The Pakistan Credit Rating Agency Limited

Rating Report

Khas Textile Mills (Pvt.) Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
23-Aug-2024	BBB-	A2	Stable	Maintain	-
23-Aug-2023	BBB-	A2	Stable	Maintain	-
23-Aug-2022	BBB-	A2	Stable	Upgrade	-
23-Aug-2021	BB+	A3	Stable	Maintain	-
28-Aug-2020	BB+	A3	Stable	Maintain	-
29-Aug-2019	BB+	A3	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The spinning industry is highly fragmented and consists of ~368 dedicated spinning units with an estimated size of PKR 775bln and 13.4mln number of spindles installed as of FY23, according to an economic survey of Pakistan. As of FY24 the projected cotton production estimate is revised and projected to be 12.8mln bales and currently, production reached up to ~10.2mln bales surpassing FY23's total production of 4.91mln bales. Pakistan's requirement for imported cotton stands at 2.5mln bales to 3mln bales this year. The recent elevation of energy tariffs and the availability of locally procured raw cotton are the prime challenges specific to the industry. Overall, the industry's cash flow and in turn liquidity remains stretched. This, along with high working capital requirements and related finance cost challenges led the industry's outlook to be placed on Watch.
Khas Textile Mills (Pvt.) Limited (“Khas Textile” or “the Company”) manufactures various types of cotton rings and open-end yarn. The Company is considered among the evolving players in the industry. The ratings reflect the Company’s adequate business profile. Holding an association with Khas Group which holds a presence in textile, energy, aluminum and hardware along with livestock farming, demonstrates stable financial strength. During FY24, the Company’s topline reflects an uptick of ~40%, driven by the revival of demand for textile products. Topline posts a tilt towards the local market (~70%) along with an evolving presence in the international markets. GP margins remain low due to increased raw yarn/fiber costs, followed by energy costs. On the net level, margins remain low as compared to peers. On the financial risk front, borrowings remain high reflecting high working capital requirements. Additionally, the Company holds related party exposure. Coverage remains insufficient, while leverage continues to be high. Efforts to strengthen the governance framework remain pivotal to ratings.

Ratings are dependent on the Company's ability to grow and sustain business profile, along with healthy margins. Any deterioration in debt coverages leading to higher financial risk or substantial losses will have a negative impact on ratings.

Disclosure

Name of Rated Entity	Khas Textile Mills (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Rating Modifiers(Apr-24),Methodology | Corporate Rating(Jul-24),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jul-24)
Related Research	Sector Study | Spinning(Sep-23)
Rating Analysts	Muhammad Moaz | muhammad.moaz@pacra.com | +92-42-35869504

Profile

Legal Structure Khas Textile Mills Private Limited ('Khas Textile' or 'the Company') was incorporated in 2001 as a private limited Company.

Background The Company is engaged in the manufacturing of yarn. In 2006, the company went through a major transformation and started manufacturing cotton rings and open-end yarn. Since its incorporation, over the years, Khas Textile has increased its production capacity.

Operations The Company currently operates 19,200 spindles and 864 rotors and has a purpose build manufacturing facility located in the industrial hub – Nooriabad. The Company has further land available for expansion. The Company has a captive generation capacity (3.5 MW) well above the required capacity (3.2MW) and further maintains a backup connection with HESCO.

Ownership

Ownership Structure The Company is wholly owned by the sponsoring family, with the ownership equally divided between the sons of Mr. Haji Ashfaq Ahmed: Mr. Khurram Ashfaq (50%) and Mr. Noman Ashfaq (50%). The third generation of both shareholders has taken over the business, though shareholding arrangements have not yet been decided.

Stability The shareholding resides with the sponsoring family with clear distribution provides stability. However, no formal succession plan has been documented.

Business Acumen The Sponsoring family has strong and diverse professional experience in diverse sectors including Spinning, Aluminum, Poultry, Socks and Knitwear, and Import of Building Hardware.

Financial Strength Khas Group of Industries has five companies operating in different sectors. Apart from a presence in diverse sectors; sponsors also have a joint venture, with the KAI Almunium - the largest aluminum manufacturer, in Bangladesh. The sponsors have adequate net worth and have demonstrated their commitment to support the Company if needed.

Governance

Board Structure The Company has a five-member board. Three of the members are Executive Directors and the remaining two are Non-Executive Directors. All directors have been affiliated with the Company since its inception.

Members' Profile Mr. Ashfaq Ahmed, Chairman of the Board, has over 45 years of experience in diverse industries including Spinning.

