



The Pakistan Credit Rating Agency Limited

## Rating Report

### Ali Embroidery Mills (Pvt.) Limited

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#### Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
23-Jan-2023	BBB	A2	Stable	Initial	-

#### Rating Rationale and Key Rating Drivers

The ratings of Ali Embroidery Mills (Private) Limited (Ali Embroidery) reflect its sustained business profile. The Company is a family-owned private limited company which operates with 30 Schiffli and 108 Multi- Heads embroidery machines. The embroidery industry consists of several players operating on small scale with informal structures. However, Ali Embroidery has tiered organizational structure with good operating capacity. The ratings reflect sustained business profile over the years where recently an improvement has been recorded in revenues. During FY22, the company's topline reflected growth to PKR 1.2bln (FY21: PKR 959mln). The company has witnessed an increasing trend of customer sales, majority of the revenues are generated from related parties, while the rest of the customer base has also contributed over the years. During the period, operating profit and PBIT margins have improved. Ratings also incorporate adequate financial risk manifested by suitable working capital and coverage. During FY22, Pakistan's textile exports surged to \$19.3bln (recording a growth of 26%). Exports grew owing to increased volumetric growth of (16% YoY) in the value-added segment, a steep rise in global demand, and record-high cotton prices. Under the value-added category, the knitwear segment remained the top performer by posting 34% YoY growth in exports to \$5.1 billion in FY22 due to a sharp rise in global demand, especially in the US and European countries. Other value-added segments such as ready-made garments, bed wear, and towel posted YoY growth of 29%, 19%, and 19% to \$3.9 billion, \$3.3 billion, and \$1.1 billion respectively. However, a slowdown is expected in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries.

The ratings are dependent on the management's ability to uphold the entity's performance trend. Meanwhile, maintaining strong margins and coverages to fulfill financial obligations will remain critical. Improvement in the governance framework is considered important.

#### Disclosure

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

## Profile

**Legal Structure** Ali Embroidery Mills (Private) Limited (Ali Embroidery) was incorporated in Pakistan in 1972 as a private limited Company. The Company is principally engaged in the manufacturing and retailing of embroidered cloth.

**Background** The Company is part of the Sefam Group of Industries headquartered in Lahore, Pakistan. The group takes pride in claiming themselves as the pioneers of introducing the concept of brands in Pakistan. Ali Embroidery was set up by Mr. J.A Zaman (late) and later became the launching pad for Sefam (Private) Limited and Sarena Textile Industries. Today, Ali Embroidery is among the largest embroidery companies in Pakistan with the highest number of Schiffli machines.

**Operations** The Company's production facility comprises two units, located on Sheikhupura Road, Lahore while the Company's head office is located on Waris Road, Lahore. Presently, the Company operates with ~30 Schiffli embroidery machines and ~108 Multi-Heads embroidery machines. The Company also operates its retail brand "The Embroidery Company" through three outlets in Lahore.

## Ownership

**Ownership Structure** Ownership of the Company is shared by the children of the late Mr. J.A Zaman. Mr. Tariq Zaman, Mr. Hamid Zaman, Ms. Seema Aziz, and Ms. Ambreen Zaman hold ~24.5% stake in the Company while Mr. Ali Zaman holds ~2%.

**Stability** While no documented agreement exists between the family members, the shareholding structure is well-defined, and no ownership change is planned in the upcoming years.

**Business Acumen** Mr. Hamid Zaman has been working since 1972 with his father, J.A Zaman, in Ali Embroidery Mills (Private) Limited. He is the co-founder and main partner, together with Ms. Seema Aziz, in the Sefam and Sarena group of companies. While Mr. Tariq Zaman the CEO of the company oversees the strategic aspect of the business and possesses vast experience in the textile sector.

**Financial Strength** Over the years, the Group has grown its presence in Pakistan by operating different fashion brands, each specialized to cater to different segments of the market. Ali Embroidery has grown into the market and contributed to the manufacturing and retailing of embroidered cloth.

## Governance

**Board Structure** Ali Embroidery's Board of Directors comprises four members, all sponsors. The absence of independent oversight undermines the role of the Board as an independent oversight function. However, the non-executive role of the three sponsors compensates the same, to some extent.

