



The Pakistan Credit Rating Agency Limited

Rating Report

Mahmood Textile Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jun-2021	A-	A2	Stable	Maintain	-
26-Jun-2020	A-	A2	Stable	Maintain	YES
27-Dec-2019	A-	A2	Stable	Maintain	-
28-Jun-2019	A-	A2	Stable	Maintain	-
28-Dec-2018	A-	A2	Stable	Maintain	-
28-May-2018	A-	A2	Stable	Maintain	-
15-Aug-2017	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect improving business profile of Mahmood Textile Mills limited ('Mahmood Textile' or 'The Company') – the flagship entity of Mahmood Group. Business operations comprise a spinning segment and two weaving units, with plans to further enhance the spinning segment and establishing a new apparel unit. Recently, the Company has gone through a change in ownership structure. One brother has effectively transferred all of his stake to the remaining three brothers, vacating his position in the Board of Directors. This change is consistent with the recent re-profile of Mahmood group. Rating watch has been removed attributable to enhanced net sales and sizable incline in net profitability. Sales mix remained dominated by healthy exports. Similarly, margins recorded favorable increase. The Company is engaged in the exports of yarn and greige fabric. Hence, does not qualify for the export refinance facility. Overall, financial profile of the Company remains stretched given highly leveraged capital structure and limited borrowing capacity. However, coverage witnessed improvement during 9MFY21. The Company has a sizeable investment portfolio, which is managed at the Group level. Although, the Company has invested in blue-chip stocks, high market risk exposes the Company to significant risks. The sponsor's vast experience and the Company's association with Mahmood Group provides comfort to the ratings of the Company. Textile sector dynamics were prone to challenges posed by the third wave of the COVID-19 pandemic. The country's textile group exports, however, have witnessed 9.06% growth during the first nine months (July-March) 2020-21 and remained at \$11.35bln compared to \$10.40bln during the same period last year.

The ratings are dependent on the Company's ability to sustain its operations in prevailing conditions. The management is cognizant of these challenges and is working on this front. Meanwhile prudent working capital management and generating sustainable cashflows from core operations are important. Significant deterioration in business profile due to prolonged downturn leading to deterioration in coverages and/or margins will impact the ratings.

Disclosure

Name of Rated Entity	Mahmood Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-20),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria Rating Modifier(Jun-20)
Related Research	Sector Study Composite(Nov-20)
Rating Analysts	Ahmad Saad Siddiqi ahmad.saad@pacra.com +92-42-35869504

Profile

Legal Structure Mahmood Textile Mills Limited ('Mahmood Textile' or 'The Company') is a public listed concern, incorporated in 1970. The Company is listed on Pakistan Stock Exchange.

Background The Company is a part of Mahmood Group, which was originally established in 1935 by entering the tannery business. The group has now evolved into a diversified business empire with Mahmood Textile as the Group's flagship Company.

Operations Mahmood Textile is engaged in the production and sale of yarn and greige fabric. Its production facilities are located in Muzaffargarh, DG Khan and Multan. The Company has 115,920 spindles and 196 looms. The Company's energy requirement of ~11MW is completely met by generation capacity of ~21MW. Furthermore, the Company has a line from MEPCO as backup.

Ownership

Ownership Structure Cumulatively, sponsors own ~45% of shareholding through group companies, directors as well as distant relatives. Remaining shareholding is held by the general public.

Stability The Group has no holding Company. Third generation of the sponsor family is actively involved in the operations of the Company but no formal succession plan has been announced. Documentation or formation of a family office will bode well with stability and succession of ownership.

Business Acumen With over eight decades of experience, the sponsors have expertise in diversified sectors including textile, tanneries, real estate and food.

Financial Strength Mahmood Group maintains an adequate financial profile with a considerable equity base through Group companies and stock market investments. Investments enhance the Group's financial profile through dividends and capital gains but also expose the Group to financial risk. The group has strong financial strength to support the Company, if needed.

Governance

Board Structure Mahmood textile has an eight-member board including two independent directors. The board is dominated by Mahmood family members.

Members' Profile Mr. Khawaja Muhammad Ilyas having more than four decades of textile experience is the Chairman of the Company. He has been a key position holder in various local corporate bodies of Pakistan. Overall, the board members possess diversified knowledge and experience which leads to a good skill mix of their individual competencies.

Board Effectiveness In line with best corporate governance practices, there are two sub-committees in place to assist the Board on relevant matters: Audit and Human Resource. Attendance of directors in meetings remains high, boding well for the board's effectiveness. Meanwhile, minutes have room for improvement.

