RATING REPORT

Comfort Knitwears (Pvt.) Limited

REPORT DATE:
July 12, 2023

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		*Initial*	
Rating Date	*July 12, 2023*		*June 02, 2022*	

COMPANY INFORMATION

Incorporated in 1985	**External Auditors:** Baker Tilly Mehmood Idrees Qamar Chartered Accountants.
Private Limited Company	**CEO:** Mr. Muhammad Asher Khurram
Key Shareholders (with stake 5% or more):	**Chairman:** Mr. Muhammad Ismail Khurram
Mr. Muhammad Asher Khurram ~35%	
Mr. Muhammad Imran Khurram ~35%	
Mr. Muhammad Ismail Khuuram ~25%	
Mrs. Irshad Begum ~5%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (May 2023)
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale: *https://docs.vis.com.pk/docs/VISRatingScales.pdf*

Comfort Knitwears (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Comfort Knitwears (Pvt.) Limited was incorporated as Private Limited Company on September 22, 1985, under the repealed Companies Ordinance 1984 (now the Companies Act, 2017). It is principally engaged in manufacturing and sale of yarn, knitwear, and garments. Registered office of the company is located at 45- Industrial Estate, Township, Kot Lakhpat, Lahore.

RATING RATIONALE

Corporate Profile

Comfort Knitwears (Private) Limited (CKPL), a part of the Comfort Group, is a vertically integrated knitwear apparel facility with spinning, knitting, dyeing and stitching units. With over three decades of operational history, CKPL specializes in dyed yarn and offers a wide range of knitted garments. The sponsoring family holds entire ownership and actively participates in day-to-day business affairs. Production infrastructure is based in Lahore, supported by a workforce of over 3,000 employees.

The company holds ISO and various other globally recognized certifications, emphasizing its commitment to high-quality standards. It also prioritizes environmental sustainability through initiatives like effluent treatment, air emission control, and solid waste management. Average energy demand of nearly 6 MW is met through an optimal mix of gas generators, gas & coal boilers and national-gridline, while diesel-based generators serve as a backup.

Group Profile

The Comfort group is involved in diverse business interests primarily focused on textiles, pharmaceuticals, and transportation. All group companies are family-owned. In textiles, the group includes Zulfiqar Knitting & Processing Mills (Pvt.) Limited (a vertically integrated knitwear manufacturing unit focused on exports), Asher Imran Spinning Mills (Pvt.) Limited (a subsidiary of CKPL, producing cotton & blended specialty yarns), and Comfort Yarn Dyeing and Surgical Cotton Mills (Pvt.) Ltd (specializing in yarn dyeing and processing). In pharmaceuticals, the group has Frontier Dextrose Limited and Curatech Pharma (Pvt.) Limited manufacturing and selling intravenous solutions and antibiotics, respectively.

Operational Performance

CKPL, with its headquarters in Lahore, operates three garment units for stitching and knitting, along with a spinning, yarn dyeing, and fabric-dyeing unit across three different locations in the city. The company also leverages synergies with its group companies for material procurement and processing requirements. In FY22, the company self-financed the installation of an additional 2,000 spindles, surpassing a total of 25K spindles in its spinning facility. In addition, as garments manufacturing is a highly labor-intensive process, management has implemented a barcode system to improve efficiency in the stitching unit. Production levels have noted a declining trend over the review period attributed to global demand slowdown. The same is reflected in lower utilization ratios.

Table: Capacity & Production Data (Units in millions)

	FY21	FY22	9M'FY23
Spinning			
Number of Spindles Installed	23,400	25,368	25,368
Installed Capacity (Kgs)	9.5	9.6	7.2
Actual Production (Kgs)	9.1	8.9	5.1
Capacity Utilization	***96%***	***92%***	***71%***
Knitting			
Installed Capacity (Kgs)	1.1	1.1	0.8
Actual Production (Kgs)	1.0	1.0	0.7
Capacity Utilization	***92%***	***94%***	***86%***

Stitching			
Installed Capacity (Pieces)	6.0	6.0	4.5
Actual Production (Pieces)	5.3	5.9	3.7
Capacity Utilization	***89%***	***98%***	***83%***
Dyeing			
Installed Capacity (Kgs)	1.5	2.0	1.5
Actual Production (Kgs)	1.4	1.9	1.3
Capacity Utilization	***93%***	***93%***	***85%***

The company sells about half of its manufactured yarn in the local market including some exports, while the other half is used internally for knitting purposes. Around 90% of garment production relies on in-house yarn, with the rest sourced locally.

Key Rating Drivers

Business risk profile is constrained by current weak macroeconomic environment both globally and locally, demand slowdown, high interest rate situation, inflationary pressures and recent floods adversely affecting cotton crop while ongoing energy crisis in the country pose a challenge to margins sustainability and future growth.

Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21), however, in FY22 exports finally broke the threshold, coming in at USD 32.4b. 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 around Rs. 4.0tr. Barring seasonal and cyclical fluctuations, textiles sector has maintained an average share of about 60% in national exports.

