The Pakistan Credit Rating Agency Limited

Rating Report

Reliance Weaving Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Jun-2019	A-	A2	Stable	Maintain	-
31-Dec-2018	A-	A2	Stable	Upgrade	-
25-Apr-2018	BBB	A3	Stable	Maintain	-
30-Jun-2017	BBB	A3	Stable	Upgrade	-
11-Nov-2016	BBB-	A3	Stable	Initial	

Rating Rationale and Key Rating Drivers

The ratings reflect sound business profile of Reliance Weaving Mills Limited (Reliance Weaving). Over the years, the Company’s revenues are on a growing trajectory, a factor of continuous BMR translating into operational efficiencies and higher production volumes. The Company has sustained its overall margins, despite challenging textile industry dynamics. Meanwhile, international yarn market has remained under pressure, which has stagnated yarn prices in local market. Hiked cotton price and rising interest rates have exerted pressure on the Company’s business profile. However, significant rupee devaluation and subsidized energy rates for textile sector has provided a requisite breather to the Company, which, in turn, translated in better margins. Fatima Group has parked a strategic investment in energy sector with Reliance Weaving. However, it is still evolving and yet to generate any profits. The Company has a relatively stretched financial profile, reflected in higher leveraging and short-term debt vis-à-vis self-liquidating current assets. Cognizant of these issues, the management is in process of re-profiling its balance sheet in favor of long term debt. The assigned ratings incorporate strong sponsors support demonstrated by explicit guarantee provided by majority sponsors on all debt related obligations of the Company.

The ratings are dependent on the management's ability to prudently mange the liquidity and debt profile of the Company, particularly working capital, while sustaining its business margins. Going forward, support from sponsors would remain critical.

Disclosure	
Name of Rated Entity	Reliance Weaving Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Criteria | Rating Modifier(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Textile(Oct-18)
Rating Analysts	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

Profile

Legal Structure Reliance Weaving Mills Limited (Reliance Weaving) commenced its operations in 1990 as a public limited company.

Background Reliance Weaving is associated with Fatima Group since its inception. The Company started its operations with a small scale weaving unit based in Multan. Later on, the Company entered into spinning segment by acquiring a company in 1999, located at Rawat, Rawalpindi. Presently, the Company operates with three weaving units, all located in Multan and two spinning units, one in Rawat and other in Multan.

Operations Currently, the Company operational capacity comprises 61,920 spindles and 392 looms. The Company is capable of producing high quality cotton yarn, and greige fabric. The Company's total energy requirement stands at 12.5MW. The power is sourced through eight gas-fired captive power generators, which is sufficient for energy requirement. Furthermore, MEPCO and LESCO connections are kept as back-up arrangement.

Ownership

Ownership Structure Reliance Weaving is a family owned business with majority stake (82%) held by Fatima Group. Out of which (79%) stake rests with Fatima family individuals. The remaining is spread among financial institutions and general public.

Stability The major positions in Reliance Weaving are held by Fatima Family members. However, succession planing and transfer of ownership to next generation is not documented yet.

Business Acumen The Sponsors have presence of around three decades in local textile industry through Reliance Weaving, developing expertise over time. Mr. Faisal Ahmed (executive director) is the key person in managing the Company's operations and he has requisite expertise of textile sector in order to spearhead the Company.

Financial Strength Fatima Group is one of the leading corporate groups in Pakistan with interests in sugar, textiles, fertilizer, packaging and foreign trade. The Sponsors have strong financial muscle and are willing to support Reliance Weaving, if needed.

Governance

Board Structure The overall control of the Company vests in seven-member board of directors with Chairman – Mr. Fawad Ahmed Mukhtar and the CEO – Mr. Fazal Ahmed Sheikh. Five directors are Fatima Group's family members, including two executive directors, while two members are independent directors.

Members' Profile Board members have diversified experience, and relatively long association with the Company. The Chairman of board, Mr. Fawad Ahmed, is a graduate and carries with him an experience of around three decades in textile value chain.

Board Effectiveness Control of the board vests with Fatima Group, with strong independent oversight providing constructive challenge; thus portraying effective governance. Meanwhile, Audit, HR and Risk management committees are in-place to assist the board on relevant matters.

Financial Transparency Shinewing Hameed Chaudhri & Co., Chartered Accountants is the external auditor of the Company. The auditor has given an unqualified opinion for the periods ended FY18 and 1HFY19.

Management

Organizational Structure The organizational structure of the Company is divided into various functions, including: (i) Finance & Accounts, (ii) Production, (iii) Procurement, iv) Marketing, (v) Administration & Human Resource and (vi) Internal Audit. The hierarchy of HoD's is channeled through Executive Directors, who then reports to the CEO. This segregation of responsibilities ensures smooth flow of the Company's operations.

