RATING REPORT

J.K Spinning Mills Limited

REPORT DATE:
April 26, 2022

RATING ANALYST:
Muhammad Tabish
muhammad.tabish@vis.com.pk

RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-1	A-	A-1
Rating Outlook	Positive		Stable	
Rating Date	*April 26, 2022*		*April 28, 2021*	

COMPANY INFORMATION	
Incorporated in 1987	**External Auditors:** Riaz Ahmad & Co. Chartered Accountants
Public Listed Company	**Chairman:** Mr. Jawed Anwar
Key Shareholding (more than 5%)	**CEO:** Mr. Faiq Jawed
Mr. Jawed Anwar ~35.22%	
Mr. Faiq Jawed ~24.74%	
Mr. Shaiq Jawed ~16.99%	
Mrs. Farhat Jehan ~15.26%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial Corporates (August 2021) *https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf*

J.K Spinning Mills Limited

OVERVIEW OF THE INSTITUTION

J.K Spinning Mills Limited is a public listed company incorporated in Pakistan in January 1987, under the repealed Companies Ordinance, 1984 (now Companies Act, 2017). The company is a composite textile unit that operates in spinning, weaving and stitching divisions. Head office of the company is located in Faisalabad.

Profile of Chairman:

Mr. Jawed Anwar serves as the Chairman of the Board. He has over 60 years of experience in the spinning industry. He served as the Vice-Chairman of Faisalabad Chamber of Commerce and Chairman of Pakistan Textile Export Association.

Profile of CEO:

Mr. Faiq Jawed serves as the CEO of the company and has 35+ years of experience in the spinning industry. He has also served as the Vice Chairman of Faisalabad Chamber of Commerce and Chairman of Pakistan Textile Export Association.

RATING RATIONALE

Corporate Profile

Headquartered in Faisalabad, J.K Spinning Mills Limited (JKSM), a part of J.K Group, is a composite textile unit that operates in spinning, weaving and stitching divisions with established operating track record of around 35 years. Product portfolio mainly comprises fine yarn and home textile. The sponsoring family who is actively involved in the business affairs holds majority shareholding. JKSM has in place a qualified senior management team with extensive experience while at present, total staff strength stands at 2.5K+ employees.

Group Profile

Initially established in 1975, the group has been restructured numerous times over the years and in 2011, operations of two textile mills were merged into JKSM. Presently, the group has investments in 4 other entities as well including J.K Power Limited, J.K Agriculture Farms (Private) Limited, Fine Fabrics (Private) Limited and J.K Tech (Private) Limited.

JKSM Operations

At present, JKSM's production facilities include three spinning units and one unit each in weaving, stitching and processing segment. Utilization levels in both the major segments (spinning & weaving) have witnessed an upward trend on account of sizeable jump in demand particularly on the export front.

Figure: Capacity & Production Data

	FY19	FY20	FY21
Production Capacity			
Spinning (Kgs)	41,508	44,501	45,365
Weaving (Sq. mtr)	18,011	18,667	22,263
Actual Production			
Spinning (Kgs)	36,755	37,051	44,501
Weaving (Sq. mtr)	12,038	14,934	18,667
Capacity Utilization			
Spinning (Kgs)	*89%*	*83%*	*98%*
Weaving (Sq. mtr)	*67%*	*80%*	*84%*

Spinning Division:

The company offers a broad range of ring spun yarn with variety of counts. Total number of spindles currently stands at 151,944 while the annual yarn production capacity, over the last two years, has increased by ~10% on the back of efficiency enhancement initiatives mainly including replacement of old spindles.

Fabric, Home Textile and Hospitality Supplies:

The fabric and weaving division offers a wide variety of fabrics. The division is involved in processed cloth production as well as made ups like bedsheets, pillow covers, and comforter shells etc. Moreover, a wide range of dyes and finishes is also offered. Total number of Sulzer looms currently stands at 110; of which 10 looms were added last year. The same has resulted in ~24% increase in production capacity over the period of last two years.

Stitching Division:

The stitching division currently has 450 stitching machines operating at ~90% capacity. Since last review, 60+ new machines have been installed in the stitching segment, increasing its total capacity to around 50m meters per annum.

Long-term capacity enhancement plans for both spinning and weaving divisions.
The management has planned to establish a new spinning unit, having 52,896 spindles. At present, the building is under construction and has a completion status of ~80%. The construction is expected to be completed within 3 months while production is planned to be started by Oct-2023. Total estimated cost of the project stands at Rs. 3.7b. Post completion of the spinning project, second expansion project will be initiated which pertains to the construction of a new weaving unit, having 144 air jet looms. Total estimated cost of the project stands at Rs. 3.2b while land has already been acquired for the same. Both projects will be funded through a mix of 60% debt and 40% equity; the company plans to mobilize bank borrowings of Rs. 2.4b for the spinning project during FY23 and Rs. 2.2b for the weaving project during FY25.

