The Pakistan Credit Rating Agency Limited

Rating Report

Ahmed Hassan Spinning Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
07-Feb-2022	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The assigned ratings of Ahmed Hassan Spinning Limited (AHSL) reflect adequate positioning of the Company in the relative universe. The Company specializes in manufacturing and export of yarn of average count of 21/1 CDD. The installed capacity is 28,152 spindles. Board comprises of four members; all the members are from sponsor family. The Company's management involves experienced professionals looking after the operations of the Company. Sales mix compromises of local and as well as export with export destination in China and Korea. Management is eying additions in export destination, going forward. Over the last few years, the Company's topline is following a growing trend. During FY21, the Company's revenues stood at PKR 3.8bln (FY20: PKR 3.7mln). Sales mix, dominated by local sales, displaying improving trend over the years. The Company's enjoys established customer base in local market which drives the major revenue. Operating profits and net profitability recorded sizeable improvement in the recent year whilst margins remain good. After recent demerger from group company, the management is focusing on harnessing related costs in addition to enhancing capacity. The financial risk matrix displays moderate leveraging and improvement in coverage compared to last year. Going forward, with planned capacity expansion, leverage is expected to increase. Hence, prudent management of affairs remains vital for the rating. Equity base, expected to improve going forward, after conversion of subordinated debt and increase in share capital. 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. 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.

The ratings are dependent upon the management's ability to capitalize on growth opportunities in a competitive landscape, operate at optimal level and sustain margins, going forward. The governance framework and financial transparency need improvement. The company is expected to adhere to conservative financial discipline, which would be crucial to ratings.

Disclosure

Name of Rated Entity	Ahmed Hassan Spinning 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	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure The Company was incorporated on: 20th October, 2016 under the companies Ordinance 1984 as Ahmed Hassan Spinning Limited. After around two years, Company converted its status from Private Limited to Public Limited Company as Ahmed Hassan Spinning Limited under Companies Act, 2017 (XIX of 2017) with same share capital.

Background Ahmad Hassan Spinning Limited was incorporated due to the process of demerger of Ahmad Hassan Textile Mills Limited. Ahmad Hassan Textile Mills Limited was incorporated in Pakistan on December 3rd, 1989 as a public Limited Company under the repealed Companies Ordinance, 1984. The Company is principally engaged in the manufacturing and sale of Yarn and Fabric.

Operations The core operation of the business resides in the manufacturing of yarn. The Company have 28,152 spindles installed and in good working conditions. With this capacity company is producing daily 560 to 570 yarn bags as per local and international market requirement.

Ownership

Ownership Structure After the demerger, Ahmed Hassan Spinning Limited (AHSL) is working now independently with the management of Mian Muhammad Parvaiz (Late) family: Mr. Muhammad Aurangzeb, Mr. Muhammad Jahanzaib, Mrs. Waheeda Parvaiz, Mr. Ahmed Hassan and Miss Faiza Parvaiz. Out of them first three shareholders have the major shareholding.

Stability Ahmed Hassan Spinning Limited is a family-oriented Company, therefore ownership rests with the family. Family has no other business except their engagement in Ginning Section as Ahmed Cotton Industries.

Business Acumen The family has been in the textile industry over three decades, which brings extensive technical knowledge into the business. Two of the major sponsors have direct involvement in day-to-day operations of the business.

Financial Strength Ahmed Hassan Spinning is flagship company of the sponsors. Hence, support in case need arises remains inevitable. Recently, the subordinated loan from sponsors is being converted to share capital which is also reflective of the same.

Governance

Board Structure The board comprises four members; all of them are representatives of sponsoring family including the Chairman Mr. Muhammad Aurangzeb and CEO Mr. Muhammad Jahanzeb. The remaining directors includes one executive director Mrs. Waheeda Parvaiz, and one is non-executive director Mr. Ahmed Hassan.

Members' Profile Board members have vast experience and relatively long association with the Company. The Chairman of board – Mr. Muhammad Aurangzeb – carries with him fourteen years of experience in the textile sector, having qualification of MBA Marketing and Finance.

Board Effectiveness Control of the board vests with sponsoring family. Adequate board size and absence of independent oversight resulting in weak governance.

