RATING REPORT

Artistic Milliners (Private) Limited

REPORT DATE:
December 28, 2021

RATING ANALYSTS:

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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	*Dec 28, 2021*		*Dec 02, 2020*	
Rating Outlook	Stable		Stable	
Outlook Date	*Dec 28, 2021*		*Dec 02, 2020*	

COMPANY INFORMATION

Incorporated in 1980	**External auditors:** EY Ford Rhodes Chartered Accountants
Private Limited Company	**Chairman of the Board and Chief Executive Officer:** Mr. Yaqoob Ahmed **Managing Director (Spinning & Fabric):** Mr. Omar Ahmed **Managing Director (Garments):** Mr. Murtaza Ahmed

APPLICABLE METHODOLOGY(IES)

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

Artistic Milliners (Private) Limited

OVERVIEW OF THE INSTITUTION

Artistic Milliners (Private) Limited (AML) was incorporated as a Private Limited Company in 2006.

AML is a family owned business with major shareholding resting held by Mr. Yaqoob Ahmed who is the Chairman of the Board. He possesses over 41 years of experience in the industry and has been responsible for the backward integration starting from Garments to Denim Weaving and Spinning. The Company has been actively involved in CSR initiatives.

The Company has also established a Research and Innovation Centre in Dubai, to offer proximity to their customers and partners; the center comprises three departments: Showroom, Stitching and Laundry. The company has also opened a display showroom in USA in the ongoing year to ease access of US based orders.

RATING RATIONALE

Artistic Milliners (Private) Limited ('AML' or 'the Company') is one of the leading denim fabric and garment manufacturers and exporters with vertically integrated operations in Pakistan. The Company deals in manufacturing of yarn, denim fabric and garments and operates through 17 facilities/units located at Korangi and Landhi in Karachi, Pakistan. Sponsors have over five decades of experience in the textile sector with extensive experience in denim fabric and garment segment. Over the years, the management has placed significant focus on sustainability initiatives. AML owns Pakistan's first LEED (Leadership in Energy and Environmental Design) Certified Garment Factory, which consumes 31% less energy, 50% less water and diverts 95% of waste away from landfills compared to conventional building. AML's fabric units are ISO 9000 certified matching international quality standards.

Table 1: Capacity & Production

	FY20	FY21
Spinning		
Installed capacity of yarn (Kgs.)	41,277,329	44,299,443
Actual production of yarn (Kgs.)	29,736,710	42,460,677
Utilization	**72%**	**96%**
Weaving		
Installed capacity of fabric - meters	85,341,500	85,341,500
Actual production of fabric - meters	66,374,385	82,459,590
Utilization	**78%**	**97%**
Garments		
Installed capacity of garments- pieces	28,348,475	28,792,800
Actual production of garments- pieces	22,940,912	28,568,251
Utilization	**81%**	**99%**

Sector Update

Table 2: 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 Exports (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
HIGH VALUE-ADDED SEGMENT	**9,854**	**10,046**	**9,669**	**12,428**	**72.9%**	**75.4%**
- KNITWEAR	2,711	2,900	2,794	3,816	20.1%	21.8%
- READYMADE GARMENTS	2,577	2,653	2,552	3,033	19.1%	19.9%
- BED WEAR	2,261	2,262	2,151	2,772	16.7%	17.0%
- TOWELS	797	786	711	938	5.9%	5.9%
- MADE-UP ARTICLES (EXCL. TOWELS & BED WEAR)	685	680	591	756	5.1%	5.1%
- ART, SILK & SYNTHETIC TEXTILE	310	297	315	370	2.3%	2.2%
- OTHERS	513	468	555	743	3.8%	3.5%
LOW TO MEDIUM VALUE-ADDED SEGMENT	**3,667**	**3,282**	**2,858**	**2,972**	**27.1%**	**24.6%**
- COTTON CLOTH	2,204	2,102	1,830	1,921	16.3%	15.8%
- COTTON YARN	1,372	1,125	984	1,017	10.1%	8.4%
- OTHERS	92	54	43	34	0.7%	0.4%
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'22 (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 mound.