Key Rating Drivers

Textile and clothing exports have registered a sizeable growth given the surge in demand on account of rerouting of orders to Pakistan and favorable sector policies. Outlook is favorable going forward.
The textile sector contributes nearly one-fourth to industrial value-added segment and 8.5% to the country's GDP, with an estimated market size of Rs. 3.8tr (FY20: Rs. 3.3tr) in FY21. Barring seasonal and cyclical fluctuations, textiles products have maintained an average share of about 60% in national exports. Given post pandemic sustained economic recovery and diversion of export orders to Pakistan, export revenues from textile segment (as per PBS) stood at USD 15.4b (FY20: USD 12.5b; FY19: USD 13.6b) in FY21, registering a sizeable year-on-year growth of ~23%. The similar growth trend has been noted in the ongoing year with exports reaching at USD 9.4b during 6M'FY22, up by 26% vis-à-vis SPLY. Knitwear, Readymade and Bed wear segments continued to contribute higher than other segments, with a cumulative contribution of more than 60% in textile exports. While primarily a volumetric driven growth, the exports also received a boost from higher prices (excluding Knitwear). During the year, while average volumes increased by around 20-30% in various segments as compared to the lock down period, average prices increased by 8-10%.

Figure: Textile Exports (as per PBS)

Segments	Value (US$ millions)		YoY(Δ)
	FY20	FY21	
Knitwear products	2,785	3,816	*37%*
Readymade Garments	2,549	3,033	*19%*
Bed wear	2,149	2,772	*29%*
Cotton Cloth	1,830	1,921	*5%*
Cotton Yarn	987	1,017	*3%*
Towels	711	938	*32%*
Made-up Articles	591	756	*28%*
Art, silk and synthetic textile	314	370	*18%*
Tents, canvas and tarpaulin	98	110	*12%*
Others	487	667	*37%*

Going forward, sector dynamics are favorable as Pakistan continues to receive export orders from global economies as competing regional countries remains hampered by the pandemic. Given the surge in demand, the industry is currently operating at full capacity and going through expansion and up-gradation to cater for additional demand.

5-Year (2020-25) textile policy continues to support the industry.
With the aim to double textile exports in five years, GoP through a five-year textile policy (2020-25) has provided incentives in form of preferential energy rates, low interest rates financing schemes (such as EFS, LTFF and TERF) and timely payments of DLTL, Income tax & Sales tax refund which would support liquidity constraints of local players. Initiatives are also being undertaken in order to increase production and yield of cotton to support the industry. Going forward, new Covid-19 variants (Omicron) and uncertainty of its impact on overall economy and political environment are the key present business risk factors. In the long run, improvement in value addition, investment in technology and optimization of energy cost would define the future of textile exports.

High cyclicality and competitiveness in the spinning sector translate into high business risk profile.
Movement in cotton prices and cotton crop levels drives performance of spinning players in Pakistan. Given sizeable deficit in local cotton production vis-à-vis demand in the recent years, cotton prices have remained elevated due to which inventory loss risk is considered limited. As with other domestic spinning players, reliance on China as major export market translates into high country concentration risk. However, business risk is supported by favorable government policies and healthy demand outlook.

Strong growth in yarn export orders has led to a sizeable jump in sales revenue during the period under review. Topline is projected to reach the Rs. 25b mark by end-FY22.
Topline of the company has registered a 4-Year CAGR of ~15% for the period (FY18-21), and amounted to Rs. 17.4b (FY20: Rs. 14.8b) in FY21. The year-on-year uptick of ~17% was mainly attributable to sizeable uptick in yarn export orders. The growth momentum has continued in the ongoing fiscal year with topline amounting to Rs. 12.4b during 6M'FY22, increasing by ~57% vis-à-vis SPLY. Going forward, the management is targeting sales revenue to reach Rs. 25b mark in FY22 on the back of continued demand growth and strong revenue visibility. Net sales have been reported at Rs. 18b during 9M'FY22.

Overall sales comprise a mix of local and export sales, with yarn majorly sold in local markets while processed fabric and made-ups are largely exported. Major exports sales are directed towards USA, UK and Belgium. Yarn sales have dominated the revenue mix over the years, representing around three-fifth of total sales. Client-wise sale concentration risk is low with top 10 clients constituting around ~20% of total sales revenue.

Profitability margins continue to witness the growth trend.
Gross margins have exhibited an increasing trend on a timeline basis (6M'FY22: 23.6%; FY21: 19.1%; FY20: 16.9%; FY19: 14.0%) on the back of higher average sale price over the years coupled with rupee devaluation and efficient cotton procurement. The healthy jump in margins during the ongoing year pertains to favorable cotton price differential which aligns with the industry trend.

Operating overheads have more than doubled during 6M'FY22, vis-à-vis SPLY, mainly due to higher exchange loss and sizeable increase in ocean freight charges and salaries expense. Financial charges were also reported higher due to increase in utilization of running finance facility. However, despite the increase in operating expenses, bottom-line during the ongoing year depicted considerable improvement due to sizeable growth in revenues. As a result, net margins were also reported higher at 13.5% (FY21: 10.4%; FY20: 7.7%).