Financial Transparency M/s Shinewing Hameed Chaudhri & Co. Chartered Accountants are the external auditors of the Company, listed in Category "B" of the State Bank's panel of auditors. The auditor expressed an unqualified opinion on the financial statements of the company for the period ended June 30th, 2020. There is also an internal audit function in place to ensure effective oversight, with the Head of Internal Audit reporting directly to the Board Audit Committee.

Management

Organizational Structure The organizational structure of Mahmood Textile is divided into various departments reporting to the CEO and CFO. The departments are as follows: (i) Audit (ii) Taxation (iii) HR and Admin (iv) IT and ERP (v) Export and (vi) Finance.

Management Team The Company CEO – Mr. Khawaja M. Iqbal – has been associated with the Company for over four decades and also acts as the group Chairman. Mr. Iqbal is supported by a team of seasoned professionals, most of whom have been associated with the Company for a reasonably long period of time.

Effectiveness Adequate IT infrastructure and related controls are maintained. There is preparation of regular reports regarding the Company's receivables and payables position, purchases and procurement, audit report, etc, to be submitted to higher management.

MIS The Company has deployed Oracle based ERP with daily and monthly MIS to ensure timely availability of information for effective decision making.

Control Environment Mahmood Textile is accredited with international certifications for compliance including ISO 9001. The company adheres to latest quality assurance standards for fabric production and trade in addition to employment of quality control procedures.

Business Risk

Industry Dynamics The country's textile exports have witnessed 9.06% growth during the first nine months (July-March) of FY21 and remained at \$11.35bln compared to \$10.4bln during the same period last year. Textile group exports have witnessed an increase of 9.85% in Mar-21 as it stood at \$1.35bln compared to \$1.2bln during Feb-21. Textile group exports have registered a growth of 30.38% year-on-year basis as it reached \$1.3bln in Mar-21 compared to \$1.03bln in Mar-20. COVID-19 pandemic and related lock down imposed by the governments around the globe in FY20 had its ramifications however Pakistani textile exports have been seen rebounding in 1HFY21. Most of the segments recorded incline in prices (USD terms) which is positive. The export outlook is likely to remain stable in the medium term as textile units have been operating at optimized capacity levels.

Relative Position With 115,920 spindles and 196 looms, Mahmood Textile is one of the large players in the industry. Cumulatively, Mahmood Group owns ~300,000 spindles and 750 air-jets looms and is one of the biggest textile manufacturing groups in Pakistan.

Revenues During 3QFY21, Mahmood Textile's topline amounted to PKR 20,305mln (3QFY20: PKR 19,889mln) growing by 2.1%. The Company's topline predominately comprises yarn sales (61%) followed by greige fabric (29%). Export market made up 81% of the total sales because of established overseas customer base and better margins on export sales.

Margins The Company's gross profit margin increased to 11.79% in 3QFY21 (3QFY20: 8.6%). Cost of sales witnessed a decline of 1.5%. Similarly, operating margin also inclined, and stands at 7.4% (3QFY20: 4.3%) due to lower cost of sales. During 3QFY21, the Company's net profit increased significantly to PKR 720mln (3QFY20: PKR 241mln). Consequently, net profit margin rose to 3.5% (3QFY20: 1.2%).

Sustainability During the last quarter of FY20 Mahmood Textile had to briefly shut down its operations as per government directive for some time. However, the Company still possessed sound financial stability on strong footing and no impairment was found in financial assets and the liabilities of the Company. SBP took some proactive measure for the revival of the economy and deferred loan payments for one year with reduction in policy rates. The Company availed these facilities that helped to ease cash flow of the Company and resumed operational activities smoothly. The Company also placed advanced Business Intelligence System for quicker and accurate reporting, analyzing and planning to make better and efficient decisions.

Financial Risk

Working Capital Mahmood Textile's net working capital cycle decreased during 3QFY21 to 138days (FY20: 141 days) due to lower inventory days (3QFY21: 104days, FY20: 109days). The Company increased its reliance on short term borrowings as it increased by 29% to PKR 11,331mln (FY20: PKR 8,764mln) to finance its working capital needs.

Coverages Free cash flows (FCFO) increased in 3QFY21 to PKR 2,063mln (3QFY20: PKR 1,863mln) factor of increased profits from operations. Consequently, interest coverage ratio increased to 2.7x (FY20: 1.8x) while debt coverage ratio decreased to 1.5x (FY20: 1.6x) as the Company increased its reliance on borrowing.

