



The Pakistan Credit Rating Agency Limited

Rating Report

Shujabad Weaving Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
31-Dec-2018	BBB-	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect modest business profile of Shujabad Weaving Mills Limited (Shujabad Weaving). The company's revenues have posted limited growth in recent years, with margins on lower end when compared to peers. The company caters to the needs of local clientele. Overtime, the company has made strong relationship with renowned local brands, which is considered positive for sustainable margins and competitive positioning. Moreover, re-imposition of custom duties and sales tax on cotton & yarn imports, coupled with increasing interest rates has stretched the textile industry. The ratings are constrained by the company's stretched financial profile characterized by highly leveraged capital structure, mainly for working capital requirements. The rising interest rate environment is expected to impact profitability as interest cost will increase. The management is cognizant of this and intends to repay its debt to create requisite room. The company's association with Shujabad Group provides comfort.

The ratings are dependent on the management's ability to improve its margins, while effectively managing its financial profile. Any substantial reduction in margins, impacting profitability will negatively impact the ratings. Similarly, maintaining adequate cashflows and coverages is critical. Improvement in governance framework will be favorable for the ratings.

Disclosure

Name of Rated Entity	Shujabad Weaving 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)
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Profile

Legal Structure Shujabad Weaving Mills Limited (Shujabad Weaving), was incorporated on April 5th 2005, as a public unlisted company.

Background Shujabad Weaving is a prominent business venture of Shujabad Group in textile concerns. The group has presence in the ginning industry through Shujabad Industries and Shabbir Cotton.

Operations Shujabad Weaving's current operational capacity comprises 250 Looms. The total energy requirement of the company clocks in at ~8.1MW which is met through a mix of captive plant and NTDC connection.

Ownership

Ownership Structure Shujabad Weaving is collectively owned by three families. Among all families major stake rests with Wahid family (~39.7%), followed by Shabbir family (~35.4%) and Akram family (~25.0%).

Stability All three families have mutual consent over the operational control of the company. The distribution of shareholding among all three families portrays a structured line of succession. The second generation has already been in business, serving at various capacities. Moreover, the transfer of ownership to the next generation is not documented.

Business Acumen The Group has presence in ginning sector, over time, the Group has integrated into weaving business through Shujabad Weaving. The decade long presence in textile industry, while developing credential expertise over time provides sufficient Business Acumen, in order to sustain through volatile textile industry.

Financial Strength Shujabad Group has a prominent standing in textile, edible oil and poultry sector. The Group had an annual turnover of PKR 25bln in FY18, with adequate profitability and strong financial strength, portraying ability to support its group companies in time of need.

Governance

Board Structure The company's board of directors comprises four members, all of them are serving as executive directors, with Mr. Abdul Wahid as Chairman of board. Two directors represent Shabbir family, including the CEO. The remaining two families have one representative each. The presence of all sponsors on board provide constructive challenge, while absence of independent oversight indicates room for improvement in the governance framework of the company.

Members' Profile All the board members have more than ten years of association with the board, except one member. Mr. Abdul Wahid – the Chairman – holds a master's degree in Arts. The board of directors have adequate experience in the textile sector, ensuring efficient decision making on board.

Board Effectiveness Attendance of the members remained strong during the year. The board meeting minutes have been appropriately recorded. Moreover, absence of board committees is considered negative for board's effectiveness.

Financial Transparency M/s Shinewing Hameed Chaudary & Co., Chartered Accountants is the external auditor of the company. The auditors have expressed unqualified opinion on the financial reports for the year ended June, 2018.

Management

Organizational Structure Management control vests with Mr. Abdul Wahid (Chairman), while Mr. Qaisar Shabbir (CEO) oversees the financial aspects of the company. The company has a well-defined reporting line to ensure smooth operations and efficiency. Moreover, the company has five functional departments.

Management Team Mr. Qaisar Shabbir - the CEO, has been associated with the company since its inception. He holds a master's degree, also carries with him over a decade of experience in the textile sector. He is supported by a team of professionals with relevant expertise of textile value chain. Moreover, Mr. Salman Rasheed - the CFO is been with the company since 2005.

Effectiveness The management meetings are held on need basis to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations.

MIS Shujabad Weaving has in place Microsoft Dynamics based enterprise resource planning (ERP) system that provides comprehensive MIS reporting.

Control Environment The company is compliant with International Certification for quality assurance; majorly including ISO 9001:2008. In addition, Shujabad Weaving's plant is connected with head office through VPN, thereby reporting on the real time basis.

Business Risk

Industry Dynamics During FY18, total textile exports of Pakistan stood at USD ~ 13.53bln, a 9% YoY growth. Re-imposition of custom duty and sales tax on cotton imports in FY19 budget, coupled with exclusion of tax rebate on yarn and greige fabric has further stretched the industry margins. However, rupee devaluation in recent times provide breather to textile ventures with net exports.

Relative Position Shujabad Weaving is associated with Shujabad Group. The Group have considerable representation in textile ginning, while Shujabad weaving is the only weaving concerns of the Group. Meanwhile, on standalone basis the company has a minimal share in local weaving industry.

