The Pakistan Credit Rating Agency Limited

Rating Report

Lucky Tex Pakistan (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
27-May-2022	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The assigned ratings of Lucky Tex Pakistan reflect adequate positioning of the company in the relative universe. It's a family-owned private company where ownership rests equally among two shareholders. Position of Chairman and CEO is segregated. The Company's management involves experienced professionals, aided by good reporting. The company has board product slate including Fabric, Bed Linen, Curtain and Kitchen Articles. Over the years, the Company's topline has been following an improving trend. During FY21, sales revenue improved to PKR 3bln (FY20: PKR 2.4bln) where sales mix remained tilted towards exports. Net profitability witnessed improvement whilst margins recorded marginal uptick. Management of receivables is essential. Customer concentration has remained high, during last few years. The management is eying sizable improvement in the same with the addition of new customers. Going forward, strategy is to focus on achieving vertical integration where special emphasis will be on business margins rather than inventory gains. The financial matrix reveals low leveraging, improved working capital cycle and good coverage. Equity base of the Company is revealing comfortable picture with good risk absorption capacity. 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 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.

The ratings are dependent upon management ability to improve margins, profitability and financial profile. This includes avoiding any asset-liability mismatch that may arise and effectively managing its position in a competitive segment. Any deterioration in debt coverage leading to higher financial risk or subdued profitability will have a negative impact on ratings.

Disclosure

Name of Rated Entity	Lucky Tex Pakistan (Pvt.) 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 | Composite and Garments(Dec-21)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure Lucky Tex Pakistan (Pvt.) Limited ('Lucky Tex Pakistan', 'The Company') commenced operations in 1993 and is a private limited company.

Background The foundation of Lucky Tex Pakistan was laid by Mr. Ahmed Tabba in 1993. Its stitching unit became operational in 1995.

Operations The products of the Company are Fabric, Bed Linen, Curtain and Kitchen Articles. Presently, the Company's Processing Unit is geared to handling fabric widths upto 3.2 meters and weights from 80 - 300 gms/square meter. The Company manufactures Bleached White, Optical White, Pigment and Reactive Printing on both Rotary and Panel, Dyeing of Pastel to Medium Pigment Shades. Lucky Tex Pakistan has a high standard of printing, utilizing both Rotational and Panel machines with Reactive and Pigment dyes upto 16 colors.

Ownership

Ownership Structure Lucky Tex Pakistan is primarily a family-owned business with equal stake held directly by Mr. Ahmed Tabba and Mr. Salman Tabba.

Stability The second generation of the family has already joined the Company, Mr. Salman Tabba is the son of the Chairman and has presence on the board as well.

Business Acumen Mr. Ahmed Tabba is the founder and chairman of the Company and has been involved in the textile business for around four decades. Tabba family was involved in the trading business, and until 1983 were commercial importers and exporters on the pattern of Japanese trading companies.

Financial Strength The group has history of around four decades and operational companies are Home Furnishing Pvt. Ltd, Premier Stitching Pvt. Ltd, Mariam Ali Mohammad Tabba Foundation, Al Wardah Energy Ltd and Al Wardah Argo Industries. The financial strength of sponsors is considered adequate where the willingness to support Lucky Tex Pakistan remains high, in case need arises.

Governance

Board Structure The overall control of the Company vests in two-member board of directors including the CEO. It's a family-oriented board with father as a chairman and position of CEO is vested with son.

Members' Profile Mr. Ahmed Tabba is the Chairman, while Mr. Salman Tabba is the CEO of the Company. The board members have vast knowledge and extensive experience of the textile industry.

Board Effectiveness The family domination on the board undermines the board mandate as an independent oversight body. The board minutes are formally maintained; however, lack the details. The board is supported by two committees 1) Audit committee and 2) HR and remuneration committee.

Financial Transparency Rahman Sarfaraz Rahim Iqbal Rafiq (a QCR rated firm by ICAP & Category "A") 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.

Management

Organizational Structure The organizational structure of the Company is divided into five main categories namely i) Finance, ii) Purchase and Projects, iii) Chief Engineer, iv) HR, and v) IT. All operational departments report directly to the CEO except for Group CFO where the reporting line is to Board of Directors.

Management Team The CEO of the Company, Mr. Salman Tabba is younger son of Mr. Ahmed Tabba. He did his BBA from USA and has presence on boards of Mariam Ali Mohammed Tabba Foundation and Al Warda Agro Industries. Mr. Ashfaq is the Group CFO and has been associated with the group since long.

Effectiveness No formal Management committee is in place. However, important matters are discussed by the Group CFO, CEO and Chairman on daily basis.

MIS The Company's operating environment depends upon an IT Infrastructure supported by an in-house programmed ERP, Sidat Financials in Finance and Oracle – EBS /In house software using in other departments.

Control Environment The Company has adequate relevant quality control standards to meet export requirements. There is a rigorous quality control department to audit the quality of the output.

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 The Company's Processing Unit is geared to handling fabric widths upto 3.2 meters and weights from 80 - 300 gms/square meter. Cut to pack division is designed and equipped for a daily production of about 5,000 curtain pairs and 10,000 bed sets (Filled / Unfilled) and it is divided into seven sub-divisions. The Company's relative position is considered among small sized players in the industry.

