the management team as Chief Executive Officer of the Company. The Company has a simple organization structure as it has four major departments i) Administration, (ii) Finance, (iii) Production and (iv) Marketing.

Management Team Mr. Wasim Dogar, the youngest brother, is mainly responsible for the overall towel business affairs and heads the operations of the business, accompanied by his brother Mr. Zia Dogar.

Effectiveness Rustam Towel has SQL based system to automate key business functions in finance, operations and HR. MIS generated reports are reviewed by senior management on regular basis.

MIS The Company's MIS can be classified into three categories based on periodicity – Daily, Weekly and Monthly. The daily and weekly reports generated for top management mainly scrutinize liquidity position, cash and stock related reports. The Company is using an SQL based system. A new ERP (SAP B1) is in parallel testing phase and will be fully implemented in the future.

Control Environment Rustam Towel is accredited with International certifications for compliance. It has valid certificates for its products and facilities and is periodically audited by internationally recognized certification bodies including Oeko Tex 100 Class-I and Class-II, BSCI, C-TPAT, Sedex, GOTS, BRC.

Business Risk

Industry Dynamics During FY21, exports clocked in at PKR~150bln (USD~938mln) as compared to PKR~112bln (USD~711mln) in FY20. The increase was attributable to greater quantitative exports as well as higher export prices during the period. During FY21, the towel sector's contribution to overall textile exports was ~6%. Meanwhile, contribution to total country exports was ~4%. The growth reflected Pakistan's recovery from the COVID-19 pandemic, as it was able to attract export orders when regional players were still struggling due to the pandemic and were unable to meet demand. In regional terms globally, Europe and USA are the largest importers of towels. The top 5 exporters consist of China, India, Pakistan Turkey, and Vietnam and together they account for approximately ~80% of the total export market.

Relative Position The business has a stable position and places itself among top towel exporters with ~4% market share in the country's towel exports followed by the highest share of Feroze 1888.

Revenues The topline of the Company is majorly export oriented. Majority of the Company's exports are concentrated in Europe. During FY21, the Company's revenue clocked in at ~PKR 5,512mln (FY20: ~PKR 4,490mln), reflecting an increase of ~23%. Growth in revenue emanated from rupee depreciation and demand uptick due to COVID-19. The trend of incremental revenues is expected to continue in future as the pandemic posed more focus towards hygiene and healthy practices, hence resulting in growing demand. In 6MFY22 the revenue stood at PKR 3,169mln, reflecting increase of 15%.

Margins During FY21, gross margin of the Company remained stable at ~17% (6MFY22: 20%, FY20: 17%), whereas operating expenses remained intact in FY21 and gross profit clocked in at ~PKR 942mln (6MFY22: PKR 628mln, FY20: PKR 764mln, FY19: ~PKR 759mln). Operating margin were ~9% (6MFY22: ~10%, FY20: ~10%). Finance cost slightly dropped to PKR 86mln as compared to last year PKR 96mln. The Company's net profit margin stood at 7% as it posted net profit of ~PKR 388mln in FY21 (6MFY22: ~PKR 230, FY20: ~PKR 320mln).

Sustainability After Covid-19 outbreak, there was an overall industry resumption which led to an increase in export orders as well. The Company is an export-oriented entity have found an increasing trend from export destinations (USA and Europe). Going forward demand and sales of the company's product are expected to grow.

Financial Risk

Working Capital During FY21, the gross working capital days remained stable at 135 days (FY20: 135 days) on the back of receivables. The Company's working capital remained in line with the industry average. However, In 6MFY22 the gross working capital stood at 134 days. The Company's room to borrow stood at ~4% in FY21 after depicting negative room to borrow in FY20 -4% (6MFY22: 11%).

Coverages In FY21, the FCFO of the Company dropped yet remained optimum at PKR 600mln(FY20: PKR 522mln). Consequently, the interest coverage ratio improved to 7x (FY20: 5.4x). However, the coverages of the entity are still considered strong. Majority of the financing is subsidized from SBP, further reducing the financial risk. In 6MFY22 FCFO of the company stood at PKR 344mln.

Capitalization Rustam Towel has moderately leveraged capital structure (6MFY22: ~41%, FY21: ~43%, FY20: ~44%). There is no long term borrowings except for SBP Salary refinancing on the books of Rustam Towel as on FY21. The expansion is being largely sourced from internal cash.



