The Pakistan Credit Rating Agency Limited

Rating Report

Masood Spinning Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Mar-2022	A-	A2	Stable	Upgrade	-
07-Apr-2021	BBB+	A2	Stable	Maintain	Yes
12-May-2020	BBB+	A2	Stable	Initial	Yes

Rating Rationale and Key Rating Drivers

Masood Spinning Mills Limited (‘Masood Spinning’ or ‘The Company’) is a public unlisted limited company. The Company is part of Mahmood Group, one of the leading textile conglomerates in the country. The Company is engaged in manufacturing 0-40 count yarn (coarse yarn) and fine count yarn. With the capacity enhancement, the topline and margins in 1HFY22 have posted strong improvement and the management expects the topline growth to remain strong in FY22. The topline primarily consists of exports. The Company mainly exports to Europe and China, with China responsible for buying more quantities. The risk of geographic concentration in Europe is considered manageable, however, client-wise concentration has remained on the higher side. Locally, the Company mostly sells to large-sized and registered customers. The financial risk matrix is reflecting good coverage, stable working capital cycle, and high leveraging. Organic growth in the equity base is positive. Going forward, the planned BMR is expected to bring in efficiency gains and healthy margins.
During the period July-December FY21-22, textile exports of the country 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 an increase in demand for textile products internationally and the 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 Company's association with Mahmood Group and vast experience of sponsors remain important rating factors. The ratings are dependent upon the management’s ability to improve margins, profitability, and financial profile of the Company. This includes keeping the debt levels manageable and improve the Company’s competitive position in the industry. Sponsor’s support and business acumen remain important for the ratings.

Disclosure

Name of Rated Entity	Masood Spinning 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 Masood Spinning Mills Limited ('Masood Spinning' or 'The Company') is a public unlisted limited concern. The Company has been operating since June 2000.

Background The Company is a part of Mahmood Group which started operations in 1935 and has since evolved into a diversified business empire. Masood Spinning Mills Limited was incorporated in 2000.

Operations The Company has three production units. Unit 1 and Unit 2 are located in Kabirwala in Khanewal district near the Company's head office in Multan. Unit 3 is located in Phool Nagar in Kasur district. All three units have a collective capacity of 98,784 spindles. The Company's total electricity requirement stands at 14.6 M.W which is met through captive generation. Additionally, the Company also has a backup line from LESCO and MEPCO to meet unforeseen energy needs.

Ownership

Ownership Structure Masood Spinning is 100% owned by Mahmood Group directly, through individuals and associated companies. Ownership is equally divided between the three families of Khawaja M. Masood (Late).

Stability The group has a clearly defined shareholding among the three brothers. Clarity among brothers with regards to operations of the group companies bodes well with stability of the Group and Masood Spinning. However, documentation of the succession plans would bring further clarity to the stability of ownership.

Business Acumen All three brothers are equipped with well-rounded experience in the textile industry. Each has over forty years of experience in running the businesses of the group. The third generation of sponsors is already actively involved in running the operations of different group companies and possesses relevant knowledge and capabilities.

Financial Strength Mehmood Group maintains a strong financial profile with an equity base of PKR 17.2bln at end-Jun21, as well as, well-diversified businesses through its multiple group companies. The Company ratings comfort from sponsors' ability and willingness to support it, in case the need arises.

Governance

Board Structure Oversight of the Company lies with an eight-member board, which includes both the Chairman and the CEO.

Members' Profile Mr. Khawaja Muhammad Iqbal – a Chairman, has over four decades of textile experience. He has held key positions in various local corporate bodies of Pakistan. Other directors' expertise in various stages of textile value-chain leads to a good skill mix overall board.

Board Effectiveness Board meetings have full attendance of directors, boding well for the board's effectiveness. Meanwhile, minutes are recorded properly, although, there is still some room for improvement. There are two sub-committees in place: Audit Committee and Human Resource Committee.

Financial Transparency M/s Yousaf Adil & Co. Chartered Accountants are the external auditors of the Company. The auditor is listed in Category "A" of the State Bank's panel of auditors. The auditors have issued an unqualified opinion on the company's financial statements for the period ended 30th June 2021.

