The Pakistan Credit Rating Agency Limited

Rating Report

Ahmed Fine Textile Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
23-Feb-2023	A	A1	Stable	Upgrade	-
23-Feb-2022	A	A2	Stable	Upgrade	-
25-Aug-2021	A-	A2	Positive	Maintain	-
28-Aug-2020	A-	A2	Stable	Maintain	-
29-Aug-2019	A-	A2	Stable	Maintain	-
28-Feb-2019	A-	A2	Stable	Maintain	-
29-Aug-2018	A-	A2	Stable	Upgrade	-
28-Feb-2018	BBB+	A2	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect Ahmed Fine Textile Mills Limited's (Ahmed Fine) association with a renowned business group in Pakistan. The Company was primarily engaged in the spinning business and now the company has also acquired the wholly owned subsidiary – Fazal Rehman Fabrics Limited – a weaving unit. This has further strengthened the positioning of the company on a standalone basis. Furthermore, the company has embarked upon a value-added segment by establishing a towel unit with an operational capacity of 25 terry looms. The entity ratings incorporate the Company's improving business profile plus its strong financial risk matrix reflected by a reasonable working capital cycle; healthy coverages; and moderately leveraged capital structure. The Company achieved commendable profitability in FY22. The momentum was maintained in the subsequent quarter. During 1QFY23, the Company's revenue grew to stand at PKR 8.9bln. Healthy margins have strengthened the net income to stand at PKR 479mln. The management is positive about sustaining the growth momentum, going forward. Furthermore, Ahmed Fine is planning on enhancing its spinning capacity by 18,000 spindles deemed to be operational in the medium term thereby improving its business profile to boost revenues. The import of raw materials has become a challenge to manage which is quite essential for continued operations. During 7MFY23, the textile exports were valued at $10.08bln compared to $10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand for yarn in international markets is also a challenge. The analysis of 5MFY23 reveals that among value-added items, bedwear has witnessed the largest decline of 19% (on an MoM basis), down to $217 million. Knitwear remained on the downward path in October 2022 and declined by 10% to $392 million. Among non-value-added items, the cotton yarn has shown the largest decline of 35%. Moreover, a slowdown is prevailing in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. The demand pattern is expected to improve post-Jun-23.

The ratings are dependent on the continuous strengthening of business operations under the current economic conditions; and a sound financial profile with good coverages and moderate leveraging. The Company's ability to generate ensuing cash flows to fulfill its financial obligations will remain critical for the ratings.

Disclosure

Name of Rated Entity	Ahmed Fine Textile 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 | Spinning(Sep-22)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure Ahmed Fine Textile Mills Limited (Ahmed Fine), a public unlisted company, was incorporated in 1989.

Background The Company is engaged in the manufacturing and marketing of different varieties of yarn, fabric, and towels. Previously, the Company was only involved in the manufacturing of yarn. In July 2021, the company acquired the wholly-owned subsidiary Fazal Rehman Fabrics; a weaving unit. Now Ahmed Fine Textile Mills Limited operates as a composite unit.

Operations The production capacity of the company stands at 78,960 spindles, 492 looms, and 25 terry looms. The Company has two state-of-the-art spinning units, one located at Multan & second one located at Rahim Yar Khan, having a consolidated annual production capacity of 20.5 million Kg yarn. The company's weaving unit is located at Multan and is engaged in the manufacturing of greige fabric and export quality towels.

Ownership

Ownership Structure The Company is jointly owned by the families of Mian Naseem and Mian Farooq. Both belong to the same family descending from the late Mr. Fazal-ur-Rehman.

Stability The clear shareholding pattern of the Company along with the mutual consent of both Groups over its controls portrays a structured line of succession. However, the transfer of ownership to the next generation is yet to be documented.

Business Acumen The sponsoring Groups have over five decades of presence in Pakistan's textile industry, developing expertise to sustain through the industry's volatility. Mr. Rehman Naseem – a textile veteran, primarily manages the Company's operations with sufficient acumen to sustain and flourish in the competitive textile industry.

Financial Strength Fazal Group maintains a dominant position in Multan's textile industry. Fazal Group, in particular, is one of the most resourceful groups with strong financial health. Strategic investment in fertilizers and textile provides ample room for financial support to Ahmed Fine if needed.

Governance

Board Structure The Company's seven-member Board consists of four Fazal Group representatives, including the Chairman and CEO.

Members' Profile The board comprises experienced professionals and has a reasonably long association with the Company. Mr. Sheikh Naseem is the Chairman of the board. He carries with him over five decades of experience in the textile industry.