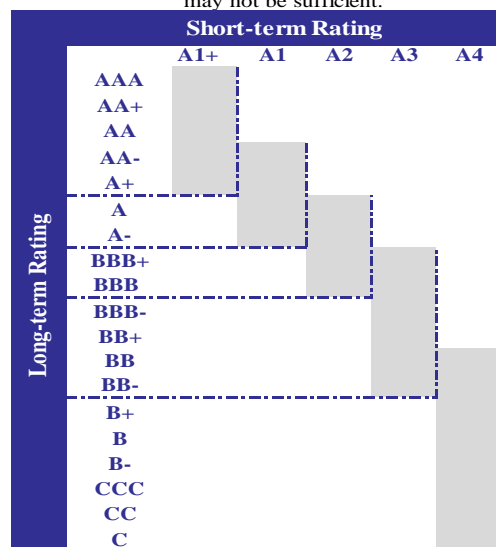
Rustam Towel (Pvt.) Limited Towel	Dec-21 6M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	2,566	2,569	2,347	2,334
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	3,381	3,138	2,710	2,195
<i>a Inventories</i>	970	1,124	851	587
<i>b Trade Receivables</i>	1,476	1,085	1,029	865
5 Total Assets	5,946	5,706	5,057	4,529
6 Current Liabilities	71	66	58	45
<i>a Trade Payables</i>	71	66	58	45
7 Borrowings	2,432	2,428	2,175	1,980
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	-	-	-	-
10 Net Assets	3,443	3,213	2,824	2,504
11 Shareholders' Equity	3,443	3,212	2,824	2,504
B INCOME STATEMENT				
1 Sales	3,169	5,512	4,490	4,275
<i>a Cost of Good Sold</i>	(2,541)	(4,570)	(3,726)	(3,516)
2 Gross Profit	628	942	764	759
<i>a Operating Expenses</i>	(315)	(439)	(324)	(310)
3 Operating Profit	312	503	440	448
<i>a Non Operating Income or (Expense)</i>	-	25	23	16
4 Profit or (Loss) before Interest and Tax	312	528	463	464
<i>a Total Finance Cost</i>	(55)	(86)	(101)	(101)
<i>b Taxation</i>	(27)	(54)	(43)	(44)
6 Net Income Or (Loss)	230	388	320	318
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	344	600	522	608
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	289	514	421	709
<i>c Changes in Working Capital</i>	(118)	(76)	(487)	(368)
1 Net Cash provided by Operating Activities	171	438	(66)	341
2 Net Cash (Used in) or Available From Investing Activities	(56)	(347)	(113)	(707)
3 Net Cash (Used in) or Available From Financing Activities	(48)	72	195	417
4 Net Cash generated or (Used) during the period	67	163	15	51
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	15.0%	22.8%	5.0%	35.1%
<i>b Gross Profit Margin</i>	19.8%	17.1%	17.0%	17.7%
<i>c Net Profit Margin</i>	7.3%	7.0%	7.1%	7.4%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	7.1%	9.5%	0.8%	5.6%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	13.8%	12.9%	12.0%	13.6%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	134	135	135	122
<i>b Net Working Capital (Average Days)</i>	130	131	131	118
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	47.4	47.3	46.5	48.6
3 Coverages				
<i>a EBITDA / Finance Cost</i>	6.8	7.6	5.9	6.0
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	6.3	7.0	5.4	6.5
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	0.0	0.1	0.1	0.0
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	41.4%	43.0%	43.5%	44.2%
<i>b Interest or Markup Payable (Days)</i>	0.0	0.0	0.0	0.0
<i>c Entity Average Borrowing Rate</i>	4.6%	3.8%	4.6%	5.5%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 surveil 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):

<p>Entities</p> <ul style="list-style-type: none"> a) Broker Entity Rating b) Corporate Rating c) Financial Institution Rating d) Holding Company Rating e) Independent Power Producer Rating f) Microfinance Institution Rating g) Non-Banking Finance Companies (NBFCs) Rating 	<p>Instruments</p> <ul style="list-style-type: none"> a) Basel III Compliant Debt Instrument Rating b) Debt Instrument Rating c) Sukuk Rating
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(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)

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- 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

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- (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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