The Pakistan Credit Rating Agency Limited

Rating Report

Al Rahim Textile Industries Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
25-Jan-2020	A-	A2	Stable	Maintain	-
26-Jul-2019	A-	A2	Stable	Maintain	-
25-Jan-2019	A-	A2	Stable	Maintain	-
27-Jul-2018	A-	A2	Stable	Maintain	-
17-Jan-2018	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Al Rahim Textile Industries Limited (Al Rahim) is a family owned textile company that enjoys a strong position in towel manufacturing. Al Rahim's primary business remains export oriented towel production. It also provides fabric and other processing facilities to its associated company – Al Rahim Retail Limited - and to other local manufacturers. Overall export volumes of the towel industry have stagnated mainly due to high cost of doing business and increasing competition in major export markets. Although the Company's volumes remained stagnated, the top-line grew due to positive impact of rupee devaluation. Towel industry enjoys relatively better margins that are reflected in Al Rahim's profitability. However, margins have come under pressure recently owing to increasing input costs, aggravated by inflationary pressure in the economy. Further, the rise in benchmark rates increased finance cost considerably, putting pressure on the Company's bottom-line. The Company's financial risk profile is considered strong characterized by low leveraging and strong coverages. The Company's working capital management needs improvement. The working capital cycle is significantly higher than industry average, creating pressure on liquidity profile. Going forward, governance framework of the Company is expected to further strengthen. The assigned ratings incorporate recent corporatization of the group, experienced management team, strong financial muscle of sponsors and their willingness to support the entity as demonstrated historically.

The ratings are dependent on sustaining business margins while maintaining strong financial risk profile. Prudent management of working capital requirements, in-line with industry average, will remain critical. Strengthening of corporate structure, governance framework and timely completion of related activity are critical.

Disclosure

Name of Rated Entity	Al Rahim Textile Industries Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-19),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-19),Criteria | Rating Modifier(Jun-19)
Related Research	Sector Study | Towel(Jul-19)
Rating Analysts	Ateeb Riaz | ateeb.riaz@pacra.com | +92-42-35869504

Profile

Legal Structure Al Rahim Textile Industries Limited (Al Rahim or 'the Company') traces its roots to Al Rahim Textile Industries, which was established in 1991. In order to strengthen the corporate structure, a public unlisted company was formed by the name of Al Rahim Textile Industries Limited in July 2019. As per agreement, all assets and liabilities of sole proprietorship were purchased by Al Rahim Textile Industries Limited. The registered office of the Company is situated in Karachi, with manufacturing facility in Nooriabad, Sindh.

Background The Company was formed by Mr. Abdul Rahim Saya. Al Rahim started its business by providing processing and weaving facilities. The Company established Nooriabad facility in 2005. After 2015 expansion, the Company has become one of the largest manufacturers of towels in Pakistan.

Operations Al Rahim is involved in manufacturing of towels and fabrics. The Company is export oriented and sells its products to large retail chains like, Family Dollar Store Inc., Primark and others. Al Rahim has total capacity of 284 Air-jet looms and current capacity utilization is ~85%. After incorporation of new company in FY20, all assets and liabilities (except land and long term borrowing) has been transferred to the newly incorporated entity. Further, it is expected that all business will be shifted to Al Rahim Textile Industries Limited by the end of FY20.

Ownership

Ownership Structure Al Rahim is owned by Saya Family. Mr. Faisal Rahim Saya holds major stake in the Company while rest of the shareholding is split equally between Mr. Moiz Saya (Son of Mr. Faisal Saya) and Mr. Abdul Rahim Saya.

Stability The Company is owned by Saya Family. Although both sons of Mr. Abdul Rahim Saya (Mr. Faisal Saya and Mr. Shehzad Saya) are involved in the operations of the Company, most of the shareholding resides with Mr. Faisal Saya. The sponsors have established a holding company in Singapore to bring all group companies under one umbrella. There is no formal succession plan but ownership and business roles are clearly divided among family members at group level.

Business Acumen Saya family is involved in textile business for last three decades. The phenomenal growth of the Company over the years reflects strong business acumen of the sponsors.

Financial Strength The members of Saya family owns adequate wealth, reflecting well on financial strength of the sponsors. The sponsors have supported the Company in the past in the form of equity injections. The family also owns Al Rahim Retail (Private) Limited and real estate properties at prime locations in Pakistan.

Governance

Board Structure The board comprises three members. The board is chaired by Mr. Abdul Rahim Saya. The board includes two executive directors (including the CEO) and one non-executive director. All members represent Saya Family. There is room for improvement at board level, through induction of more members, including independent directors.

Members' Profile Saya family is in textile business since 1991 and has vast experience of textile industry. The acumen of the members is reflected in the growth of the Company in last three decades.

Board Effectiveness Board members are actively involved in the Company's operations. Board meetings are held on as and when required basis. The board has not formed any committees. There is no formal policy of recording board minutes.