Financial Transparency M/s PKF F.R.A.N.T.S, Chartered Accountants is the external auditor of the Company. The company's auditors are QCR rated.

Management

Organizational Structure Ahmad Hassan Spinning Limited is working under the supervision of Chairman Mr. Muhammad Aurangzeb and Chief Executive Officer Muhammad Jahanzaib. They are directly overseeing all the operations of the Company from initial stage to end process of yarn.

Management Team Mr. Muhammad Jahanzaib, having qualification MBA and he has vast experience in Ginning section of Ahmad Hassan Textile Mills Limited namely Ahmad Cotton Industries of more than 10 years.

Effectiveness Management of Ahmed Hassan Spinning Limited is focusing their business and working together by arranging meeting on weekly basis or at the end of every month, to do analyses of their achievement performance in accordance with the Company's goals.

MIS A fully functional installation of ERP software has been done by the company which has improved the efficiency. The company deploys MS Windows Server 2003 for operating system. Oracle 9i is being utilized for back-end database working whereas Oracle Developer 6i is used for front-end developer working. While HR MIS Implemented with ZKTeco and Barcode Reader Machines.

Control Environment The core software can manage from comprehensive reports of sales, as well as tax reports, financials and HRMS. The system, while integrating the business functions of the company, helps the management in timely decision making. Moreover, it assists the management in establishing a better control environment and achieving efficiency in MIS reporting.

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 Ahmed Hassan Spinning Limited is a mid-sized spinning unit and one of the textile ventures of the Ahmed Cotton Industries.

Revenues Over the last few years, the company's topline is following growing trend. The company has achieved geographical diversification as Company's sales increased mostly in Faisalabad, Karachi, Multan and Lahore region. In 1QFY22, the export revenue collection country wise is as follows: China (~PKR 361mln of total export revenue), followed by South Korea (~PKR 52.2mln of total export revenue). The Company enjoys long-term working relationship with the top brands of the Pakistan including Nishat Mills Limited, Sapphire Industries, Colony Textile Mills Limited and Mahmood Group. During 1QFY22, the company's top-line clocked in at PKR 1,256mln.

Margins The Company's gross margin increases slightly (FY21: 8%, FY20: 7.2%) due to adequate implementation of actions/procedures to mitigate the impact of pandemic. Similarly, due to improved sector dynamics and high yarn prices, operating margin increased marginally (FY21: 5.7%, FY20: 6.1%). The Company gained profit on sale of assets of PKR 18mln in FY21. The significant decrease in finance cost (FY21: PKR 27mln, FY20: PKR 65mln) led to a high net margin (FY21: 4.4%, FY20: 3.1%) as the Company posted a net profit of PKR 168mln in FY21 (FY20: PKR 116mln)

Sustainability The company have planned to increase their export business from current portion of 10% of total sales to 25% of total sales. Therefore, AHSL is aiming to increase its operational capacity from 28,152 spindles to 32,376 spindles to support the future export business.

Financial Risk

Working Capital The Company meets its working capital requirements through a mix of internal generation and short-term borrowings (STBs). Though payables and receivables were stretched to an extent, higher inventory days led to a slight increase in net working capital days (FY21: 54days, FY20: 51days).

Coverages The FCFO is almost on the stagnant trajectory, as on YoY basis (FY21 PKR 256mln; FY20 PKR 246mln). During 1QFY22, Ahmed Hassan Spinning Limited Limited cashflows (FCFO) stood at PKR 88mln. Consequently, Interest coverage increased (FY21: 9.7x, FY20: 3.9x), remained strong. However, Debt coverages declined (FY21: 2.0x, FY20: 3.0x) because of higher CMLTD as the Company has opted to avail one-year deferral option of long-term loan repayments by SBP due to pandemic. The Company's TCF debt coverage also decreases (FY21: 1.9x; FY20: 3.0x).

Capitalization Ahmed Hassan Spinning Limited has a low leveraged capital structure, despite of significant increase in leveraging ratio which stood at ~47.9% in 1QFY22. Ahmed Hassan Spinning Limited still remains a relatively low leveraged company (FY21: 31.7%; FY20: 33.5%). Out of total debt of PKR 838mln in 1QFY22, short term borrowings debt comprises ~72.7%.

