The Pakistan Credit Rating Agency Limited

Rating Report

AL Textile (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Sep-2019	BBB	A2	Stable	Maintain	-
05-Mar-2019	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The assigned ratings of AL Textile (Pvt.) Limited (AL Textile) reflect strong financial profile of Sponsors and their support to the entity in the form of guarantee and subordinated loan. The Company mainly caters to the need of local market and has developed brand based clientele over the years. The Company's revenue has witnessed growth in harmonization with textile industry in the past. However, the top line remain stagnant during FY19. The relatively smaller capacity of AL Textile has limited its margins. Recently, the Company's margins and profitability have come under pressure on the back of higher input and finance costs, leading to net loss in FY19. The imposition of sales tax on local sales is expected to have a negative effect on local demand. However, favorable government policies towards textile industry, subsidized utilities, and rupee depreciation is expected to bode will for export-oriented textile players. While incorporating these factors, the Company expects its business profile to improve in near future. The Company has a moderately leveraged capital structure characterized by adequate coverages and moderate inventory days. The management intends to implement further financial discipline by limiting leveraging. The ratings take comfort from explicit commitment of sponsors to provide support to the Company.

The ratings are dependent on the Company’s ability to improve its margins and financial profile. Any further reduction in margins, impacting cash-flows and profitability for a long period will impact the ratings. Similarly, prudent working capital management is considered important. Going forward, sponsors support to the Company would remain critical for the ratings.

Disclosure

Name of Rated Entity	AL Textile (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Crtieria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study | Textile(Oct-18)
Rating Analysts	Ateeb Riaz | ateeb.riaz@pacra.com | +92-42-35869504

Profile

Legal Structure AL Textile (Pvt.) Limited (AL Textile or "the Company"), was incorporated in 2002, as a private limited company and commenced its operations in 2003.

Background Mr. Abdul Latif started Fine Gases in the early 80's. He formerly had a business in Dubai. In 1985, Latif family diversified their business by setting up Fine Crystoplast (Pvt.) Limited, a plastic molding plant. Later in 2002, the family entered into the textile sector through AL Textile with 15,000 spindles.

Operations AL Textile operates with one spinning unit, having 25,200 spindles. Their production facility is located on Main Multan road (43 km), Lahore, an 130 acre of land. The Company has arranged a line of 3.2MW from LESCO, which is the only source of power.

Ownership

Ownership Structure AL Textile is a family owned business, with majority stake owned by Mr. Omer Latif (~61%) and the remaining shareholding distributed equally (~19% each) among his brother and sister.

Stability The Company is owned entirely by the Latif family. The distribution of shareholding with Mr. Omer Latif as majority stake holder portrays a stable line of succession. Moreover, the second generation has already been incorporated into the business, serving at various capacities with clearly defined roles.

Business Acumen AL Textile is the only textile business venture of Latif family. Over the years, the growth of the Company was limited. However, it has sustained through the volatility of the textile industry in recent years. Mr. Abdul Latif's (Ex-Chairman) counsel remains a key factor in ensuring sustainable operations of the Company.

Financial Strength Apart from AL Textile, Latif family has interests in industrial gases and plastic molding through Fine Gas and Fine Crystoplast, respectively. Meanwhile, the sponsors have sufficient financial strength to support AL Textile, when needed, as evident historically.

Governance

Board Structure The Company's board of directors comprise two members, with Mr. Omer Latif as Chairman of board. The size of the Board is considered adequate as per the Company's operational size. However, room for improvement in governance framework exists.

Members' Profile The board members have been associated with the Company since its inception. Apart from AL Textile, both the directors sit on the board of associated companies, Fine Gas and Fine Crystoplast. Mr. Omer Latif holds a Master's degree in Industrial Management from USA.

Board Effectiveness Attendance of the members remained strong during the year. The board meeting minutes have been appropriately recorded. There is no subcommittee in place, which hampers the board effectiveness.

Financial Transparency M/s Naveed Mukhtar & Co., Chartered Accountants, QCR rated by ICAP, is the external auditor of the Company. The auditors have expressed unqualified opinion on the financial reports for the year ended June, 2018. The audit for FY19 is under progress.