Board Effectiveness The Board has Audit Committee in place to assist the board on relevant matters. Additionally, the attendance of board members in meetings remained strong and meeting minutes are documented.

Financial Transparency M/s Yousuf Adil & Co., Chartered Accountants are the external auditor of the Company. They have expressed an unqualified opinion on the company's annual financial statements for FY22.

Management

Organizational Structure The management control of the Company vests with Fazal Group, with Mr. Rehman Naseem as CEO of the Company. The organizational structure of the Company is divided into five functional departments.

Management Team Mr. Rehman Naseem – the – CEO is a Columbia University graduate and carries over two decades of experience in the textile sector. Moreover, Ahmed Fine employs long-associated professionals, which bodes well for the Company's sustainable growth. Mr. Naveed Amer is serving in the capacity of CFO, carrying almost three decades of experience.

Effectiveness The management meetings are held periodically with the formal recording of meeting minutes, followed by need-based meetings to resolve bottlenecks and to ensure smooth operations.

MIS Ahmed Fine has deployed Oracle based Enterprise Resource Planning (ERP) system that provides comprehensive MIS reporting.

Control Environment Ahmed Fine is accredited with various international certifications for compliance. The Company is following the latest Quality Assurance Standards for yarn and fabric production. A few of the prominent certification includes ISO 9001, Lycra assured, and Fair Trade.

Business Risk

Industry Dynamics During 7MFY23, the textile exports were valued at $10.08bln compared to $10.93bln, reflecting an 8% decline YoY – the declining trend has been recorded in the last few months. The decline in exports is driven by attrition in the demand pattern of export avenues. The hike in cotton prices and low demand for yarn in international markets is also a challenge. The analysis of 5MFY23 reveals that among value-added items, bedwear has witnessed the largest decline of 19% (on an MoM basis), down to $217 million. Knitwear remained on the downward path in October 2022 and declined by 10% to $392 million. Among non-value-added items, cotton yarn has shown the largest decline of 35%. Moreover, a slowdown is prevailing in textile demand amid burgeoning inflationary pressures in the exporting destinations, especially in the US and European countries. The demand pattern is expected to improve post-Jun-23.

Relative Position The Company possesses 78,960 spindles and the company has also acquired a weaving unit that comprises 492 looms & 25 towel looms. Hence, on a standalone basis, the company is among the medium-term players of the market.

Revenues During FY22, the revenues of the company increased by 61% to stand at PKR 30,126mln (FY21: PKR 18,673mln) attributable to the better prices at international level. During 1QFY23, the revenues of the company recorded at PKR 8,090mln with the increased concentration of the local sales to total sales clocked in at 75%.

Margins During FY22, the gross margin of the company largely remained stagnant at 15.6% (FY21: 15.2%). The operating margin of the company witnessed a similar trend clocking in at 12.3% (FY21: 12.9%). The Finance cost of the company increased to PKR 935mln (FY21: 417mln) owing to the increase in the policy rate. The net income of the company was recorded at PKR 2,405mln (FY21: PKR 1,626mln). Subsequently, the net margin declined to 7.98% (FY21: 8.71%). During 1QFY23, the gross profit margin of the company was recorded at 16.4%, whereas, the operating profit margin of the company inched down to 12%. The finance cost of the company was recorded at PKR 462mln. Subsequently, the net profit margin of the company declined to 5.9%.

Sustainability Ahmed Fine had planned an expansion of its spinning facilities, which came to a halt due to the coronavirus pandemic. However, going forward, the Company has resumed the expansion process in which spinning production facilities are to be increased by 50,000 spindles, this whole expansion process was to be done in two phases. In the first phase, 32,000 spindles are installed at an estimated cost of PKR 6bln and have been operational since Dec-22. In the second phase, the other 18,000 spindles will be installed for which LCs are opened.

Financial Risk

Working Capital At end-Sept22, the net working capital cycle days increased to 123 days (end-Jun22: 75 days) on the back of increased inventory days. Furthermore, trade assets of the company increased by 25% to stand at PKR 17,969mln (end-Jun22: PKR 14,389mln) owing to a higher inventory level clocking in at PKR 10,596mln (end-Jun22: 8,289mln). Ahmed Fine's working capital needs are mostly fulfilled through internal cash flows along with a high portion of short-term borrowing clocking in at PKR 10,115mln (end-Jun22: 8,858mln). This results in ST trade leverage of 22.1% (end-Jun22: 23.1%).

Coverages During 1QFY23, The Company recorded free cash flows clocking in at PKR 1,141mln (FY22: PKR 4,240mln). The interest coverage was recorded at 2.5x (FY22: 5.0x). Whereas, debt coverage was recorded at 1.8x (FY22: 2.4x).