Management Team Mr. Fazal Ahmed Sheikh is the CEO of the Company and he has been associated with the Company since its inception. Meanwhile, Mr. Faisal Ahmed (Executive Director), a textile industry veteran, primarily manages the Company's affairs. He is supported by a team of seasoned professionals.

Effectiveness The Company's management meetings are held on periodic basis to highlight potential challenges and to devise both counter and growth strategies. In these meetings the Company's current performance and liquidity position is reviewed. Furthermore, need based meeting are called in order to resolve bottlenecks, ensuring efficiency in operations.

MIS Cognizant of the importance of real-time information, Reliance Weaving has deployed Oracle based ERP solution with advanced technology infrastructure.

Control Environment Reliance Weaving maintains a documented 'quality policy' with clear focus on customer satisfaction and commitment to excellence. The Company is accredited with number of certifications for compliance to the following latest Quality Assurance Standards, including: ISO 9001, Oeko-Tex Standard 100 (AITEX Spain), Better Cotton Initiative (Switzerland), Global Organic Textile Standard.

Business Risk

Industry Dynamics Pakistan's textile exports stagnated in 9MFY19 (~0.1% growth YoY). Even though major segments including cotton cloth, knitwear, garments and bed-wear displayed strong volumetric growth, a unit price dip resulting from sharing currency devaluation benefits with export clientele, curbed overall growth. Cotton yarn also displayed double-digit volumetric decline on account of the US-China trade war. Going forward, the withdrawal of zero-rated sales tax status from textile sector coupled with the increase in interest rate may impact liquidity and profitability of Pakistan's textile industry.

Relative Position Reliance Weaving is the only textile venture of Fatima Group with minimal share in local spinning and weaving segment. However, standard quality machinery has made the Company capable of producing diverse product range in weaving segment, hence, developing a niche clientele.

Revenues In 9MFY19, the Company's top-line clocked in at PKR 11,901mln, posting a growth of 17%. The growth is attributable to continuous BMR activities resulting in volumetric growth. This coupled with better pricing of yarn and gerige fabric in local market and improved export market for gerige fabric has resulted in revenue growth. Revenue is pre-dominated by weaving segment (9MFY19: ~53%, 9MFY18: 55%), while the remaining share rests with spinning segment. The Company's sales have remained tilted towards local market (9MFY19: 65%, 9MFY18: ~69%) with top three exporting reigns being Asia, Europe and Africa.

Margins The Company's gross margin has shown improvement (9MFY19: 10.3%, 9MFY18: 9.0%), owing to better pricing and cost efficiency through BMR. Additionally, the subsidized gas and electricity cost has yielded lower conversion cost. Collectively, these factors have translated into better gross margins. This was followed by improved operating margin (9MFY19: 8.2%, 9MFY19: 6.8%), owing to lower than proportionate increase in operating expense. Meanwhile, the Company has booked an exchange gain of PKR 117mln on the back of rupee devaluation against dollar offsetting the share of loss PKR 32mln form associates and hiked finance cost. Resultantly, the Company's net margin has improved (9MFY19: 2.3%, 9MFY18: 1.3%) and net profit reported at PKR 269mln (9MFY18: PKR 134mln).

Sustainability Reliance Weaving has incurred a CAPEX of PKR 500mln in ongoing financial year. It includes addition of 48 Air jet looms (operational since November 2018) in Unit 5 at cost of PKR 450mln. This will ensure cost efficiency, along with wider product range and better margins. Going forward, the Company plans to add 2 energy efficient gas generators (2.5MW & 2.0MW) and upgrade its backup process (spinning segment). Additionally, the Company's investment in its associated company - Fatima Energy Limited - is still under developing stages and its materialization, in turn, dividend inflow will take some time.

Financial Risk

Working Capital In 9MFY19, the Company's reliance on STB has significantly increased, in order to meet higher working capital needs. Reflected form increased gross working capital days (9MFY19: 147days, 9MFY18: 120days); on account of higher trade debtor days. Meanwhile, the Company has a negative room to borrow when compared to net trade assets (9MFY19, -11%, 9MFY18: -32%); though it has improved over the year but remained below adequacy level.

Coverages The Company's operating cashflow (FCFO) improved in 9MFY19, largely resultant of higher profitability. Meanwhile, higher than proportionate increase in finance cost led to deteriorated interest coverage (9MFY19: 2.0x, 9MFY18: 2.2x). Furthermore, lower CMLTD in 9MFY19 translated into improved debt coverage (9MFY19: 0.8x, 9MFY18: 0.6x), though remained weak.

Capitalization Reliance Weaving has a aggressively leveraged capital structure (9MFY19: 73.3%, 9MFY18: 70.0%). The Company's leveraging has increased over the year, owing to BMR and higher STB in order to meet its increased working capital needs. Out of total debt PKR 9,192mln, STB comprises 76.7%.