Management

Organizational Structure Mr. Omer Latif is the CEO of AL Textile. The Company has a lean organizational structure and is broadly divided into five functional departments. All department heads report directly to Mr. Omer Latif.

Management Team Mr. Omer Latif, the CEO, has been associated with the Company since inception. He is supported by a team of professionals with relevant expertise of textile value chain. Long association of senior management with the Company bodes well for sustainability of the Company.

Effectiveness There are multiple management committees in place. The meetings are held on periodic bases to resolve or proactively address operational issues. Moreover, the matters drafted in these meetings are presented to board for approval, portraying an active participation of senior management in carrying the Company's operations.

MIS AL Textile has installed a local version of Oracle based ERP solution (Vision Plus), which is fully operational.

Control Environment The Company is compliant with International Certification for quality assurance, ISO 9001:2008. In addition, it has maintained a quality management system since the start.

Business Risk

Industry Dynamics During FY19, exports stagnated despite major segments including cotton cloth, knitwear, garments and bedwear displaying strong quantitative growth. Industry players needed to share the benefit of the currency depreciation with their buyers, which resulted in a unit price dip across all major categories, curbing overall growth. This, coupled with cotton yarn displaying double-digit quantitative decline on account of the US-China trade war as well as strong domestic demand for yarn, resulted in overall increase in exports of only ~0.1% YoY. Going forward, withdrawal of textile's zero rated status will impact industry's overall liquidity and margins.

Relative Position AL Textile is a small sized spinning unit and the only textile venture of the Latif family. However, standard quality Japanese machinery has made the Company capable of producing top quality yarn. Hence, the Company has managed to secure niche clientele. Meanwhile, on a standalone basis the Company has a minimal share in local spinning industry.

Revenues The top-line of the Company remained stagnant during FY19 and clocked in at PKR 2,780mln (FY18: PKR 2,737mln), showing meager growth of ~1.5%. The top-line of the Company is derived from local sales.

Margins The gross margins of the Company declined slightly during FY19 and stood at ~5.2% (FY18:6%), due to higher input costs. The operating margins of the Company also diminished (FY19: ~4%, FY18: ~5%) due to trickle down effect of lower gross margins. The finance cost increased by a massive 125% during the year (FY19: PKR 99mln, FY18: PKR 44mln). On this backdrop, the Company incurred a net loss of PKR 29mln during FY19 (FY18: PKR 50mln profit).

Sustainability The Company has incurred a BMR of ~PKR 435mln since FY14 for up-gradation of machinery and capacity enhancement. Around 5,040 spindles of adequate quality has been added in the production facility. These are expected to be operational soon. Additional capacity will help the Company in optimizing its fixed cost and improving its margins. The Company has recently designated a spinning line with a capacity of 130 bags per day for production of CF yarn - a better margin product. Majority of the Company's buyers are registered tax payers. This will limit the impact of imposition of sales taxes on the Company's domestic sales, since it generates its revenue through sales to local players.

Financial Risk

Working Capital Working capital is a function of inventory and trade receivables and is financed partly via in house generated cash flows and mainly from short-term borrowings. The Company's reliance on short-term borrowings has increased significantly during FY 19 and clocked in at ~PKR 595mln (FY18: ~PKR 326mln). The cash cycle increased during FY19 (Gross- FY19: 63days, FY18: 42 days, Net- FY19: 52days, FY18: 39days) due to higher inventory levels. Net trade assets of the Company stood at PKR 518mln (FY18: PKR 291mln), showing excess borrowings of PKR 77mln (FY18: PKR 35mln).

Coverages The free cash flows (FCFO) of the Company has remained in-line with previous year and clocked in at ~PKR 135mln during FY19 (FY18: PKR 149mln). The coverages weakened during the year but remain adequate. The interest coverage ratio dropped to 1.4x during FY19 (FY18: 3.4x) on the backdrop of higher finance cost. The debt coverage ratio also decreased to 1.1x during FY19 (FY18: 3.4x).

