

RATING REPORT

Arshad Corporation (Pvt.) Limited

REPORT DATE:

March 06, 2024

RATING ANALYSTS:

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RATING DETAILS				
Rating Category	Latest Ratings		Previous Ratings	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Date	March 06, 2024		December 29, 2022	
Rating Action	Reaffirmed		Reaffirmed	
Rating Outlook	Stable		Stable	

COMPANY INFORMATION

Incorporated in 1973	External auditors: Zahid Jamil & Co. Chartered Accountants.
Private Limited Company	Chairman/CEO: Mr. Shahzad Ahmed Sheikh
Key Shareholders (with stake 10% or more):	
Mr. Shahzad Ahmed Sheikh – 66.8%	
Mr. Muhammad Arshad – 20.0%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates.

<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>

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 Limited was incorporated in 1973 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017).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 and sale of fabric and made up.

RATING RATIONALE
Company Profile

Arshad Corporation (Private) Limited ('ACL' or 'the Company') is incorporated in Punjab, Pakistan as a private limited company since January 12, 1973. The registered office of the Company is situated on the 16th floor, Tricon Corporate Centre Main Jail Road, Gulberg 2, Lahore. The Company is principally engaged in the business of manufacturing and selling fabric and made-up.

Operational Performance

The Company's manufacturing facilities are in Shahkot and two additional sites in Khurrianwala. In FY23, ACL faced a notable decline in plant capacity utilization, mainly due to challenges in raw material acquisition, a global demand slowdown, and operational interruptions from gas and electricity disruptions by SNGPL and FESCO. During the fiscal year, the weaving machines' capacity increased to 75,000 meters per day, up from 51,689 meters per day in FY22. Approximately 70% of the Rs. 1.4b expansion was funded via long-term financing, with the remaining portion being sourced internally.

Capacity and Production	FY20A	FY21A	FY22A	FY23A
Processing Machine - Meters				
Installed Capacity per day	90,000	90,000	90,000	90,000
Actual Production per day	77,000	82,066	79,259	50,704
Capacity Utilization	86%	91%	88%	56%
Stitching Unit I - Meters				
Installed Capacity per day	65,000	70,000	70,000	70,000
Actual Production per day	43,240	53,038	63,580	40,870
Capacity Utilization	67%	76%	91%	58%
Printing Machines - Meters				
Installed Capacity per day	115,000	115,000	125,000	125,000
Actual Production per day	101,065	98,670	112,091	82,900
Capacity Utilization	88%	86%	90%	66%
Weaving Machines - Meters				
Installed Capacity per day	51,600	51,600	51,600	75,000
Actual Production per day	41,354	42,630	50,958	70,000
Capacity Utilization	80%	83%	99%	93%
Stitching Unit II - Kgs				
Installed Capacity per day	1,000	1,000	1,000	1,000
Actual Production per day	600	912	620	350
Capacity Utilization	60%	91%	62%	35%
Garment Machines - Pieces				
Installed Capacity per day	2,700	5,572	5,572	5,668

Actual Production per day	1,641	4,179	3,588	3,511
Capacity Utilization	61%	75%	64%	62%

Key Rating Drivers

Business risk profile characterized by challenging local and global economic and geopolitical conditions, and intense competition on a global level as an export-oriented industry.

Assigned ratings incorporate the medium to high business risk profile of the textile sector in Pakistan, marked by high exposure to economic cyclicality and intense competition. The sector's performance is influenced by broader economic conditions, rendering it susceptible to demand fluctuations driven by economic factors. Furthermore, as a substantial contributor to total exports, the textile industry faces exposure to global economic cyclicality, geopolitical challenges, and liquidity constraints due to government delays in sales tax refunds.

Moreover, the industry is also sensitive to supply-side risks, including local cotton crop production which impacts margins, and reliance on imported raw materials, exposing the sector to significant exchange rate risk and government import restrictions.

Despite these challenges, textile companies have demonstrated resilience by maintaining operational efficiency, consistent product quality, strategic raw material procurement, and better supply chain control, achieving economies of scale and managing risks associated with the volatile business environment.

Export-oriented nature supports the top line and margins, despite deterioration in volumetric sales.

In FY23, the Company sustained a stable top line, experiencing only a marginal decrease ~3%. Despite volume pressures, sales were supported by a slight increase in export sales. This growth in export revenue was fueled by higher export prices denominated in rupees, a consequence of the significant depreciation of the PKR during FY23. Moreover, during the period the Company managed to improve its gross margins to 23.7% (FY22: 17.0%) despite operational challenges. With ~92% of the Company's gross sales being exports, and around 10% of its total raw material costs being imported, ACL experienced a net benefit of currency depreciation on its gross margins in FY23. In 1HFY24, gross margins have remained mostly intact at 22.7%, depicting a marginal decline of 1%, amid a relatively stable period for the local currency.

Improvement in the capitalization profile on account of equity expansion from higher profit generation, albeit elevated.

