The Pakistan Credit Rating Agency Limited

Rating Report

Prosperity Weaving Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
28-Sep-2019	A-	A2	Stable	Maintain	-
30-Mar-2019	A-	A2	Stable	Maintain	-
28-Dec-2018	A-	A2	Stable	Maintain	-
30-Jun-2018	A-	A2	Stable	Maintain	-
28-Dec-2017	A-	A2	Stable	Maintain	-
15-Jun-2017	A-	A2	Negative	Maintain	-
29-Dec-2016	A-	A2	Negative	Maintain	-
29-Dec-2015	A-	A2	Negative	Maintain	-
29-Dec-2014	A-	A2	Stable	Maintain	-
20-Mar-2014	A-	A2	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect modest profile of Prosperity Weaving Mills Limited (Prosperity Weaving). The Company's revenues are on growing trajectory over the years, owing to continuous BMR translating into operational efficiency, eventually higher production volumes. The Company caters to the need of local industry as well as export markets. Textile industry has suffered from low international commodity prices in recent times. However, the impact largely mitigated by recent rupee devaluation. On standalone basis, the Company's margins have improved on account of improved product quality and prudent inventory management. Financial profile of the Company is characterized by lean working capital cycle, adequate coverages and high leveraging. Mainly emanating from BMR related borrowings. However, predominant portion of long term borrowing is availed at the State Bank's concessionary rates which has insulated the Company's interest rate exposure, amidst high interest rate environment. The Company intends to gradually build a sizable investment portfolio. This exposes the Company to market risk as exhibited by historic volatility in stock exchange. Any significant decline in investments leading to losses, and eventually equity erosion, will impact the financial profile of the Company. The management's ability to manage this risk is critical. However, the assigned ratings derive comfort from Prosperity Weaving's association with Nagina Group.

The ratings are dependent upon sustained market position of the Company. Moreover, the Company's ability to generate enough cash flows to fulfill its financial obligations is critical. At the same time, prudent management of investment portfolio is important.

Disclosure

Name of Rated Entity	Prosperity Weaving Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Crtieria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study | Weaving(Sep-19)
Rating Analysts	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

Profile

Legal Structure Prosperity Weaving Mills Limited (Prosperity Weaving) was incorporated on November 20, 1991 as a public limited company.

Background Prosperity Weaving is associated with Nagina Group since its inception. The group has presence in spinning sector through Ellcot Spinning and Nagina Cotton. The Company's production facility is located in the vicinity of Sheikhupura.

Operations The Company's current operational capacity comprises 324 Looms. The total energy requirement of the Company is ~5MW which is wholly met through captive plant. Furthermore, the Company has LESCO connection as an alternative source.

Ownership

Ownership Structure The majority stakes (~84%) of the Company is held by Nagina Group, through group companies and sponsoring individuals. The remaining shareholding rests with general public and financial institutions.

Stability The considerable positions in Nagina Group are held by Ellahi Family. The Group has a structured line of succession, reflected from equal distribution of shareholding among Ellahi brothers and their family members. Meanwhile, third generation has already been in business, serving at various capacities.

Business Acumen Nagina Group is one of the oldest medium-sized textile houses in Pakistan. Operating under Ellahi's for five decades, developing credential expertise in spinning and weaving over the period of time. The Group has adequately expanded its operations despite competitive textile industry.

Financial Strength Nagina Group comprises three listed public limited companies Ellcot Spinning Mills, Prosperity Weaving Mills and Nagina Cotton Mills Limited and six private limited companies. This portrays adequate financial strength of the Group to support the Company, if needed.

Governance

Board Structure Prosperity Weaving's board comprises eight members out of which six members are non-executive directors, while one director carries the executive role and one is an independent director.

Members' Profile Mr. Shahzada Ellahi Shaikh – the Chairman – carries with him over two decades of experience in local textile industry. The board members have vast knowledge of textile industry; though diversity in experiences exists as well. The directors' expertise on different stages of the textile value-chain benefits the board in efficient decision making.

Board Effectiveness Three committees: Audit, Executive and Human Resource & Remuneration, are in place to assist the board in relevant matters and ensure proper oversight. Attendance of board members remains strong and meeting minutes were formally documented. Out of total, seven directors are Nagina Group nominees (including six sponsoring family individuals). Their dominance on board along with control over key management positions poses limited challenge to the management, thus, hampers effective governance.

Financial Transparency M/s. Deloitte Yousuf Adil, Chartered Accountants are the external auditors of the Company. They have expressed unqualified opinion on the financial statements of the Company for the periods ending FY18 and 1HFY19.