Revenues The analysis of revenue base reveals continuous improvement over the last three years attributable to improved demand. During FY21, the company's revenue improved to PKR 3bln (FY20: PKR 2.4bln). Revenue is generated from both local and export market. Sales mix remained tiled towards exports as it constitutes 66% of total sales of the Company. The main export destination for Lucky Tex Pakistan is Holland which constitutes 62% export sales. Other important destination is South Africa which constitutes 13.3% of export sales.

Margins During FY21, the Company's gross margin slightly improved to 9.8% (FY20: 8.6%). This is attributable to enhanced demand and improved international prices.

Sustainability The Company is carrying out regular BMR to increase the installed capacity which has led to improved revenue and margins. Customer concentration has remained high, during last few years. The management is eying sizable improvement in the same with the addition of new customers. Going forward, strategy is to focus on achieving vertical integration where special emphasis will be on business margins rather than inventory gains. The Company will be availing subsidized financing only to finance planned capacity expansions.

Financial Risk

Working Capital The Company meets its working capital requirements through a mix of internal cash generation and short-term borrowings. The Company's short-term borrowings stood at PKR 67mln and PKR 50mln as at end-Jun21 and Dec-21 respectively. Net working capital cycle stood at 58 days as at end-Dec21 (end-Jun21: 55days). During FY21, the Company's room to borrow stood at 48%, which is lower than the same period last year (FY20: 53%).

Coverages During FY21, the Company's operating cash flow from operations (FCFO) remained largely intact at PKR 209mln (FY20: PKR 208mln). Free cashflow from operations stood around PKR 80mln during last six months. Meanwhile, due to a lower finance cost, interest coverage ratio reflected comfortable position (FY21: 16.6x, FY20: 18.9x) whereas debt coverage ratio remained at 3x (FY20: 6.7x).

Capitalization The Company has been operating on low leveraged capital structure since last three years. The total debt stood around PKR 254mln as at end- Dec21 (end-Jun21: PKR 299mln). The Company's debt primarily consists of ILTFF of PKR 176mln in FY21 consisting of 42% of long-term debt as at end-Jun21.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Lucky Tex Pakistan (Pvt.) Ltd	Dec-21	Jun-21	Jun-20	Jun-19
Textile	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	2,710	2,708	2,747	2,511
3 Related Party Exposure	27	17	18	18
4 Current Assets	1,485	1,369	1,207	966
5 Total Assets	5,354	5,221	4,811	4,331
6 Current Liabilities	851	677	611	383
a Trade Payables	*736*	*576*	*523*	*316*
7 Borrowings	254	299	232	81
8 Related Party Exposure	29	29	5	-
9 Non-Current Liabilities	250	250	127	-
10 Net Assets	3,969	3,967	3,837	3,867
11 Shareholders' Equity	3,969	3,967	3,837	3,867
B INCOME STATEMENT				
1 Sales	1,580	3,001	2,462	2,058
2 Gross Profit	128	294	213	301
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*80*	*209*	*208*	*405*
b Net Cash from Operating Activities before Working Capital Changes	*67*	*252*	*242*	*394*
c Changes in Working Capital	*32*	*(74)*	*(31)*	*(79)*
1 Net Cash provided by Operating Activities	99	178	212	315
2 Net Cash (Used in) or Available From Investing Activities	(81)	(243)	(371)	(404)
3 Net Cash (Used in) or Available From Financing Activities	(44)	67	151	81
4 Net Cash generated or (Used) during the period	(27)	2	(8)	(8)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	5.3%	21.9%	19.6%	27.9%
b Gross Profit Margin	8.1%	9.8%	8.6%	14.6%
c Net Profit Margin	1.6%	7.7%	6.1%	9.7%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	7.1%	4.5%	7.2%	15.8%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	1.3%	5.9%	3.9%	5.2%
2 Working Capital Management				
a Gross Working Capital (Average Days)	134	122	120	121
b Net Working Capital (Average Days)	58	55	57	75
c Current Ratio (Current Assets / Current Liabilities)	1.7	2.0	2.0	2.5
3 Coverages				
a EBITDA / Finance Cost	26.0	21.0	22.4	125.4
b FCFO / Finance Cost+CMLTB+Excess STB	2.5	3.0	6.7	19.8
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.5	1.3	1.2	0.2
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	6.7%	7.6%	5.8%	2.0%
b Interest or Markup Payable (Days)	92.4	62.9	55.0	85.3
c Entity Average Borrowing Rate	2.7%	4.5%	6.9%	4.3%

Credit Rating

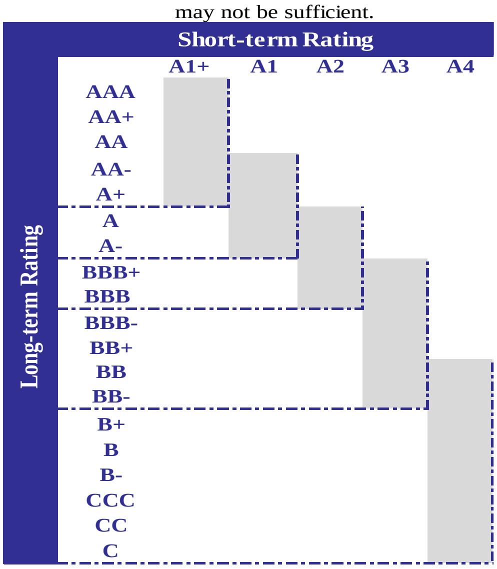
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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