Management

Organizational Structure The Company essentially operates in two distinct divisions before delegating strategic decisions to one overseeing body. At this highest level, departments are as follows: (i) Audit, (ii) Taxation, (iii) HR and Admin, (iv) IT and ERP, (v) Export and Import, (vi) Purchase & Production, (vii) Corporate affairs, (viii) Marketing and (ix) Finance.

Management Team The Company CEO – Mr. Khawaja M. Younus – has over four decades of experience in the textile sector. He also sits on the board of various group companies. Mr. Younus is supported by a team of seasoned professionals. Mr. Muhammad Anees s/o Mr. Khawaja Muhammad Younus and Mr. Khawaja Muhammad Mehr s/o Mr. Khawaja Muhammad Ilyas look after day-to-day operations of Kabirwala (unit 1 & 2) and Phool Nagar (unit 3) facilities respectively.

Effectiveness The division of duties among the management is clearly defined. While there are no formal management committees, the Company maintains adequate IT infrastructure and related controls for smooth running of operations.

MIS Masood Spinning Mills Limited implemented an Oracle-based ERP solution – Oracle EBS – in 2008 with multiple operational modules.

Control Environment The Company is following the latest quality assurance standards for the production and trade of yarn. On an operational level, samples of cotton and yarn are tested for quality under the laboratories of each unit.

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 Overall, Mahmood Group has a strong presence in the country's textile sector, while Masood Spinning Mills Limited with 98,784 spindles is also adequately positioned. Going Forward, the Company is planning to start a BMR, on Unit 3 is located in Phool Nagar.

Revenues The Company manufactures and sells a wide range of yarn. During FY21, Masood Spinning's topline rise by 26% to PKR 17,355mln (FY19: PKR 13,759mln) due to the better yarn prices, both locally and internationally. The topline primarily consists of exports. The exports increased by PKR 2.9bln YoY to clock in at PKR 14.2bln, which primarily consists of Indirect exports – Yarn of PKR 8.4bln. In 1HFY22, the Company recorded a revenue of PKR 10.99bln (1HFY20: PKR 7,735mln), an increase of 7% period on period. During this period, exports constituted 80% of total sales at PKR 8,790mln.

Margins During FY21, the Company's gross margin increased to 13.7% (FY20: 6.2%) on the back of improved revenue. Despite the increase in expenses, the operating profit margin improved to 11.2% (FY20: 3.8%) . Margins witnessed improvement in 1HFY22. Gross profit margin increased to 22.4% and operating profit margin to 18.5%, in line with the increase in revenue fueled by better yarn prices, both locally and internationally.

Sustainability The Company will invest PKR 400mln in a number of projects such as; Solar System, AC Plant, and up-gradation of existing machinery during FY21. The Company also has planned to invest PKR 500mln in FY22 and PKR 420mln in FY23 to further upgrade the existing three production units.

Financial Risk

Working Capital During FY21, the Company's net working capital cycle days showed a slight increase to 145days (FY20: 144days) because of an increase in receiveable days (FY21 44days; FY20: 39days). Short-term trade leverage during FY21, improved to 11% (FY20: -7%) due to some increase in net trade assets. Net working cycle decreased to 142days in 1HFY22.

Coverages During FY21, Masood Spinning's free cash flows (FCFO) up by 174% to PKR 1,988mln (FY20: PKR 726mln) due to the higher EBITDA. Due to the increase in FCFO, the Company's interest coverage ratio also increased to 2.5x (FY20: 0.8x) and debt coverage ratio 1.4x (FY20: 0.7x); also attributable to a decrease in finance cost. FCFO in 1HFY22 increased to PKR 1,486mln (1HFY21: PKR 618mln) and the interest coverage ratio also witnessed improvement at 3.4x while the debt coverage ratio recorded at 2.5x.

Capitalization At end-Jun21, the Company had a highly leveraged capital structure with a leveraging ratio of 74% (FY20: 78%). The leveraging ratio increased year-on-year as the Company's borrowings increased to PKR 9,563mln (FY20: PKR 9,142mln) mainly due to a rise in short-term borrowings. The majority portion of debt comprised short-term borrowings (72%) from various commercial banks. Leveraging ratio almost remained stagnant at 72.2% in 1HFY22.