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Financial Summary
PKR mln

Reliance Weaving Mills Limited Composite	Mar-19 9M	Jun-18 12M	Jun-17 12M	Jun-16 12M
A BALANCE SHEET				
1 Non-Current Assets	6,038	5,724	5,451	5,238
2 Investments	109	107	110	111
3 Related Party Exposure	831	866	884	849
4 Current Assets	9,007	6,570	4,777	3,953
a Inventories	*5,605*	*3,222*	*3,009*	*2,346*
b Trade Receivables	*1,922*	*2,006*	*604*	*528*
5 Total Assets	15,985	13,267	11,221	10,151
6 Current Liabilities	2,185	1,649	998	972
a Trade Payables	*1,121*	*801*	*540*	*563*
7 Borrowings	9,894	7,948	7,179	6,250
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	307	268	185	155
10 Net Assets	3,600	3,402	2,859	2,774
11 Shareholders' Equity	3,600	3,402	2,859	2,774
B INCOME STATEMENT				
1 Sales	11,901	13,914	11,342	10,049
a Cost of Good Sold	*(10,676)*	*(12,568)*	*(10,358)*	*(9,162)*
2 Gross Profit	1,225	1,346	984	887
a Operating Expenses	(247)	(310)	(263)	(252)
3 Operating Profit	977	1,036	721	634
a Non Operating Income	*48*	*28*	*(14)*	*(4)*
4 Profit or (Loss) before Interest and Tax	1,025	1,064	707	630
a Total Finance Cost	*(670)*	*(622)*	*(540)*	*(523)*
b Taxation	*(86)*	*(131)*	*(67)*	*(104)*
6 Net Income Or (Loss)	269	311	101	3
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,207*	*1,353*	*895*	*809*
b Net Cash from Operating Activities before Working Capital Changes	*627*	*758*	*376*	*284*
c Changes in Working Capital	*(1,946)*	*(1,327)*	*(755)*	*(70)*
1 Net Cash provided by Operating Activities	(1,319)	(569)	(379)	213
2 Net Cash (Used in) or Available From Investing Activities	(496)	(199)	(515)	(11)
3 Net Cash (Used in) or Available From Financing Activities	1,852	750	913	(196)
4 Net Cash generated or (Used) during the period	37	(18)	19	7
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	14.0%	22.7%	12.9%	-7.6%
b Gross Profit Margin	10.3%	9.7%	8.7%	8.8%
c Net Profit Margin	2.3%	2.2%	0.9%	0.0%
d Cash Conversion Efficiency (EBITDA/Sales)	11.1%	10.2%	9.0%	9.3%
e Return on Equity (ROE)	10.2%	9.9%	3.6%	0.1%
2 Working Capital Management				
a Gross Working Capital (Average Days)	147	116	104	98
b Net Working Capital (Average Days)	125	98	87	82
c Current Ratio (Total Current Assets/Total Current Liabilities)	4.1	4.0	4.8	4.1
3 Coverages				
a EBITDA / Finance Cost	2.2	2.5	2.1	2.0
b FCFO / Finance Cost+CMLTB+Excess STB	0.8	0.6	0.4	0.5
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.8	3.7	8.1	9.2
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	73.3%	70.0%	71.5%	69.3%
b Short-Term Borrowings / Total Borrowings	0.8	0.8	0.6	0.6
c Average Borrowing Rate	9.2%	7.5%	7.3%	7.4%

Rating Scale

Credit Rating Scale & Definitions

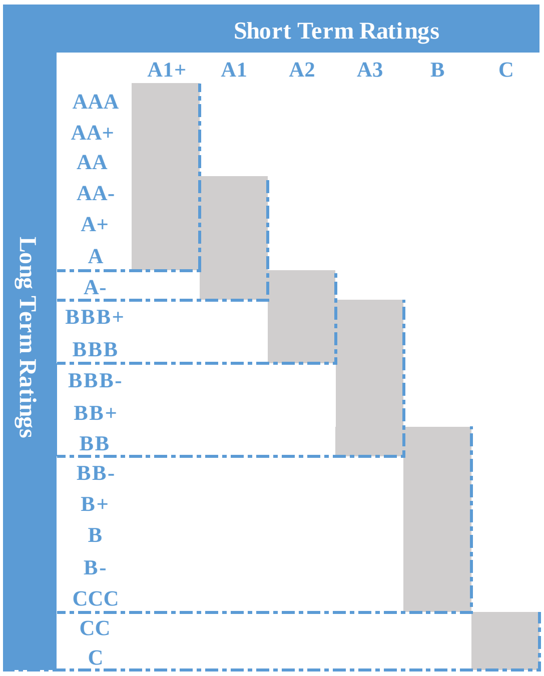
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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 Ratings

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.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults., or/and f) 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.

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(Credit Rating Companies Regulations,2016)

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Conduct of Business
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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.
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