



The Pakistan Credit Rating Agency Limited

Rating Report

Diamond Fabrics Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
15-Jul-2022	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings of Diamond Fabrics Limited reflect the Company's strong business profile emanating from its presence in the broader value chain in the international market; enabling the Company to fare better against volatility. The Company has a presence with four divisions (i) Spinning, (ii) Weaving iii) Denim iv) Apparel. In the last few years, the topline recorded growth where the mix largely remained tilted towards exports. During FY21, Company's margins exhibited attrition while the net probability recorded an uptick. Other income supplemented the overall profitability of the company. Further, the expansion in the operations also includes backward and upward integration. Coverage witnessed recent improvement though the leverage is high. Ratings further incorporate the association of the Company with the well-established Sapphire Group which enjoys a distinguishing presence in several sectors. Sponsor's support, in case of need, will be available. During 9MFY22 (Jul21-Mar22), Pakistan textile exports surged to \$14.2bln (recording a growth of 25%) as compared to \$11.3bln in the same period last year. This is attributable to an increase in demand for textile products and channeling export orders toward the Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth. Going forward, the textile sector's outlook is expected to stay good in the medium term where demand for textile products is expected to sustain.

The ratings are dependent on sustaining the business profile of the Company by maintaining profitability and margins achieved from core textile operations. Sustainability of non-core income and prudent management of surplus funds will be ratings critical.

Disclosure

Name of Rated Entity	Diamond Fabrics Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jun-22),Methodology Correlation Between Long-term & Short-term Rating Scales(Jun-22),Mehtodology Rating Modifiers(Jun-22)
Related Research	Sector Study Composite and Garments(Dec-21)
Rating Analysts	Sehar Fatima sehar.fatima@pacra.com +92-42-35869504

Profile

Legal Structure The Company was incorporated as a private limited company in Pakistan on February 10, 1988, and later on converted into a public unlisted company on October 8, 1988.

Background The Company is a vertically integrated composite textile unit, manufacturing cotton yarn, fabric, and garments. The Company is associated with Sapphire Group.

Operations Diamond fabric is in the business of manufacturing and selling yarn, cloth, and garments. The Company is producing 100% Cotton, Polycotton, Greige, Bleached, Dyed, and Printed Fabrics in different widths and constructions. Currently, the Company has installed 22,000 spindles and 346 looms with all backup process machinery for weaving. The geographical location of major business units including mills /plants of the Company is as under: Karachi: registered office, Lahore: head office, and Shiekhupura: production plant.

Ownership

Ownership Structure The Company is a public limited company where the majority shareholding vests with Sapphire Holding Limited (38.28%) and SFL (30.69%). The remaining shareholding is divided among different family members of sapphire namely Mr. Hassan Abdullah (8.10%), Mr. Umer Abdullah (7.55%), and Mr. Ali Abdullah (7.41%).

Stability The ownership structure is expected to stay the same in the foreseeable future.

Business Acumen Founded by Mr. Mohammad Abdullah in 1969, the Group has acquired expertise in composite textiles. It further has interests in diversified sectors including textile, power, dairy and investment companies.

Financial Strength Sapphire Group is one of the largest vertically integrated textile setups in Pakistan, employing over 18,000 people and having more than 30 production units ranging from spinning, Denim weaving, finishing, home textiles, power plants, dairy, and some others. Sapphire Group is one of the largest vertically integrated textiles setups in Pakistan with Group has an annual turnover of over US \$800 million with an asset base of over US \$500 million. The Group has shown a willingness and ability to support the Company if the need arises.

Governance

Board Structure The Company has a seven-member board including the CEO, Mr. Amer Abdullah. The board also included the group CFO of Sapphire group, Mr. Abdul Sattar. All other board members belonged to the sponsoring family.

Members' Profile The CEO, Mr. Amer Abdullah has been associated with the sapphire group since 1980. Being a director of various companies of Sapphire Group, he has actively participated in planning for the new projects and served ably for expansion and development.

