



The Pakistan Credit Rating Agency Limited

Rating Report

Fazal Holdings (Pvt.) Limited

Report Contents

1. Rating Analysis
2. Financial Information
3. Rating Scale
4. Regulatory and Supplementary Disclosure

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
24-Nov-2020	A	A1	Stable	Maintain	-
25-Nov-2019	A	A1	Stable	Maintain	-
28-May-2019	A	A1	Stable	Maintain	-
26-Nov-2018	A	A1	Stable	Maintain	-
07-May-2018	A	A1	Stable	Maintain	-
31-Aug-2017	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Fazal Holdings (Pvt.) Limited ('Fazal Holdings' or 'the Company') is holding company for Fazal Group*. It's investment portfolio comprises a combination of strategic investments (long-term investments in subsidiaries and associates) and trading portfolio (with short to medium term time horizon). The ratings reflect diverse nature and profitability of strategic portfolio and strong support from sponsors. Trading portfolio comprises a combination of blue chip companies spread across diverse sectors of the economy. Fazal Holdings drives its revenue mainly from dividend income and capital gains. The dividend stream was impacted due to downturn in capital markets as an aftermath of Covid-19. The Company incurred capital losses leading to suppressed earnings and a net loss during FY20. However, the recent upturn in stock market should improve valuations. The Company has designed a conservative investment policy accordance with the Company's equity. This should help absorb the effects of volatility in stock market to an extent and keep financial risk manageable. Investment decisions are mainly led by Mr. Rehman Naseem with assistance from resources within Fazal Group and certain research/brokerage houses. Herein, institutionalization of investment policies would be beneficial. Continued sponsor support remains a key rating factor. (* The term 'Group' may be defined differently in Prudential Regulations for Corporate/Commercial Banking and/or other laws).

Ratings are dependent on the management's initiative to strengthen investment making and performance monitoring mechanism of underlying portfolio. This would facilitate Fazal Holdings assimilation into an effective holding company. At the same time, adhering to agreed financial matrix and keeping debt coverages at adequate level remains critical.

Disclosure

Name of Rated Entity	Fazal Holdings (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-20),Methodology Holding Company(Jun-20),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria Rating Modifier(Jun-20)
Related Research	Sector Study Holding Company(Aug-20)
Rating Analysts	Faiqa Qamar faiqa.qamar@pacra.com +92-42-35869504



Profile

Legal Structure Fazal Holdings (Pvt.) Limited ("Fazal Holdings" or "the Company") is a private limited company incorporated in Pakistan on April 23, 1995, under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017).

Background After incorporation in 1995, the Company was named Amir Fine Exports (Pvt.) Limited. It was engaged in the trading of yarn and cloth along with listed investments and unlisted securities. In 2016, the Company's name was changed to Fazal Holdings (Pvt.) Limited. The registered office of the Company is in Multan.

Operations Fazal Holdings principally acts as the holding company for Fazal Group's* investments (strategic investment) and also holds short term investments in quoted and un-quoted securities (trading portfolio). The Company is engaged in purchasing investment property for agricultural and rental purposes as well. (* The term 'Group' may be defined differently in Prudential Regulations for Corporate/Commercial Banking and/or other laws).

Ownership

Ownership Structure Fazal Holdings is owned by the members of the sponsoring family i.e. Fazal family. Majority shares resides with Mr. Rehman Naseem (49%). Mr. Amir Naseem Sheikh's family owns a stake of 49%; through his sons, Mr Yousaf Amir and Mr. Abdullah Amir, owning 22% each, in the Company. While, remaining shareholding resides with Mr. Sheikh Naseem.

Stability Ownership of the business is seen as stable as the major ownership vests with the sponsors with clear succession.

Business Acumen Fazal Group was incorporated in 1966 and is a renowned textile Group in Pakistan. Fazal Cloth Mills Ltd. – flagship Company of the Group, was incorporated in 1966 and had set up its first spinning unit in 1972 in Muzaffargarh. Fazal Group also operates Ahmed Fine textile Mills, Fazal Weaving Mills and Fazal Rehman Fabrics Limited among many others businesses.

Financial Strength The sponsoring Group has a prominent position in Pakistan's corporate sector, with interests in textile, fertilizer, energy and trading. The Group has strong financial muscle, portraying its ability to support Fazal Holdings, if needed

Governance

Board Structure BoD comprises three members; two directors and CEO of the Company. Limited size of the Board and dominance of sponsoring family indicates room for improvement in the overall governance framework.

