RATING REPORT

Feroze1888 Mills Limited

REPORT DATE:
January 07, 2022

RATING ANALYST:
Arsal Ayub, CFA
arsal.ayub@vis.com.pk

Musaddeq Ahmed Khan, MBA
musaddeq@vis.com.pk

RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	AA-	A-1	AA-	A-1
Rating Date	*January 07, 2022*		*December 07, 2020*	
Rating Outlook	Stable		Stable	
Outlook Date	*January 07, 2022*		*December 07, 2020*	

COMPANY INFORMATION	
Incorporated in 1972	**External auditors:** EY Ford Rhodes Chartered Accountants
Public Listed Company	**Chairman:** Jonathan R. Simon
Key Shareholders (with stake 5% or more)[1]:	**Chief Executive Officer:** Rehan Rahman
Mr. Shabbir Ahmed	**Chief Financial Officer:** Javeria Siddiqui
M/s. Grangeford USA Inc	
M/s. EFU Life Assurance Limited	
Mr. Omair Rehman	
Mr. Perwez Ahmed	
M/s. Liberty Mills Limited	

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

Feroze1888 Mills Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Feroze1888 Mills Limited was incorporated in Pakistan as a Public Limited Company in October 1972. The shares of the Company are quoted on Pakistan Stock Exchange Limited. The Company is principally engaged in the production and export of towels. The registered office of the company is situated at H-23/4-A Scheme # 3, Landhi Industrial Area, Karachi.

Feroze1888 Mills Limited ('FML' or 'the Company') specializes in the production and export of terry products with its main export destinations being United States and Europe. The Company offers a wide selection of terry items, including hand towels, bath towels, bath robes, kitchen towels, and beach towels, in a variety of sizes and categories. FML is a vertically integrated company that processes materials from start to finish, from spinning to packing.

FML operates through various units at different locations, including Hub, SITE and Landhi, which comprise spinning, weaving, dyeing and stitching units. The Company has a strategic alliance with 1888 Mills USA.

Sector Update

Table 1: Pakistan Export Statistics

	FY19	FY20	FY21	Q1'FY21	Q1'FY22
PAKISTAN EXPORTS (IN USD' MILLIONS)	24,257	22,536	25,632	5,354	7,241
TEXTILE (IN USD' MILLIONS)	13,659	12,867	14,488	3,086	4,240
PKR/USD RATE (AVERAGE)	136.3	158.2	160.3	167.0	164.6
SOURCE: SBP					

- Subsequent to posting export contraction in FY20 - owing to the pandemic-induced slowdown experienced in H2'FY20 – Pakistan's export base grew by 14% in FY21, which is partly attributable to a low base effect. Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21). So the uptick is largely aligned with historical numbers and is not considered material.
- Share of textile exports in total exports has oscillated in the range of 54-59%, coming in at 57% during the past 2-years (FY20-21). In FY21, owing to the similar low-base effect, as discussed above, textile exports were up 13%.
- In USD' terms textile exports have grown at a CAGR of 4.4% during the past 3-year period (FY19-FY21), despite depreciation in average USD/PKR parity of 24%, 16%, and 1% in FY19, FY20 and FY21 respectively.
- As illustrated in the table above, textile exports in Q1'FY22 were 37% higher than SPLY. Inclusive of textile exports for Oct'2021, the number for 4M'FY22 textile exports came in at USD 6b. With additional capacities coming online in January 2022, textile exports for FY22 are likely to exceed the annualized figure of USD 18b.
- As illustrated in the table below, the composition of textile exports has depicted improvement in the last 4-yar period, with contribution from higher value added segment increasing from 72.9% in FY18 to 80.7% in FY21 of aggregate textile exports.

Table 2: Segment-wise textile Exports (All Figures in USD' Millions, except for percentages)

	FY18	FY19	FY20	FY21	FY18	FY19	FY20	FY21
HIGH VALUE-ADDED SEGMENT	**9,854**	**10,046**	**9,669**	**12,428**	**72.9%**	**75.4%**	**77.2%**	**80.7%**
- KNITWEAR	2,711	2,900	2,794	3,816	20.1%	21.8%	22.3%	24.8%
- READYMADE GARMENTS	2,577	2,653	2,552	3,033	19.1%	19.9%	20.4%	19.7%
- BED WEAR	2,261	2,262	2,151	2,772	16.7%	17.0%	17.2%	18.0%
- TOWELS	797	786	711	938	5.9%	5.9%	5.7%	6.1%
- MADE-UP ARTICLES (EXCL. TOWELS & BED WEAR)	685	680	591	756	5.1%	5.1%	4.7%	4.9%
- ART, SILK & SYNTHETIC TEXTILE	310	297	315	370	2.3%	2.2%	2.5%	2.4%
- OTHERS	513	468	555	743	3.8%	3.5%	4.4%	4.8%
LOW TO MEDIUM VALUE-ADDED SEGMENT	**3,667**	**3,282**	**2,858**	**2,972**	**27.1%**	**24.6%**	**22.8%**	**19.3%**
- COTTON CLOTH	2,204	2,102	1,830	1,921	16.3%	15.8%	14.6%	12.5%
- COTTON YARN	1,372	1,125	984	1,017	10.1%	8.4%	7.9%	6.6%