Revenues During FY18, the company's top-line registered a limited growth PKR 6,158mln (FY17: PKR 6,167mln), on the back of lower volumetric production. The company's sales mix continues to be dominated by local sales ~79% (FY17: 87%); though exports picked up during the year, on account of rupee devaluation making exports more feasible. The top ten customers' revenue concentration in both local (FY18: ~81%, FY17: ~81%) and export markets (FY18: ~71%, FY17: ~46%) is considered high. Whereas during 1QFY19, revenues increased by ~12% on QoQ basis, which is attributable to rupee devaluation.

Margins During FY18, Shujabad Weaving's gross margins improved (FY18: 7.0 %, FY17: 6.9%). This was followed by slightly lower operating margins (FY18: 4.6 %, FY17: 4.9%), due to higher distribution cost, a factor of increased exports. The finance cost increased by ~12.5%, due to increased interest rate. Moreover, the company has secured an exchange gains of ~PKR 22mln supplementing its bottom-line. While on account of taxation the company's net profit stood at (FY18: ~PKR 74mln, FY17: ~PKR 53mln), posting a growth of ~40%. Moreover, the company's margins slightly improved in 1QFY19 (gross – 7.3, net - 5.3), an impact passed on from higher revenues.

Sustainability The company has incurred a BMR of ~PKR 174mln during recent years, for the purpose of maintenance and mechanical efficiency. Furthermore, Shujabad Weaving is planning to enhance its marketing efforts in order to capture new markets and opportunities. This will help in improving the business fundamentals of the company.

Financial Risk

Working Capital Though the company's reliance on STB has increased, owing to increased inventory procurement. Higher STB led to negative room to borrow (FY18: -5%, FY17: -13%); though improved over the year. Moreover, finished goods swelled, reflected from increased inventory days (FY18: 96days, FY17: 81days), eventually translating into higher net working capital days (FY18: 116days, FY17 105days). The working capital cycle improved in 1QFY19, reflected from decreased working capital days (gross – 1QFY19: 125days, net – 1QFY19: 106days), a factor of lower finished goods inventory, eventually decreasing inventory days.

Coverages During FY18, the company's operating cash flows largely remained at same level, due to lower profitability. Meanwhile, the considerable increase in finance cost (~12.5%) has resulted in deteriorated interest and debt coverages (FY18: 1.6x, FY17: 1.8x) and (FY18: 0.8x, FY17: 0.9x), respectively. While, in 1QFY19 interest coverage improved (1QFY19: 2.0x), while the debt coverage deteriorated (1QFY19: 0.7x) on account of uncovered STB. Going forward, despite the hike in interest rate the company's coverages may improve, as no major CAPEX is expected in near future.

Capitalization Shujabad Weaving has a highly leveraged capital structure (~72.5%) at end-June 18 (end-June 17: 74.1%). Total debt stood at PKR 2,843mln, mainly comprising current debt ~ 96%. During 1QFY19, the company's leveraging decreased (~69.8%), on account of declined STB.



Shujabad Weaving Mills Limited

BALANCE SHEET

	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	3M	FY	FY	FY
Non-Current Assets	1,483	1,509	1,653	1,778
Investments (Incl. Associates)	-	-	-	-
Equity	-	-	-	-
Loans to Associates/Debt Securities	-	-	-	-
Investment Property	-	-	-	-
Current Assets	2,816	3,044	2,820	2,433
Inventory	1,590	1,792	1,436	1,294
Trade Receivables	674	681	593	664
Others	552	571	791	474
Total Assets	4,299	4,553	4,473	4,211
Debt/Borrowings	2,495	2,816	2,846	2,683
Short-term	2,270	2,551	2,379	2,027
Long-term (Incl. Current Maturity of Long-Term Debt)	225	265	467	656
Other short-term liabilities	647	584	467	396
Other long-term liabilities	58	74	156	178
Shareholders' Equity	1,101	1,079	1,006	954
Total Liabilities & Equity	4,299	4,553	4,473	4,211

INCOME STATEMENT

Turnover	1,726	6,158	6,167	5,877
Gross Profit	125	429	426	363
Net Other Income	1	21	1	7
Financial Charges	(65)	(244)	(217)	(228)
Net Income	22	74	53	13

Cashflow Statement

Free Cash Flow from Operations (FCFO)	131	399	396	449
Net Cash changes in Working Capital	298	(86)	(289)	(441)
Net Cash from Operating Activities	350	64	(90)	(231)
Net Cash from Investing Activities	(13)	(25)	(55)	(73)
Net Cash from Financing Activities	(321)	(30)	163	303

Ratio Analysis

Performance

Turnover Growth (vs. SPLY)	12%	0%	5%	-89%
Gross Margin	7%	7%	7%	6%
Net Margin	1%	1%	1%	0%

Coverages

Interest Coverage (FCFO/Gross Interest)	2.0	1.6	1.8	2.0
Core: (FCFO) / (Gross Interest+CMLTD+Uncovered Total STB)	0.7	0.8	0.9	1.0
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	0.7	0.8	0.9	1.0
Debt Payback (Total LT Debt Including Uncovered Total STBs) / (FCFO- Gross Interest)	2.3	2.5	2.9	3.1

Liquidity

Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	105.7	116.4	104.8	108.4
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Capital Structure (Total Debt/Total Debt+Equity)

	70%	72%	74%	74%
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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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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 surveil the opinion due to lack of requisite information.

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

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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)

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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- (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

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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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- (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)
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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
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- (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)
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- (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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