Board Effectiveness Since the board is dominated by Sapphire Group, independent oversight is lacking, though the same is compensated, through the non-executive role of three (of five) family members to some extent.

Financial Transparency M/s. Shinewing Hameed Chaudhri & Company, Chartered Accountants, gave an unqualified opinion on the company's financial statements for the year ended June 30, 2021.

Management

Organizational Structure The company's overall operations are segregated into four divisions namely 1) Spinning Division, 2) Weaving Division 3) Denim Division 4) Apparel Division. All four divisions are headed by a co-managing director and managing director, who are directly reporting to the CEO, Mr. Amer Abdullah.

Management Team The CEO is supported by a team of qualified and experienced professionals. Most of the senior management have been associated with Diamond Fabric for a reasonably long time.

Effectiveness While there are no formal management committees, MIS reports relating to daily operations are generated and submitted to senior management for discussion on regular basis along with need-based meetings for discussion of issues.

MIS Given the large scale of operations spread at various locations and divided into various segments and processes, the need for quality information systems is paramount to control and maintain the efficiency of operations. The company has implemented SAP with operational modules including (i) Financial Accounting, (ii) Financial Assets Management, (iii) Production Planning, (iv) Materials Management, (v) Plant Maintenance & Services Management, (vi) Quality Management, (vii) Sales & Distribution, (viii) HRM and (ix) Business Information warehouse.

Control Environment The company's products are Oeko-Tex certified and meet the human-ecological requirements of the standards presently established for products with direct contact with the skin. The certified goods fulfill requirements of reach (including the use of azo-dyes, nickel, etc.) as well as the American requirement exception of accessories made from glass.

Business Risk

Industry Dynamics During 9MFY22 (Jul21-Mar22), Pakistan textile exports surged to \$14.2bln (recording a growth of 25%) as compared to \$11.3bln in the same period last year. This is attributable to an increase in demand for textile products internationally and the channeling of export orders toward the Pakistani market. On a YoY basis, the exports of raw cotton, cotton (carded or combed) and cotton cloth recorded notable growth. However, month on month basis, textile exports have declined by 3.5%. Going forward, the textile sector's outlook is expected to stay good in the medium term where demand for textile products is expected to sustain.

Relative Position The Company is categorized among small-sized players. However, the Company is a vertically integrated composite textile unit, manufacturing cotton yarn, fabric, and garments recording good growth in the last few years.

Revenues The analysis of the revenue base reveals continuous improvement over the last three years attributable to improved export demand. During FY21, the company's revenue improved to PKR 19.2bln (FY20: PKR 16.2bln). Sales mix largely tilted towards the export market recorded at 84%. Slight attrition in gross profit was witnessed in FY21 and recorded at PKR 2.6bln (FY20: PKR 2.8bln) attributable to increased cost of sales. Operating expenses recorded a slight increase YoY. Dividend income (CY21: PKR 72mln, CY20: PKR 40mln) from investment in associated group companies supported the profitability. During FY21, net profitability clocked in at PKR 323mln where the Company recorded a loss of PKR 117mln in CY20.

Margins During FY21, the Company's gross margin declined to 13.7% as compared to 17.6% in the same period last year. The net profit margin recorded a slight gain and was recorded at 1.7% in FY21.

Sustainability The company is continuously enhancing its production units from past three to four years and still working to enhance the capacity in order to meet emerging demand of international market.

Financial Risk

Working Capital The Company meets its working capital requirements through a mix of internal generation and short-term borrowings (STBs). The short-term borrowings of the company recorded a decline (end-June21: PKR 5.5bln; end-Jun20: PKR 6.2bln). The inventory days remained largely the same at 114days (end-Jun20: 117days). Receivable days recorded a sizable decline and the net-working capital days as of end-Jun21 clocked in at 97days (end-June'20: 115days).

Coverages During FY21, the Company's free cash flow from operations (FCFO) was enhanced to PKR 2.6bln (CY20: PKR 1.1bln). The interest coverage ratio clocked in at 1.8x (end-Jun20: 0.7x).

