The Pakistan Credit Rating Agency Limited

Rating Report

Kohat Textile Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
01-Jul-2022	A-	A2	Stable	Maintain	-
01-Jul-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	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect the moderate business profile of Kohat Textile Mills Limited (Kohat Textile). The Company caters to the needs of local industry and deals in specialized products i.e. polyester yarn, acrylic yarn, and viscose yarn. During 9MFY22, Company's revenue improved to PKR 3.3bln (9MFY21: PKR 2.5bln); sales are done locally. Margins and net profitability are enhanced attributable to favorable sector dynamics. In the current year, lower finance costs supported profitability. Non-core expenses emerged in 9MFY22 and should be contained going forward. The financial risk matrix reveals moderate leveraging with room for improvement in coverage. Further augmentation in core coverage will provide comfort with approaching scheduled principal repayments. The equity base recorded limited growth in the last few years due to restricted profitability and limited funds retained. The assigned ratings derive comfort from an experienced management team, the strong financial muscle of the Sponsors, and their timely support to the Entity in the form of subordinated loans. Going forward, the Company is planning to acquire debt to finance CAPEX. Material improvement in cash flows in line with upcoming debt obligations remains imperative. During 9MFY22 (Jul21-Mar22), Pakistan textile exports surged to $14.2bln (recording a growth of 25%) as compared to $11.3bln in the same period last year. This is attributable to an increase in demand for textile products internationally and the channeling of export orders toward the Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth. However, month on month basis, textile exports have declined by 3.5%.

The ratings are dependent on the Company's ability to sustain its operations in prevailing conditions. Significant deterioration in revenues and/or debt coverages due to the prolonged downturn leading to higher financial risk or subdued profitability will have a negative impact on the ratings. Saif Group's support of the Company will remain critical.

Disclosure	
Name of Rated Entity	Kohat Textile Mills 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 | Spinning(Sep-21)
Rating Analysts	Iram Shahzadi | iram.shahzadi@pacra.com | +92-42-35869504

Profile

Legal Structure Kohat Textile Mills Limited. (Kohat Textile) commenced operations in 1967 and was listed on Pakistan Stock Exchange in 1970.

Background Kohat Textile is the first textile venture of Saif Group, later on the Group expanded its presence in textile sector through Saif textile and Mediterranean Textile. The Company's production facilities are located in Kohat, KPK.

Operations Kohat Textile operates with a single spinning unit having a capacity of 38,460 spindles. The Company manufactures specialized yarn form polyester, viscose and acrylic. The Company caters its power needs via in-house production (4.22MW) which is sufficient for its energy requirement. Meanwhile, it has PESCO connection as an alternative source.

Ownership

Ownership Structure Kohat Textile's majority stake (77.98%) is owned by Saif Group, through Saif Holdings. The remaining shareholding rests with financial institutions (10.01%), general public (10.65%), joint stock companies & others (1.06%) and directors (0.31%).

Stability The representation of Saif Group's textile ventures in Pakistan's spinning industry remains critical. The Group has a holding company in place, portraying structured line of succession. However, the succession planning is not document yet.

Business Acumen Saif Group is one of the oldest medium-sized business conglomerate in Pakistan with considerable interests in textile. The sponsors have a presence of five decades in local Spinning industry, eventually developing expertise. However, the Group's growth in textile sector was limited but it has sustained through the volatility of textile industry.

Financial Strength Saif Group is one of the leading industrial and services conglomerates in Pakistan. The Group's interests lies in oil and gas exploration, power generation, textiles manufacturing, real estate development and health care services, through 7 subsidiaries and 4 associated companies across different sectors. Saif Group has a strong financial muscle and Sponsors are willing to support Kohat Textile, if needed.

Governance

Board Structure The board comprises seven members with major concentration of Saif Family members on board, including Chairman of BoD, Mr. Osman Saifullah Khan. The board constitutes five non-executive directors, one executive director, while one member is independent director.

Members' Profile Mr. Osman Saifullah – Chairman – holds a post graduate degree in engineering from University of Oxford and post graduate degree in business administration from University of Stanford. Mr. Osman has overall experience of over two decades in textile industry and he is also a senator. The board members have vast knowledge and expertise of textile industry, though diversity in experiences exists as well, ensuring a requisite skill mix for strategic planing.

