The Pakistan Credit Rating Agency Limited

Rating Report

Allawasaya Textile & Finishing Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Mar-2022	BBB	A2	Stable	Upgrade	-
26-Apr-2021	BBB-	A3	Stable	Maintain	Yes
30-Apr-2020	BBB-	A3	Stable	Maintain	Yes
30-Oct-2019	BBB-	A3	Stable	Maintain	-
30-Apr-2019	BBB-	A3	Stable	Maintain	-
28-Dec-2018	BBB-	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan is the fourth-largest producer of cotton in the world. Punjab is of special importance in this regard as about 80% of the total production is produced in Punjab. This year, the cotton crop is being cultivated on about 4 million acres, which is expected to yield an average of more than 17 million per acre. The Punjab government is providing Rs. 1,000 per bag of approved varieties of seeds and whitefly protection to cotton growers for an area of more than 200,000 acres at a subsidy of Rs. 4.4 billion. The approved BT varieties of cotton are IUB 13, MNH 886, BS 15, Niab 878, and FH 142 while other approved varieties for specific districts should be selected in consultation with local agronomists.
Allawasaya Textile and Finishing Mills's (the Company) is involved in the manufacturing and sale of PC Yarn, PV Yarn which is man-made fiber & CVC Yarn. The upgrade reflects the partial completion of the planned expansion as well as an improvement in the financial risk profile. Due to better yarn prices in the local market, the Company's topline grew by double digits in FY21. Similarly, the company's total profitability profile increased in FY21, owing to better gross margins, mostly due to inventory increases. In the medium term, however, rising interest rates on short-term operating funds are likely to be a drag on the Company's profitability. The financial risk matrix performed reflects notable improvement comprising improved cash cycle, healthy gross coverage, and decline in leveraging. Going forward, the Company is planning to acquire debt to finance Planned capacity expansion. Material improvement in cash flows in line with upcoming debt obligations remains imperative.

The ratings are dependent upon the sponsor support and management's ability to improve margins, profitability and the Company's competitive position in the industry. This includes keeping the debt levels manageable. Any further deterioration in margins or coverages will have a negative impact on the ratings.

Disclosure	
Name of Rated Entity	Allawasaya Textile & Finishing 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 Allawasaya Textile & Finishing Mills Limited is a listed entity on the Pakistan Stock Exchange.

Background The Company was established in 1958 as a single unit of spinning in Multan. The Company is engaged in the production and sale of cotton yarn and made fibers.

Operations The Company currently operates with 38,712 spindles under a single spinning unit in Multan and has the capacity to produce 15.3mln kgs of yarn annually. The Company is self-sufficient in energy and has an in-house production capacity of 4.2MW and a 3.5MW total electricity demand.

Ownership

Ownership Structure The Company is owned by three established business families of Multan. Namely i) Tauqir Family (38%) ii) Jamil Family (36%) and Maqbool Family (25%).

Stability The sponsor families are all related and the third generation of the Jamil and Tauqir families has already joined the Company. However, no formal succession plan has been documented.

Business Acumen Besides the Company, sponsor families have investments in seed oil extraction, ginning, value-adding segments of the textile industry and other spinning companies.

Financial Strength Out of three sponsor families, i) Maqbool Family has investments in other textile companies and hospitality sector, ii) Tauqir family has a diverse portfolio of investments in a number of other textile companies and the iii) Jamil family has a 100% stake in Allawasaya Spinning Mills Pvt Ltd. Cumulatively, the sponsors have enough financial strength to support the Company, if a need arises.

Governance

Board Structure Eleven-member board is comprised of representatives from sponsor families and two independent directors. Despite a good mix of executive and nonexecutive members, sponsor domination on the board undermines the governance structure. Mrs. Nusrat Jamil, a member of Jamil family is the Chairman of the board.

Members' Profile All the board members are highly qualified in different disciplines and carry ample experience in textile as well as other industries. Chairman, Mrs. Nusrat Jahan, has been affiliated with the board for two years. Mian Jamil (Jamil Family) is a textile engineer and carries 45 years of industry experience. Mian Tanvir Ahmad Sheikh (Maqbool Family) has an overall experience of over 36 years. Mian Tauqir Ahmed Sheikh (Tauqir Family) is an MBA and acts as a non-executive director on the board. Other board members also possess years of industry relevant experience.

Board Effectiveness In line with the guidelines of the corporate governance best practices, the board is supported by an i) Audit Committee and ii) HR & Remuneration committee. However, the quality of board minutes still has room for improvement.