**Members' Profile** All Directors, with exception of Ms. Ambreen Zaman, possess rich experience in the textile sector and are engaged in the management of different Group companies. Each member has been associated with the Company for over a decade.

**Board Effectiveness** Board meetings are held on quarterly basis and attendance is considered satisfactory.

**Financial Transparency** M/s Arshad Raheem & Co. Chartered Accountants, who are not rated by the SBP but have a satisfactory QCR rating by ICAP, are the external auditors of the Company. External auditors have expressed an unqualified opinion on the financial statements for the year ending June 30th, 2022. While the Company does have an internal audit function, reporting is done to the CFO, hence compromising the effectiveness of the function.

## Management

**Organizational Structure** The organizational structure of the Company is divided into broad functional departments, namely Production, Marketing, Finance, Purchase, Admin, Store, Mechanical, Electrical, HR, and Checking.

**Management Team** Mr. Tariq Zaman, the CEO of the Company, possesses extensive experience in the textile sector. While Mr. Hafiz Umair Nadeem, is the CFO of the company. Designing and sales fall under the purview of the General Manager of Marketing while the remaining production and administrative functions are overseen by General Manager Factories, Mr. Mubashir Abdali. Management of the group comprises experienced individuals with a wide range of skills and relevant experience.

**Effectiveness** MIS reports are compiled and reviewed by senior management at varying intervals. While financial position and shop sales reports are submitted to the CEO daily, production efficiency reports (of Multi-Heads machines) are compiled on real time basis. Going forward, Schiffli machine production reports will also be shifted to real time FPS software.

**MIS** The Company implemented Sidat Hyder (GL Mode) as the financial accounting MIS solution in Dec-17, provided by D-Biz Solutions (Pvt.) Ltd. The Company has also deployed several in-house software solutions. These include FPS (Factory Production System) which is used for billing management and monitoring the flow of plain and processed fabric for Multi-Heads embroidery machines.

**Control Environment** The Company places great importance on ensuring premium quality product for its customers. It allows its main customer, Sefam, to prepare its quality report to allow for an accurate and unbiased assessment.

## Business Risk

**Industry Dynamics** During FY22, Pakistan's textile exports surged to \$19.3bln (recording a growth of 26%). Exports grew owing to increased volumetric growth of (16% YoY) in the value-added segment, a steep rise in global demand, and record-high cotton prices. Under the value-added category, the knitwear segment remained the top performer by posting 34% YoY growth in exports to \$5.1 billion in FY22 due to a sharp rise in global demand, especially in the US and European countries. However, a slowdown is expected in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. Floods have added another challenge, especially pertaining to the availability of the cotton crop.

**Relative Position** Ali Embroidery is a relatively small Company operating in the value-added textile segment with only local presence. It is one of the largest embroidery companies in Pakistan with competitors including Hira Embroidery Mills in Lahore and a few other players in Karachi.

**Revenues** The Company's sales reflected growth over the years. During FY22, the topline clocked in at PKR 1.2bln (FY21: PKR 959mln). The major customer of the company is related parties, while the rest of the customer base has also contributed over the years.

**Margins** The gross profit margin declined to 19.9% (FY21: 23.6%) whereas the operating margin reflected a slight improvement (FY22: 8.1%, FY21: 7.4%) attributable to controlled operating expenses. The Company's bottom line recorded a slight improvement in the recent year (FY22: PKR 36mln, FY21: PKR 28mln). Hence, the net profit margin remained largely the same 2.9%.

**Sustainability** The Company has identified the retail market as an opportunity for business expansion and plans to expand its retail network by adding more shops. Moreover, planning to add doubling and twisting unit for diversification.

## Financial Risk

**Working Capital** During FY22, the net working capital days of the company witnessed a sizable increase to 133 days (FY21: 105 days) attributable to a sizable increase in inventory days (FY22: 114 days, FY21: 56 days) where short-term trade leverage of the company recorded improvement.