- OTHERS	92	54	43	34	0.7%	0.4%	0.3%	0.2%
TOTAL	**13,521**	**13,328**	**12,527**	**15,400**			-	
SOURCE: PBS								

- Cotton production in Pakistan, on the other hand, was at its lowest level in decades for FY21. Cotton prices rose to a new 11-year high of ~Rs. 13,000/maund as a result of the production shortage, and cotton imports have climbed by 59.8% in quantity and 68.1% in USD terms, for FY21 vis-à-vis preceding year.

Table 3: Cotton Prices

	FY18	*FY19*	*FY20*	*FY21*
Per Maund (Rs.)	**6,953**	**8,770**	**8,860**	**13,000**
% Change	*6%*	*26%*	*1%*	*32%*

- Given favorable weather conditions, cotton production in Pakistan posted strong growth in FY22, with cotton crop for Jul-Nov'21 (Rabi) season being 81% higher than SPLY. Nevertheless, the upward momentum in cotton pricing continued in FY22, with prices as of November 2021 hovering at ~Rs. 16,000 per maund.
- The margins of textile operators have broadly depicted improvement despite the uptick in raw material costs, given that the same was offset by exchange rate movement. Nevertheless, higher raw material pricing has increased the working capital requirements for textile operators, which is likely to weigh on the liquidity of textile players.

Operations and Business Update

Table 4: Operating Capacity

	FY20	FY21
NUMBER OF SPINDLES INSTALLED (RING)	45,828	48,072
NUMBER OF SPINDLES WORKED (RING)	42,258	46,950
NUMBER OF LOOMS INSTALLED	378	371
NUMBER OF LOOMS WORKED	363	366
INSTALLED CAPACITY	62,445,309	74,388,971
ACTUAL PRODUCTION	56,852,875	67,382,160
INSTALLED CAPACITY METERS	135,607,345	154,149,648
ACTUAL PRODUCTION METERS	128,300,408	150,612,635

- As illustrated in the table above, FML has undertaken capacity enhancement in both, spinning and weaving segments, increasing their production capacity by 19% and 14% respectively.
- The spinning segment's capacity utilization remained stable at 91%, while the weaving segment's capacity utilization has improved to 97.7% (FY20: 94.6%) in FY21.

Table 5: P&L (Extract)

	FY19	FY20	FY21	Q1'FY22
SALES	29,348	31,206	42,575	11,356
GROSS MARGIN	26.40%	24.10%	23.60%	16.25%
GROSS PROFIT	7,748	7,507	10,066	1,845
EBIT MARGIN	21.73%	11.63%	12.56%	6.25%
NET MARGIN	20.40%	9.40%	10.10%	3.84%
NET PROFIT	5,990	2,937	4,311	436

- Given the pandemic-induced slowdown, wherein neighboring countries were relatively more affected vis-à-vis Pakistan, textile exports depicted notable growth. In tandem with industry growth, FML's topline depicted strong growth of 36.4% vis-à-vis preceding year.
- Gross margins were slightly lower in FY21, as illustrated in the table above, mainly being weighed down by higher input costs. However, given volumetric growth in offtake, gross profit was 34% higher on a YoY basis.
- The Company's net margin remains stable at around 10%. In absolute terms, the Company's net profit amounted to Rs. 4.3b, lower than pre-pandemic (FY19) bottom line of Rs. 6.0b.
- We have noted the stress on margins, as indicated by the sharp decline in gross margin in Q1'FY22. As per management, this stress is mainly a result of higher (weighted average) cost of raw material, which has not been fully passed onto the consumers. Given significant depreciation in PKR in Q2'FY22, margins are projected to improve.

Key Rating Driver

FML ratings incorporate FML's market positioning, as a vertically integrated terry textile operator

- Based on its affiliation with 1888 Mills, FML enjoys a competitive advantage over other players in terms of access to US Market. Resultantly, sales in the US market account for majority of the Company's offtake.
- The rating incorporates business risk profile of FML as a vertically integrated terry textile exporter. In addition the rating also takes into account regional and counterparty concentration inherent in FML's revenue base.

