



The Pakistan Credit Rating Agency Limited

## Rating Report

### C.A Textile Mills (Pvt.) Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-Dec-2019	BB+	A3	Stable	Maintain	-
28-Jun-2019	BB+	A3	Stable	Maintain	-
31-Dec-2018	BB+	A3	Stable	Maintain	-
30-Jun-2018	BB+	A3	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

The ratings reflect the modest business profile of C.A. Textile Mills (Pvt.) Limited (C.A. Textile), involved in the manufacturing of cotton and viscose yarn. The Company's revenues have shown growth over recent years, benefiting from increase in local sales volumes on the back of recently completed expansion. However, the profitability of the Company remains thin while margins remain low compared to industrial peers. The Company caters to the needs of local industry and has introduced new products including viscose yarn. However, with the withdrawal of zero-rated status of the textile sector since Jul19, sales to unregistered customers have become a challenge. Thus, the Company has increased focus on sale of cotton yarn. This, coupled with increased interest rates, has put pressure on margins and coverages. Meanwhile, liquidity position is considered adequate while leveraging remains low.

The ratings are dependent on the Company's ability to improve its margins and maintain prudent working capital and financial profile. Any negative movement in margins affecting the profitability and cash flows will impact the ratings. Meanwhile, improvement in profitability and governance framework will be favorable for the ratings.

#### Disclosure

<b>Name of Rated Entity</b>	C.A Textile Mills (Pvt.) Limited
<b>Type of Relationship</b>	Solicited
<b>Purpose of the Rating</b>	Entity Rating
<b>Applicable Criteria</b>	Methodology   Corporate Ratings(Jun-19),Methodology   Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria   Rating Modifier(Jun-19)
<b>Related Research</b>	Sector Study   Spinning(Sep-19)
<b>Rating Analysts</b>	Muhammad Hassan   muhammad.hassan@pacra.com   +92-42-35869504

## Profile

**Legal Structure** C.A. Textile Mills (Pvt.) Limited was incorporated in 2002 as a private limited company.

**Background** Ch. Salamat Ali acquired Naveed Textile in 2001, later on the Company was renamed as C.A. Textile.

**Operations** C.A. Textile is engaged in the production and marketing of cotton yarn and viscose yarn with an operational capacity of 40,584 spindles. The total energy requirement of the Company clocks in at ~4.75MW, met completely through captive power plant. Furthermore, the Company has LESCO connection as backup.

## Ownership

**Ownership Structure** C.A. Textile is a family owned venture. Shareholding is dominated by Ch. Salamat Ali with ~63% stake, while two other family members (Ali Wahid Cheema and Hina Wahid Cheema) have ~5% shareholding. The remaining shares ~32% are owned by Ch. Muhammad Atique Ur Rehman Cheema.

**Stability** Considerable positions in C.A. Textile are held by Ch. Salamat Family. Second generation is already in business, serving at various capacities. However, the transfer of ownership to the next generation is not documented.

**Business Acumen** C.A. Textile is the only textile Venture for Ch. Salamat Ali, formerly involved in Basmati Ghee business. However, he has developed expertise in spinning sector over time, providing requisite business acumen.

**Financial Strength** Apart from C.A. Textile, Ch. Salamat Ali owns multiple residential and business properties in Lahore. These are provided as collateral to procure short term financing for C.A. Textile, portraying enough financial strength to support business, if needed. Moreover, Ch. Muhammad Atique Ur Rehman Cheema, other major sponsor of C.A. Textile, is associated with Hino Motors Japan.

## Governance

**Board Structure** The Board of Directors comprises three members, with Ch. Salamat Ali as Chairman. All Board members are representative of the same family, reflecting sponsors' dominance and absence of independent oversight. Moreover, the positions of Chairman and CEO are occupied by the same person, indicating room for improvement in the governance framework of the Company

**Members' Profile** Ch. Salamat Ali – the Chairman – holds a Bachelors degree and carries with him over a decade of experience in textile spinning. The Board members have adequate know-how of the industry, which aids the Board in efficient decision making.

**Board Effectiveness** At present, there are no Board committees to assist the Board. However, informal meetings are carried out on a regular basis to discuss routine business matters. However, these are not formally documented.

**Financial Transparency** The external auditor of the Company, Anwar Tariq & Co. Chartered Accountants, expressed an unqualified opinion on the Company's financial statements for the year ended 30th June 2019. The auditor is QCR rated and placed in category 'C' on the SBP panel of auditors.

## Management

**Organizational Structure** Management control vests with the CEO – Ch. Salamat Ali – with defined reporting line to ensure smooth operations and efficiency. Moreover, the Company has four functional departments, with all departmental heads reporting directly to the CEO.

