

RATING REPORT

Arshad Corporation (Pvt.) Limited

REPORT DATE:

April 23, 2020

RATING ANALYSTS:Syed Fahim Haider Shah
fahim.haider@vis.com.pkMaimoon Rasheed
maimoon@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Long-term	Long-term	Long-term
Entity	BBB+	A-2	BBB+	A-2
Rating Outlook	<i>Rating Watch – Negative</i>		<i>Stable</i>	
Rating Action	Maintained		Initial	
Rating Date	23 rd Apr'20		3 rd Apr'19	

COMPANY INFORMATION

Incorporated in 1973	External auditors: Zahid Jamil & Co. Chartered Accountants.
Private Limited Company	Chairman/CEO: Mr. Muhammad Arshad Sheikh
Key Shareholders (with stake 5% or more):	
Mr. Muhammad Arshad Sheikh – 27.50%	
Mr. Shahzad Ahmed Sheikh – 26.0%	
Mr. Nisar Ahmed Sheikh – 24.0%	
Mr. Sharhyar Arshad – 5.0%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (May 2016)

<https://www.vis.com.pk/kc-meth.aspx>

Arshad Corporation (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Arshad Corporation (Pvt.) Limited was incorporated in 1973 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017).

The company is principally engaged in manufacturing of sale of fabric and made-ups.

Profile of the Chairman/CEO

Mr. Arshad Sheikh is the Chairman of the Board and Chief Executive Officer (CEO). Mr. Arshad is a graduate and has over 50 years of textile industry experience.

Financial Snapshot

Tier-1 Equity: 1HFY20: Rs. 3.4b; FY19: Rs. 3.0b; FY18: Rs. 2.6b.

Assets: 1HFY20: Rs. 11.3b; FY19: Rs. 11.2b; FY18: Rs. 9.7b.

Profit After Tax: 1HFY20: Rs. 395m; FY19: Rs. 427m; FY18: Rs. 227m.

RATING RATIONALE

Arshad Corporation (Pvt.) Limited (ACL) is an export-oriented composite textile unit and primarily operates four business segments, including grey fabric, fabric processing, processed fabric and made-ups. Shareholding of the company is held by sponsoring family, who have been in the industry since 1954. Haji Muhammad Ishaq and his four sons laid the foundation of Arshad Group in 1954 with the establishment of a yarn trading company. Arshad Group ventured into textile exports business in 1968 and subsequently established its first textile mill in 1973. Three companies are currently operating under the umbrella of Arshad Group, including ACL, Arshad Textile Mills Limited (ATML), and Arshad Energy Limited (AEL). ATML is a blended cotton yarn spinning mills while AEL is a public listed company and the principal activity is to generate power through furnace-fired power station having gross capacity of 12 MW. The family members of Arshad Group also own around 5% stake in MCB Bank Limited (MCB) as well as 250 acres of land in Faisalabad.

ACL is an export-oriented composite textile unit involved in manufacturing and sale of fabric and made-ups, with the U.S. and Europe being the primary target markets. Share of exports in overall sales mix has averaged at 85% over the past four years. The product portfolio of ACL is composed of grey fabric, and a wide range of made-ups including home textile and work-wear garments. ACL also provides fabric processing services to other textile units. No capacity enhancements were made during FY19. Grey fabric facility comprises 275 Sulzer and Picanol looms which were imported from Switzerland and Belgium and can weave up to 18.1m meters fabric per annum. Fabric processing facility is equipped with continuous thermasol dyeing and bleaching machines, having cumulative processing capacity of up to 31.5m meters per annum. Garments manufacturing unit has capacity to produce 0.42m pairs of uniform per annum and made-ups stitching unit has capacity of 20.7m meters per annum.