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Financial Summary
PKR mln

Ahmad Hassan Textile Mills Limited	Sep-21	Jun-21	Jun-20	Jun-19
##	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	1,172	1,390	1,417	1,304
2 Investments	-	33	44	8
3 Related Party Exposure	-	-	-	-
4 Current Assets	1,087	1,355	975	918
a Inventories	*370*	*839*	*580*	*538*
b Trade Receivables	*375*	*404*	*288*	*248*
5 Total Assets	2,259	2,777	2,435	2,230
6 Current Liabilities	428	711	577	374
a Trade Payables	*302*	*574*	*404*	*205*
7 Borrowings	838	615	586	1,064
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	82	130	107	82
10 Net Assets	912	1,322	1,165	710
11 Shareholders' Equity	912	1,322	1,165	710
B INCOME STATEMENT				
1 Sales	1,256	3,816	3,754	3,432
a Cost of Good Sold	*(1,145)*	*(3,510)*	*(3,483)*	*(3,234)*
2 Gross Profit	111	307	270	198
a Operating Expenses	(24)	(72)	(58)	(63)
3 Operating Profit	87	234	213	135
a Non Operating Income or (Expense)	*(0)*	*5*	*(9)*	*(0)*
4 Profit or (Loss) before Interest and Tax	87	239	204	135
a Total Finance Cost	*(16)*	*(27)*	*(65)*	*(121)*
b Taxation	*(15)*	*(45)*	*(22)*	*(33)*
6 Net Income Or (Loss)	55	168	116	(18)
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*88*	*256*	*246*	*14*
b Net Cash from Operating Activities before Working Capital Changes	*69*	*219*	*171*	*14*
c Changes in Working Capital	*44*	*(200)*	*66*	-
1 Net Cash provided by Operating Activities	113	19	237	14
2 Net Cash (Used in) or Available From Investing Activities	(33)	(11)	8	-
3 Net Cash (Used in) or Available From Financing Activities	(55)	(10)	(161)	-
4 Net Cash generated or (Used) during the period	25	(2)	84	14
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	31.6%	1.7%	9.4%	--
b Gross Profit Margin	8.8%	8.0%	7.2%	5.8%
c Net Profit Margin	4.4%	4.4%	3.1%	-0.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	10.5%	1.5%	8.3%	0.4%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sl*	19.8%	13.5%	12.4%	-2.6%
2 Working Capital Management				
a Gross Working Capital (Average Days)	72	101	80	71
b Net Working Capital (Average Days)	40	54	51	49
c Current Ratio (Current Assets / Current Liabilities)	2.5	1.9	1.7	2.5
3 Coverages				
a EBITDA / Finance Cost	6.4	11.5	4.4	0.1
b FCFO / Finance Cost+CMLTB+Excess STB	2.7	2.0	3.0	0.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.8	1.8	2.1	-4.9
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	47.9%	31.7%	33.5%	60.0%
b Interest or Markup Payable (Days)	79.3	64.8	51.3	104.8
c Entity Average Borrowing Rate	8.9%	4.4%	7.7%	11.1%

Credit Rating

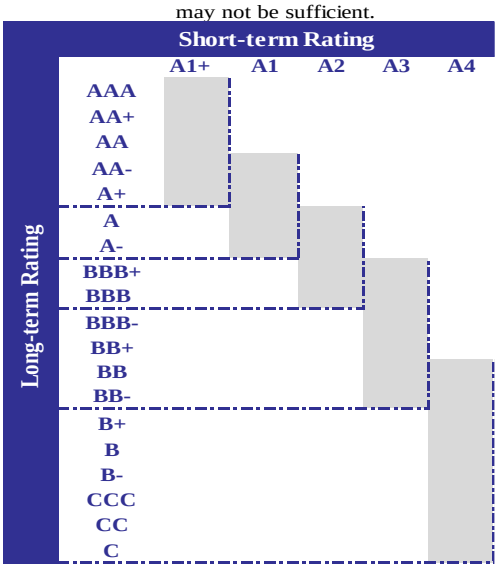
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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