The Pakistan Credit Rating Agency Limited

Rating Report

Liberty Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
07-Jul-2023	A+	A1	Stable	Maintain	-
09-Jul-2022	A+	A1	Stable	Maintain	-
10-Jul-2021	A+	A1	Stable	Maintain	-
10-Jul-2020	A+	A1	Stable	Maintain	-
12-Jul-2019	A+	A1	Stable	Maintain	-
11-Jan-2019	A+	A1	Stable	Maintain	-
09-Apr-2018	A+	A1	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

Liberty Mills is engaged in the business of manufacturing and processing textile fabrics and made-ups. The Company is a family-owned textile unit operating in apparel, institutional, and home textile segments. The Company's emphasis on the well-defined niche of quality-conscious institutional purchasers has resulted in customer concentration, long-lasting relationships with high-profile clients, and consistent quality that aids in risk management. Currently, the company is operating a spinning unit with 10,776 rotors/spindles with a production capacity of 1,600 bags per day and Air Jet weaving unit of 145 looms having a production capacity of 100,000 meters of fabric per day in Nooriabad location. In addition to this the company is also operating another weaving unit of 106 Sulzer looms in Karachi having a capacity of 28,000 meters of fabric per day. The total number of machines in finishing mill / wet processing are 128 having a final production capacity of 350,000 meters per day and made-ups (stitching machines: 1,900 machines). The business profile of Liberty Mills is solid; it derives strength from being a value-added textile operator. The multiplicity in revenue streams acts as a buffer, protecting the Company's profitability to a large extent. The Company has seen a significant boost in topline over the last few years. During FY22, sales were recorded at PKR 50.2bln (FY21: PKR 34.1bln). In 9MFY23, revenue stood at PKR 48.8bln comprising mainly of exports. The Company has managed to cut down its expenses which contributed to a higher gross profit margin and ultimately, recorded a net profitability of PKR 6.6bln. The financial risk matrix of the Company displayed a decent performance as borrowings diluted, whereas the equity base of the Company reflected a robust increase to PKR 32.7bln in 9MFY23. Availed borrowings are under LTFF and TERF (at minimal rates). Liberty Group - the Sponsor - intends to expand its industrial footing with a diversification philosophy. Pakistan Aluminum Beverage Cans Limited, a large long-term project is fully in operation. Several medium and long-term projects are underway at the group- level including (i) Pharmaceutical projects and (ii) Hydro Power projects. Future success will depend on the business's ability to expand in scope and maintain dividends or other sources of income.

During 9MFY23, the textile exports were valued at $12.47bln compared to $14.24bln, reflecting a 12% decline YoY - the declining trend has been recorded in the last two quarters. The Country’s textile exports for the month of March clocked in at US$1.26bln, up 7% MoM. The decline in the previous overall exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand in international markets is also a challenge. In volume terms, Knitwear, Readymade Garments, Bedwear, and Towels increased by 18%, 13%, 5%, and 2% MoM respectively. The demand pattern is expected to improve in the upcoming quarters.

Disclosure

Name of Rated Entity	Liberty Mills 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),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Composite and Garments(Dec-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure Liberty Mills Limited (Liberty Mills) is an unlisted, public limited concern incorporated in 1964.

Background Liberty Mills commenced operations in 1964 as a private limited company. Later, in 1969, its legal status was changed to a public, listed company. In Dec'13, the company was delisted from the stock exchange.

Operations Liberty Mills is in the business of manufacturing and processing textile fabrics and made-ups. It operates in two main segments: processing (dyeing and printing) and home textile. The company has set up its backward integration units of spinning and weaving which are fully in operation and these will enhance efficiency along with limited dependency, going forward. The company generates electricity for its in-house use through captive power generation. Its manufacturing facility is located at Sindh Industrial and Trading Estate in Karachi and Nooriabad.

Ownership

Ownership Structure Liberty Mills is the flagship company of the Liberty Group. It is owned wholly by the Mukaty Family, mainly through the family members.

Stability In the absence of a group holding company and the personal relationship that exists between the sponsors, there is no formal succession plan, which may have implications for the stability of the company.

Business Acumen With almost four decades of experience, the Liberty Group has expertise in the textile and energy sectors of Pakistan. The sponsors carry extensive diversified industrial experience.

Financial Strength Apart from its presence in textile, and energy including wind power projects and aluminum, the Group also has interests in the pharmaceutical sector. The sponsors have shown a willingness and ability to support the company in times of need.

Governance

Board Structure The Board of Directors comprises seven members of the Mukaty family. The Board is Chaired by Mr. Muhammad Ashraf who also holds the CEO office. The absence of independent oversight indicates a need for improvement in the governance structure of the company.

Members' Profile The Chairman, Mr. Muhammad Ashraf, brings with him over 30 years of experience in the local textile industry. Meanwhile, all board members have significant industry-related as well as diversified experience and have a long association with the Liberty Group.