Capitalization The Company has moderately leveraged capital structure. The leveraging stood at ~49% during FY19 (FY18: ~35%). The increase in leveraging is attributable to higher short-term borrowings to finance the increasing working capital requirements. Short-term borrowings comprise ~96% of total borrowings. The leveraging of the Company is expected to remain at the same level, going forward.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

AL Textile (Private) Limited	Jun-19	Jun-18	Jun-17
Spinning	12M	12M	12M
A BALANCE SHEET			
1 Non-Current Assets	605	637	644
2 Investments	-	-	-
3 Related Party Exposure	-	-	-
4 Current Assets	952	471	478
a Inventories	*594*	*254*	*316*
b Trade Receivables	*64*	*52*	*21*
5 Total Assets	1,557	1,108	1,122
6 Current Liabilities	259	58	82
a Trade Payables	*161*	*12*	*48*
7 Borrowings	620	352	398
8 Related Party Exposure	-	-	-
9 Non-Current Liabilities	28	30	22
10 Net Assets	650	669	619
11 Shareholders' Equity	650	669	619
B INCOME STATEMENT			
1 Sales	2,780	2,737	1,851
a Cost of Good Sold	*(2,636)*	*(2,572)*	*(1,808)*
2 Gross Profit	144	165	43
a Operating Expenses	(27)	(34)	(28)
3 Operating Profit	117	131	15
a Non Operating Income	*(9)*	*(4)*	*0*
4 Profit or (Loss) before Interest and Tax	108	127	15
a Total Finance Cost	*(102)*	*(46)*	*(36)*
b Taxation	*(35)*	*(32)*	*(10)*
6 Net Income Or (Loss)	(29)	50	(31)
C CASH FLOW STATEMENT			
a Free Cash Flows from Operations (FCFO)	*135*	*149*	*45*
b Net Cash from Operating Activities before Working Capital Changes	*33*	*102*	*14*
c Changes in Working Capital	*(529)*	*5*	*(137)*
1 Net Cash provided by Operating Activities	(496)	107	(123)
2 Net Cash (Used in) or Available From Investing Activities	-	(34)	(56)
3 Net Cash (Used in) or Available From Financing Activities	419	(46)	212
4 Net Cash generated or (Used) during the period	(77)	26	34
D RATIO ANALYSIS			
1 Performance			
a Sales Growth (for the period)	1.6%	47.9%	40.4%
b Gross Profit Margin	5.2%	6.0%	2.3%
c Net Profit Margin	-1.0%	1.8%	-1.7%
d Cash Conversion Efficiency (EBITDA/Sales)	6.1%	6.3%	3.0%
e Return on Equity (ROE)	-4.4%	7.8%	-4.9%
2 Working Capital Management			
a Gross Working Capital (Average Days)	63	43	54
b Net Working Capital (Average Days)	52	39	46
c Current Ratio (Total Current Assets/Total Current Liabilities)	3.7	8.2	5.8
3 Coverages			
a EBITDA / Finance Cost	1.7	3.9	1.6
b FCFO / Finance Cost+CMLTB+Excess STB	1.1	3.4	0.8
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.7	0.2	6.8
4 Capital Structure (Total Debt/Total Debt+Equity)			
a Total Borrowings / Total Borrowings+Equity	48.9%	34.5%	39.1%
b Short-Term Borrowings / Total Borrowings	96%	93%	81%
c Average Borrowing Rate	20.5%	11.8%	11.5%

Rating Scale | Corporate

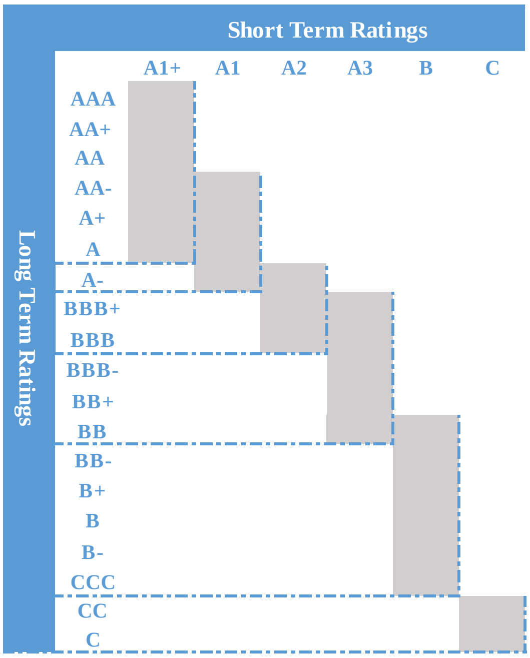
2019

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.

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