Capitalization At end-Sept22, Ahmed Fine's leverage increased to 67.6% (end-Jun22: 65.5%) as total debt increased. The total borrowings of the company increased to PKR 19,844mln (end-Jun22: 17,101mln) out of which ST borrowing constitutes 51%. The equity base of the company increased to stand at PKR 9,491mln (end-Jun22: 9,024mln).

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Ahmed Fine Textile Mills Limited Textile | Composite	Sep-22 3M	Jun-22 12M	Jun-21 12M	Jun-20 12M
A BALANCE SHEET				
1 Non-Current Assets	14,748	13,778	1,922	1,812
2 Investments	40	-	-	-
3 Related Party Exposure	1,674	1,841	355	355
4 Current Assets	19,291	15,503	2,934	2,228
a Inventories	*10,596*	*8,289*	*1,298*	*935*
b Trade Receivables	*5,059*	*3,735*	*1,191*	*963*
5 Total Assets	35,753	31,122	5,211	4,396
6 Current Liabilities	5,875	4,465	883	626
a Trade Payables	*3,876*	*1,991*	*166*	*46*
7 Borrowings	19,844	17,101	1,430	1,409
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	542	532	150	165
10 Net Assets	9,491	9,024	2,749	2,196
11 Shareholders' Equity	9,491	9,024	2,749	2,196
B INCOME STATEMENT				
1 Sales	8,090	30,126	6,290	4,590
a Cost of Good Sold	*(6,766)*	*(25,396)*	*(5,294)*	*(3,996)*
2 Gross Profit	1,324	4,729	996	593
a Operating Expenses	(356)	(998)	(139)	(90)
3 Operating Profit	968	3,731	857	504
a Non Operating Income or (Expense)	*75*	*139*	*(58)*	*(32)*
4 Profit or (Loss) before Interest and Tax	1,043	3,870	799	471
a Total Finance Cost	*(462)*	*(935)*	*(117)*	*(210)*
b Taxation	*(101)*	*(530)*	*(127)*	*(63)*
6 Net Income Or (Loss)	479	2,405	555	198
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,141*	*4,240*	*887*	*579*
b Net Cash from Operating Activities before Working Capital Changes	*824*	*3,443*	*745*	*385*
c Changes in Working Capital	*(2,379)*	*(5,648)*	*(395)*	*(476)*
1 Net Cash provided by Operating Activities	(1,555)	(2,205)	350	(91)
2 Net Cash (Used in) or Available From Investing Activities	(1,180)	(7,369)	(275)	(173)
3 Net Cash (Used in) or Available From Financing Activities	2,815	9,443	21	(44)
4 Net Cash generated or (Used) during the period	80	(131)	96	(307)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	7.4%	378.9%	37.0%	-5.4%
b Gross Profit Margin	16.4%	15.7%	15.8%	12.9%
c Net Profit Margin	5.9%	8.0%	8.8%	4.3%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	-15.3%	-4.7%	7.8%	2.2%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	20.7%	40.9%	22.4%	9.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	156	88	127	128
b Net Working Capital (Average Days)	123	75	121	124
c Current Ratio (Current Assets / Current Liabilities)	3.3	3.5	3.3	3.6
3 Coverages				
a EBITDA / Finance Cost	3.1	5.5	9.7	3.2
b FCFO / Finance Cost+CMLTB+Excess STB	1.8	2.4	1.9	2.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.5	2.4	1.8	3.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	67.6%	65.5%	34.2%	39.1%
b Interest or Markup Payable (Days)	76.3	100.7	76.2	84.6
c Entity Average Borrowing Rate	14.9%	10.0%	6.7%	12.6%

Credit Rating

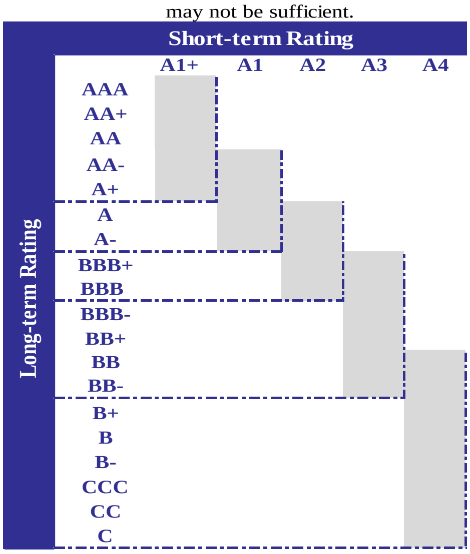
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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

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

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