The Pakistan Credit Rating Agency Limited

Rating Report

Ibrahim Fibres Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
10-Aug-2018	AA-	A1+	Stable	Maintain	-
26-Jan-2018	AA-	A1+	Stable	Maintain	-
22-Jun-2017	AA-	A1+	Stable	Maintain	-
17-Dec-2016	AA-	A1+	Stable	Maintain	-
18-Dec-2015	AA-	A1+	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect IFL’s (i) robust ownership profile (Ibrahim group) that has demonstrated strong support, (ii) leading market position in the local polyester staple fibre (PSF) industry, and (iii) intentions to keep leveraging at low levels. Imposition of anti-dumping duty on PSF imported from China since Feb-16 has supported volumetric growth and margin - performance has also gained from increasing demand. Adverse movements in crude oil prices, and, PSF feedstock prices were set off by volumetric increase in sales, providing benefit to the company’s core margins. Given demand pattern and efficient production, IFL is expected to hold performance trend. In recent years, the company’s bottomline had been a function of a reliable dividend stream of IFL's investment in Allied Bank Limited (ABL), an associated company. Lately, the said investment was sold to the group holding company. Though the recurring stream of income from ABL stopped, the resulting cash flows were primarily used to adjust debt levels. In turn, significant financial cost savings. Meanwhile improved core profitability would bode well for its financial profile.

The ratings are dependent on profitable operation of the company, supported by input prices and duty protection. Moreover, association with Ibrahim Group bodes well for the company. Going forward, induction of independent board members should benefit governance framework.

In order to formalize its corporate structure, sponsors of Ibrahim Group established a holding company – Ibrahim Holdings (Private) Limited (IHL). The new structure envisages consolidation of investments in IFL and ABL at holdco level, thus changing ownership and investment structure of investee companies. ABL’s ownership has been restructured as per plan, with restructuring of the group’s investment in IFL (currently via individuals) to follow. Nevertheless, sponsors remain committed to support IFL if need arises; the holdco structure should provide a convenient mechanism.

Disclosure	
Name of Rated Entity	Ibrahim Fibres 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 | Jun18(Jun-18)
Related Research	Sector Study | Polyester(Jan-18)
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Profile

Legal Structure Ibrahim Fibres Limited was incorporated as a Public Limited Company in 1986.

Background The company was expanded by establishing additional spinning mills and a power generation company, all of which were merged into one entity, Ibrahim Fibres Limited (IFL) in 2000.

Operations IFL is primarily engaged in the production and marketing of polyester staple fibre (PSF) and blended yarns with manufacturing facilities located at Shahkot near Faisalabad.

Ownership

Ownership Structure The majority (88%) of IFL is owned by Ibrahim Group (IG) directly through the individuals of Mukhtar family.

Stability IG established Ibrahim Holdings Ltd. (IHL) for the purposes of succession planning and managing investments in subsidiary and associated companies. It was incorporated in December, 2015.

Business Acumen The sponsors of the company carry extensive industry-related experience as well as professional experience relating to banking, finance and power.

Financial Strength The net worth of IG is considered strong. The sponsors have shown willingness and ability to support the business as demonstrated in the past through an interest free loan to support operations. IG group holds majority (84.35%) ownership of Allied Bank of Pakistan.

Governance

Board Structure The BoD consist of seven members comprising three directors from the sponsoring family, three group affiliates and one independent member. The inclusion of more independent members should benefit the governance framework.

Members' Profile Board members have significant industry related as well as diversified experience and they have been associated with the company for a reasonably long period of time.

Board Effectiveness To ensure proper oversight, two committees are in place: Audit and Human Resource. Attendance of members in the meetings remains strong.

Financial Transparency The company's external auditor, M/s. Deloitte Yousuf Adil, Chartered Accountants, provided unqualified audit opinion on financial statements for the periods ended June 2017 and December 2017.

Management

Organizational Structure IFL has a well-tiered, functionally departmentalized structure which is segregated for polyester units, spinning plants and power generation.

Management Team The management team has vast experience in their related fields and have been associated with IFL for a long time.

Effectiveness Meetings are conducted by the senior management on a need basis for discussion and decision-making purposes.

MIS The company has deployed Oracle as the ERP solution. This produces comprehensive MIS reporting.

Control Environment IFL has an internal auditory function in place to ensure impartial oversight. There is a well-trained quality control department. The company is ISO 9002 certified.

Business Risk

Industry Dynamics During 3QFY18, textile exports showed ~8% YoY growth. However, production and earning capacity still lags compared to regional countries like India, Bangladesh and Vietnam owing to higher costs of doing business. National Tariff Commission's imposition of anti-dumping duty on Chinese PSF benefitted industry players in terms of volumes and margins.

Relative Position IFL is the largest manufacturer of polyester in Pakistan in terms of volume sold (Market share FY17: 66%). It is the only synthetic textile manufacturer in the KSE100 list of companies.

Revenues IFL's topline predominantly comprises revenue from the PSF segment (9MFY18: ~85%) followed by the spinning segment. Almost the entire revenue is generated through domestic sales. Turnover showed increase of ~25% YoY which is attributable to volumetric increase since the anti-dumping duty and devaluation of the rupee shifted consumption towards domestic textile products.