- 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

Denim Segment

- Demand for denim and denim garments suffered a setback during the pandemic-induced lockdowns, as consumer patterns shifted towards comfort wear, suited more for in-door living, instead of denim wear, which is considered more of an attire for outdoors. In FY21, we have noted some recovery in demand for denim products as key markets, EU & North America, have posted improvement in retail spending.

- In tandem with the contraction in demin demand, most South Asian denim manufactures recorded revenue and margin contraction. With gradual demand recovery in key markets, offtake and margins of denim manufacturers have started to normalize towards its long term trend.

Business Update AML

Table 3: P&L (Extract)

	FY19	FY20	FY21	1QFY21
Net Sales (PKR million)	38,055	43,542	56,297	17,349
Gross Margin (%)	23.7%	26.1%	28.6%	25.2%
EBIT margin (PKR million)	24.3%	22.0%	26.1%	19.8%
Net Margin (%)	21.8%	19.2%	23.1%	17.6%

- Despite pandemic-induced slowdown, which affected several denim-based exporters, AML has continued posting growth in topline and gross margin, as illustrated in the table above.
- In FY21, the Company posted topline growth of 29% exceeding preceding year growth of 14%. During the past 5-year period (FY17-FY21), the Company's topline has grown at a CAGR of 16%.
- Growth in FY21 is mainly a product of quantitative growth in offtake, wherein fabric & garment sales were up 28% and 25% (YoY) respectively, with only about a tenth of the growth being contributed by pricing increase.
- The Company's export base features concentration with more than 60% of the fabric and garment sales being to Bangladesh and USA respectively. Client concentration is also there with top 5 clients comprising contributing 55% of the Company's topline. We have not noted a material shift in concentration since our last review. Comfort is derived from long standing association with of AML with its major clientele.
- As per management, the gross margin for FY21 depicted improvement mainly as a result of inventory gains, as lower cost raw material purchased earlier and finished goods inventory left over at end-FY20, was sold in FY21. Accordingly, given the uptick in raw cotton prices, some pressure on gross margin may be seen going forward, as also observed so far in Q1'FY22.
- We have noted an uptick in inventory levels, which used to constitute 19% of asset base as of Jun'20, had grown to 23% as of Jun'21. As of Sep'21, the inventory holdings were even higher, albeit this is in line with industry phenomenon, wherein raw material holdings are usually elevated as of September.
- Given the aforementioned uptick in inventory holdings, the cash conversion cycle has increased on a timeline, as illustrated in the table below.

Table 4: Cash Conversion Cycle (in Days)

	FY19	FY20	FY21
Cash Conversion Cycle	**108**	**128**	**143**
- **Days Inventory Outstanding**	105	133	154
- **Days Sales Outstanding**	67	47	30
- **Days Payable Outstanding**	63	52	40

- Nevertheless, debt utilization remains conservative and given the growth in bottom line, the cash flow coverage indicators remain comfortable as illustrated in the table below.

Table 5: Cash flow Analysis

	FY19	FY20	FY21	1QFY21
FFO (Mn.) (PKR million)	10,112	10,388	15,304	14,364 *
FFO to Total Debt (%)	55.7%	42.0%	49.1%	44.5%
FFO to Long Term Debt (%)	107.1%	126.0%	123.7%	115.3%
Debt Servicing Coverage Ratio (x)	6.96	5.04	8.52	6.75
Current Ratio	1.73	1.73	1.92	1.83
(Stock in trade+ trade debts)/STD	1.98	1.06	1.36	1.89
***Annualized**				

Table 6: Balance Sheet (Extract)

	FY19	FY20	FY21	1QFY21
Total Assets (PKR million)	55,016	70,171	88,776	95,876
Total Liabilities (PKR million)	25,690	33,622	41,487	44,673
Total Equity (PKR million)	29,326	36,549	47,289	51,203
Long Term Debt (PKR million)	9,440	8,241	12,367	12,454
Short Term Debt (PKR million)	8,700	16,514	18,790	19,790
Total Debt (PKR million)	18,140	24,755	31,157	32,244
Leverage (x)	0.88	0.92	0.88	0.87
Gearing (x)	0.62	0.68	0.66	0.63