Capitalization The leveraging of the company is considered high at 78.9% in FY21. Out of total borrowing, 36.1% constitutes short-term borrowing and clocked at PKR 5.5bln in FY21. The equity base of the Company remained largely the same over the last few years (end-Jun21: PKR 4.0bln, end-Jun20: PKR 3.6bln).



Diamond Fabric Limited Textile	Mar-22 9M	Jun-21 12M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	11,481	10,391	10,255	10,090
2 Investments	626	654	558	905
3 Related Party Exposure	1,723	1,723	1,160	1,316
4 Current Assets	12,882	9,313	9,584	7,797
<i>a Inventories</i>	7,952	5,726	6,298	4,128
<i>b Trade Receivables</i>	2,219	1,484	1,515	2,515
5 Total Assets	26,712	22,081	21,557	20,107
6 Current Liabilities	2,744	2,743	2,896	2,112
<i>a Trade Payables</i>	2,399	2,366	2,478	1,782
7 Borrowings	18,631	15,142	14,922	13,726
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	161	159	147	120
10 Net Assets	5,175	4,038	3,592	4,149
11 Shareholders' Equity	5,175	4,038	3,592	4,149
B INCOME STATEMENT				
1 Sales	17,951	19,226	16,224	15,964
<i>a Cost of Good Sold</i>	(14,068)	(16,592)	(13,368)	(13,037)
2 Gross Profit	3,883	2,635	2,856	2,927
<i>a Operating Expenses</i>	(2,003)	(1,757)	(1,639)	(1,653)
3 Operating Profit	1,880	877	1,217	1,274
<i>a Non Operating Income or (Expense)</i>	60	383	54	231
4 Profit or (Loss) before Interest and Tax	1,940	1,260	1,270	1,506
<i>a Total Finance Cost</i>	(609)	(708)	(1,203)	(866)
<i>b Taxation</i>	(171)	(229)	(184)	(84)
6 Net Income Or (Loss)	1,159	323	(117)	555
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	1,856	1,135	716	639
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	1,295	357	(544)	639
<i>c Changes in Working Capital</i>	3,014	819	(945)	-
1 Net Cash provided by Operating Activities	4,309	1,176	(1,489)	639
2 Net Cash (Used in) or Available From Investing Activities	(1,738)	(1,182)	(889)	-
3 Net Cash (Used in) or Available From Financing Activities	3,489	(45)	1,207	-
4 Net Cash generated or (Used) during the period	6,061	(51)	(1,171)	639
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	24.5%	18.5%	1.6%	--
<i>b Gross Profit Margin</i>	21.6%	13.7%	17.6%	18.3%
<i>c Net Profit Margin</i>	6.5%	1.7%	-0.7%	3.5%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	27.1%	10.2%	-1.4%	4.0%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	33.6%	8.5%	-3.0%	13.4%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	133	143	163	152
<i>b Net Working Capital (Average Days)</i>	96	97	115	111
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	4.7	3.4	3.3	3.7
3 Coverages				
<i>a EBITDA / Finance Cost</i>	3.8	1.7	0.8	0.8
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	0.6	0.4	0.5	0.3
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	6.0	19.3	-22.1	-50.7
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	78.3%	78.9%	80.6%	76.8%
<i>b Interest or Markup Payable (Days)</i>	0.0	0.0	0.0	0.0
<i>c Entity Average Borrowing Rate</i>	4.3%	4.2%	7.6%	5.8%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 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.

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

<p>Entities</p> <ul style="list-style-type: none"> 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 	<p>Instruments</p> <ul style="list-style-type: none"> a) Basel III Compliant Debt Instrument Rating b) Debt Instrument Rating c) Sukuk Rating
--	---

Disclaimer: PACRA has used due care in preparation of this document. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information. Contents of PACRA documents may be used, with due care and in the right context, with credit to PACRA. Our reports and ratings constitute opinions, not recommendations to buy or to sell.

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 | 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

(23) All information contained herein is considered proprietary by PACRA. Hence, none of the information in this document can be copied or, otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA's prior written consent