RATING REPORT

Rajby Textiles (Private) Limited

REPORT DATE:
December 26, 2018

RATING ANALYSTS:
Talha Iqbal
talha.iqbal@jcrvis.com.pk

Asfia Aziz
asfia.aziz@jcrvis.com.pk

RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-1	A-	A-1
Rating Date	*Dec 26, 2018*		*Dec 29, 2017*	
Rating Outlook	Stable		Stable	
Outlook Date	*Dec 26, 2018*		*Dec 29, 2017*	

COMPANY INFORMATION

Incorporated in 2014	**External auditors:** M/s Muniff Ziauddin & Co, Chartered Accountants
Private Limited Company	**Chairman:** Mr. Saleem Sultan
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Nafees Sultan
Mr. Saleem Sultan – 50.0% Mr. Nafees Sultan – 50.0%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Industrial Corporates (May, 2016) http://www.jcrvis.com.pk/kc-meth.aspx

Rajby Textiles (Private) Limited

OVERVIEW OF THE INSTITUTION

Rajby Textiles (Private) Limited (RTPL) is a private limited company incorporated on December 29, 2014 to takeover business operations of Rajby Textiles; an Associations of Persons (AOP) set up in February 2005.

Shareholding of RTPL is split between two brothers, namely Mr. Saleem Sultan (Director) and Mr. Nafees Sultan (Chief Executive Officer) who are also the owners of Rajby Industries (RI) under the umbrella of Rajby Group.

RATING RATIONALE

Rajby group (Rajby) has extensive experience in the textile sector (over 4 decades) and has been operating in the denim manufacturing business since 1988. The group operates through two different companies Rajby Industries (RI) (involved in manufacturing of denim garments) and Rajby Textiles (Private) Limited (RTPL) (involved in manufacturing of denim fabric).

Operations

During 2017, the company enhanced its installed capacity of denim fabric to 3m meters/month from 1.7m meters/month. While actual production increased by 60%, utilization levels were lower during FY18 at 89% (FY17: 97%) owing to higher growth in capacity addition. Aggregate power requirement of the plant based on expanded capacity is 6MWs which is being met through a combination of gas and diesel generators. Adequate back-up arrangements are also in place. The company has also focused on obtaining certifications in order to demonstrate its compliance with best practices. Going forward, management plans expansion through setting up a spinning unit in two phases which will allow the operations of the group to become vertically integrated. First phase of the proposed expansion in the spinning segment will cater to around 40% of the total yarn requirement. Moreover, an Effluent Treatment Plant (ETP) is also targeted to be set-up in FY19.

Key Rating Drivers

Business Risks

Business risk profile is supported by stable and growing demand for denim products. However, local and international expansion by major players is expected to keep pricing power and hence margins slightly under pressure. The company's operations are currently concentrated with exposure to the denim industry which might significantly impact business risk profile in case of change in demand patterns or any other industry specific factors. Therefore, keeping pace with rapid changes in fashion trends is considered important. JCRVIS expects demand for denim products to remain stable over the medium term. Given the favorable policies & incentives of the government on enhancing exports and imposition of duties on Chinese exports to USA, there is significant opportunity for Denim players to enhance exports. In this regard, RTPL is well positioned to tap this opportunity given the recent expansion in the denim fabric segment and improved competitiveness post addition of the planned spinning unit.

Sales

Net sales of the company have grown at a CAGR of 19% over the last four years with revenues comprising a mix of local and exports sales. Sales revenue reported a jump of 67% during FY18 largely on account of higher quantum of fabric sold while average selling prices also increased. Given increased marketing efforts and focus towards enhancing exports, proportion of exports sales in total sales rose to 37% (FY17: 25%) during FY18. Exports sales are largely concentrated in Turkey and Bangladesh with management focusing on increasing sales to value added customers. Around three-fifth of the domestic sales revenue was generated from RI (associated company) with the remaining emanating from other denim apparel manufacturers in the country. With higher capacity utilization in the ongoing year and increase in selling prices given rupee depreciation, management projects sales revenue for FY19 to post double digit growth. Proportion of export sales in overall sales is expected to increase further in the ongoing year.

Profitability

Gross Margins (GMs) trended downwards and were reported at 11% (FY17: 14%) primarily on account of higher depreciation and to some extent due to rise in input cost. Adjusting for the impact of incremental depreciation, GMs were higher in FY18 vis-à-vis FY17. Margins were supported by export rebate and drawback of local taxes and levies. The company has also undertaken full provisioning against GIDC with total impact on balance sheet aggregating to Rs. 296m (FY17: Rs. 225.8m). Going forward, GMs are expected to sustain despite significant rise in input cost (yarn, chemical and gas) due to impact of rupee depreciation and higher sales volume. Moreover, impact of higher finance cost will be offset by sizeable exchange gain due to rupee depreciation. Tax credit available will be fully utilized in the ongoing fiscal year. Over the medium term, management projects profitability to improve due to margin improvement upon realization of benefit from backward integrated operations.

Liquidity
Liquidity profile of the company improved during FY18 with sufficient cash flows in relation to outstanding obligations with FFO to LTD reported at 52% (FY17: 38%) and strong debt servicing ability with debt service coverage ratio recorded at 3.3x (FY17: 2.7x) during FY18. With current assets being greater than current liabilities, current ratio of RTPL was reported above 1x at end-FY18. The company has an extended working capital cycle with time to taken to convert inventory into cash being higher than payment for trade creditors. Working capital cycle of the company has increased during the outgoing year necessitating higher utilization of short term borrowing. Sizeable receivables from related party are a constraint on the company's liquidity profile. Improvement in working capital cycle from RI and timely receipt of receivables from GoP will augment liquidity profile.

Capitalization
Capitalization levels have strengthened over time through equity injection and profit retention. Equity base of the company has increased at a 4-yr CAGR of 25%. Given increase in short term borrowings to fund higher trade debts, gearing and leverage indicators slightly trended upwards to 1.47x (FY17: 1.42x) and 1.93x (FY17: 1.85x) at end-FY18 and continue to remain on the higher side. Given proposed expansion plan of setting up the spinning division, leverage indicators are expected to remain elevated over the medium term. Maintaining leverage indicators within benchmarks for the assigned ratings is considered important.

Corporate Governance
Ratings of RTPL are constrained by the current corporate infrastructure where authority is concentrated with two family members. The same can be strengthened through improvement in board composition and oversight. Senior management team is supported by stable and professional management team. External auditors of the company lie in Category 'A' on the SBP Panel of Auditors.

ISSUE/ISSUER RATING SCALE & DEFINITION — Appendix I

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 II

Name of Rated Entity	Rajby Textiles (Private) Limited
Sector	Textiles
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				
December 26, 2018	A-	A-1	Stable	Reaffirmed
December 29, 2017	A-	A-1	Stable	Reaffirmed
October 27, 2016	A-	A-1	Stable	Initial

Instrument Structure	N/A
Statement by the Rating Team	JCR-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.
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