Board Effectiveness Board meetings are conducted at regular intervals. However, documentation of discussion in meetings needs improvement. To ensure proper oversight, the company has also formed two committees – Audit, and Human Resource & Remuneration – to assist the board on relevant matters.

Financial Transparency M/s Kreston Hyder Bhimji & Co. Chartered Accountants is the external auditor of the company. They are classified by the State Bank of Pakistan in "Category A" on its panel of auditors. The auditor gave an unqualified opinion on the company's financial statements for the year ended June 30, 2022.

Management

Organizational Structure The structure of the company is currently divided into ten functional departments, with the Head of each department reporting directly to CEO, Mr. Muhammad Ashraf.

Management Team Mr. Muhammad Ashraf – CEO of the company is supported by a team of experienced professionals. Most of the senior management has been associated with the company for a reasonably long period of time. Prior to joining Liberty Mills, he was also the CEO of Liberty Power Tech Limited.

Effectiveness Liberty Mills maintains adequate IT infrastructure and related controls. The company has a comprehensive reporting system for the management to keep track of activities.

MIS Oracle based Enterprise Resource Planning (ERP) system has been deployed which provides an integrated view of business processes, facilitating comprehensive MIS reporting.

Control Environment Liberty has a well-trained quality control department. The company is ISO 9001 certified. It also has an internal audit department that reports directly to the CEO, while it should report to the Audit Committee of the Board, to ensure the effectiveness of the function.

Business Risk

Industry Dynamics During 9MFY23, the textile exports were valued at $12.47bln compared to $14.24bln, reflecting a 12% decline YoY - the declining trend has been recorded in the last two quarters. The Country's textile exports for the month of March clocked in at US$1.26bln, up 7% MoM. The decline in the previous overall exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand in international markets is also a challenge. During the month of March, value-added textile exports increased by 6% MoM to US$863mln mainly due to Readymade Garments and Knitwear increasing by 8% and 12% MoM respectively while towels decreased by 6% MoM. Basic textiles witnessed an increase of 8% MoM to US$230mln in Mar-23. In volume terms, Knitwear, Readymade Garments, Bedwear, and Towels increased by 18%, 13%, 5%, and 2% MoM respectively. The demand pattern is expected to improve in the upcoming quarters.

Relative Position Liberty Mills is placed among the major value-added textile exporters of Pakistan. The company faces competition from other large players such as Yunus Textile Mills, Kohinoor Textile Mills, Gul Ahmed and Nishat Mills.

Revenues The company's topline has recorded a sizable increase to PKR 50.2bln during FY22 (FY21: PKR 34.12bln) mainly attributable to enhanced exports and rupee depreciation. The company's sales have remained tilted towards exports (FY22: 96%). Sales are moderately diversified in several geographical regions. During 9MFY23, sales were recorded at PKR 48.8bln comprising mainly of exports.

Margins The company's gross margins recorded improvement (FY22: 14%, FY21: 9.9%). Operating margins also recorded an increase to 6.3% (end-Jun21: 3.1%). Whereas, in 9MFY23, gross and operating profit margins stood at 21.7% and 15.8% respectively. During FY22, net income was reduced to PKR 446mln (FY21: PKR 2.19bln). During 9MFY23, the operating profit enhanced to PKR 7.7bln; supplemented by other income PBIT clocked in at PKR 10bln. Despite an increase in finance cost to PKR 2.5bln, the net profitability was recorded at PKR 6.6bln.

Sustainability Currently, the company is operating a spinning unit with 10,776 rotors/spindles with a production capacity of 1,600 bags per day and Air Jet weaving unit of 145 looms having a production capacity of 100,000 meters of fabric per day in Nooriabad location. In addition to this the company is also operating another weaving unit of 106 Sulzer looms in Karachi having a capacity of 28,000 meters of fabric per day. The total number of machines in finishing mill / wet processing are 128 having a final production capacity of 350,000 meters per day and made-ups (stitching machines: 1,900 machines). Liberty Wind Power 1 Limited and Liberty Wind Power 2 Limited (of 50 MW each) are wholly owned subsidiaries of the company and are operational. Tariff True up of both projects have been submitted with NEPRA. Further Interim Relief applications with respect to tariff indexation have been submitted to the Authorities. Both the projects are supplying electricity to the National Grid.

Financial Risk

Working Capital Liberty's working capital requirements are a function of its inventory and receivables, for which the company relies on a mix of internal generation and short-term borrowings (STBs). The company's net cash cycle was reduced to (9MFY23: 156 days, FY22: 162 days). Moreover, inventory days also dropped down to 108 days from 148 days in FY22.