Ratings take into account profitability margins and cash flow coverage indicators of FML

Table 6: Cash flow analysis

	FY19	*FY20*	*FY21*	*Q1'FY22*
FFO (Mn.)	**7,008**	**4,447**	**6,124**	**799**
Debt	**8,757**	**15,171**	**19,490**	**20,539**
- ***Short Term Debt***	6,490	9,640	11,750	12,800
- ***Long Term Debt***	2,267	5,531	7,740	7,739
FFO/Total Debt (%)	**80%**	**29%**	**31%**	**16%**
FFO/LTD (%)	**309%**	**80%**	**79%**	**41%**
DSCR (x)	**24.9**	**8.8**	**7.4**	**3.9**
Current Ratio (x)	**1.7**	**1.5**	**1.6**	**1.5**
Cash Conversion Cycle (days)	**121**	**107**	**115**	**130**
No. of days in inventory	108	127	95	117
No. of days in receivable	95	80	87	85
No. of days in Creditors	83	100	67	72

- Given strong growth in revenue base, the FFO was 38% higher YoY.
- However, with higher debt utilization, cash flow coverage indicators had been affected, which have come under further stress in Q1'FY22. As per management, cash flow coverage should improve in remaining part of the year, as margins normalize. VIS will continue to closely monitor the trends in the same.
- Stock in trade and receivables coverage of short-term borrowings remains adequately high.

Ratings incorporate financial risk indicators of FML

- Given increase debt utilization, we have noted increase in FML's gearing and leverage indicators, as illustrated in the table below. The Company's debt is entirely composed of financings under SBP's concessionary financings schemes for exporters.
- Nevertheless, despite the increase, gearing & leverage remains aligned with peers.

Table 7: Balance Sheet (Extract)

	FY19	*FY20*	*FY21*	*Q1'FY22*
Total Assets	33,967	43,097	51,867	54,890
Total Liabilities	13,864	21,950	27,414	30,000
Equity (Exc. Surplus on reval.)	18,604	19,661	22,967	23,403
ST Debt	6,490	9,640	11,750	12,800
LT Debt	2,267	5,531	7,740	7,739
Total Debt	8,757	15,171	19,490	20,539
Gearing (x)	0.47	0.77	0.85	0.88
Leverage (x)	0.75	1.12	1.19	1.28

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**Jun'19**	**Jun'20**	**Jun'21**	**Sep'21**
Fixed Assets	13,459	17,595	20,308	21,303
Stock-in-Trade	6,411	8,270	8,437	12,170
Trade Debts	7,630	6,810	10,116	10,531
Cash & Bank Balances	3,268	2,248	1,625	549
Total Assets	20,304	25,456	31,473	33,484
Trade and Other Payables	4,911	6,481	5,958	7,458
Long Term Debt	2,267	5,531	7,740	7,739
Short Term Debt	6,490	9,640	11,750	12,800
Total Debt	8,757	15,171	19,490	20,539
Paid Up Capital	3,768	3,768	3,768	3,768
Total Equity	18,604	19,661	22,967	23,403
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**Q1'FY22**
Net Sales	29,348	31,206	42,575	11,356
Gross Profit	7,748	7,507	10,066	1,845
Operating Profit	6,377	3,631	5,348	710
Profit Before Tax	6,221	3,284	4,789	563
Profit After Tax	5,990	2,937	4,311	436
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**Q1'FY22**
Gross Margin (%)	26.1%	24.1%	23.6%	16.2%
Net Margin (%)	20.5%	9.4%	10.1%	3.8%
Net Working Capital	8,575	8,896	11,915	11,235
Trade debts/Sales	26%	22%	24%	23%
FFO	7,008	4,447	6,124	799
FFO to Total Debt (%)	80%	29%	31%	16%
FFO to Long Term Debt (%)	309%	80%	79%	41%
Debt Servicing Coverage Ratio (x)	24.9	8.8	7.4	3.9
Current Ratio (x)	1.7	1.5	1.6	1.5
Stock+Trade Debts/STD	216%	156%	158%	177%
Gearing (x)	0.47	0.77	0.85	0.88
Leverage (x)	0.75	1.12	1.19	1.28
ROAA (%)	21%	8%	9%	3%
ROAE (%)	36%	15%	20%	8%

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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	Feroze1888 Mills Limited
Sector	Textiles
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	
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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2021 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.
Due Diligence Meetings Conducted	

Rating History:

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
07-Jan-2022	AA-	A-1	Stable	Reaffirm
07-Dec-2020	AA-	A-1	Stable	Reaffirm
13-Nov-2019	AA-	A-1	Stable	Reaffirm
12-Nov-2018	AA-	A-1	Stable	Initial

Due Diligence Meetings Conducted:

Name	Designation	Date
Javeria Siddiqui	CFO	26-Nov-2021