Members' Profile Mr. Rehman Naseem, member of BoD, is a Columbia University graduate. He is CEO of Ahmed Fine Textile Mills Limited, Rehman Amir Fabrics Ltd and Fazal Cloth Mills. The BoD members experience is mostly concentrated towards textile and fertilizer industry.

Board Effectiveness Four board meetings were held during FY20, with majority attendance. Minutes of these meetings are formally documented. Keeping in view the investment book of the Company, absence of Board sub-committees indicates a room for improvement in effective governance.

Financial Transparency The external auditor, M/s Shingwing Hameed Chaudhri & Co, have expressed unqualified opinion on the financial statements of FY19. The firm is QCR rated and is on SBP panel of auditors category 'B'.

Management

Organizational Structure Fazal Holdings is headed by the CEO, Mr. Sheikh Naseem Ahmed. The Company operates through two main functions, Finance and MIS, headed by the Company's CFO. He reports to the CEO. Company Secretary looks after compliance related matters and reports to CEO & CFO, both.

Management Team Mr. Sheikh Naseem Ahmed has an overall experience of above 5 decades in textile and in fertilizer sector. He is also on the Board of other Fazal Group Companies. Mr. Azam, Group CFO, is an FCA and FCMA. He is associated with Fazal Group for over a decade .

Effectiveness There are no management committees in place. However, to facilitate the senior management, various reports are generated on daily, weekly and monthly basis highlighting the performance of the investment portfolio.

MIS The Company has implemented Investment Management and Accounting Software and has adopted parallel changeover method for the implementation of new system.

Control Environment The internal audit function is placed at Group level. Investment policy and Risk management are handled by the management and Director, Mr. Rehman Naseem, set investment management procedures and develop risk management policies. These practices suggest a need for improvement in the control environment of Fazal holdings.

Business Risk

Industry Dynamics Holding companies are an emerging phenomena in Pakistan. Some operating companies diversified and grew by gradually making strategic investments. Eventually, they de-merged their operations and structured themselves as a holding company to focus on existing and new investments.

Relative Position Fazal Holdings has an investment book of PKR 10.8bln comprising of Strategic Investments (PKR 7.9bln), Trading Investments (PKR 2.1bln) and Investment Properties (PKR 0.8bln). Strategic Investments comprise Fazal Group's flagship Company - Fazal Cloth (maintains a prominent position in spinning sector on a standalone basis), Fatima Energy Limited, Fatima Transmission Company Limited, Reliance Weaving Mills and Pakarab Fertilizers Limited. Trading Investments include primarily blue chip companies that keeps business risk of the Company (exposure to stock market) relatively in check.

Revenues Fazal Holdings receives dividend income from its investment portfolio, Long Term – Strategic Investment Book and Short Term Trading Portfolio. The Company's strategic investments portfolio is divided into listed and unlisted entities from textile, fertilizer and energy infrastructure sectors. Valuation of these investments decreased by 0.7% in FY20 supported by share of profits from associates, mainly from Fazal Cloth. In the Short Term Trading Portfolio, the Company's dividend income posted an increase of 1.5% and reached to PKR 133mln in FY20 (FY19: PKR 130mln). The Company increased its stake in oil and gas sectors. The Company has diluted its stake in mutual funds, commercial banks, and power sectors. In comparison to the return on KSE-100 Index, return on the Company's trading book has underperformed. On standalone basis, the Company's operating income experience a slight decline of 0.45% and reported an operating loss of PKR 266.1mln in FY20 (FY19: PKR 264.9mln). The major contributor in the operating loss is loss on remeasurement of short term investments (FY20: PKR 516mln; FY19: PKR 516mln). Furthermore, dividend income experience a rise of 9% and reached to PKR 241mln in FY20 (FY19: PKR 221mln), mainly emanating from trading portfolio.

Margins Finance costs increased by 48% (FY20: PKR 372mln, FY18: PKR 251mln) owing to an increase in the short term running finance obtained to support the Company's short term trading portfolio. Share of profits from associates helped in curtailing the losses to an extent. The Company posted net loss of PKR 520mln in FY20 (FY19: PKR 156mln).