**Management Team** Ch. Salamat Ali has been associated with the Company since its incorporation. Meanwhile, Muhammad Nasarullah, Resident Director of C.A. textile has experience of more than four decades in textile sector, supplementing the capabilities and expertise of senior management.

**Effectiveness** Management meetings are held on need basis to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations.

**MIS** The Company has in place Oracle based Enterprise Resource Planning (ERP) system that provides comprehensive MIS reporting.

**Control Environment** C.A. Textile is a member of Better Cotton Initiative (BCI). Different portals are used to facilitate common business needs. Adequate data management and back-up policies are in place, to ensure smooth and sound operations.

## Business Risk

**Industry Dynamics** During FY19, exports stagnated despite major segments including cotton cloth, knitwear, garments and bedwear displaying strong quantitative growth. Industry players needed to share the benefit of the currency depreciation with their buyers, which resulted in 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. Recently, withdrawal of textile's zero rated status has impacted the industry's overall liquidity and local sales.

**Relative Position** C.A. Textile is small sized spinning entity, with minimal share in local spinning industry. However, the Company holds a sizable share in the viscose yarn market.

**Revenues** The Company's revenue emanates from the sale of yarn in the local market. The top line has shown growth over recent years, amounting to ~PKR 3,141mln in FY19, a ~16% increase YoY. The growth was mainly attributable to the addition of a new product line, i.e. viscose yarn. However, following the withdrawal of zero-rated status of the textile, many unregistered customers stopped purchase of viscose yarn. Consequently, the Company has once again shifted its product mix to include cotton yarn again as it can be sold to registered customers.

**Margins** The Company's gross margin showed slight YoY improvement in FY19 (FY19: ~6%, FY18: ~5%) as it was able to pass on some of the higher costs incurred on imported raw material to its customers. This translated into slightly improved operating margin of ~5% (FY18: ~4%). Finance cost witnessed an increase of ~60% YoY, amounting to ~PKR 50mln, due to the spike in interest rates over the year. While pre-tax profit showed an increase of ~41% YoY, amounting to ~PKR 99mln, deferred tax led to a significant increase in tax expense for the year (FY19: ~PKR 348mln, FY18: ~PKR 9mln). This led to a net loss of ~PKR 286mln for the year, compared to a profit of ~PKR 28mln in FY18.

**Sustainability** Going forward, the main focus of the Company will be on widening the market share in the local market owing to capitalize on increasing demand. Withdrawal of Zero rating status has lowered demand from unregistered customers which may impact profitability in FY20. Further, the rupee devaluation may keep the Company's margins under pressure, as C.A Textile is a net importer.

## Financial Risk

**Working Capital** The Company meets its working capital requirements through a mix of internal cash generation and short term borrowings. The Company's reliance on short-term borrowings increased in FY19 due to the currency devaluation, increasing the cost of imported viscose and yarn. While net cash cycle showed a decline of 5 days to stand at ~51 days, the Company's borrowing cushion at trade assets level deteriorated significantly, portraying narrow cushion for further borrowing.

**Coverages** The FCFO of the Company improved ~32% YoY to stand at PKR 142mln for FY19, driven by improved profitability. However, both the interest coverage and debt coverage ratios declined to stand at 3.7x (FY18: 4.4x) owing to increased finance cost incurred over the period. With no further hike in interest rates anticipated, coverages are unlikely to deteriorate.

**Capitalization** C.A. Textile has a low leveraged capital structure. Due to revaluation of fixed assets in FY19, leveraging declined YoY to stand at ~18% (FY18: ~27%), wholly comprising short term borrowing and Directors' loan. Further, in absence of any major capacity expansion in near future, the leveraging is expected to remain low.



C.A Textile Mills (Private) Limited Spinning	Jun-19 12M	Jun-18 12M	Jun-17 12M
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**A BALANCE SHEET**

1 Non-Current Assets	2,259	1,027	1,037
2 Investments	8	8	33
3 Related Party Exposure	33	33	-
4 Current Assets	667	594	565
a Inventories	486	419	398
b Trade Receivables	9	43	37
<b>5 Total Assets</b>	<b>2,967</b>	<b>1,662</b>	<b>1,635</b>
6 Current Liabilities	151	128	84
a Trade Payables	44	34	37
7 Borrowings	324	308	430
8 Related Party Exposure	49	67	-
9 Non-Current Liabilities	746	124	118
<b>10 Net Assets</b>	<b>1,697</b>	<b>1,035</b>	<b>1,003</b>
<b>11 Shareholders' Equity</b>	<b>1,697</b>	<b>1,035</b>	<b>1,003</b>