Financial Transparency M/s M. Yousaf Adil & Co. Chartered Accountants (Deloitte) are the external auditors of the Company. The auditors have issued an unqualified opinion on the company's financial statements for the period ending 30th June 2021. They have performed an interim review on the financial statements for the six months ending December 2021.

Management

Organizational Structure The organization structure of the Company is divided into four main departments namely i) Finance, Admin & Procurement ii) Audit & Planning iii) Sales & Marketing and iv) Production. The Chairman overseas production while the CEO looks after finance, admin & procurement. All other departments are headed by executive directors.

Management Team Mian Tanvir, the Company's CEO did his MBA from USA and has diverse professional experience, spanning over 38 years. All other members of the management team are also well qualified and experienced.

Effectiveness All department heads have access to MIS to generate reports, relevant to their departments. Management frequently meets to discuss any issues affecting the smooth flow of business operations, however, there are no management committees.

MIS The Company has developed an in-house ERP system to cater to the needs of the business. Senior management, including the CEO and Chairman monitor the business performance through certain key MIS reports.

Control Environment Production is completely order driven. The QC and HSE departments seem appropriate. The Company is ISO 9001 and ISO 14001 certified.

Business Risk

Industry Dynamics During the period July-December FY21-22, textile exports surged 26 percent YoY, fielding $9.39 billion in total export remittances, as compared to $7.44 billion 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 value-added textile items increased in both quantity and value in December 2021. Going forward, the textile sector's outlook is expected to stay positive in the medium term where the demand for textile products is expected to sustain. In the local market, the textile sector has recorded strong performance. The relief measures introduced by the State Bank of Pakistan such as deferment of loan payments for one year, low-interest rates, and salary refinance scheme also provided comfort to the sector. Many players have also availed the TERF scheme announced by the Central Bank. This will lead to overall leverage of the sector to increase; however, on relaxed financing rates. The sustainability of demand pattern for the current higher orders from Europe and USA remains essential for the feasible utilization of added capacity by textile players.

Relative Position Allawasaya Textile and Finishing's position in Pakistan Spindle capacity is considered small. However, combined with the spindle capacity of Allawasaya Spinning Mills Limited (38,232 Spindles), this share increases to a moderate extent but still remains lower than other similar groups in the spinning industry. Going Farward, the Company is planning to start a BMR, which will add 12,000 Spindles to existing capacity.

Revenues During FY21, the Company's revenue showed an increase of 33% and clocked in at PKR 3,547mln (FY20: PKR 2,657mln) due to better yarn prices in the local market. The Company's revenues wholly comprise local yarn sales with adequate customer concentration. On the other side Company also improved its revenues in the 1HFY22 by 42% stood at PKR 2,357mln (1HFY21: PKR 1,656mln).

Margins During FY21, the Company's gross profit margin witnessed improvement from FY20 to 10.2% (FY20: 6.7%) and operating profit margin to 7.8% (FY20: 3.9%) due to lower personnel cost, higher revenue. The finance cost of the Company decreased to PKR 51mln in FY21 (FY20 PKR 78mln). The Company's profitability showed witnessed improvement by 867% and was recorded at PKR 145mln (FY20: PKR 15mln), indicating an improving trend in profitability. During 1HFY22, the Company's gross profit margin and operating profit margin reported at 10.5% and 8.0% respectively.

Sustainability In line with improving business environment, the Company is planning to start a BMR, which will add 12,000 Spindles to existing capacity and also installing NCS machines. BMR is expected to bring in efficiency gains, lowering cost per spindle and will consequently improve margins.

Financial Risk

Working Capital During FY21, the Company's working capital requirement has deteriorated which is evident from the decrease in net working capital days (FY21: 60 days, FY20: 64days). The reasons behind this decrease were the higher amount of i) inventory PKR 271mln (FY20: PKR 538mln). Furthermore, room-to-borrow at the trade level increased (FY21: PKR 387mln; FY20: PKR 124mln) due to both; a contraction in short-term borrowing (FY21: PKR 207mln; FY20: PKR 514mln) and a decrease in net trade assets (FY21: PKR 637mln; FY20: PKR 835). During 1HFY22, the Company's net working capital days slightly increase to 64 days.

Coverages The company's cash flows from operations – a factor of its profitability has witnessed a significant increase (FY21: PKR 277mln, FY20: PKR 124mln) because of the higher EBITDA. This impact showed positivity on the coverages immensely, with interest coverage ratio during FY21 rising up to 5.6x (FY20: 1.6x) and debt coverage ratio to 1.8x (FY20: 1.2x).