Management

Organizational Structure The management team is headed by Mr. Raza Ellahi Shaikh (CEO), with defined reporting line. The Company has five functional departments and all HOD's reports directly to the CEO.

Management Team The management team is headed by the CEO Mr. Raza Ellahi who holds a graduate degree, in Economics. He is well verse with the textile business providing requisite acumen.

Effectiveness The management meetings are held on daily basis with follow-up points to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations. In addition to this, daily and weekly reports are generated for top management with main focus on production and liquidity position of the Company. Whereas, on monthly basis the Company's P&L is presented and discussed in the meetings.

MIS Prosperity Weaving has in place Oracle based Enterprise Resource Planning (ERP) system with comprehensive MIS reporting.

Control Environment The Company is compliant with multiple safety and quality assurance standard; including ISO 9001:2008, Global Organic Textile Standards and Organic Content Standard.

Business Risk

Industry Dynamics The export performance of Pakistan's textile industry remained stagnated during FY19, despite ~34% currency devaluation and incentives introduced by the government to promote exports. While the current deficit has shown improvement, overall exports showed lackluster performance with the textile sector displaying negative YoY growth of ~1% in dollar terms. Even though leading textile categories including ready-made garments, knitwear, bed ware and cotton cloth displayed double-digit volumetric growth, the hit to unit prices on account of exporters having to share the benefit of the currency depreciation with buyers in the extremely competitive international market, curbed overall growth. Meanwhile, cotton yarn exports fell by ~18% YoY. This decline was driven by falling yarn prices due to decreasing trend in international cotton prices during the year, as well as volumetric decline owing to the US-China trade war. The withdrawal of zero rating status may cause liquidity crunch for the companies with majority exports. This, along with restriction on sales to unregistered person has resulted in a slowdown in textile's operations, in local market.

Relative Position Prosperity Weaving is associated with Nagina Group. The Group has a long history of operations in Pakistan's spinning and weaving sectors. This, strengthens the Company's market position. However, on standalone basis Prosperity weaving's share in local weaving industry is minimal.

Revenues Prosperity Weaving's revenues are on growing trajectory since FY17, on account of materialization of BMR and improved industry dynamics. During 9MFY19, the Company's revenues clocked in at PKR 5,112mln, posting a growth of ~14% YoY. The Company's exports have declined in 9MFY19 due to more attractive prices of greige fabric in local market.

Margins During 9MFY19, the Company's cost of sales increased in lower than proportionate of sales owing to subsidized utilities and cost efficiency through BMR. This has eventually strengthened the Company's gross margins (9MFY19: 8.4%, 9MFY18: 5.3%). Likewise, operating margins have witnessed improvement (9MFY19: 5.6%, 9MFY18: 2.6%) despite ~21% increase in operating cost. The Company received dividend income of ~PKR 19mln (9MFY18: PKR 16mln). Despite increase in finance cost by 29%, the Company's net margin has improved (9MFY19: 1.7%, 9MFY18: 0.8%) as it booked net profit of PKR 88mln (9MFY18: PKR 22mln).

Sustainability Consistent BMR activities resulting in mechanical up gradation along with concerted marketing efforts have strengthened the Company's margins, in turn, better profitability. Currently, the Company is planning a CAPEX of 16 sate of art looms, upon materialization this will partially improve the cost efficiency of the Company with diversified product range. Meanwhile, the Company has build an investment portfolio of ~PKR 506mln which constitutes 47% of its equity base in 9MFY19.

Financial Risk

Working Capital During 9MFY19, the Company's reliance on STB has slightly declined (FY18: PKR 1,018mln, 9MFY18: PKR 1058mln), on the back of improved cash generation; portraying efficiency in working capital cycle. At the same time, STB remains well covered when compared to net trade assets (9MFY19: 17%, 9MFY18: 9%). In 9MFY19, the Company's receivable and inventory days have remained stagnated at 35days and 27days, respectively, despite notable increase in yarn prices. Consequently, the gross working capital cycle has remained the same and stood at 62days in 9MFY19.

Coverages In 9MFY19, the Company's operating cash flows (FCFO) increased significantly (9MFY19: PKR 428mln, 9MFY18: PKR 267mln). The Company's finance cost has increased in lower than proportionate to FCFO, eventually translating into improvement in coverages (9MFY19: 3.4x, 9MFY18: 2.8x). Similarly, the debt coverage of the Company witnessed an improvement (9MFY19: 1.3x, 9MFY18: 1.1x) despite considerable increase in CMLTD.

Capitalization The Company's leveraging has declined ~70.8% (9MFY19: 73.9%) on YoY basis; though remained high. Out of total debt, STB comprises ~39% of total debt. Predominant portion of long term borrowing is availed at the State Bank's concessionary rates which has kept the Company's interest rate exposure quite low, amidst high interest rate environment.