**Coverages** As of end-Jun22, FCFO clocked in at PKR 170mln (FY21: PKR 159mln) attributable to improved profitability. Interest coverage ratio reflected attrition to 2.6x (end-Jun21: 3.8x) due to enhanced finance costs whereas core coverage inched up to 1.2x (end-Jun21: 1.0x). Debt payback of the company increased to 9.7 years (end-Jun21: 5.3 years).

**Capitalization** The company's leverage is considered high (end-Jun22: 68%, end-Jun21: 58%) - majorly consisting of long-term borrowing. The equity base of the company reflected a meager increase in the last few years (end-Jun22: PKR 480mln, end-Jun21: PKR 445mln). The strengthening of the equity base over the years remains essential for the risk absorption capacity of the company.



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Financial Summary  
PKR mln

Ali Embroidery Mills Textile   Composite	Jun-22 12M	Jun-21 12M	Jun-20 12M
<b>A BALANCE SHEET</b>			
1 Non-Current Assets	725	692	635
2 Investments	51	-	-
3 Related Party Exposure	-	20	-
4 Current Assets	960	576	376
<i>a Inventories</i>	542	234	59
<i>b Trade Receivables</i>	256	100	158
5 Total Assets	1,736	1,288	1,011
6 Current Liabilities	235	217	155
<i>a Trade Payables</i>	88	138	55
7 Borrowings	1,021	625	436
8 Related Party Exposure	-	-	-
9 Non-Current Liabilities	-	1	3
10 Net Assets	480	445	416
11 Shareholders' Equity	480	445	416
<b>B INCOME STATEMENT</b>			
1 Sales	1,242	959	874
<i>a Cost of Good Sold</i>	(994)	(733)	(681)
2 Gross Profit	248	226	192
<i>a Operating Expenses</i>	(147)	(155)	(125)
3 Operating Profit	101	71	68
<i>a Non Operating Income or (Expense)</i>	18	15	8
4 Profit or (Loss) before Interest and Tax	118	86	75
<i>a Total Finance Cost</i>	(65)	(42)	(40)
<i>b Taxation</i>	(17)	(16)	(6)
6 Net Income Or (Loss)	36	28	29
<b>C CASH FLOW STATEMENT</b>			
<i>a Free Cash Flows from Operations (FCFO)</i>	170	159	120
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	154	93	102
<i>c Changes in Working Capital</i>	(544)	(62)	(17)
1 Net Cash provided by Operating Activities	(390)	30	85
2 Net Cash (Used in) or Available From Investing Activities	(89)	(37)	21
3 Net Cash (Used in) or Available From Financing Activities	354	(105)	(181)
4 Net Cash generated or (Used) during the period	(125)	(112)	(75)
<b>D RATIO ANALYSIS</b>			
<b>1 Performance</b>			
<i>a Sales Growth (for the period)</i>	29.5%	9.8%	-5.1%
<i>b Gross Profit Margin</i>	19.9%	23.6%	22.0%
<i>c Net Profit Margin</i>	2.9%	2.9%	3.3%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-30.2%	10.1%	11.8%
<i>e Return on Equity [ Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity) ]</i>	7.7%	6.5%	7.2%
<b>2 Working Capital Management</b>			
<i>a Gross Working Capital (Average Days)</i>	166	105	83
<i>b Net Working Capital (Average Days)</i>	133	68	59
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	4.1	2.6	2.4
<b>3 Coverages</b>			
<i>a EBITDA / Finance Cost</i>	2.9	3.7	3.5
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.2	1.0	1.1
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	9.7	5.3	5.5
<b>4 Capital Structure</b>			
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	68.0%	58.4%	51.2%
<i>b Interest or Markup Payable (Days)</i>	530.7	388.4	628.6
<i>c Entity Average Borrowing Rate</i>	7.9%	7.9%	9.0%

### 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	<b>Highest credit quality.</b> Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+	
AA	<b>Very high credit quality.</b> 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	<b>High credit quality.</b> 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+	<b>Good credit quality.</b> 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	
BBB-	
BB+	<b>Moderate risk.</b> 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	<b>High credit risk.</b> 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	<b>Very high credit risk.</b> 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.
CC	
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):

- 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 Companies Rating

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- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
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- (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).
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- (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)

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