The Pakistan Credit Rating Agency Limited

Rating Report

Maqbool Textile Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
21-Feb-2019	BBB+	A2	Stable	Maintain	-
31-Aug-2018	BBB+	A2	Stable	Initial	-
31-Aug-2018	BBB+	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Maqbool Textile Mills Limited's (Maqbool Textile) track record and association with Maqbool Group, an established group with presence in textile and seed oil extraction industry. Despite challenging textile industry dynamics, Maqbool Textile managed to maintain its capacity utilization. The commoditized nature of spinning products keeps margins in check due to strong competition in local and international markets. Sales volume declined in 1QFY19, however these are expected to normalize in near future. Recent withdrawal of custom duty and sales tax on cotton imports, coupled with subsidized gas rates for textile industry has made the local textile industry cost competitive. On standalone basis better industry dynamics may nourish the Company's margins, and eventually better cash flows generation to settle debts related obligations. The Company’s margins remain on the lower side when compared with peers resulting in relatively subdued profitability. Maqbool Textile is in process of capacity enhancement for fixed cost optimization and better efficiency. The financial profile of the company is constrained due to high leverage and adequate coverages. The debt structure is skewed towards short-term borrowings, which may lead to the asset-liability mismatch.

The ratings are dependent upon the management's ability to improve margins, profitability and financial profile of the Company. This includes avoiding any asset-liability mismatch that may arise and effectively managing its position in a competitive segment. Any deterioration in debt coverages leading to higher financial risk or subdued profitability will have a negative impact on ratings.

Disclosure

Name of Rated Entity	Maqbool Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Criteria | Rating Modifier(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Textile(Oct-18)
Rating Analysts	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

Profile

Legal Structure Maqbool Textile Mills Limited (Maqbool Textile), was incorporated in 1989, as a public limited company.

Background The Company was set up by Maqbool family a well-reputed business family of industrialists in Multan. The Company is engaged in manufacturing and sale of yarn.

Operations Maqbool Textile operates with 70,440 spindles and has a production capacity of 15mln Kgs of yarn per year. To meet its energy requirement the Company relies on MEPCO and hires generator in case of power failure. The manufacturing facilities are located at Muzaffargarh (units I & II) and Toba Tek Singh (unit III), while the head office is situated in Multan.

Ownership

Ownership Structure The Company is primarily owned by Maqbool family (72.5%), comprising stakes of brothers and sisters of Mr. Tanvir Ahmed. The remaining shareholding rests with National investment Trust (9.9%), general public (16.7%) and NBP employees pension fund (0.9%).

Stability The second generation of the family has already joined the Company, Mr. Mian Atta Tanvir Sheikh (BBA) is the son of the Chairman and sits on the BoD and oversees procurement. However, the succession planning is not documented yet.

Business Acumen The sponsors have developed credential expertise in textile business, over the years, providing sufficient business acumen to sustain through the competitive textile industry.

Financial Strength Maqbool Group has interest in textile, edible oil extraction and hospitality, portraying sufficient financial strength of the Group to support its entities, if needed.

Governance

Board Structure The board comprises seven members, out of which two directors are non-executive, three directors occupy executive role, while two directors are independent. Dominance of sponsors on board along with control over key management positions, hampers the effective governance.

Members' Profile Mr. Mian Tanvir Ahmed Sheikh (MBA) is the Chairman, while Mr. Mian Anis Ahmed Sheikh (BBA) is the CEO of the Company. The board members have vast knowledge and extensive experience of the textile industry. The directors' expertise in textile industry benefits the board in efficient decision making.

Board Effectiveness Two committees: Audit and Human Resource & Remuneration, are in place to assist the board in relevant matters and ensures proper oversight. Attendance of board members in meetings remained Strong and meeting minutes were appropriately documented.

Financial Transparency M/s. Deloitte Yousaf Adil, Chartered Accountants is the external auditor of the Company. The auditors have expressed unqualified opinion on the financial reports for the year ended 30th June, 2018.

Management

Organizational Structure The management control of the Company vests with Maqbool family. There is a well-defined organizational structure with clear segregation of responsibilities. There are three functional departments including, i) sales and marketing, ii) procurement and production and iii) finance & admin. Moreover, sales & marketing, production and procurement are headed by executive directors, while finance & admin is headed by the CFO.