Margins Cost of sales increased less proportionately due to efficiency gains resulting from BMR, translating into better gross and operating margins (9MFY18:~8%, 9MFY17:~6.6%) and (9MFY18: 5.9%, 9MFY17: 4.2%) respectively, due to cost controls. This was followed by a reduction in finance cost by ~41% owing to significant deleveraging. Net profits amounted to PKR 1,439mln for 9MFY18.

Sustainability BMR activities (replacement of machinery) were completed in 3QFY18 to ensure utilization of IFL's existing PSF capacity. A coal-fired power plant has also been commissioned. These measures aim to maximize cost savings.

Financial Risk

Working Capital IFL manages its inventory through a mix of internal generation and short term borrowings. During 9MFY18, good working capital management led to net cash cycle days remaining low (9MFY18: 46 days, 9MFY17: 46 days).

Coverages YoY increase of ~27% in FCFO (9MFY18: PKR 3,379 9MFY18: PKR 2,656) and repayment of short and long term borrowing led to an increase in debt-service coverage (9MFY18: 2.4x, 9MFY17: 1.4x). A portion of the receivable from Ibrahim Holdings (1HYFY17: PKR 3,644mln) against disposal of shares in ABL will improve cash flow position.

Capitalization IFL has a low leveraged capital structure. Debt to debt plus equity ratio stood reduced at ~16% at end-3QFY18 from ~24% during the corresponding period of previous year. Going forward, leveraging is expected to go down on account of further loan repayment.

Ibrahim Fibres Limited

BALANCE SHEET	31-Mar-18	30-Jun-17	30-Jun-16	30-Jun-15
	9M	FY	FY	FY
Non-Current Assets	**29,259**	**28,610**	**24,817**	**24,228**
Investments (Incl. associates)	**-**	**-**	**13,762**	**12,594**
Equity	-	-	13,762	12,594
Debt	-	-	-	-
Current Assets	**20,486**	**23,671**	**12,479**	**12,782**
Inventory	8,575	7,393	5,197	6,462
Trade Receivables	285	228	206	178
Others	11,626	16,050	7,076	6,142
Total Assets	**49,745**	**52,281**	**51,058**	**49,604**
Debt	**7,437**	**11,403**	**17,418**	**17,761**
Short-term	3,887	4,924	2,691	4,528
Long-term (Incl. Current Maturity of Long-Term Debt)	3,550	6,479	14,727	13,232
Other Short-term Liabilities	1,809	1,915	2,226	1,945
Other Long-term Liabilities	2,125	1,717	2,604	2,552
Shareholder's Equity	**38,375**	**37,246**	**28,811**	**27,346**
Total Liabilities & Equity	**49,745**	**52,281**	**51,058**	**49,604**

INCOME STATEMENT				
Turnover	**37,728**	**39,911**	**34,710**	**37,274**
Gross Profit	3,027	2,425	980	838
Net Other Income (Share of profit + Other income - Other expenses)	(96)	7,074	2,755	3,001
Net Finance Cost	(315)	(693)	(897)	(1,601)
Net Income	**1,439**	**8,480**	**1,535**	**803**

Cashflow Statement				
Free Cashflow from Operations (FCFO)	3,379	3,254	2,177	2,288
Net Cash changes in Working Capital	397	(4,421)	663	(115)
Net Cash from Operating Activities	3,480	(1,166)	3,211	1,886
Net Cash from InvestingActivities	855	(2,620)	(2,929)	(1,739)
Net Cash from Financing Activities	(4,275)	3,781	(343)	(69)

Ratio Analysis				
Performance				
Turnover Growth	25%	15%	-7%	-22%
Gross Margin	8%	6%	3%	2%
Net Margin	4%	21%	4%	2%
ROE	5%	23%	5%	3%
Coverages				
Interest Coverage (FCFO/Gross Interest)	10.7	4.7	2.4	1.4
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	2.4	1.2	0.8	1.1
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	2.4	1.4	1.4	1.8
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest)	0.9	2.5	11.5	19.3
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	46	49	53	55
Capital Structure (Total Debt/Total Debt+Equity)	16%	23%	38%	39%

Credit Rating Scale & Definitions

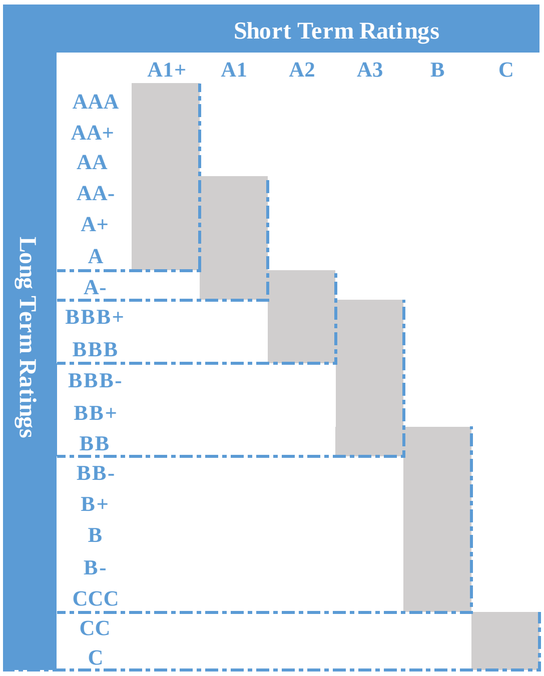
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

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

Short Term Ratings

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



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

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

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

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

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

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(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)
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