Table: Pakistan Export Statistics (in USD millions)

	FY20	FY21	FY22		10M'FY22	10M'FY23
Pakistan Total Exports	22,536	25,639	32,450		26,858	23,211
Textile Exports	12,851	14,492	18,525		15,174	14,178
PKR/USD Average Rate	158.0	160.0	177.5		174.4	245.4

Source: SBP

Export revenues from textile sector have noted sizeable growth over the years (FY22: $19.3b FY21: $15.4b; FY20: $12.5b; FY19: $13.6b). Knitwear, Readymade and Bed wear segments continue to contribute higher than other segments, with a cumulative contribution of more than 60% in textile exports. While the growth was primarily driven by volume (excluding knitwear and cotton yarn), higher prices also boosted exports in FY22. However, current fiscal year has been significantly impacted and 10M export proceeds (in value terms) reflect a year-on-year (YoY) decline of ~14%.

Table: Textile Export Details (in USD millions)

	FY20	FY21	FY22		10M'FY22	10M'FY23
High Value-Added Segment	**9,669**	**12,427**	**15,605**		**12,908**	**11,337**
- Knitwear	2,794	3,815	5,121		4,218	3,712
- Readymade Garments	2,552	3,033	3,905		3,214	2,905
- Bed wear	2,151	2,772	3,293		2,727	2,250
- Towels	711	938	1,111		928	825
- Made-up Articles	591	756	849		710	585
- Art, Silk & Synthetic Textile	315	370	460		385	343
- Others	555	743	866		725	718

Low to medium Value-Added Segment	**2,858**	**2,972**	**3,717**		**3,074**	**2,372**
- Cotton Cloth	1,830	1,921	2,438		2,006	1,685
- Cotton Yarn	984	1,017	1,207		1,006	637
- Others	43	34	72		62	51
Total	**12,527**	**15,399**	**19,332**		**15,982**	**13,709**

Source: PBS

Cotton prices rose to a new 12-year high of ~Rs. 21,600/maund as of March'22, as a result of the shortage and higher input costs of fertilizer and energy. Cotton imports were also up 19.8%, in USD terms, for FY22 vis-à-vis preceding year.

Table: Cotton Prices Trend (In Rs.)

	FY19	FY20	FY21	FY22	10M'FY23
Per Maund	8,770	8,860	13,000	17,380	20,235
YoY % Change	26%	1%	32%	34%	*n/a*

Floods in Sindh and Southern Punjab during recent monsoon season have caused significant damage to the cotton crop. According to industry estimates, ~45% of the crop has been washed, worth more than $2.5b, resulting in significant price increases. The government has announced facilitation for raw materials imports to compensate for domestic shortages. Nonetheless, in addition to affecting profit margins, higher raw material pricing is expected to increase the working capital requirements, which is likely to have a negative impact on the liquidity profile of textile operators, particularly spinners, weavers and dying companies.

Global and domestic challenges, such as slowdown in export demand (primarily from North America and the EU, which has begun to materialize in Pakistan's monthly export proceeds) due to recessionary trend, industrial gas load shedding expected in the country, and rising production costs due to inflation, will weigh on the business risk profile going forward. These factors may result in competitive market pricing for exporters.

High cyclicality and competitiveness in the spinning sector add to 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 compared to demand in recent years, cotton prices remained high. However, availability of imported yarn kept yarn prices competitive in the current fiscal year and thus resulting in weakening of profitability profile for spinning players.

Record high sales revenue recorded in FY22; however, recent demand slowdown has impacted volumetric off-take this fiscal year. Client concentration in sales indicate room for improvement.

Net sales achieved strong double-digit annual growth for two consecutive years, reaching a record high of Rs. 9.6b in FY22. The YoY uptick of ~47% was primarily fueled by factors such as rupee depreciation, higher volumes and increased dollar prices for garment exports. Additionally, significant contribution from raw material sales (cotton trading) played a notable role while local yarn sales remained stable in value compared to the previous year. On average, proportionate share of exports to local sales has remained relatively stable at 60:40. In value terms, both export and local sales experienced growth of ~45% and ~50%, respectively during the year.

Most of the revenue, about two-thirds, comes from exporting knitted garments while the rest is derived from yarn sales primarily focused on the local market. Exports mainly target European markets, with a focus on countries like Norway, Denmark, UK, Spain, and Germany as well as US. Client concentration remains high, with top ten clients consistently generating more than four-fifth of revenues. Major clients include Shok Activewear Ltd, Bersheka, Innovative Clothing Ltd., Pull & Bear, Matrix Sourcing, Fifth Avenue and Hummel.

Recent demand slowdown due to the economic downturn in major world economies led to a sizeable dip in volumes and impacted growth in the current fiscal year, with revenues amounting to Rs. 7.7b in 11M'FY23.

Profitability margins have noted significant improvement over the review period.
Profitability margins, both gross and net, have improved significantly during the review period mainly due to consistent rupee devaluation and limited reliance on imported cotton. However, imported cotton utilization has notably risen from 10% to 30% in the past 21 months due to quality issues and supply constraints in the local market. Adequate stock levels are maintained to fulfill confirmed sale orders. Zulfikar Knitting & Processing Mills (Pvt.) Limited, an associate undertaking, handles ~75% of CKPL's processing requirements, with ~10% managed in-house and the rest outsourced.