Board Effectiveness Control of the board vests with Saif Group which ensures smooth operational control. Moreover, Audit and HR Committees are in place to assist the board on relevant matters. Despite presence on board of other Group companies their attendance has remained strong. Board meeting minutes were formally documented. Meanwhile, overall strategy of the Company is discussed in bi-annual meeting of Saif Group, whereas, operational matters are discussed in board meetings.

Financial Transparency M/s Shinewing Hameed Chaudri & Co., Chartered Accountants is the external auditor of the Company. The auditors have expressed an unqualified opinion on the financial reports for the periods ending June 2022.

Management

Organizational Structure Management control vests with Saif Group. Mr. Assad Saifullah – the CEO – With defined reporting line which ensures smooth flow of operations. Furthermore, the Company has five functional departments and all HoD's reporting directly to CEO.

Management Team Mr. Assad Saifullah - the CEO - has been associated with the Company for a decade. He is supported by a team of seasoned professionals, most of them have been associated with the Company for a reasonably long period of time.

Effectiveness There is no formal management committee, however, the Company maintains an adequate IT infrastructure and related controls. Additionally, the delegation of power by sponsors to management is considered positive for management effectiveness. The Company's MIS can be classified into two categories on the basis of periodicity – daily and monthly. The daily and weekly reports are generated for top management with main focus on production and liquidity position whereas P&L is discussed on need basis in the meetings.

MIS Kohat Textile has in place Microsoft Dynamics based Enterprise Resource Planning (ERP) system that provides comprehensive MIS reporting.

Control Environment Kohat Textile's plant is connected with head office through VPN, thereby reporting on real time basis. Moreover, international certifications includes ISO 9001:2015 and 45001:2018.

Business Risk

Industry Dynamics During 9MFY22 (Jul21-Mar22), Pakistan textile exports surged to $14.2bln (recording growth of 25%) as compared to $11.3bln in the same period last year. This is attributable to increase in demand for textile products internationally and channeling of export orders towards Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth. However, month on month basis, textile exports have declined by 3.5%. Going forward, the textile sector's outlook is expected to stay good in the medium term where demand for textile products is expected to sustain.

Relative Position Kohat Textile is one of the pioneer of Pakistan's spinning industry; though it has sustained through the market volatility and industry driven crises over the period of five decades but the growth in textile segment was limited. However, on standalone basis, Kohat Textile's share in local spinning industry is minimal.

Revenues During FY21, the Company's revenues surged by 40% and were recorded at PKR 3,620mln (FY20: PKR 2,591mln) due to the better prices of local yarn. The Company's revenues wholly comprises local yarn sales with adequate customer concentration. Despite an increase in cost of goods sold, the Company's gross profit improved to PKR 745mln as a result of the higher sales. While the 9MFY22, Company's revenue recorded at PKR 3,346mln (9MFY21: PKR 2,553mln).

Margins The incline in revenue is also reflected on the Company's margins. During FY21, gross profit margin rise to 20.6% (FY20: 8.2%) and operating profit margin to 16.8% (FY20: 4.1%). During 9MFY22, Company's gross and operating margin remain stagnant and clocked 18.0% (9MFY22: 17.6%) and 14.2% (9MFY22: 13.7%) respectively.

Sustainability Going forward, the Company is planning to acquire debt to finance CAPEX. Material improvement in cash flows in line with upcoming debt obligations remains imperative.

Financial Risk

Working Capital Working Capital requirement of Kohat Textile that emanates from financing receivables and inventory. The Company meet its requirements through short term borrowings. In FY21, the Company's Net working capital days decreased to 64days (FY20: 91days) on the back of decline in trade receivable days (FY21: 57days, FY20: 65days) and inventory days (FY21: 56days, FY20: 79days). During 9MFY22, the Company's net working capital days surged to 89 days owing to the increase in inventory days (84days).

Coverages The Company's FCFO witnessed a significant increase to PKR 654mln during FY21 (FY20: PKR 196mln) as the Company made a net profit in the period. This affected the coverages immensely, with interest coverage ratio improved to 6.1x (FY20: 1.1x) and operating coverage ratio to 1.9x (FY20: 0.8x). In 9MFY22, Company's interest coverage decreased and stood at 4.1x.

Capitalization The Company's leverage decreased during FY21 to 41.0% (9MFY22: 54.0%; FY20: 43.3%), mainly due to increase of 18% in equity. Furthermore, the Company's showed improvement in equity base over many last years has been minimal due to low profitability and stood at PKR 2,120mln in the 9MFY22 (FY21: PKR 1,949mln).