Capitalization During 3QFY21, the Company's capital structure remained highly leveraged at 65.4% (FY20: 62.7%). The Company's leveraging deteriorated due to increase in total borrowings to PKR 17,575mln (FY20: PKR 14,441mln) on account of increase in short term borrowings. Shareholder's equity increased during 3QFY21 to PKR 9,302mln (FY20: PKR 8,582mln).



Mehmood Textile Mills Limited Composite	Mar-21 9M	Jun-20 12M	Jun-19 12M	Jun-18 12M
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A BALANCE SHEET

1 Non-Current Assets	8,249	8,591	8,951	5,603
2 Investments	1,672	725	1,370	2,508
3 Related Party Exposure	4,231	4,190	3,889	1,539
4 Current Assets	14,451	11,942	11,056	8,980
<i>a Inventories</i>	8,440	7,059	7,593	4,247
<i>b Trade Receivables</i>	2,375	3,103	1,686	2,195
5 Total Assets	28,603	25,448	25,266	18,629
6 Current Liabilities	1,547	2,312	2,006	1,561
<i>a Trade Payables</i>	186	303	222	219
7 Borrowings	17,575	14,441	14,647	11,935
8 Related Party Exposure	5	8	49	5
9 Non-Current Liabilities	175	104	81	-
10 Net Assets	9,302	8,582	8,484	5,128
11 Shareholders' Equity	9,302	8,582	8,484	4,854

B INCOME STATEMENT

1 Sales	20,305	24,465	24,387	18,154
<i>a Cost of Good Sold</i>	(17,911)	(22,352)	(21,813)	(16,874)
2 Gross Profit	2,394	2,114	2,574	1,280
<i>a Operating Expenses</i>	(892)	(1,034)	(906)	(794)
3 Operating Profit	1,502	1,079	1,667	487
<i>a Non Operating Income or (Expense)</i>	356	750	921	531
4 Profit or (Loss) before Interest and Tax	1,859	1,829	2,588	1,018
<i>a Total Finance Cost</i>	(913)	(1,527)	(1,526)	(743)
<i>b Taxation</i>	(226)	(231)	(312)	(63)
6 Net Income Or (Loss)	720	72	751	212

C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	2,063	2,326	3,397	739
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	836	165	702	41
<i>c Changes in Working Capital</i>	(3,183)	(611)	(1,771)	(1,325)
1 Net Cash provided by Operating Activities	(2,347)	(446)	(1,069)	(1,284)
2 Net Cash (Used in) or Available From Investing Activities	(816)	672	(1,613)	(2,323)
3 Net Cash (Used in) or Available From Financing Activities	3,135	(205)	2,675	3,626
4 Net Cash generated or (Used) during the period	(28)	20	(8)	19

D RATIO ANALYSIS

1 Performance				
<i>a Sales Growth (for the period)</i>	10.7%	0.3%	34.3%	15.3%
<i>b Gross Profit Margin</i>	11.8%	8.6%	10.6%	7.1%
<i>c Net Profit Margin</i>	3.5%	0.3%	3.1%	1.2%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-5.5%	7.0%	6.7%	-3.2%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	10.9%	0.8%	10.2%	4.9%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	141	145	118	131
<i>b Net Working Capital (Average Days)</i>	138	141	114	128
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	9.3	5.2	5.5	5.8
3 Coverages				
<i>a EBITDA / Finance Cost</i>	3.0	1.9	2.7	1.4
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.5	1.6	1.5	0.8
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	3.6	5.4	2.1	29.2
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	65.4%	62.7%	63.3%	71.1%
<i>b Interest or Markup Payable (Days)</i>	85.7	83.8	101.8	113.9
<i>c Entity Average Borrowing Rate</i>	6.6%	8.8%	9.1%	6.6%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



*The correlation shown is indicative and, in certain cases, may not hold.

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. ‘Stable’ outlook means a rating is not likely to change. ‘Positive’ means it may be raised. ‘Negative’ means it may be lowered. Where the trends have conflicting elements, the outlook may be described as ‘Developing’.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

<p>Entities</p> <ul style="list-style-type: none"> a) Broker Entity Rating b) Corporate Rating c) Financial Institution Rating d) Holding Company Rating e) Independent Power Producer Rating f) Microfinance Institution Rating g) Non-Banking Finance Companies (NBFCs) Rating 	<p>Instruments</p> <ul style="list-style-type: none"> a) Basel III Compliant Debt Instrument Rating b) Debt Instrument Rating c) Sukuk Rating
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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)
- 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.
- (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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