Management Team Management team comprises long associated and experienced individuals, including Mr. Ehsanullah Khan (MBA) in the capacity of CFO, Mr. Mohd. Ilyas (BSC Textile Engineering) as GM production for units I & II and Mr. Zafar Akhtar (BSC Textile Engineering) as GM production unit III.

Effectiveness There are no formal management committees in place, however key management personal meet on regular basis to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations.

MIS The Company has built an in-house ERP to cater the business needs. The system for reporting has been designed as per the Company's requirement.

Control Environment The Company is compliant with quality assurance standard; ISO 9001:2008. Moreover, the Company has in place rigorous quality control department for quality check of output.

Business Risk

Industry Dynamics During FY18, total textile exports of Pakistan stood at USD ~ 13.53bln, a 9% YoY growth. The withdrawal of custom duty and sales tax on cotton imports, coupled with subsidized gas rates for textile industry has made the local textile industry cost competitive. Additionally, rupee devaluation in recent times has further improved the textile industry dynamics, particularly for the entities with net exports.

Relative Position The Maqbool family has been associated with the textile business since 1958, through its investment in "Allawasaya Textile & Finishing Mills Limited", strengthening Maqbool Textile's position. However, as a group and on a stand-alone basis their market share in the spinning sector is minimal.

Revenues During FY18, the Company's revenues clocked in at PKR 5,598mln, posting a growth of ~15%. This is attributable to favorable industry dynamics. The Company's sales mix continues to be dominated by local sales ~58% (FY17: 63%); though the exports have picked up in FY18. The main export destination for the Company lies in China. Whereas during 1QFY19, revenues reported at PKR 1,036mln, down by ~12.5% on QoQ basis, owing to lower volumetric sales; a factor of lower demand prospect in local market.

Margins In FY18, Maqbool Textile's gross and net margins improved (FY18: 7.1%, FY17: 6.8%) and (FY18: 3.6%, FY17: 3.0%), respectively. The finance cost increased by ~23%, due to higher short term borrowing. Moreover, the Company has secured an exchange gain of ~PKR 33.5mln supplementing its bottom-line. On account of taxation the Company's net profit increased (FY18: ~PKR 55mln, FY17: ~PKR 26mln), posting a growth of ~110%. The trend of improving margins continued in 1QFY19 (gross: 8.8%, net: 5.1%). This is attributable to rationalization of distribution expense, a factor of declined exports. The Company's finance cost increased by ~24%, while on account of taxation the Company posted a profit of PKR 17mln.

Sustainability In line with the improving business environment, the Company is planning to enhance the production capacity by adding another 9,000 spindles. Installation of new spindles will be completed by end Mar-19. This is expected to bring in efficiency gains, in turn, improved margins going forward. The total cost for the CAPEX has been estimated at PKR 160mln.

Financial Risk

Working Capital The company meets its working capital requirements through a mix of internal cash generation and short term borrowings. The Company's reliance on STB has increased (FY18: PKR 1,429mln, FY17: PKR 1,204mln), on the back of higher receivables. The Company has a negative room to borrow (FY18: -4%, FY17: -4%). Moreover, receivables have piled up (FY18: PKR 611mln, FY17: PKR 269mln), as reflected from higher receivable days (FY18: 29days, FY17: 22days). However, on account of lower inventory days, working capital marginally improved (FY18: 113days, FY17, 118days). Whereas in 1QFY19, working capital cycle was higher (gross – 1QFY19: 110days, net – 1QFY19: 91days), a factor of seasonal inventory procurement.

Coverages During FY18, the Company's operating cash flows (FCFO) improved (FY18: PKR 264mln, FY17: PKR 206mln), largely led by better profitability. Meanwhile, despite the increase in finance cost the interest and debt coverages slightly improved (FY18: 2.1x, FY17: 2.0x) and (FY18: 1.3x, FY17: 1.2x), respectively. The trend followed in 1QFY19, as the coverages further improved (interest - 1QFY19: 2.3x, debt – 1QFY19: 1.6x). Going forward, on account of debt driven expansion and hiked interest rate may put pressure on the Company's coverages.

