The Pakistan Credit Rating Agency Limited

Rating Report

A.J. Textile Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
08-Oct-2024	A-	A2	Stable	Maintain	-
11-Oct-2023	A-	A2	Stable	Maintain	-
12-Oct-2022	A-	A2	Stable	Maintain	-
12-Oct-2021	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan's spinning sector, with an estimated size of ~PKR 775bln, has lately come under pressure due to heightened commodity prices and high cost of business emanating from increased cotton/fibre prices leading to significant working capital requirements. This has eroded the bottom-line margins for the spinning sector players. The recent hike in energy tariffs further elevated the challenges for the industry. Overall, the industry's cash flow and in turn liquidity remains stretched. This led the industry's overall outlook to be placed on a Watch.
AJ Textile Mills Limited ("AJ Textile" or “the Company”) ratings incorporate affiliation with Aziz Group ("the Group") having presence across various sectors of the economy. The Group holds interests in Textile (Yarn Production); FMCG (Match Manufacturing), Laminated Boards, MDF and Particles Chip Board Production. The Company is engaged in yarn production, and currently, operates with a capacity of 113,264 spindles. The ratings take comfort from the Company's consistent and sustained growth in its business risk performance. During FY24, the topline of the Company improved by ~28% mainly triggering from local sales (~90%), followed by exports (~10%). Topline gathered a value driven support i.e. from an increase in yarn price. However, margins and inturn profitability posted a dip due to a substantial increase in raw material (fiber) cost along with inflated energy prices and higher wages have significantly impacted the Company's manufacturing cost. On net level, escalated finance cost has impacted profits, and in turn margins. The Company has incurred substantial CAPEX on solar energy (currently at 9MW). This is expected to reduce the operational expenses, going forward. On the financial risk front, the Company maintains adequate cashflow to meet its short-term & long-term obligations as evident from interest cover (FY24: ~4.8x, FY23: ~3.4x). The ratings also take comfort from the Company's reduced borrowing exposure leading to strong capital structure along with adequate working capital management.

The ratings are dependent on management’s ability to sustain its growth in revenues, margins and profitability. Prudent management of the working capital, and maintaining sufficient cash flows and coverages are imperative. Improvement in governance structure and alignment of the Company's performance with its financial projections remains vital for the ratings.

Disclosure

Name of Rated Entity	A.J. Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Rating Modifiers(Apr-24),Methodology | Corporate Rating(Jul-24),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-24)
Related Research	Sector Study | Spinning(Sep-23)
Rating Analysts	Mir Muhammad Hamza | Mir.Hamza@pacra.com | +92-42-35869504

Profile

Legal Structure A.J. Textile Mills Limited ('A.J. Textile' or 'the Company') was incorporated in 1992 as a private limited company under the repealed Companies Act'17.

Background A.J. Textile was the first initiative by the Aziz Group of Industries (the Group) in the spinning sector. The Group holds presence across multiple sectors, including textiles (yarn production), FMCG (match manufacturing), real estate (AJ Tower), and the production of laminated boards and particle chipboards.

Operations The Company specializes in the manufacturing and sale of different varieties of yarn, operating through two units with a combined installed capacity of 113,264 spindles. The energy requirements are fulfilled through multiple sources, including a 9MW solar power plant, with 4.5MW generated from renewable energy. The remaining energy is supplied by PEDO, PESCO, and genset. The Company's registered office is located at Industrial Estate, Peshawar, while manufacturing units are located in Industrial Estate, Gadoon Amazai, Sawabi.

Ownership

Ownership Structure AJ Textile's ownership vests with the sponsoring family: Mr. Afan Aziz (~65%), followed by Mr. Mohsin Aziz (~34%), Ms. Sahiba Imtiaz (~0.7%) and Ms. Huma Mohsin (~0.03%).

Stability Ownership stability is ensured with the majority stake residing with the sponsoring family. However, there is no formally documented succession plan.

Business Acumen The Group formally came into existance in 1940's and holds interests in various ventures across textile and allied. The Group has adequately expanded its operations with the sponsors having an experience of more than six decades.

Financial Strength AJ Textile Mills Limited remains the prime cash genertaing venture of the Group. However, holds interests in Mohsin Match Factory (Pvt.) Limited, AJ Match (Pvt.) Limited, Premier Formica Industries Limited, Premier Chipboard (Pvt.) Limited, and Premier MDF (Pvt.) Limited, along with Aziz Ice Factory and Cold Storage. The Group holds stable financial muscle and the sponsors are willing to support the Company, if needs be.

Governance

Board Structure Overall control of the Board vests with the sponsoring family. The Bod comprises one Executive Director and three Non-Executive Directors. Independent oversight may add strength to the governance frameowrk.