Board Effectiveness The engagement of the Directors in day to day running of the business bodes well with the effectiveness of strategic oversight. There are no committees formed by the Board.

Financial Transparency Clarkson Hyde Saud Ansari, Chartered Accountants are the external auditors of the Company. The auditors are QCR-rated. The auditors have expressed an unmodified opinion on the Company's financial statements for FY23.

Management

Organizational Structure The Company has five main departments—Production, Power House, Finance, Factory Admin, and HR—with department heads reporting to the CFO. Group management oversees operations, ensuring clear reporting lines and segregation of duties.

Management Team Mr. Khurram Ashfaq, Managing Director, has over 2 decades of experience, is responsible for overseeing all matters related to Khas Textile. He is supported by a team of seasoned professionals.

Effectiveness There are no formal management committees; however, key management members meet on regular basis to resolve and proactively address operational issues, if any, eventually ensuring a smooth flow of operations.

MIS The Company uses a customized SAP-B1-8.82 system by Abacus Consulting, covering key modules such as Payable, Receivable, Inventory, and more. Reports are regularly reviewed by top management.

Control Environment The Company has an updated technological infrastructure in all its manufacturing and support functions, to ensure quality and cost-effectiveness. The Company has an internal audit department in place.

Business Risk

Industry Dynamics The spinning industry is highly fragmented and consists of ~368 dedicated spinning units with an estimated size of PKR 775bln and 13.4mln number of spindles installed as of FY23, according to an economic survey of Pakistan. As of FY24 the projected cotton production estimate is revised and projected to be 12.8mln bales and currently, production reached up to ~10.2mln bales surpassing FY23's total production of 4.91mln bales. Pakistan's requirement for imported cotton stands at 2.5mln bales to 3mln bales this year. The recent elevation of energy tariffs and the availability of locally procured raw cotton are the prime challenges specific to the industry. Overall, the industry's cash flow and in turn liquidity remains stretched. This, along with high working capital requirements and related finance cost challenges led the industry's outlook to be placed on Watch.

Relative Position With 19,200 spindles and 864 rotors, the Company's share in the spinning sector of the textile industry is minimal and is classified in the lower tier of the spinning sector.

Revenues The Company's main revenue driver is Yarn sales, with ~70% generated from local sales and the remainder from direct exports. During FY24, the Company's revenue reflected a substantial uptake of ~40%, reporting at PKR 5,963mln reflecting a significant rebound in industry demand (FY22: PKR 4,244mln).

Margins Despite revenue growth in FY24, the Company's gross margins slightly declined to ~10.4% (FY23: ~11.1%). However, operating margins improved significantly, rising from ~6.2% in FY23 to ~7.4% in FY24, with operating profit increasing to PKR 442mln from PKR 261mln in FY23. This improvement was largely due to reduced selling and marketing expenses, enhancing cost management and operational efficiency. Net profit margin saw a decline, reporting at ~1.8% (FY23: ~1.1%) due to tax impacts, with a PAT of PKR 65mln (FY23: PKR 75mln).

Sustainability The Company's strategy focuses on optimizing capacity utilization and managing risks by securing shorter-term purchase orders. To address high markup costs, management plans to leverage the Export Finance Scheme, which will help reduce financing expenses and enhance cash flow. Efficient utilization of additional capacity is crucial for long-term success.

Financial Risk

Working Capital The Company's working capital needs are driven by holding raw materials to mitigate price volatility, cyclicality, and supply shocks, as well as funding trade receivables. Short-term borrowings, used to meet these needs, decreased to PKR 1,184mln in FY24 from PKR 1,494mln in FY23. Net working capital improved to 147 days (FY23: 181 days), and short-term trade leverage increased to ~38.2% in FY24 from 31% in FY23.

Coverages The Company's financial coverages improved during FY24, with free cash flow from operations (FCFO) increasing by ~54% to PKR 664mln from PKR 430mln in FY23. This growth enhanced the interest coverage ratio to 1.7x, up from 1.5x in FY23. Additionally, the debt coverage ratio improved to 1.5x, compared to 1.3x in FY23, indicating stronger financial stability.

Capitalization The Company has a moderately leveraged capital structure. As at FY24, the leveraging decreased to ~59.3% (FY23: ~63.9%). As of FY24, the equity base of the Company reflected an uptake of ~4% and reported at PKR 1,827mln (FY23: 1,762mln). The growth in the equity is attributed to the increase in the unappropriated profits.