Coverages The company's coverage improved (Interest coverage: FY22: 2.6x, FY21: 0.5x) due to a massive improvement in cash flow from operations. Further, in 9MFY23, the interest coverage ratio increased to 3.7x. Also, short-term trade leverage improved recently (9MFY23: 21%, FY22: 9.7%)

Capitalization Liberty maintains a moderately leveraged capital structure. Total borrowings recorded at PKR 37bln in 9MFY23, (FY22: PKR 38bln) resulted in leveraging of 53% against 59% as of end-Jun22. During 9MFY23, the equity base of the company has also sizably improved to PKR 32.7bln (end-Jun22: PKR 26bln).

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Liberty Mills Limited	Mar-23	Jun-22	Jun-21	Jun-20
Textile	9M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	17,525	16,988	10,050	5,830
2 Investments	8,377	7,444	10,648	8,877
3 Related Party Exposure	9,499	8,793	8,674	7,782
4 Current Assets	42,974	41,411	28,719	23,657
a Inventories	*20,644*	*24,464*	*16,349*	*11,284*
b Trade Receivables	*13,350*	*7,902*	*5,919*	*3,770*
5 Total Assets	78,376	74,635	58,092	46,145
6 Current Liabilities	7,354	10,262	5,178	4,458
a Trade Payables	*3,728*	*6,812*	*3,197*	*2,852*
7 Borrowings	37,045	38,157	27,621	20,021
8 Related Party Exposure	809	1,053	230	1,691
9 Non-Current Liabilities	466	104	450	51
10 Net Assets	32,702	25,059	24,613	19,925
11 Shareholders' Equity	32,702	25,059	24,613	19,868
B INCOME STATEMENT				
1 Sales	48,881	50,293	34,125	28,316
a Cost of Good Sold	*(38,291)*	*(43,274)*	*(30,747)*	*(23,980)*
2 Gross Profit	10,590	7,018	3,378	4,337
a Operating Expenses	(2,864)	(3,830)	(2,311)	(1,923)
3 Operating Profit	7,726	3,189	1,067	2,414
a Non Operating Income or (Expense)	*2,355*	*(837)*	*3,080*	*410*
4 Profit or (Loss) before Interest and Tax	10,081	2,352	4,147	2,824
a Total Finance Cost	*(2,647)*	*(1,632)*	*(1,031)*	*(608)*
b Taxation	*(766)*	*(274)*	*(922)*	*(349)*
6 Net Income Or (Loss)	6,667	446	2,194	1,867
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*9,323*	*3,918*	*411*	*2,373*
b Net Cash from Operating Activities before Working Capital Changes	*7,102*	*2,537*	*(447)*	*2,398*
c Changes in Working Capital	*14*	*(7,845)*	*(5,275)*	*(3,896)*
1 Net Cash provided by Operating Activities	7,116	(5,308)	(5,722)	(1,498)
2 Net Cash (Used in) or Available From Investing Activities	(2,252)	(6,048)	(2,601)	(8,005)
3 Net Cash (Used in) or Available From Financing Activities	(430)	3,838	5,862	797
4 Net Cash generated or (Used) during the period	4,433	(7,518)	(2,461)	(8,706)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	29.6%	47.4%	20.5%	--
b Gross Profit Margin	21.7%	14.0%	9.9%	15.3%
c Net Profit Margin	13.6%	0.9%	6.4%	6.6%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	19.1%	-7.8%	-14.3%	-5.4%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	30.8%	1.8%	9.9%	9.4%
2 Working Capital Management				
a Gross Working Capital (Average Days)	186	198	200	194
b Net Working Capital (Average Days)	156	162	167	157
c Current Ratio (Current Assets / Current Liabilities)	5.8	4.0	5.5	5.3
3 Coverages				
a EBITDA / Finance Cost	3.7	3.1	1.1	6.4
b FCFO / Finance Cost+CMLTB+Excess STB	2.9	1.6	0.2	3.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.2	4.7	-15.1	2.3
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	53.6%	61.0%	53.1%	52.2%
b Interest or Markup Payable (Days)	94.2	110.3	85.4	102.9
c Entity Average Borrowing Rate	8.8%	5.2%	3.5%	2.1%

Credit Rating

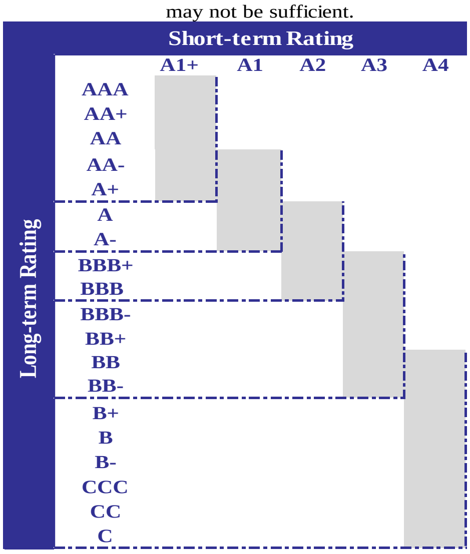
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

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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Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

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

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(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)

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(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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