Administrative and selling overheads nearly doubled in FY22, primarily driven by a significant increase in freight costs, higher salaries, and depreciation expenses. Despite increased debt levels and higher benchmark rates, financing charges have remained limited over the review period. Strong revenue growth and improved gross margins drove a 2.5x increase in the bottom-line, with additional support coming from reversal of allowance for trade debts and rental income.

Debt coverage metrics have noted slight weakening; liquidity profile is adequate with slightly elevated working capital days.
Funds flow from operations (FFO) experienced a significant three-fold increase compared to the previous year, in line with strong growth in net profitability. However, contrasting cash flow trend due to decline in bottom-line this fiscal year led to a slight weakening of debt coverage ratios. Current ratio is reported above 1.3x over the past five fiscal years and coverage of short-term borrowings in relation to trade debts and inventory remains sufficient, indicating a satisfactory liquidity profile.

Despite extended credit payable days, cash conversion cycle has stretched to 119 days in 9M'FY23 from 82 days in FY21, due to timeline increase in inventory holding and debtor days. Local yarn sales have 15 to 30-day credit terms, while export sales require advance payment, usance, and LC on site. Yarn suppliers are typically paid within 30 to 60 days, while cotton procurement is mainly done on an advance basis. Ageing profile of trade debts remains sound, as nearly 90% receivables are settled within 30 days; no bad debt has been reported.

Retained profits supported capitalization; leverage ratios have slightly increased but remain within manageable levels.
Supported by healthy bottom-line growth and all-out profit retention, equity base grew by ~46% in the last 21 months, reaching Rs. 3.4b at end-9M'FY23. The company has not paid dividends on a timeline basis. Debt profile is a mix of short-term and long-term debt, with total interest-bearing liabilities increasing to Rs. 3.4b (FY22: Rs. 2.4b) at end-9M'FY23; ~97% constituted short-term debt and aggregated running finance lines stands at nearly

	Rs.4.1b. Gearing and leverage ratios have slightly increased with rising debt levels, but remain within manageable levels.

Comfort Knitwears (Pvt.) Limited — Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**FY20**	**FY21**	**FY22**	**9M'FY23**
Property & Equipment	1,181.0	1,422.0	1,451.2	1,401.1
Long-Term Investments	259.9	259.9	249.9	266.5
Stock in Trade	1,194.5	1,052.8	1,740.0	2,597.1
Trade Debts	812.7	653.1	1,177.2	1,444.5
Loans, Advances, Deposits & Prepayments	666.6	705.8	851.2	1,154.8
Cash & Bank Balances	86.4	170.6	362.8	369.0
Total Assets	**4,407.9**	**4,643.7**	**6,290.4**	**7,739.1**
Trade and Other Payables	518.9	437.2	831.8	785.4
Short Term Borrowings	1,574.3	1,409.2	2,147.1	3,353.2
Long-Term Borrowings *(Incl. Current Maturity)*	106.4	397.7	216.7	94.7
Total Debt	1,680.6	1,806.9	2,363.8	3,447.9
Total Liabilities	**2,288.4**	**2,336.7**	**3,297.9**	**4,368.5**
Paid Up Capital	100.0	100.0	100.0	100.0
Tier-1/ Total Equity	**2,119.5**	**2,307.0**	**2,992.4**	**3,370.7**
INCOME STATEMENT				
Net Sales	3,865.8	6,541.5	9,609.1	6,754.0
Gross Profit	505.6	799.2	1,609.1	1,050.3
Finance Cost	167.5	193.6	219.3	189.8
Profit Before Tax	**132.9**	**262.8**	**787.6**	**457.6**
Profit After Tax	**89.9**	**188.0**	**685.7**	**378.2**
RATIO ANALYSIS				
Gross Margin (%)	13.1	12.2	16.7	15.6
Net Margins (%)	2.3	2.9	7.1	5.6
Current Ratio (x)	1.33	1.32	1.38	1.37
Net Working Capital	724	670	1,205	1,585
FFO to Total Debt (x)	0.10	0.15	0.35	0.17*
FFO to Long Term Debt (x)	1.58	0.66	3.84	6.20*
Debt Leverage (x)	1.08	1.01	1.10	1.30
Gearing (x)	0.79	0.78	0.79	1.02
Debt Servicing Coverage Ratio (x)	1.75	1.43	3.11	2.71*
ROAA (%)	2.2	4.2	12.5	7.2*
ROAE (%)	4.3	8.5	25.9	15.8*
(Stock in Trade+ Trade Debt)/Short-Term Borrowing (x)	1.28	1.21	1.36	1.21

**Annualized*

REGULATORY DISCLOSURES	**Appendix II**
Name of Rated Entity	Comfort Knitwears (Pvt.) Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
12 July, 2023	A-	A-2	Stable	Reaffirmed
02 June, 2022	A-	A-2	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.
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.

Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Azam Saeed	Senior Manager Finance	June 21, 2023
Mr. Jamal Sikandar	Senior Manager Accounts	