The Pakistan Credit Rating Agency Limited

Rating Report

Nishat Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
15-Nov-2018	AA	A1+	Stable	Maintain	-
25-Apr-2018	AA	A1+	Stable	Maintain	-
30-Jun-2017	AA	A1+	Stable	Maintain	-
27-Sep-2016	AA	A1+	Stable	Maintain	-
28-Oct-2015	AA	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect diversity of Nishat Mills underlying businesses, along with a conservative capital structure. This emanates from its implicit holdco structure within Nishat Group, providing resilience to adversities in underlying sectors, particularly textile, while upholding the overall profile of Nishat Mills. Significant as well as diverse strategic investment portfolio of the company generates a regular dividend stream. However, the current stock market volatility remains critical. Nishat Mills is one of the market leaders in textile industry, maintaining a sizeable, export-oriented composite unit in the country's textile sector. Superior profile is characterized by requisite diversification, in terms of both geography and customer base. However, re-imposition of custom duties and sales tax on cotton & yarn imports, coupled with inflated interest rates has stretched the textile industry. Meanwhile, the rupee devaluation has provided a requisite breather to the company to sustain its business margins. The management is focusing on capitalizing enhanced facilities in order to achieve overall cost efficiencies.

The ratings are dependent on the company's ability to sustain its profitability. Low leveraged capital structure provides room for expansion; should be managed prudently. Moreover, induction of independent members on board for better governance is considered important.

Disclosure

Name of Rated Entity	Nishat Mills 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	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

Profile

Legal Structure Nishat Mills Ltd. (Nishat Mills) a listed concern, commenced operations in 1951. The company is engaged in textile manufacturing process – spinning, combing, weaving, bleaching, dyeing, printing and stitching.

Background Nishat Mills is associated with Nishat Group since its inception. Nishat Group is one of the renowned business conglomerates in Pakistan.

Operations Nishat Mills' current operational capacity comprises 238,032 Spindles, 794 Looms, 4 Rotary Printing Machines, 8 Digital Printing Machine, 5 Thermosole Dyeing and 4,239 Stitching Machines. Overall, Nishat Mills has 32 manufacturing units each specializing in a specific product range. The company caters its power needs via in-house production with cumulative capacity standing at (130 MW), as well as NTDC connections.

Ownership

Ownership Structure Nishat Mills is the flagship company of Nishat Group. The Mian Mansha family collectively own majority (~51%) shares of the company directly through individuals (~42%) and group companies (~8%). Remaining (~49%) stake is spread among financial institutions, companies, and the general public.

Stability The considerable positions in Nishat Mills are held by Mansha family. Moreover, the next generation is already in business, serving at various capacities in Nishat Group.

Business Acumen Nishat Mills is among the pioneer of advance textile manufacturers of Pakistan, with almost seven decades of textile production; growing in capacity against all odds, securing Nishat Mill’s leading position in local market.

Financial Strength Nishat Group is one of the most distinguished business groups in Pakistan. The Group - maintains substantial presence in the country's financial sector, and strong foothold in textile, cement, power sectors, dairy and hospitality sector. Recently, the group has entered in Pakistan's automobile assembly industry.

Governance

Board Structure The board comprises seven members; two directors are representatives of sponsoring family– including the Chairman – Mr. Hassan Mansha and CEO. The remaining directors include, one independent member, one Nishat Mill’s executive director, while all other members are non-executive directors working with Nishat Group entities.

Members’ Profile Board members have diversified experience, and relatively long association with the company. The Chairman of board – Mr. Hassan Mansha, carries experience of over two decades in textile value chain.

Board Effectiveness Control of the board vests with Nishat Group, with high proportion of Nishat Group executives on the board, though enhances quality, but undermines independence of the board. Meanwhile, Audit and HR committees are in place to assist the board on relevant matters.

Financial Transparency M/s. Riaz Ahmad & Company, Chartered Accountants is the external auditor of the company. The auditors have expressed unqualified opinion on the financial reports for the year ended 30th June, 2018.

Management

Organizational Structure Management control vests with Nishat Group, with well-defined reporting line to ensure smooth operations and excellence.

Management Team Mr. Umer Mansha – the CEO– primarily manages the company’s affairs, supported by a team of seasoned professionals. Mr. Umer Mansha is associated with the company since 1994.

Effectiveness The company’s management meetings are held on periodic basis to ensure efficiency and strategic planning. The management tier ensures effective delegation of functional responsibility across various departments, facilitating a smooth flow of operations.

MIS Nishat Mills deploys Oracle based Enterprise Resource Planning (ERP) system that provides comprehensive MIS reporting.

Control Environment The company is accredited with International certifications for compliance. Nishat Mills has valid certificates for its products and facilities and is periodically audited by internationally recognized certification bodies.

Business Risk

Industry Dynamics During FY18, total textile exports of Pakistan stood at USD ~ 13.53bln, a 9% YoY growth. Re-imposition of custom duty and sales tax on cotton imports in FY19 budget, coupled with exclusion of tax rebate on yarn and greige fabric has further stretched the industry margins. However, rupee devaluation in recent times provide breather to textile ventures with net exports.

Relative Position Nishat Mills is the single largest composite textile unit in Pakistan with considerable representation, throughout textile value chain. Moreover, the company is leading exporter with ~2% (FY18) share in country’s total textile exports.

Revenues During FY18, the company’s revenues clocked in at PKR 53.7 bln, posting a growth of ~9%, with major contribution from Processing & Home textile (P&HT) segment, followed by weaving, spinning and garment segments. The share of exports in total revenue declined to 72% (FY17: 74.5%) with the top three exporting regions being Asia & Africa (49%) and Europe (~42%).

