The Pakistan Credit Rating Agency Limited

Rating Report

Prosperity Weaving Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
30-Mar-2019	A-	A2	Stable	Maintain	-
28-Dec-2018	A-	A2	Stable	Maintain	-
30-Jun-2018	A-	A2	Stable	Maintain	-
28-Dec-2017	A-	A2	Stable	Maintain	-
15-Jun-2017	A-	A2	Negative	Maintain	-
29-Dec-2016	A-	A2	Negative	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings reflect modest business profile of Prosperity Weaving Mills Limited (Prosperity Weaving). The Company's revenues are on growing trajectory over the years, owing to continuous BMR translating into operational efficiency, eventually higher production volumes. The Company caters to the need of local industry as well as export markets. Textile industry in general and spinning industry in particular suffered from low international commodity prices. On standalone basis, the Company has improved its business profile on account of better product quality and efficient raw material procurement. Financial profile of the company is characterized by lean working capital cycle, adequate coverages and high leveraging. The Company maintains a highly leveraged structure with borrowing utilized for working capital and CAPEX. The Company intends to gradually build a sizable investment portfolio. This exposes the Company to market risk as exhibited by recent volatility in stock exchange. Any significant decline in investments leading to losses, and eventually equity erosion, will impact the financial profile of the Company. The management's ability to manage this risk is critical. However, the assigned ratings derive comfort from Prosperity Weaving Mills association with Nagina Group.

The ratings are dependent upon sustained market position of the Company. Moreover, the Company's ability to generate enough cash flows to fulfill its financial obligations is critical. At the same time, prudent management of investment portfolio is important.

Disclosure	
Name of Rated Entity	Prosperity 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)
Rating Analysts	Muhammad Hassan | muhammad.hassan@pacra.com | +92-42-35869504

Profile

Legal Structure Prosperity Weaving Mills Limited (Prosperity Weaving), was incorporated in 1991 as a public limited company.

Background Prosperity Weaving is associated with Nagina Group since its inception. The group has presence in spinning sector through Ellcot Spinning and Nagina Cotton. The Company's production facility is located in the vicinity of Sheikhupura.

Operations The Company's current operational capacity comprises 324 Looms. The total energy requirement of the Company is ~5MW which is wholly met through captive plant; comprising 5.4MW gas based and 6.9MW furnace oil based generator. Furthermore, the Company has LESCO connection as an alternative source.

Ownership

Ownership Structure Prosperity Weaving is majorly (~84%) owned by Nagina Group, through group companies and sponsoring individuals. The remaining stakes rests with general public and financial institutions.

Stability The considerable positions in Nagina Group are held by Ellahi Family. The Group has a structured line of succession, while the transfer of ownership to the next generation is not documented. Moreover, third generation has already been in business serving at various positions.

Business Acumen Nagina Group is one of the oldest medium-sized textile houses in Pakistan. The Group is operating under Ellahi's for over five decades, eventually developing expertise in spinning and weaving sector. However, the growth was limited but the Group sustained its business profile, despite the volatility of local textile industry.

Financial Strength Nagina Group comprises three listed public limited companies Ellcot Spinning Mills, Prosperity Weaving Mills and Nagina Cotton Mills Limited and six private limited companies. This portrays adequate financial strength of the Group to support its entities, if needed.

Governance

Board Structure Prosperity Weaving's board comprises eight members out of which six members are non-executive, one member occupy executive roles, while one director is independent. Sponsors dominance on board along with control over key management positions poses challenge to the management, thus, it hampers effective governance.

Members' Profile Mr. Shahzada Ellahi Shaikh, the Chairman, carries with him over two decades of experience. The board members have vast knowledge and extensive experience of textile industry, though diversity in experiences exists as well. The directors' expertise on different stages of the textile value-chain benefits the board in strategic planing.

Board Effectiveness Three committees: Audit, Executive and Human Resource & Remuneration, are in place to assist the board on relevant matters and ensure proper oversight. Attendance of board members in meetings remains strong and meeting minutes are formally documented.

Financial Transparency M/s. Deloitte Yousuf Adil, Chartered Accountants are the external auditors of the Company. They have expressed unqualified opinion on the financial statements of the Company for the periods ended June 30, 2018 and December 31 2018.