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Financial Summary
PKR mln

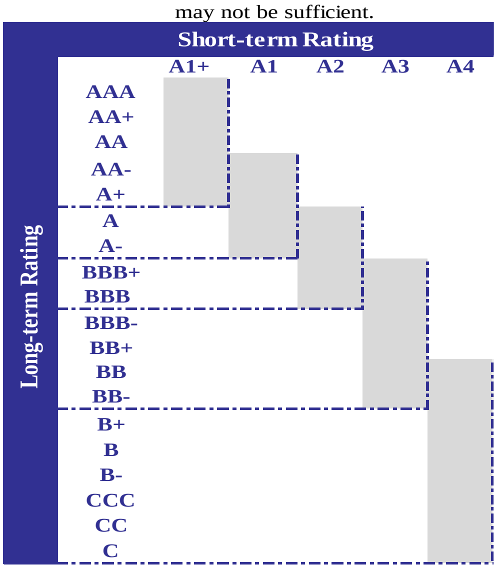
Masood Spinning Mills Limited	Dec-21	Jun-21	Jun-20	Jun-19
Spinning	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	5,487	3,904	3,694	3,982
2 Investments	1,025	719	1,120	1,424
3 Related Party Exposure	455	405	303	283
4 Current Assets	11,417	9,231	7,203	5,981
a Inventories	*7,293*	*5,855*	*4,025*	*4,172*
b Trade Receivables	*2,203*	*2,081*	*2,113*	*828*
5 Total Assets	18,384	14,257	12,320	11,671
6 Current Liabilities	1,550	1,175	659	612
a Trade Payables	*234*	*156*	*125*	*129*
7 Borrowings	12,074	9,563	9,142	8,257
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	102	102	3	-
10 Net Assets	4,657	3,417	2,516	2,801
11 Shareholders' Equity	4,657	3,417	2,516	2,801
B INCOME STATEMENT				
1 Sales	10,987	17,355	13,759	14,853
a Cost of Good Sold	*(8,529)*	*(14,977)*	*(12,910)*	*(13,770)*
2 Gross Profit	2,458	2,379	848	1,083
a Operating Expenses	(428)	(427)	(328)	(295)
3 Operating Profit	2,030	1,952	520	788
a Non Operating Income or (Expense)	*(189)*	*81*	*256*	*114*
4 Profit or (Loss) before Interest and Tax	1,841	2,033	776	902
a Total Finance Cost	*(458)*	*(830)*	*(926)*	*(877)*
b Taxation	*(113)*	*(302)*	*(129)*	*136*
6 Net Income Or (Loss)	1,270	901	(280)	161
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,486*	*1,988*	*726*	*1,357*
b Net Cash from Operating Activities before Working Capital Changes	*1,073*	*1,189*	*(218)*	*536*
c Changes in Working Capital	*(1,373)*	*(1,332)*	*(1,115)*	*(232)*
1 Net Cash provided by Operating Activities	(300)	(143)	(1,333)	304
2 Net Cash (Used in) or Available From Investing Activities	(2,115)	(246)	473	146
3 Net Cash (Used in) or Available From Financing Activities	2,482	420	894	(446)
4 Net Cash generated or (Used) during the period	66	31	33	4
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	26.6%	26.1%	-7.4%	25.2%
b Gross Profit Margin	22.4%	13.7%	6.2%	7.3%
c Net Profit Margin	11.6%	5.2%	-2.0%	1.1%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	1.0%	3.8%	-2.8%	7.6%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	62.9%	30.4%	-10.5%	6.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	145	148	148	122
b Net Working Capital (Average Days)	142	145	144	119
c Current Ratio (Current Assets / Current Liabilities)	7.4	7.9	10.9	9.8
3 Coverages				
a EBITDA / Finance Cost	4.6	2.9	1.0	1.7
b FCFO / Finance Cost+CMLTB+Excess STB	2.5	1.4	0.7	1.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.9	2.2	-14.5	3.5
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	72.2%	73.7%	78.4%	74.7%
b Interest or Markup Payable (Days)	99.2	89.1	67.2	78.8
c Entity Average Borrowing Rate	8.5%	8.4%	10.8%	9.8%

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