Historically, leverage indicators have been on the higher side, due to elevated debt levels and the nature of the business. Nevertheless, equity expansion in FY23, primarily driven by profit retention, has led to improvements in capitalization indicators during the year. In FY23, gearing and leverage improved to 1.7x (FY22: 2.1x) and 2.5x (FY22: 2.9x), respectively. This enhancement sustained in 1HFY24 with gearing and leverage ratios reported at 1.6x and 2.3x, respectively. Nevertheless, the capitalization is still considered elevated for assigned ratings and need continued sponsor support to provide comfort.

Debt service coverage adequate albeit deterioration on account of higher financial burden.

The Company has consistently maintained an adequate coverage profile, as evidenced by a debt service coverage ratio (DSCR) of 1.5x (FY22: 1.5x) and a short-term debt coverage ratio of 1.6x (FY22: 1.4x). However, in 1HFY24, the DSCR deteriorated to 1.2x, on account of escalating pressure from the finance costs during the period on the Funds from Operations (FFO).

Stable liquidity profile, supported by sufficient internal cash generation in FY23.

The Company has maintained a historically stable liquidity profile, with a 5-year average current ratio of 1.1x. In FY23, ACL current ratio inched higher to 1.2x, attributed to increased current assets. Adequate internal cash generation in FY23 facilitated the financing of a substantial portion of the working capital requirement, preventing a proportional rise in current liabilities. The current ratio remained at 1.2x in 1HFY24.

Consideration for future reviews

While adequate, deterioration of the coverage profile in 1HFY24 has resulted in pressure on ratings, compounded by elevated capitalization profile. Going forward, ratings will remain sensitive to the Company's ability to improve its coverage profile and capitalization profile to be commensurate with assigned ratings. Moreover, further enhancement of the liquidity profile and maintenance of profitability metrics will also remain important considerations for future reviews.

Arshad Corporation (Pvt.) Limited
Annexure I

FINANCIAL SUMMARY				
<i>(PKR Millions)</i>				
Balance Sheet	FY21A	FY22A	FY23A	6MFY24A
Property, plant and equipment	2,865.6	4,372.6	4,368.2	4,328.6
Stock-in-trade	6,603.6	7,587.6	8,547.4	8,760.8
Trade debts	3,688.3	5,464.9	6,326.5	6,467.2
Cash & Bank Balances	110.6	133.7	56.4	64.5
Total Assets	15,886.9	20,507.9	22,080.8	22,304.6
Trade and Other Payables	3,408.6	4,229.1	4,530.1	4,686.0
Long-term Debt	780.8	1,620.5	1,308.6	1,170.2
Short-Term Borrowings	7,489.4	9,180.9	9,481.4	9,397.8
Total Debt	8,270.2	10,801.4	10,790.0	10,567.9
Total Liabilities	11,816.1	15,227.4	15,730.9	15,633.0
Paid up Capital	500.0	500.0	500.0	500.0
Equity (excl. Revaluation Surplus)	4,070.7	5,280.6	6,349.8	6,671.6
Income Statement				
Net Sales	13,199.5	18,260.8	17,750.3	9,429.3
Gross Profit	2,084.9	3,106.7	4,207.3	2,138.9
Operating Profit	1,258.6	1,844.7	2,985.2	1,517.0
Finance Costs	541.1	826.3	1,672.2	1,066.9
Profit Before Tax	669.8	956.5	1,205.7	419.2
Profit After Tax	531.4	722.1	1,024.9	321.7
Ratio Analysis				
Gross Margin (%)	15.8%	17.0%	23.7%	22.7%
Net Margin (%)	4.0%	4.0%	5.8%	3.4%
Funds from Operation (FFO)	694.6	1,036.1	1,495.2	356.3
FFO to Total Debt* (%)	8.4%	9.6%	13.9%	6.7%
FFO to Long Term Debt* (%)	89.0%	63.9%	114.3%	60.9%
Gearing (x)	2.0	2.0	1.7	1.6
Leverage (x)	2.9	2.9	2.5	2.3
Debt Servicing Coverage Ratio* (x)	1.3	1.5	1.5	1.2
Current Ratio	1.1	1.1	1.2	1.2
(Stock in trade + trade debts) / STD (x)	1.4	1.4	1.6	1.6
Return on Average Assets* (%)	3.7%	4.0%	4.8%	2.9%
Return on Average Equity* (%)	14.0%	15.4%	17.6%	9.9%

*Annualized, if required

REGULATORY DISCLOSURES		Annexure II			
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				
	Mar - 06 - 2024	A-	A-2	Stable	Reaffirmed
	Dec-29-2022	A-	A-2	Stable	Reaffirmed
	Sep-27-2021	A-	A-2	Stable	Upgrade
	Apr-23-2020	BBB+	A-2	Rating Watch- Negative	Maintained
	Apr-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.				
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Due Diligence Meetings Conducted	Name	Designation	Date		
	Irfan Shahzad Rafiq	CFO	February 28, 2024		
	Zain Ul Abideen	Manager - Finance			