**B INCOME STATEMENT**

1 Sales	3,141	2,700	2,079
a Cost of Good Sold	(2,956)	(2,560)	(2,037)
<b>2 Gross Porfit</b>	<b>186</b>	<b>141</b>	<b>42</b>
a Operating Expenses	(38)	(38)	(34)
<b>3 Operating Profit</b>	<b>147</b>	<b>102</b>	<b>8</b>
a Non Operating Income	1	(1)	3
<b>4 Profit or (Loss) before Interest and Tax</b>	<b>148</b>	<b>102</b>	<b>12</b>
a Total Finance Cost	(50)	(31)	(27)
b Taxation	(384)	(43)	9
<b>6 Net Income Or (Loss)</b>	<b>(286)</b>	<b>28</b>	<b>(7)</b>

**C CASH FLOW STATEMENT**

a Free Cash Flows from Operations (FCFO)	170	129	30
b Net Cash from Operating Activities before Working Capital Changes	122	98	2
c Changes in Working Capital	(9)	(0)	(97)
<b>1 Net Cash provided by Operating Activities</b>	<b>113</b>	<b>97</b>	<b>(95)</b>
<b>2 Net Cash (Used in) or Available From Investing Activities</b>	<b>(54)</b>	<b>(47)</b>	<b>3</b>
<b>3 Net Cash (Used in) or Available From Financing Activities</b>	<b>(3)</b>	<b>(54)</b>	<b>77</b>
<b>4 Net Cash generated or (Used) during the period</b>	<b>56</b>	<b>(4)</b>	<b>(14)</b>

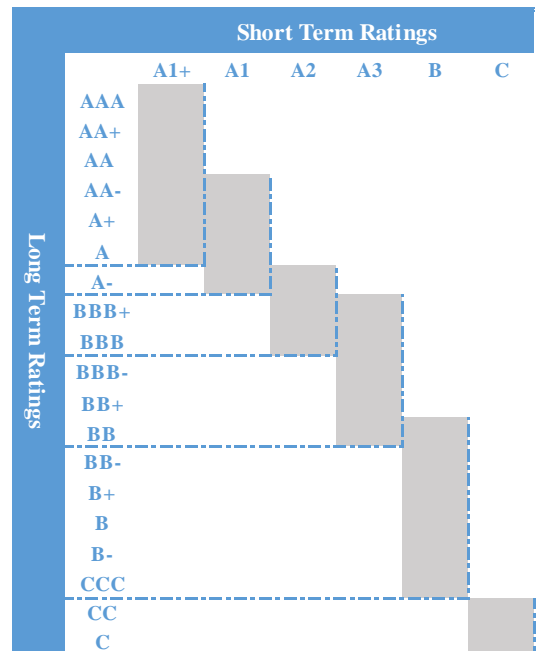
**D RATIO ANALYSIS**

<b>1 Performance</b>			
a Sales Growth (for the period)	16.3%	29.9%	-8.5%
b Gross Profit Margin	5.9%	5.2%	2.0%
c Net Profit Margin	-9.1%	1.0%	-0.3%
d Cash Conversion Efficiency (EBITDA/Sales)	6.6%	5.9%	3.0%
e Return on Equity (ROE)	-20.9%	2.7%	-0.7%
<b>2 Working Capital Management</b>			
a Gross Working Capital (Average Days)	56	61	73
b Net Working Capital (Average Days)	51	56	65
c Current Ratio (Total Current Assets/Total Current Liabilities)	4.4	4.7	6.7
<b>3 Coverages</b>			
a EBITDA / Finance Cost	4.5	5.5	2.5
b FCFO / Finance Cost+CMLTB+Excess STB	3.7	4.4	1.2
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.4	0.7	0.0
<b>4 Capital Structure (Total Debt/Total Debt+Equity)</b>			
a Short-Term Borrowings / Total Borrowings	18.0%	26.6%	30.0%
b Interest or Markup Payable (Days)	0.9	0.8	1.0
c Average Borrowing Rate	12.3%	7.2%	6.5%

## 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	
<b>AAA</b>	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	<b>A1+</b>	The highest capacity for timely repayment.
<b>AA+</b> <b>AA</b> <b>AA-</b>	<b>Very high credit quality.</b> 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.	<b>A1</b>	A strong capacity for timely repayment.
<b>A+</b> <b>A</b> <b>A-</b>	<b>High credit quality.</b> 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.	<b>A2</b>	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
<b>BBB+</b> <b>BBB</b> <b>BBB-</b>	<b>Good credit quality.</b> 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.	<b>A3</b>	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
<b>BB+</b> <b>BB</b> <b>BB-</b>	<b>Moderate risk.</b> 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>	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
<b>B+</b> <b>B</b> <b>B-</b>	<b>High credit risk.</b> 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>C</b>	An inadequate capacity to ensure timely repayment.
<b>CCC</b> <b>CC</b> <b>C</b>	<b>Very high credit risk.</b> 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.		
<b>D</b>	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.

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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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- 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)

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- (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)
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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)
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- (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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