Sustainability Sponsors intend to expand Fazal Holdings by investing in energy sector. Moreover, valuation and performance of the Company's investment books (strategic and trading) was impacted due to Covid-19. However, the recent upturn in stock market should improve valuations.

Financial Risk

Working Capital Fazal Holdings obtains long term and short term debt to finance strategic investments (Investment Property and Investments in Associates) and trading portfolio. Long term debt obtained in previous years was fully repaid in FY19. In FY20, the Company undertakes a long term debt of PKR 40mln to purchase new stocks. Short term debt increased to PKR 2.9bln in FY20 (FY19: PKR 2.7bln). Dividend inflows from these investments provides the risk absorption capacity to the Company, however, remains low.

Coverages During FY20, coverage ratio deteriorated and stood at 0.7x (FY19:1.0x), due to significant increase in finance cost . Short term debt to Trading Portfolio stood at 83% in FY20 (including Fatima Fertilizer Company Limited). This has reduced the cushion but short term investments remain in liquid scrips. In the current low interest rate scenario, the Company's coverages may improve.

Capitalization The Company has moderately leveraged capital structure. In FY20, Fazal Holdings debt to equity ratio moderately stood at 35% (FY19:31%) owing to increase in the Company's higher YoY basis short term debt. Equity base mainly represents profits accumulated over the years.



	Jun-20	Jun-19	Jun-18
	12M	12M	12M
	Audited	Audited	Audited
A BALANCE SHEET			
1 Investments	2,934	3,179	3,060
2 Related Party Investments	7,956	7,751	7,393
3 Non-Current Assets	2	2	3
4 Current Assets	178	147	83
5 Total Assets	11,071	11,079	10,539
6 Current Liabilities	286	105	71
7 Borrowings	2,964	2,705	2,143
8 Related Party Exposure	1,675	1,438	1,210
9 Non-Current Liabilities	662	685	718
10 Net Assets	5,483	6,147	6,397
11 Shareholders' Equity	5,483	6,147	6,323
B INCOME STATEMENT			
1 Total Investment Income	(169)	85	520
<i>a Cost of Investments</i>	<i>(374)</i>	<i>(252)</i>	<i>(171)</i>
2 Net Investment Income	(543)	(166)	349
<i>a Other Income</i>	<i>80</i>	<i>41</i>	<i>0</i>
<i>b Operating Expenses</i>	<i>(7)</i>	<i>(9)</i>	<i>(9)</i>
4 Profit or (Loss) before Interest and Tax	(470)	(134)	341
<i>a Taxation</i>	<i>(50)</i>	<i>(12)</i>	<i>(186)</i>
6 Net Income Or (Loss)	(520)	(146)	154
C CASH FLOW STATEMENT			
<i>a Total Cash Flow</i>	<i>271</i>	<i>243</i>	<i>219</i>
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	<i>(90)</i>	<i>23</i>	<i>43</i>
<i>c Changes in Working Capital</i>	<i>(31)</i>	<i>(156)</i>	<i>(155)</i>
1 Net Cash provided by Operating Activities	(121)	(133)	(112)
2 Net Cash (Used in) or Available From Investing Activities	(393)	(572)	708
3 Net Cash (Used in) or Available From Financing Activities	497	714	(611)
4 Net Cash generated or (Used) during the period	(17)	9	(14)
D RATIO ANALYSIS			
1 Performance			
<i>a Asset Concentration (Market Value of Largest Investment / Market Value of Total Investments)</i>	46.6%	51.5%	51.2%
<i>b Core Investments / Market Value of Total Investments</i>	0.1%	0.0%	0.0%
<i>c Marketable Investments / Total Investments</i>	19.7%	21.9%	24.3%
2 Coverages			
<i>a TCF / Finance Cost</i>	0.7	1.0	1.3
<i>b TCF / Finance Cost + CMLTB</i>	0.7	1.0	0.9
<i>c Loan to Value (Funding / Market Value of Total Investments)</i>	1.0	1.0	0.7
3 Capital Structure (Total Debt/Total Debt+Equity)			
<i>a Leveraging [Funding / (Funding + Shareholders' Equity)]</i>	35.1%	30.6%	26.0%
<i>b (Funding + Off Balance Sheet Exposure) / Shareholders' Equity</i>	54.1%	44.4%	35.1%

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.

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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(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)

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- 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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- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
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- (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)
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- (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)
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- (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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