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Financial Summary
PKR mln

Kohat Textil Mills Limited Spinning	Mar-22 9M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	3,480	2,930	2,481	2,353
2 Investments	3	2	2	3
3 Related Party Exposure	-	-	-	-
4 Current Assets	2,307	1,300	1,129	1,159
a Inventories	*1,342*	*714*	*399*	*668*
b Trade Receivables	*864*	*513*	*610*	*308*
5 Total Assets	5,789	4,232	3,612	3,514
6 Current Liabilities	758	589	461	432
a Trade Payables	*683*	*564*	*411*	*330*
7 Borrowings	2,415	1,277	1,163	985
8 Related Party Exposure	74	82	103	103
9 Non-Current Liabilities	421	335	234	286
10 Net Assets	2,120	1,949	1,651	1,708
11 Shareholders' Equity	2,120	1,949	1,651	1,708
B INCOME STATEMENT				
1 Sales	3,346	3,620	2,591	2,966
a Cost of Good Sold	*(2,742)*	*(2,875)*	*(2,378)*	*(2,656)*
2 Gross Profit	604	745	213	310
a Operating Expenses	(128)	(137)	(108)	(96)
3 Operating Profit	476	607	105	214
a Non Operating Income or (Expense)	*(25)*	*(29)*	*(1)*	*(12)*
4 Profit or (Loss) before Interest and Tax	451	579	104	202
a Total Finance Cost	*(127)*	*(112)*	*(181)*	*(116)*
b Taxation	*(132)*	*(154)*	*12*	*(19)*
6 Net Income Or (Loss)	192	312	(65)	67
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*497*	*654*	*196*	*273*
b Net Cash from Operating Activities before Working Capital	*407*	*527*	*28*	*176*
c Changes in Working Capital	*(885)*	*(78)*	*28*	*(80)*
1 Net Cash provided by Operating Activities	(478)	449	56	96
2 Net Cash (Used in) or Available From Investing Activities	(626)	(539)	(207)	(101)
3 Net Cash (Used in) or Available From Financing Activities	1,108	83	157	4
4 Net Cash generated or (Used) during the period	3	(7)	6	(2)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	23.2%	39.7%	-12.7%	32.2%
b Gross Profit Margin	18.0%	20.6%	8.2%	10.5%
c Net Profit Margin	5.7%	8.6%	-2.5%	2.3%
d Cash Conversion Efficiency (FCFO adjusted for Working C	-11.6%	15.9%	8.6%	6.5%
*e Return on Equity [Net Profit Margin * Asset Turnover * (T*	12.6%	17.3%	-3.9%	5.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	140	113	144	110
b Net Working Capital (Average Days)	89	64	91	75
c Current Ratio (Current Assets / Current Liabilities)	3.0	2.2	2.4	2.7
3 Coverages				
a EBITDA / Finance Cost	4.4	6.4	1.2	2.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.7	1.9	0.8	1.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fi	2.4	1.7	34.9	2.4
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equit	54.0%	41.0%	43.3%	38.8%
b Interest or Markup Payable (Days)	129.0	77.3	84.1	95.9
c Entity Average Borrowing Rate	9.3%	8.0%	14.6%	10.3%

Credit Rating

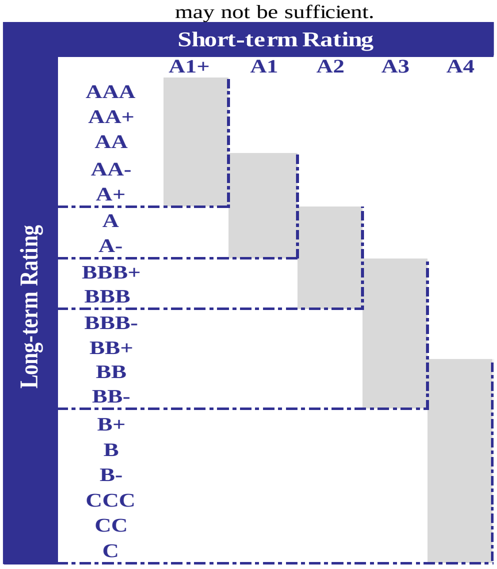
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

Entities

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

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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 | 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)

Proprietary Information