- Equity base of the Company has grown at a CAGR of 25% over the last 5 years (FY17-21) on account of healthy internal capital generation and adequate retention.
- The Company's debt is almost entirely composed of financings under concessionary debt financing schemes of SBP for exporters.
- The management remains focused on diversifying the operations. In this regard, a new unit has been set up for non-denim processing, which is expected to come online within FY22.
- As the new unit comes online by mid-FY22, it will contribute to the topline. Inclusive of growth from the same and expected uptick in pricing, the management expects to grow the topline in the range of Rs. 70-75b for FY22.

Key Rating Drivers

Rating incorporate AML's market positioning as a leading exporter

AML is one of the leading denim fabric and garment manufacturers and exporters with vertically integrated operations. As of FY21, AML was the third largest exporter of Pakistan. The ratings take into account business risk of denim sector and regional & counterparty concentration inherent in AML's revenue base. Although primarily a denim company, the management has recently made foray towards diversifying to non-denim fabric, which should translate in improvement in business risk profile of AML.

Ratings take into account consistent uptick in capacities, topline, stability of margins and comfortable cash flow coverage indicators

During the past 5-year period (FY17-FY21), the Company's topline has grown at a CAGR of 16%. At the same time, the margins have depicted stability and improvement over a timeline. Cash flow coverage indicators have remained strong and aligned with peer median. Given capacity growth and increase in commodity prices, the management projects revenue strong growth for FY22, which has been incorporated into our analysis. Cash conversion cycle has tipped up on a timeline, albeit this is in line with industry trend and is mainly attributable to sharp price increases in raw cotton prices.

Rating incorporates conservative capital structure of AML

The Company's debt utilization remains conservative, as reflected by the gearing & leverage levels. The Company's debt is almost entirely composed of financing under SBP's concessionary debt financing scheme. Furthermore, the Company has sizable liquidity available on the balance sheet, which has largely been placed in money market mutual funds. In addition to enhancing the liquidity buffers of AML, these placements also diversify AML's revenue base. Inclusive of dividend from subsidiary, income from financial assets has contributed 4.3% of the gross revenue for FY21. In addition, including the liquid assets in gearing calculations, net debt of the Company reduced to Rs. 15.9b translating in gearing of 0.3x, which is considered to be on the lower side.

Artistic Milliners (Private) Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	FY16	FY17	FY18	FY19	FY20	FY21	1QFY21
Paid Up Capital	1,000	1,000	1,000	1,000	1,000	1,000	1,000
Total Equity	15,729	17,622	21,291	29,326	36,549	47,289	51,203
INCOME STATEMENT							
Net Sales	26,539	26,514	30,036	38,055	43,542	56,297	17,349
Profit Before Tax	4,050	3,296	4,017	8,765	9,028	13,777	3,229
Profit After Tax	3,845	3,058	3,882	8,293	8,369	13.029	3,054
RATIO ANALYSIS							
FFO	4,845	4,227	4,911	10,112	10,388	15,304	3,591
Current Ratio (x)	1.33	1.60	1.50	1.73	1.73	1.92	1.83
Gearing (x)	0.35	0.41	0.62	0.62	0.68	0.66	0.63

ISSUE/ISSUER RATING SCALE & DEFINITION — 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	Artistic Milliners (Private) Limited
Sector	Textile Industry
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 28,2021	AA-	A-1	Stable	Reaffirmed
December 02, 2020	AA-	A-1	Stable	Reaffirmed
November 01., 2019	AA-	A-1	Stable	Reaffirmed
November 14, 2018	AA-	A-1	Stable	Reaffirmed
December 28, 2017	AA-	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 Meetings Conducted	

Name	Designation	Date
Mr. Mohammed Munir	CFO	3-Dec-2021