Financial Transparency Reanda Haroon Zakaria & Company, Chartered Accountants, are the external auditors of the Company. They gave an unqualified opinion on financial statements for the year end June 30, 2019. The firm is QCR rated by ICAP and is classified in Category 'B' in the panel of auditors maintained by SBP.

Management

Organizational Structure The Company's management structure is divided into divisions and functional departments with clear lines of responsibilities. Head office and site management functions are headed by Mr. Faisal Saya.

Management Team Mr. Faisal Saya (CEO) leads the management team. He has been associated with the family business for last 26 years and has played a key role in the success of the Company. The CEO is supported by an able and professional team.

Effectiveness The Company has no management committees in place. However, senior management members meet on daily basis to discuss ongoing issues and plans.

MIS Al Rahim is using Oracle EBS 12.1.3 as its main ERP software. Oracle was fully implemented in 2015. Al Rahim uses three modules of Oracle. Regular MIS reports are submitted to top management relating to liquidity and profitability profile of the Company.

Control Environment Sponsors of the Company are part of both the Board and management. Al Rahim has established internal audit department, which is an integral part of the management control system. Further, the Company has rigorous quality control procedures in place. The Company has valid certificates from Oeko Tex 100 Class-I and Class-II, BSCI, C-TPAT, Sedex, GOTS and BRC, reflecting well on overall control environment.

Business Risk

Industry Dynamics During 5MFY20, the total textile exports saw an increase of ~4.9% (5MFY20: ~USD 5.76bln, 5MFY19: ~USD 5.5bln) in value terms, whereas, towels showed only a meagre increase of ~1% and clocked in at ~USD 317mln (5MFY19: USD 314mln). Despite significant rupee depreciation and favorable government policies towards textile, the industry was unable to boost its exports significantly. Fluctuation in cotton prices due to poor cotton crop in Pakistan could impact the margins. However, withdrawal of import duties on raw cotton from January 2020 will ease some pressure on industry, going forward.

Relative Position Al Rahim is one of the biggest players of towel industry in Pakistan with ~8% share in total towel exports of the Country during FY19. Whereas, Feroze 1888 is considered leader in towel industry with a share of ~27%.

Revenues The Company derives its revenue mainly from manufacturing and sales of towels. The topline is export oriented, which accounted for ~83% (FY18: ~82%) of the total revenue in FY19, whereas, rest of the revenue was contributed by local sales. During FY19, the Company's revenue clocked in at ~PKR 9,841mln (FY18: ~PKR 8,651mln), reflecting an increase of 14%. The growth in top-line mainly emanated from rupee depreciation, while volumes remained in-line with FY18.

Margins During FY19, gross margin of the company fell to ~27.7% (FY18: ~29.3%), as the input cost increased considerably due to higher inflation. The Company was able to maintain its operating margins (FY19: ~19%, FY18: ~18%) on the back of better control over operating margins. Further, finance cost increased to ~PKR 510mln (FY18: ~PKR 382mln) due to higher benchmark rates. Higher finance cost narrowed net profit margin to ~13.4% (FY18: 16.7%) with the bottom-line standing at ~PKR 1,319mln (FY18: ~PKR 1,443mln).

Sustainability Going forward, the Company plans to consolidate its position and invest in BMR activities in order to maintain operational efficiency and its market position. The Company aims to increase its capacity utilization, which currently stands at ~85%.

Financial Risk

Working Capital During FY19, the Company's gross working capital days increased substantially to 245 days (FY18: 198 days), mainly because of significant increase in receivable days to 101 days (FY18: 67 days). The Company's receivables are on a higher side on the back of significant receivables due from a related party. The inventory level has also increased considerably (38%) to ~PKR 4,420mln (FY18: ~PKR 3,187mln). The trade payable days clocked in at 63 days (FY18: 53 days), resulting in net working capital days of 182 days in FY19 (FY18: 146 days). the Company's working capital were significantly higher than industry average, creating pressure on liquidity. The Company had a short term trade leverage of ~48% in FY19 (FY18: ~39%), showing sufficient room to borrow against working capital.

Coverages The Company's free cash flows (FCFO) remained strong and clocked in at ~PKR 2,525 in FY19 (FY18: ~PKR 2,452). Meanwhile, finance cost increased significantly due to higher benchmark rates. Resultantly, the interest coverage ratio declined to 5x during FY19 (FY18: 7.4x) but remained strong. As the Company has paid its current maturity of long term debt, debt coverage ratio improved to 5x (FY18: 2.7x).

Capitalization The Company's capital structure is low leveraged at ~28% (FY18: ~33%). Leveraging decreased during FY19. The leveraging is expected to come around ~35% once all of the borrowings are shifted to the Company.