Management

Organizational Structure The management team is headed by Mr. Raza Ellahi Shaikh (CEO), with defined reporting line to ensure smooth operations and efficiency. Moreover, the Company have five functional departments and all HOD's reports directly to CEO.

Management Team The management team is headed by the CEO Mr. Raza Ellahi who holds a Bachelors degree in Economics. He is well versed with the textile business and has a strong business acumen. He is supported by a team of seasoned professionals that supplements his expertise.

Effectiveness The management meetings are held on daily basis with follow-up points to resolve or pro-actively address operational issues, if any, eventually ensuring smooth flow of operations. The Company's MIS can be classified into three categories on the basis of periodicity – Daily, Weekly and Monthly.

MIS Prosperity Weaving has in place Oracle based Enterprise Resource Planning (ERP) system with comprehensive MIS reporting.

Control Environment The Company is compliant with multiple safety and quality assurance standard; including ISO 9001:2008, Global Organic Textile Standards and Organic Content Standard. In order to ensure better productivity and compliance with relevant certifications the plants are regularly inspected.

Business Risk

Industry Dynamics During 1HFY19, textile exports stagnated despite ~15% rupee devaluation during the period. Knitwear showed a relatively stronger performance ensuring that textile exports' growth stayed in positive territory. Falling cotton production, rising cotton prices and issue of outstanding refunds continue to be major hindrances for the textile sector. The devalued currency, recently announced relief in gas and electricity tariffs for zero-rated sectors and removal of duties on imported cotton are expected to boost overall exports, going forward.

Relative Position Nagina Group maintains a considerable position in Pakistan's spinning and weaving sector, consequently strengthening the Company's market position. However, on standalone basis Prosperity Weaving's share in local weaving industry is minimal.

Revenues During FY18, the Company's revenues clocked in at PKR 6,212mln, posting a growth of ~6.7% YoY. Whereby rise in local sales has offset the impact of lower exports. Consequently the Company's sales mix has shifted towards local sales ~75% (FY17: 40%). Top ten customers' revenue concentration in local market is high (FY18: ~54%). Whereas, during 1HFY19 the growth trend continues and the Company's revenues posted growth of ~6.5%.

Margins During FY18, the Company's cost of sales increased in lower than proportionate of sales. Though the change was minimal, however translated into better gross and operating margins (FY18: 5.7%, FY17: 5.2%) and (FY18: 3.1%, FY17: 2.3%), respectively. Despite the increase in finance cost by (~41%), the Company posted a profit of ~PKR 55mln (FY17: PKR 56mln). The Company's margins improved significantly in 1HFY19 (gross -1HFY19: 8.2%, net - 1HFY19: 5.4%), largely led lower yarn prices and subsidized utilities for textile sector effectively lowering conversion cost.

Sustainability Balancing Modernization and Replacement (BMR) is a regular feature at the Company. The Company has incurred a BMR of ~PKR 961mln in last two years to increase its operational efficiencies, while diversifying product range, a key factor in order to improve margins in competitive textile industry. Moreover, the Company has an investment portfolio.

Financial Risk

Working Capital The Company's reliance on Short term borrowing has increased during the year though STB remains well covered when compared to net trade assets (FY18: 12%, FY17: 20%), portraying further room to borrow. Meanwhile, considerable increase in receivable days (FY18: 40days, FY17: 29days), led to higher net working capital days (FY18: 54days, FY17 44days). The Company's working capital cycle marginally increased in 1HFY19, reflected from higher net working capital days (1HFY19: 58days, 1HFY18 51days) on the back of higher inventory levels.

Coverages During FY18, the Company's operating cash flows (FCFO) increased by ~30% (FY18: PKR 406mln, FY17: PKR 311mln). However, higher than proportionate increase in finance cost has resulted in deteriorated interest coverage (FY18: 2.8x, FY17: 3.0x). while the debt coverage slightly improved (FY18: 1.2x, FY17: 1.0x). Whereas, coverages improved in 1HFY19 and stood at (interest: 3.4x, debt: 1.3x) on account of better FCFO generation, largely offsetting the impact of higher finance cost, when compared on half yearly basis. Going forward, further interest rate hike may stretch the Company's coverages.