Members' Profile Mr. Mohsin Aziz, Chairman of the Board, brings over four decades of industrial experience and has previously served as a member of Pakistan's Senate. His leadership is complemented by Mr. Afan Aziz, who contributes over two decades of industrial expertise. They provide strategic direction and seasoned oversight to the Company.

Board Effectiveness The Board has formed two committees (Audit and HR) to assist the Board on relevant matters. However, the absence of a structured system for recording Board meeting minutes highlights a need for improvement in the overall governance framework.

Financial Transparency The External Auditors of the Company, M/s. RSM Avais Hyder Liaquat Nauman, Chartered Accountants, has expressed an unqualified opinion on the financial statements of the Company for FY23. Audit for Jun-24 is still in process. The firm is QCR rated and in 'A' category of auditors.

Management

Organizational Structure The Company employs a horizontal organizational structure, with each department managed by department heads reporting directly to the CEO. The Company is managed through various functional departments, namely; (i) Marketing, (ii) Finance, (iii) Legal, (iv) HR & IT, (v) Corporate Finance & Treasury, (vi) Purchase, and (vii) Internal Audit, (viii) Sales, (ix) Projects.

Management Team The management team is led by the CEO - Mr. Afan Aziz. He holds a bachelor's degree from London School of Economics and has been with the Company since 2002. He brings strong business acumen to his role with over 2 decades of industrial experience. He is assisted by a team of qualified professionals.

Effectiveness The management meetings are held regularly with follow-up points to resolve operational issues, if any. This ensures smooth flow of operations.

MIS AJ Textile has been using SAP Business One version 9.2 (9.20.160) PL: 06, since 2013. The following are the operating modules: Financials, Sale AR Module, Purchasing AP Module, Business Partners, Banking Module, Inventory Module, Production Module, Human Resource, and Project Management.

Control Environment The Company maintains an in-house internal audit function which enhances risk management, control, and governance processes. The Company is accredited with multiple certifications for compliance and quality assurance, namely; Standard 100 by OEKO-TEX, Global Organic Textile Standards (GOTS), Organic Content Standard, and Sustainable (PRIMARK).

Business Risk

Industry Dynamics Pakistan's spinning industry comprises approximately ~368 dedicated spinning units, with an estimated size of ~PKR 775bln and ~13.4mln spindles installed as of FY23, as per an economic survey. The projected cotton production estimate has been revised to ~11.5mln bales, with current production reaching ~8.26mln bales, surpassing FY23's total of ~4.91mln bales. In FY24, better local raw cotton yield is expected to support import substitution. Pakistan's demand for imported cotton has risen from ~3.5mln bales to ~4 million bales this year. Challenges include recent energy tariff hikes and the availability of locally procured raw cotton, impacting the industry's outlook

Relative Position The Company's maintains an adequate market share of (~1%) in terms of the spindles installed. The installed capacity stands at 113,264 spindles.

Revenues AJ. Textile generates revenue from both local (~90%) and export (~10%) sales. During FY24, the topline of the Company witnessed an increase of ~28%, reported at ~PKR 15.5bln (FY23: PKR 12.1bln). Improvement in revenue was attributed to an increase in demand coupled with price change. Looking ahead, management is optimistic about maintaining growth momentum. Due to high finance costs and the implementation of standard taxation on exporters, many textile units have ceased operations. In this context, AJ Textile is strategically exploring these opportunities to enhance its market share, by improving top-line performance.

Margins During FY24, the gross margin of the Company witnessed a decline and stands at ~10.3% (FY23: ~11.1%) due to higher procurement costs. The operating margin had a trickled-down effect and posted a decline (FY24: ~8.8%, FY23: ~9.7%). However, net profit of the Company was supported by other income owing to which the net profit margin remained stable and reported at ~4.6% (FY23: ~4.5%). Going forward, the recent reduction in the policy rate is expected to positively impact the Company's overall margins.

Sustainability Looking ahead, the Company intends to strategically explore new opportunities to drive revenue growth. Additionally, it aims to reduce energy costs by increasing its reliance on solar energy, while effectively managing operational expenses. These efforts are expected to lead to improved financial performance.

Financial Risk

Working Capital As of FY24, the Company's net working capital days improved to 100 days (FY23: 139 days). The reduction in net working capital days is attributable to a decrease in inventory days, which improved to ~69 days as of FY24 (FY23: ~99 days) due to maintaining optimum inventory turnover strategically. Moreover, the Company reduced its reliance on short-term borrowings to lower financial charges, a move primarily associated with improved inventory management. This reduction positively impacted the Company's inventory performance. Receivable days of the Company also improved to ~37 days as of FY24 (FY23: ~45 days). Trade paybale days of the Company stands at ~7 days as of FY24 (FY23: ~5 days). The Company maintains a sufficient buffer to support borrowing. Going forward the working capital cycle will remain unchanged.