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Financial Summary
PKR mln

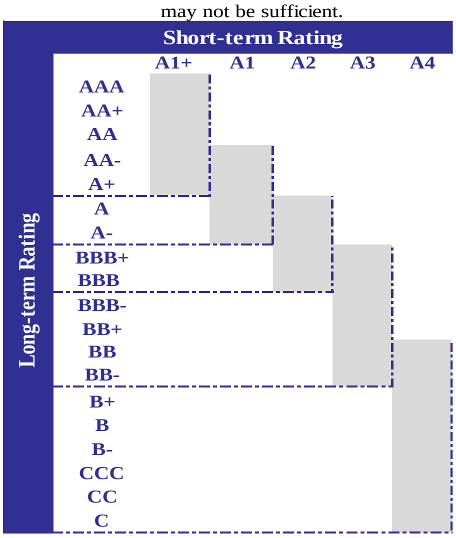
Khas Textile Mills Limited Spinning	Jun-24 12M	Jun-23 12M	Jun-22 12M	Jun-21 12M
A BALANCE SHEET				
1 Non-Current Assets	2,401	2,486	2,528	2,254
2 Investments	105	57	46	1
3 Related Party Exposure	1	3	112	65
4 Current Assets	2,524	3,051	1,936	1,484
a Inventories	*735*	*1,480*	*518*	*572*
b Trade Receivables	*1,563*	*1,038*	*1,165*	*704*
5 Total Assets	5,031	5,596	4,621	3,804
6 Current Liabilities	495	663	354	158
a Trade Payables	*308*	*446*	*188*	*82*
7 Borrowings	1,658	2,014	1,358	1,018
8 Related Party Exposure	1,003	1,105	1,082	1,071
9 Non-Current Liabilities	46	51	140	102
10 Net Assets	1,830	1,762	1,687	1,455
11 Shareholders' Equity	1,827	1,762	1,687	1,455
B INCOME STATEMENT				
1 Sales	5,963	4,244	4,994	3,581
a Cost of Good Sold	*(5,313)*	*(3,772)*	*(4,427)*	*(3,236)*
2 Gross Profit	649	473	567	345
a Operating Expenses	(208)	(211)	(104)	(85)
3 Operating Profit	442	261	464	261
a Non Operating Income or (Expense)	*51*	*69*	*(12)*	*(63)*
4 Profit or (Loss) before Interest and Tax	493	330	452	198
a Total Finance Cost	*(385)*	*(300)*	*(125)*	*(114)*
b Taxation	*(43)*	*45*	*(96)*	*(21)*
6 Net Income Or (Loss)	65	75	230	63
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*664*	*430*	*647*	*284*
b Net Cash from Operating Activities before Working Capital Changes	*246*	*187*	*527*	*284*
c Changes in Working Capital	*270*	*(697)*	*(365)*	*114*
1 Net Cash provided by Operating Activities	517	(510)	162	398
2 Net Cash (Used in) or Available From Investing Activities	(56)	(125)	(490)	(69)
3 Net Cash (Used in) or Available From Financing Activities	(458)	679	351	(330)
4 Net Cash generated or (Used) during the period	2	44	23	(1)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	40.5%	-15.0%	39.4%	40.6%
b Gross Profit Margin	10.9%	11.1%	11.4%	9.6%
c Net Profit Margin	1.1%	1.8%	4.6%	1.8%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	15.7%	-6.3%	5.6%	11.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholder*	3.6%	4.3%	14.6%	5.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	147	181	108	139
b Net Working Capital (Average Days)	124	153	98	128
c Current Ratio (Current Assets / Current Liabilities)	5.1	4.6	5.5	9.4
3 Coverages				
a EBITDA / Finance Cost	1.7	1.8	5.3	2.8
b FCFO / Finance Cost+CMLTB+Excess STB	1.5	1.3	4.2	1.4
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	5.2	12.2	2.9	7.9
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	59.3%	63.9%	59.1%	58.9%
b Interest or Markup Payable (Days)	99.7	119.3	73.7	53.9
c Entity Average Borrowing Rate	13.1%	11.6%	5.3%	4.9%

Credit Rating

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

Long-term Rating	
Scale	**Definition**
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 Rating	
Scale	**Definition**
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

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

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

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

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):
a) Broker Entity Rating
b) Corporate Rating
c) Debt Instrument Rating
d) Financial Institution Rating
e) Holding Company Rating
f) Independent Power Producer Rating
g) Microfinance Institution Rating
h) Non-Banking Finance Companies Rating

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 | Clause 11-(A)(p).
(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 | 17-(a)
(19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

Proprietary Information