Capitalization Prosperity Weaving has a significantly leveraged capital structure (~73.2%) at end-June 18 (end-June 17: 74.2%). Total debt stood at PKR 2,730mln, with a balanced mix of current debt (~45.3%) and non-current debt (~54.7%). At end-Dec18, the Company's leveraging largely remained the same.

PKR mln

Prosperity Weaving Mills Limited
Listed Public Limited

BALANCE SHEET	Dec-18	Jun-18	Jun-17	Jun-16
	6M	12M	12M	12M
a Non-Current Assets	**2,143**	**2,248**	**2,273**	**1,763**
b Investments (Incl. Associates)	**470**	**451**	**549**	**120**
Equity Instruments	470	451	549	120
Debt Instruments	-	-	-	-
c Current Assets	**1,636**	**1,560**	**1,476**	**1,058**
Inventory	595	358	386	297
Trade Receivables	669	713	632	283
Others	372	489	458	477
d Total Assets	**4,250**	**4,260**	**4,299**	**2,941**
e Debt/Borrowings	**2,717**	**2,730**	**2,787**	**1,570**
Short-Term	1,072	1,030	969	297
Long-Term (Incl. Current Maturity of Long-Term Debt)	1,645	1,700	1,819	1,274
Other Short-Term Liabilities	458	429	437	321
Other Long-Term Liabilities	108	100	107	93
f Shareholder's Equity	**967**	**1,001**	**968**	**957**
g Total Liabilities & Equity	**4,250**	**4,260**	**4,299**	**2,941**

INCOME STATEMENT				
a Turnover	**3,307**	**6,212**	**5,820**	**5,211**
b Gross Profit	271	356	303	360
c Net Other Income	(1)	2	5	(10)
d Financial Charges	(86)	(144)	(102)	(111)
e Net Income	**53**	**55**	**56**	**40**

CASH FLOW STATEMENT				
a Free Cash Flow from Operations (FCFO)	274	406	311	343
b Total Cashflows (TCF)	293	437	329	345
c Net Cash changes in Working Capital	(233)	37	(379)	(116)
d Net Cash from Operating Activities	(16)	338	(149)	114
e Net Cash from InvestingActivities	(86)	(91)	(1,139)	(79)
f Net Cash from Financing Activities	(49)	(94)	1,185	77
g Net Cash generated during the period	(152)	152	(103)	112

RATIO ANALYSIS				
a Performance				
Turnover Growth	6%	7%	12%	-10%
Gross Margin	8%	6%	5%	7%
Net Margin	2%	1%	1%	1%
ROE	11%	6%	6%	4%
b Coverages				
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	1.3	1.2	1.1	1.4
Interest Coverage (X) (FCFO/Gross Interest)	3.4	3.0	3.3	3.4
Debt Payback (Years) (Total Debt (excluding Covered Short Term Borrowings)	4.2	6.3	8.4	5.3
c Capital Structure (Total Debt/Total Debt+Equity)				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	58	54	44	34
d **Capital Structure** (Total Debt/Total Debt+Equity)	74%	73%	74%	62%

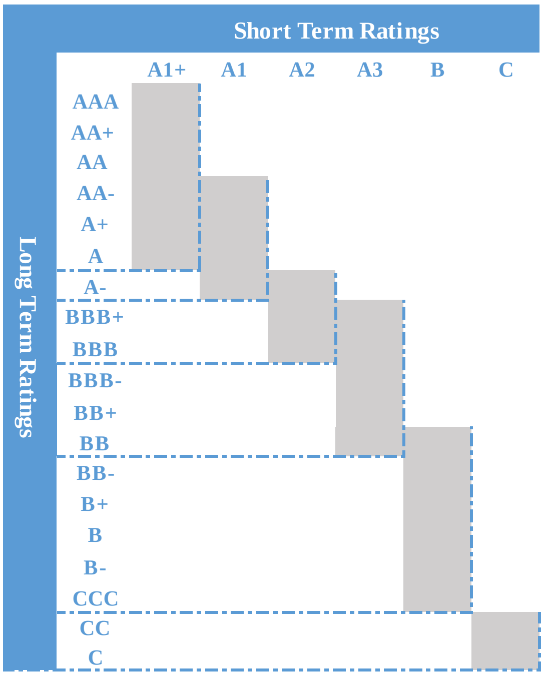
Rating Scale

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