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Financial Summary
PKR mln

Al Rahim Textile Industries Limited	Sep-19	Jun-19	Jun-18	Jun-17
Towel	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	6,432	6,584	5,886	4,560
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	242	294
4 Current Assets	10,245	9,278	6,860	5,566
a Inventories	*4,398*	*4,420*	*3,187*	*3,033*
b Trade Receivables	*3,911*	*3,184*	*2,159*	*1,030*
5 Total Assets	16,677	15,863	12,989	10,420
6 Current Liabilities	2,836	2,851	1,289	1,650
a Trade Payables	*2,000*	*2,282*	*1,045*	*1,461*
7 Borrowings	3,791	3,666	3,858	3,232
8 Related Party Exposure	-	-	-	0
9 Non-Current Liabilities	47	36	-	-
10 Net Assets	10,003	9,310	7,841	5,538
11 Shareholders' Equity	10,003	9,310	7,841	5,539
B INCOME STATEMENT				
1 Sales	3,051	9,841	8,651	6,239
a Cost of Good Sold	*(2,552)*	*(7,111)*	*(6,115)*	*(4,658)*
2 Gross Profit	499	2,730	2,535	1,581
a Operating Expenses	(205)	(821)	(963)	(569)
3 Operating Profit	294	1,909	1,572	1,012
a Non Operating Income	*97*	*16*	*340*	*89*
4 Profit or (Loss) before Interest and Tax	391	1,925	1,912	1,101
a Total Finance Cost	*(129)*	*(510)*	*(382)*	*(182)*
b Taxation	*(37)*	*(96)*	*(87)*	*(62)*
6 Net Income Or (Loss)	225	1,319	1,443	857
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*529*	*2,525*	*2,452*	*1,392*
b Net Cash from Operating Activities before Working Capital Changes	*401*	*2,015*	*2,070*	*1,210*
c Changes in Working Capital	*(6,369)*	*(639)*	*(1,400)*	*(3,588)*
1 Net Cash provided by Operating Activities	(5,969)	1,377	670	(2,378)
2 Net Cash (Used in) or Available From Investing Activities	6,187	(1,315)	(1,091)	(212)
3 Net Cash (Used in) or Available From Financing Activities	(232)	(43)	409	2,562
4 Net Cash generated or (Used) during the period	(13)	19	(12)	(28)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	24.0%	13.8%	38.6%	1.5%
b Gross Profit Margin	16.4%	27.7%	29.3%	25.3%
c Net Profit Margin	7.4%	13.4%	16.7%	13.7%
d Cash Conversion Efficiency (EBITDA/Sales)	18.2%	26.8%	29.0%	24.4%
e Return on Equity (ROE)	9.3%	15.4%	21.6%	17.6%
2 Working Capital Management				
a Gross Working Capital (Average Days)	238	240	198	180
b Net Working Capital (Average Days)	174	178	146	71
c Current Ratio (Total Current Assets/Total Current Liabilities)	3.6	3.3	5.3	3.4
3 Coverages				
a EBITDA / Finance Cost	4.4	5.2	7.6	10.3
b FCFO / Finance Cost+CMLTB+Excess STB	4.2	5.0	2.7	2.6
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	1.0	0.9	0.5	1.0
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Total Borrowings / Total Borrowings+Equity	27.5%	28.3%	33.0%	36.8%
b Short-Term Borrowings / Total Borrowings	0.6	0.5	0.7	0.6
c Average Borrowing Rate	13.5%	13.5%	9.4%	8.3%

#	Notes
	The above figures include financial position and performance of Al Rahim Industries Limited as these will be transferred to Al Rahim Textile Industries by the end of FY20

Rating Scale | Corporate

2019

Credit Rating Scale & Definitions

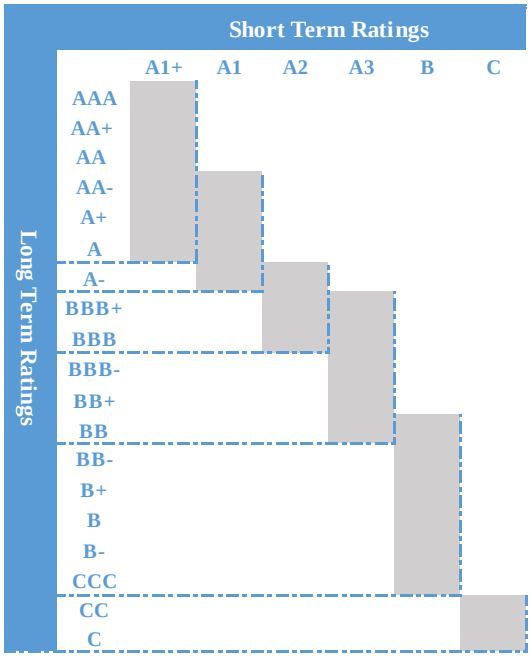
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short Term Ratings

A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
C	An inadequate capacity to ensure timely repayment.



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

Rating Watch Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

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

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

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

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.
(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