Capitalization The Company's leverage decreased during FY21 to 27.0% (FY20: 39.6%), mainly due decrease in its borrowings. Short-term borrowings, which make up 45% of the total borrowings (FY21: PKR 462mln, FY20: PKR 724mln) increased to PKR 207mln (FY20: PKR 514mln), and long term borrowings clocked in at PKR 151mln (FY20: PKR 179mln).

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Financial Summary
PKR mln

Allawasaya Textile and Finishing Mills Limited	Dec-21	Jun-21	Jun-20	Jun-19
Spinning	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	1,527	1,395	1,426	1,435
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	1,609	724	931	650
a Inventories	*656*	*271*	*538*	*292*
b Trade Receivables	*496*	*332*	*248*	*215*
5 Total Assets	3,136	2,119	2,357	2,085
6 Current Liabilities	366	238	412	326
a Trade Payables	*61*	*35*	*192*	*174*
7 Borrowings	1,314	462	724	521
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	134	170	118	149
10 Net Assets	1,323	1,249	1,104	1,089
11 Shareholders' Equity	1,323	1,249	1,104	1,089
B INCOME STATEMENT				
1 Sales	2,357	3,547	2,657	2,091
a Cost of Good Sold	*(2,111)*	*(3,184)*	*(2,481)*	*(1,992)*
2 Gross Profit	247	363	177	99
a Operating Expenses	(57)	(85)	(74)	(71)
3 Operating Profit	190	278	103	27
a Non Operating Income or (Expense)	*(11)*	*(10)*	*(2)*	-
4 Profit or (Loss) before Interest and Tax	179	268	101	27
a Total Finance Cost	*(36)*	*(51)*	*(78)*	*(37)*
b Taxation	*(41)*	*(71)*	*(8)*	*(7)*
6 Net Income Or (Loss)	102	145	15	(16)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*133*	*277*	*124*	*20*
b Net Cash from Operating Activities before Working Capital Changes	*111*	*218*	*46*	*(3)*
c Changes in Working Capital	*(776)*	*39*	*(204)*	*10*
1 Net Cash provided by Operating Activities	(666)	256	(158)	7
2 Net Cash (Used in) or Available From Investing Activities	(154)	(16)	(39)	(270)
3 Net Cash (Used in) or Available From Financing Activities	826	(261)	529	518
4 Net Cash generated or (Used) during the period	6	(21)	332	255
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	32.9%	33.5%	27.1%	-3.6%
b Gross Profit Margin	10.5%	10.2%	6.7%	4.7%
c Net Profit Margin	4.3%	4.1%	0.6%	-0.8%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	-27.3%	8.9%	-3.0%	1.5%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	15.8%	12.4%	1.4%	-1.7%
2 Working Capital Management				
a Gross Working Capital (Average Days)	68	71	89	78
b Net Working Capital (Average Days)	64	60	64	61
c Current Ratio (Current Assets / Current Liabilities)	4.4	3.0	2.3	2.0
3 Coverages				
a EBITDA / Finance Cost	6.2	6.6	2.1	2.0
b FCFO / Finance Cost+CMLTB+Excess STB	1.6	1.8	1.2	0.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.6	1.1	4.4	-12.8
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	49.8%	27.0%	39.6%	32.4%
b Interest or Markup Payable (Days)	124.8	76.4	87.9	195.5
c Entity Average Borrowing Rate	8.4%	7.7%	12.8%	8.8%

Credit Rating

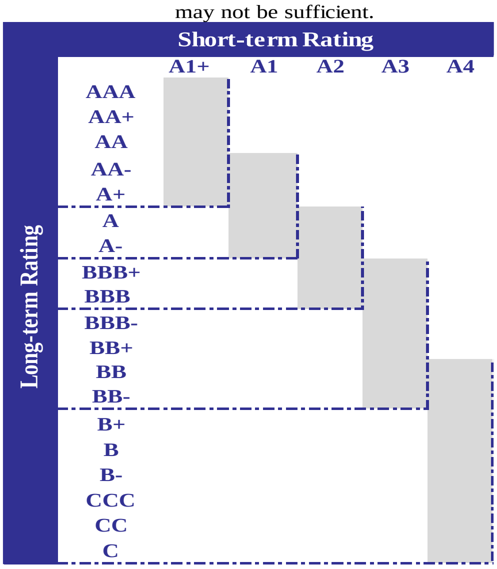
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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.
(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