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Financial Summary
PKR mln

Prosperity Weaving Mills Limited Weaving	Mar-19 9M	Jun-18 12M	Jun-17 12M	Jun-16 12M
A BALANCE SHEET				
1 Non-Current Assets	2,141	2,248	2,273	1,763
2 Investments	506	451	549	120
3 Related Party Exposure	-	-	-	-
4 Current Assets	1,676	1,560	1,476	1,058
a Inventories	*640*	*358*	*386*	*297*
b Trade Receivables	*609*	*713*	*632*	*283*
5 Total Assets	4,322	4,260	4,299	2,941
6 Current Liabilities	513	429	437	321
a Trade Payables	*130*	*108*	*131*	*70*
7 Borrowings	2,617	2,730	2,787	1,570
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	113	100	107	93
10 Net Assets	1,079	1,001	968	957
11 Shareholders' Equity	1,079	1,001	968	957
B INCOME STATEMENT				
1 Sales	5,112	6,212	5,820	5,211
a Cost of Good Sold	*(4,681)*	*(5,857)*	*(5,517)*	*(4,852)*
2 Gross Profit	431	356	303	360
a Operating Expenses	(144)	(163)	(168)	(167)
3 Operating Profit	287	192	135	193
a Non Operating Income	*(6)*	*7*	*27*	*(10)*
4 Profit or (Loss) before Interest and Tax	281	199	162	183
a Total Finance Cost	*(132)*	*(144)*	*(102)*	*(111)*
b Taxation	*(61)*	-	*(2)*	*(32)*
6 Net Income Or (Loss)	88	55	58	39
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*428*	*406*	*311*	*343*
b Net Cash from Operating Activities before Working Capital Changes	*320*	*301*	*230*	*230*
c Changes in Working Capital	*(134)*	*37*	*(379)*	*(116)*
1 Net Cash provided by Operating Activities	186	338	(149)	114
2 Net Cash (Used in) or Available From Investing Activities	(99)	(91)	(1,139)	(79)
3 Net Cash (Used in) or Available From Financing Activities	(150)	(94)	1,185	77
4 Net Cash generated or (Used) during the period	(63)	152	(103)	112
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	9.7%	6.7%	11.7%	-10.3%
b Gross Profit Margin	8.4%	5.7%	5.2%	6.9%
c Net Profit Margin	1.7%	0.9%	1.0%	0.7%
d Cash Conversion Efficiency (EBITDA/Sales)	9.1%	7.2%	6.1%	7.5%
e Return on Equity (ROE)	11.3%	5.6%	6.0%	4.1%
2 Working Capital Management				
a Gross Working Capital (Average Days)	62	61	50	38
b Net Working Capital (Average Days)	56	54	44	34
c Current Ratio (Total Current Assets/Total Current Liabilities)	3.3	3.6	3.4	3.3
3 Coverages				
a EBITDA / Finance Cost	3.7	3.3	3.8	3.9
b FCFO / Finance Cost+CMLTB+Excess STB	1.3	1.2	1.1	1.4
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.9	6.3	8.4	5.3
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	70.8%	73.2%	74.2%	62.1%
b Short-Term Borrowings / Total Borrowings	0.4	0.4	0.3	0.2
c Average Borrowing Rate	6.2%	4.9%	4.3%	6.7%

Credit Rating Scale & Definitions

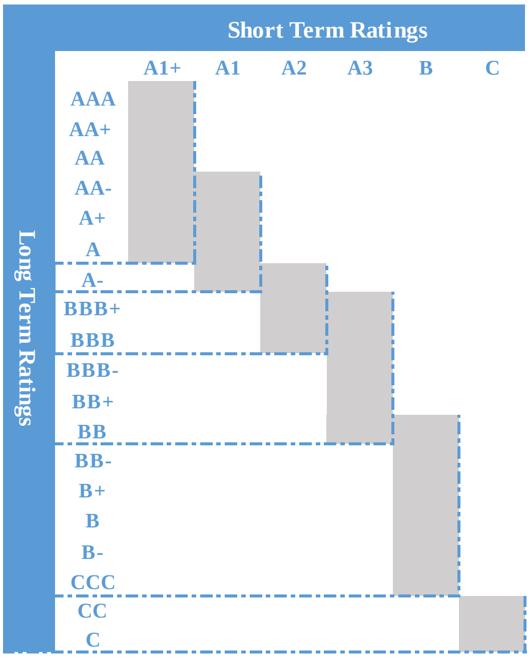
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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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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)
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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)
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