Margins The company’s gross margins slightly deteriorated (FY18: 10.3%, FY17: 10.9%), as cost of goods sold increased by ~9.8% - due to higher raw material and energy costs, followed by stable operating margin (FY18: 3.8%, FY17: 3.8%). The continuous inflow of dividend income from equity investment (FY18: PKR 3,391 mln, FY17: PKR 3,404 mln) supplement the profitability; comprising ~83% of net profits. However, increase in finance cost by ~8.6% has resulted in declined profitability (FY18: PKR 4,097 mln, FY17: PKR 4,262 mln).

Sustainability Nishat Mills' maintains a hefty investment portfolio (PKR 51,626mln) – ~68% of equity at end-June18, mainly comprising strategic holdings (PKR 47,339mln). With presence in diversified sectors, the company has prudently managed its overall risk profile. Moreover, continuous BMR in recent times has resulted in better capitalization of market with improved efficiency.

Financial Risk

Working Capital The company meets its working capital requirements through a mix of internal cash generation and short term borrowings. During FY18, company’s working capital management improved, as reflected from better gross and net working days (FY18: 106days, FY17: 108days) and (FY18: 76days, FY17: 78days), respectively.

Coverages Sizeable FCFO (PKR 3,745mln), topped up with strong cashflows from investment (PKR 3,571mln); remain at same level portraying stable interest and debt coverages (FY18: 3.8x; FY17: 4.0x) and (FY18: 1.2x; FY17: 1.0x), respectively. Meanwhile, dividend income from investment has supplemented the total cashflows, reflected from strong total debt coverage (FY18: 2.3x; FY17: 2.0x). Going forward, recent hike in interest rate will stretch the coverages.

Capitalization Nishat Mills has a low-leveraged capital structure ~ 20.8% (end-Jun18; 20%), out of total leveraging ~73% (end-Jun18; 76.2%) of debt comprises current debt.

The Pakistan Credit Rating Agency Limited

Textile

Financials (Summary)

PKR mln

Nishat Mills Limited

BALANCE SHEET	30-Jun-18	30-Jun-17	30-Jun-16
	FY	FY	FY
Non-Current Assets	**28,471**	**28,057**	**24,877**
Investments (Incl. Associates)	**51,626**	**68,354**	**61,661**
Equity	47,339	62,544	57,464
Loans to Associates/Debt Securities	3,823	5,343	3,724
Investment Property	465	467	473
Current Assets	**22,639**	**21,119**	**20,061**
Inventory	12,244	12,723	9,934
Trade Receivables	4,030	2,246	2,253
Others	6,365	6,151	7,874
Total Assets	**102,736**	**117,530**	**106,599**
Debt/Borrowings	**19,843**	**22,036**	**17,086**
Short-term	12,508	14,697	10,476
Long-term (Incl. Current Maturity of Long-Term Debt)	7,336	7,339	6,610
Other short-term liabilities	6,608	5,948	7,097
Other long-term liabilities	572	783	262
Shareholders' Equity	**75,713**	**88,763**	**82,155**
Total Liabilities & Equity	**102,736**	**117,530**	**106,599**

INCOME STATEMENT			
Turnover	**53,729**	**49,248**	**47,999**
Gross Profit	5,550	5,380	6,264
Net Other Income	3,913	4,052	3,762
Financial Charges	(994)	(915)	(1,046)
Net Income	**4,097**	**4,262**	**4,923**

Cashflow Statement			
Free Cash Flow from Operations (FCFO)	3,745	3,668	4,163
Net Cash changes in Working Capital	(596)	(4,129)	1,696
Net Cash from Operating Activities	5,725	2,157	8,517
Net Cash from Investing Activities	(1,719)	(7,428)	(3,077)
Net Cash from Financing Activities	(3,944)	3,201	(3,378)

Ratio Analysis			
Performance			
Turnover Growth (vs. SPLY)	9%	3%	-6%
Gross Margin	10%	11%	13%
Net Margin	8%	9%	10%
Coverages			
Interest Coverage (FCFO/Gross Interest)	3.8	4.0	4.0
Core: (FCFO) / (Gross Interest+CMLTD+Uncovered Total STB)	1.2	1.0	1.4
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	2.3	2.0	2.6
Debt Payback (Total LT Debt Including Uncovered Total STBs) / (FCFO- Gross Interest	2.7	2.9	2.1
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	75.7	78.1	74.0
Capital Structure (Total Debt/Total Debt+Equity)	21%	20%	17%

Rating Scale

Credit Rating Scale & Definitions

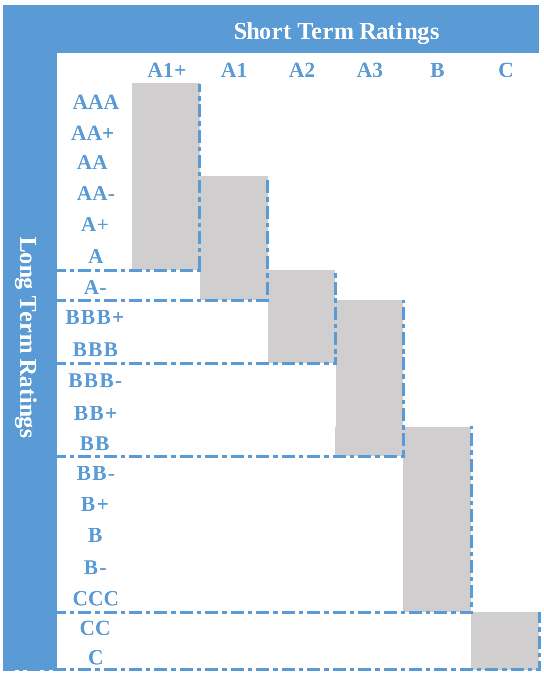
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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 Ratings

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.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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 surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

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)

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)
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