Net sales of the company increased to Rs. 10.4b during FY19 (FY18: Rs. 8.2b) on account of volumetric gains both in the local and export markets as well as favorable pricing due to rupee depreciation. Exports sales increased to 8.7b (FY18: Rs. 7.2b) due to higher made-ups and garments volumes, while sales also increased to Rs. 2b (FY18: Rs. 1.3b) representing slightly higher 19.2% (FY18: 15.9%) of total sales. Gross profit amounted to Rs. 1.5b (FY18: Rs. 1.1b) with slightly improved margin of 14.6% (FY18: 13.0%) and net profit increased to Rs. 427m (FY18: Rs. 227m) with margin of 4.1% (FY18: 2.8%). Net sales and profit were recorded at Rs. 5.9b and Rs. 395m during 1HFY20. Debt profile of the company comprises a mix of short-term and long-term borrowings. In line with the accumulation of tier-1 equity due to retention of profits and slightly lower borrowings, gearing and debt leverage ratios stood at 1.71x (FY19: 2.0x) and 2.34x (FY19: 2.8x) respectively, at end-1HFY20.

With the advent of global Coronavirus disease (COVID-19) pandemic, the demand outlook for textile products in general and especially value-added, export-oriented units looks weak. Given ACL is highly dependent on exports sales for cash flows generation and servicing of its financial obligations, status of the assigned rating is therefore uncertain as an event of deviation from expected trend has occurred; additional information will be necessary to take any further rating action, warranting a 'Rating-Watch' status. With the demand compression emerging from ongoing global economic crisis and continued lockdown situation coupled relatively high financial risk profile vis-à-vis peer companies, ratings are being placed on 'Negative' outlook. The ratings are dependent upon maintenance of overall sales, market share in exports, profit margin, debt service coverage, and gearing ratios at an adequate level, with outlook subject to be reviewed once the situation stabilizes.

Arshad Corporation (Pvt.) Limited
Annexure I

FINANCIAL SUMMARY <i>(amounts in PKR millions)</i>				
BALANCE SHEET				
Non-Current Assets	FY17	FY18	FY19	1HFY20
Stores, Spares. And Loose Tools	2,619	2,576	2,590	2,346
Stock-in-Trade	334	369	407	422
Trade Debts	3,301	3,679	4,154	4,262
Other Receivables	1,185	1,981	3,034	3,025
Tax Refund Due From Government	253	389	272	316
Other Current Assets	390	391	454	597
Total Assets	211	289	304	299
Trade and Other Payables	8,293	9,674	11,215	11,267
Other Liabilities	1,392	1,387	2,070	2,069
Short-Term Borrowings	42	75	110	48
Long-Term Borrowings <i>(Inc. current matur)</i>	4,237	5,043	5,580	5,299
Total Liabilities	299	609	475	475
Tier-1/Total Equity	5,970	7,114	8,235	7,891
Paid-Up Capital	2,323	2,561	2,980	3,376
	500	500	500	500
INCOME STATEMENT				
Net Sales	FY17	FY18	FY19	1HFY20
Gross Profit	7,373	8,174	10,385	5,827
Operating Profit	942	1,062	1,517	876
Profit Before Tax	486	577	876	506
Profit After Tax	203	303	526	470
FFO	135	227	427	395
	210	364	593	195
RATIO ANALYSIS				
Gross Margin (%)	FY17	FY18	FY19	1HFY20
Net Working Capital	12.8	13.0	14.6	15.0
FFO to Total Debt (x)	(120)	437	749	1,300
Debt Servicing Coverage Ratio (x)	0.05	0.07	0.10	0.07*
Gearing (x)	1.21	1.34	1.76	1.62
Debt Leverage (x)	1.95	2.21	2.03	1.71
Current Ratio	2.57	2.78	2.76	2.34
Inventory + Receivable/Short-term Borrowings (x)	0.98	1.07	1.10	1.17
	1.06	1.12	1.29	1.38

*Annualized

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Annexure 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		Annexure III			
Name of Rated Entity	Arshad Corporation (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
	RATING TYPE: ENTITY				
	23-04-2020	BBB+	A-2	Rating Watch – Negative	Maintained
	03/04/2019	BBB+	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. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. 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 2020 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.				
Due Diligence Meetings Conducted	Name	Designation	Date		
	Mr. Zain ul Abideen	Manager Finance	17 th Apr'20		