Overall liquidity profile remains strong with sizeable cash flow generation.

Liquidity profile is considered strong with sizeable cash flows to support debt repayment obligations. In absolute terms, Funds from Operations (FFO) increased to Rs. 2.1b (FY21: Rs. 2.4b; FY20: Rs. 1.6b) at end-1H'FY22. As a result, FFO to total debt and FFO to long-term debt also increased considerably to 0.70x (FY21: 0.44x) and 2.42x (FY21: 1.41x), respectively. Healthy cash flow generation in the ongoing year has positively impacted the debt coverage metrics as reflected by strong growth in DSCR to 4.70x (FY21: 4.25x; FY20: 2.90x). Working capital cycle of the company necessitates utilization of short term borrowings mainly to fund inventory levels. Current ratio remains strong at over 1.5x, while coverage of short-term borrowings in relation to stock in trade and trade debts is more than sufficient. Aging profile of trade debts remains within manageable levels with no receivable outstanding for more than six months.

Strong capitalization levels; leverage indicators have improved marginally in the ongoing year.

Equity base while crossing the Rs. 8b mark has depicted a more than two-fold increase over the past 24 months. The timeline growth has been achieved through bonus issue and profit retention. The cash dividend payout ratio stood at 15% (FY20: 10%) in FY21. Debt profile comprises a mix of short-term and long-term debt with total interest bearing liabilities increasing to Rs. 5.9b (FY21: Rs 5.5b; FY20: Rs. 4.7b) at end-1H'FY22; short-term debt (ERF) constituted ~70% of total debt. Despite increase in overall borrowings, gearing and debt leverage improved marginally to 0.71x (FY21: 0.82x) and 0.92x (FY21: 0.99x), respectively. Equity base while crossing the Rs. 8b mark has depicted a more than two-fold increase over the past 24 months.

J.K Spinning Mills Limited Appendix I

FINANCIAL SUMMARY					*(amounts in PKR millions)*
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**FY21**	**HFY22**
Non-Current Assets	3,571	4,347	4,579	5,502	6,093
Stores, Spares. And Loose Tools	95	87	105	142	172
Stock-in-Trade	2,461	3,747	4,806	5,810	6,197
Trade Debts	867	786	1,267	1,269	2,838
Advances, Deposits and Other Receivables	200	99	99	220	289
Tax Refund Due From Government	340	304	283	368	651
Cash and Bank Balance	59	125	92	118	201
Total Assets	**7,594**	**9,495**	**11,252**	**13,887**	**16,440**
Trade and Other Payables	470	662	813	871	1,304
Long-Term Borrowings *(Inc. current maturity)*	1,136	1,489	1,493	1,733	1,701
Short-Term Borrowings	2,098	2,645	3,173	3,817	4,202
Other Liabilities	275	442	347	300	428
Tier-1 Equity	**3,390**	**4,033**	**5,029**	**6,768**	**8,286**
Total Equity	3,615	4,258	5,425	7,164	8,805
Paid-up Capital	731	731	731	1,023	1,023
INCOME STATEMENT					
Net Sales	9,900	13,687	14,827	17,403	12,358
Gross Profit	1,045	1,914	2,499	3,332	2,912
Operating Profit	632	1,280	1,704	2,409	2,101
Profit Before Tax	430	894	1,307	2,142	1,902
Profit After Tax	338	716	1,142	1,812	1,672
RATIO ANALYSIS					
Gross Margin (%)	10.6	14.0	16.9	19.1	23.6
Net Margin (%)	3.4	5.2	7.7	10.4	13.5
Net Working Capital	1,145	1,445	2,215	3,038	3,981
Current Ratio	1.40	1.39	1.50	1.57	1.63
FFO to Long-Term Debt	0.54	0.81	1.05	1.41	2.42
FFO to Total Debt	0.19	0.29	0.34	0.44	0.70
DSCR (x)	2.15	2.65	2.90	4.25	4.70
Gearing (x)	0.95	1.02	0.93	0.82	0.71
Debt Leverage (x)	1.17	1.30	1.16	0.99	0.92
Inventory + Receivable/Short-term Borrowings (x)	1.59	1.71	1.91	1.97	2.15

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES					Appendix III
Name of Rated Entity	J.K Spinning Mills Limited				
Sector	Textile				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	26/04/2022	A-	A-1	Positive	Maintained
	28/04/2021	A-	A-1	Stable	Maintained
	24/04/2020	A-	A-1	Rating Watch-Developing	Maintained
	28/03/2019	A-	A-1	Stable	Initial
Instrument Structure	N/A				
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.				
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.				
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Due Diligence Meeting Conducted	**Name**	**Designation**	**Date**		
	Mr. Amjad Ali	Chief Financial Officer	April 15, 2022		