Coverages As of FY24, the Company reported an FCFO of ~PKR 1,598mln (FY23: ~1,490mln). The increase was attributed to higher profitability. Finance costs also decreased due to strategic changes to reduce short-term borrowing exposure. The interest coverage ratio (FCFO/Finance Cost) of the Company stood at 4.1x as of FY24 (FY23: 3.0x) reflecting the Company's ample capacity to fulfill its short-term obligations. Going forward, management is focused on reducing its borrowing exposure, which is expected to positively impact the company's coverage ratios.

Capitalization As of FY24, the Company significantly reduced its borrowing exposure to lower financial charges resulting in an improved capital structure with a debt-to-equity ratio of ~38% (FY23: ~48%). Short-term borrowings (STBs) notably decreased to ~PKR 904mln (FY23: ~PKR 2,206mln), reflecting a strategic shift. Total borrowings stand at ~PKR 4,133mln for FY24 (FY23: ~PKR 5,832mln), while total equity improved to ~PKR 6,672mln (FY23: ~PKR 6,391mln). This increase is primarily attributed to higher unappropriated profits, which rose to ~PKR 5,613 mln as of FY24 (FY23: ~PKR 4,831mln).

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Financial Summary
PKR mln

AJ Textile Mills Limited Spinning	Jun-24 12M	Jun-23 12M	Jun-22 12M	Jun-21 12M
A BALANCE SHEET				
1 Non-Current Assets	7,844	8,088	7,671	6,299
2 Investments	422	121	227	232
3 Related Party Exposure	31	31	29	29
4 Current Assets	4,996	5,859	5,752	3,747
a Inventories	*2,627*	*3,260*	*3,319*	*1,896*
b Trade Receivables	*1,681*	*1,502*	*1,518*	*1,056*
5 Total Assets	13,293	14,099	13,679	10,307
6 Current Liabilities	1,642	1,082	937	697
a Trade Payables	*395*	*198*	*167*	*93*
7 Borrowings	4,133	5,832	6,522	3,936
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	847	793	676	628
10 Net Assets	6,672	6,391	5,543	5,046
11 Shareholders' Equity	6,672	6,391	5,542	5,046
B INCOME STATEMENT				
1 Sales	15,531	12,165	11,206	7,877
a Cost of Good Sold	*(13,927)*	*(10,819)*	*(9,842)*	*(6,781)*
2 Gross Profit	1,603	1,347	1,364	1,096
a Operating Expenses	*(242)*	*(163)*	*(242)*	*(147)*
3 Operating Profit	1,361	1,183	1,122	949
a Non Operating Income or (Expense)	*13*	*61*	*(98)*	*(38)*
4 Profit or (Loss) before Interest and Tax	1,374	1,245	1,024	911
a Total Finance Cost	*(389)*	*(512)*	*(329)*	*(142)*
b Taxation	*(270)*	*(191)*	*(181)*	*(42)*
6 Net Income Or (Loss)	715	541	514	727
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,598*	*1,490*	*1,305*	*1,150*
b Net Cash from Operating Activities before Working Capital Changes	*1,209*	*1,005*	*1,029*	*1,017*
c Changes in Working Capital	*1,194*	*7*	*(1,725)*	*(980)*
1 Net Cash provided by Operating Activities	2,403	1,012	(696)	37
2 Net Cash (Used in) or Available From Investing Activities	-	(721)	(1,811)	(2,069)
3 Net Cash (Used in) or Available From Financing Activities	-	(330)	2,592	2,010
4 Net Cash generated or (Used) during the period	2,403	(39)	84	(22)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	27.7%	8.6%	42.3%	38.1%
b Gross Profit Margin	10.3%	11.1%	12.2%	13.9%
c Net Profit Margin	4.6%	4.5%	4.6%	9.2%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	18.0%	12.3%	-3.7%	2.2%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	10.9%	9.1%	9.7%	15.9%
2 Working Capital Management				
a Gross Working Capital (Average Days)	107	144	127	116
b Net Working Capital (Average Days)	100	139	123	112
c Current Ratio (Current Assets / Current Liabilities)	3.0	5.4	6.1	5.4
3 Coverages				
a EBITDA / Finance Cost	4.8	3.4	4.8	9.7
b FCFO / Finance Cost+CMLTB+Excess STB	1.7	1.5	2.1	2.3
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	2.7	3.6	3.4	2.6
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	38.2%	47.7%	54.1%	43.8%
b Interest or Markup Payable (Days)	44.7	90.7	111.0	117.5
c Entity Average Borrowing Rate	8.0%	8.5%	6.0%	4.3%

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.

Scale	Long-Term Rating
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.

Scale	Short-Term Rating
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.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.

Rating Modifiers | Rating Actions

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 surveil 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. Rating actions may include "maintain", "upgrade", or "downgrade".

Note: This scale is applicable to the following methodology(s):

a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Company

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 | 17-(a)
(19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

Proprietary Information