Capitalization Maqbool Textile has a intermediately leveraged capital structure (~56.5%) at end-June 18 (end-June 17: 54.5%). Total debt stood at PKR 1,677mln, mainly comprising current debt ~ 90%. While at end-Sep 18, the Company's leveraging decreased (~51.7%), owing to declined STB. Consequently, the current debt declined to (~88%) at end-Sep 18. Going forward, the Company's leveraging is expected to increase on account of debt driven expansion.

Maqbool Textile Mills Limited

PKR mln

BALANCE SHEET	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	1QFY19	FY18	FY17	FY16
Non-Current Assets	**1,810**	**1,806**	**1,846**	**1,856**
Investments (Incl. Associates)	-	-	-	-
Equity	-	-	-	-
Debt Instruments	-	-	-	-
Current Assets	**1,342**	**1,626**	**1,261**	**1,305**
Inventory	659	607	674	787
Trade Receivables	424	611	269	320
Others	259	409	318	197
Total Assets	**3,152**	**3,432**	**3,107**	**3,161**
Debt	**1,277**	**1,574**	**1,342**	**1,433**
Short-Term	1,153	1,429	1,128	1,183
Long-Term (Incl. Current Maturity of Long-Term Debt)	124	145	214	250
Other short-term liabilities	316	297	263	251
Other long-term liabilities	270	269	270	291
Shareholders' Equity	**1,289**	**1,292**	**1,236**	**1,186**
Total Liabilities & Equity	**3,152**	**3,432**	**3,107**	**3,161**
INCOME STATEMENT				
Turnover	**1,036**	**5,599**	**4,863**	**4,281**
Gross Profit	91	399	332	227
Net Other Income	9	34	19	8
Financial Charges	(31)	(127)	(103)	(96)
Net Income	**17**	**55**	**26**	**(60)**
CASH FLOW STATEMENT				
Free Cashflow from Operations (FCFO)	72	264	206	113
Net Cash changes in Working Capital	227	(291)	80	(215)
Net Cash from Operating Activities	267	(144)	186	(186)
Net Cash from InvestingActivities	(27)	(48)	(80)	(167)
Net Cash from Financing Activities	(298)	233	(91)	322
RATIO ANALYSIS				
Performance				
Turnover Growth	-12.5%	15.1%	13.6%	158.5%
Gross Margin	8.8%	7.1%	6.8%	5.3%
Net Margin	1.7%	1.0%	0.5%	-1.4%
ROE	1.5%	8.5%	2.1%	-5.6%
Coverages				
Interest Coverage (FCFO/Gross Interest)	2.3	2.1	2.0	1.2
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	0.9	0.9	0.7	0.4
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	0.9	0.9	0.7	0.4
Debt Payback (Total LT Debt Including Uncovered Total STBs) / (FCFO- Gross Interest)	2.2	2.5	4.2	28.9
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	90.9	63.7	69.9	26.5
Capital Structure (Total Debt/Total Debt+Equity)	51.7%	56.5%	53.7%	56.6%

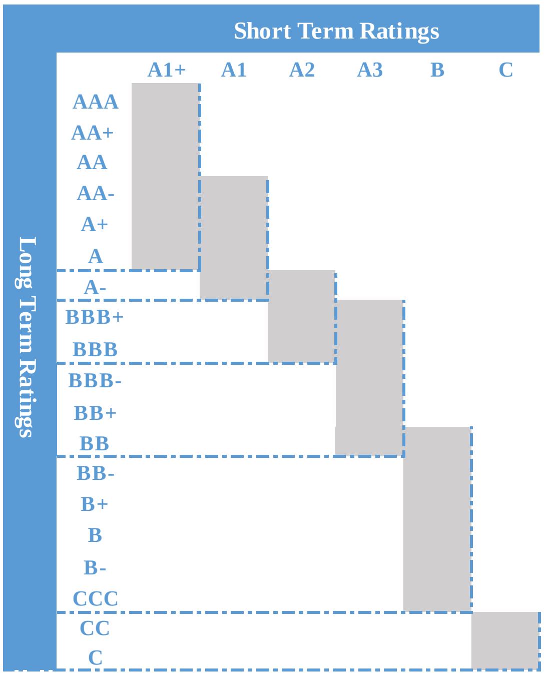
Rating Scale

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.

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.
(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