RATING REPORT

Riaz Textile Mills (Pvt.) Limited (RTML)

REPORT DATE:
January 02, 2019

RATING ANALYSTS:
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RATING DETAILS		
	Initial Rating	
Rating Category	Long-term	Short-term
Entity	A	A-1
Rating Outlook	*Stable*	
Rating Action	Initial	
Rating Date	*December 31 '18*	

COMPANY INFORMATION	
Incorporated in 2001	External auditors: Sarwar Awan & Co. Chartered Accountants
Private Limited Company	Chairman of the Board/CEO: Mr. Sheikh Riaz Ahmad
Key Shareholders (with stake 5% or more):	
Sheikh Riaz Ahmad – 25.75%	
Nadeem Riaz – 25.00%	
Aamer Najeeb – 25.00%	
Hamza Nadeem – 12.125%	
Umer Najeeb – 12.125%	

APPLICABLE METHODOLOGY(IES)
JCR-VIS Entity Rating Criteria: Industrial Corporates (May 2016) *http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf*

Riaz Textile Mills (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Riaz Textile Mills (Pvt.) Limited was incorporated in 2001 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The company is primarily involved in manufacturing and sale of cotton yarn.

Profile of the Chairman/CEO

Mr. Sheikh Riaz Ahmed is the founder of Riaz Textile Mills (Pvt.) Ltd. He serves as the Chairman of the Board and Chief Executive Officer.

Financial Snapshot

Total Equity: end-FY18: Rs. 8.2b; end-FY17: Rs. 7.6b; end-FY16: Rs. 6.7b.

Assets: end-FY18: Rs. 12.3b; end-FY17: Rs. 9.4b; end-FY16: Rs 7.1b.

Profit After Tax: FY18: Rs. 571m; FY17: Rs. 886m; FY16: Rs. 109m.

RATING RATIONALE

Rating Rationale

Riaz Textile Mills (Pvt.) Limited (RTML) is amongst the large spinning units operating in Pakistan. Shareholding of the company is vested with the sponsoring family who is actively involved in the day to day affairs of the company. Recent enhancement of production capacity owing to the completion of third spinning unit is expected to boost RTML's competiveness and sales, which, in turn, is expected to positively impact the overall profitability and cash flow generation. Being primarily an export oriented company, recent rupee devaluation also bodes well for the profitability. The ratings also take into account low leveraged capital structure and sound liquidity profile. As a policy, the company prefers to finance working requirements from internally generated cash. Ratings are constrained by vulnerability of the spinning sector to raw material prices, adverse changes in the regulatory duties structure, and high geographic concentration. Corporate governance framework has room for improvement.

Business Strategy

RTML manufactures mainly a coarse count yarn from imported and locally procured cotton. As a policy, the company procures around 70% of cotton from international markets. Moreover, around 80% of the produced yarn is exported, with China being the primary target market. For local sales, RTML has well-established relationships with major weaving mills in Pakistan. The company's newly established spinning unit – III commenced commercial production in January 2018 with 32,448 spindles. As a result, cumulative number of spindles increased to 93,228 (FY17: 60,780). Recent investment in spinning unit – III has augmented the production capacity of yarn to 29.97m kgs per annum (FY17: 19.54m kgs per annum). Overall capacity utilization decreased to 57% during FY18 (FY17: 74%) with the addition of new spindles; the capacity utilization is expected to enhance in FY19 with spinning unit – III to be operational for full year.

Performance

During FY18, the company reported net sales of Rs. 11.3 (FY17: Rs. 7.7b; FY16: Rs. 7.1b), driven largely by notable increase in volumetric sales and favorable average selling prices of yarn in the local and international markets. RTML generally fetches relatively higher selling price due to a blend of imported and local cotton and strict quality control protocols. However, gross profits of the company decreased to Rs. 1.0b (FY17: Rs. 1.3b) due to a higher average procurement price of raw cotton. As per the management, RTML has recorded net sales of Rs. 6.6b during 5MFY19. Revenue generation is expected to grow to approximately Rs. 18b during FY19 on account of higher production output from unit-III and recent devaluation of rupee. The company follows a practice of procuring local cotton between July and December and imported cotton between January and June, while maintaining a buffer stock of six months. At end-FY18, RTML held raw material inventory of worth Rs. 4.4b (FY17: Rs. 1.5b) which is sufficient to meet product requirements through March 2019. Hence, the company is expecting notable improvement in margins during 9MFY19 as the prices of both cotton and yarn have moved up in the past six months.

Liquidity & Cash Flow

Funds from operations (FFO) were recorded lower at Rs. 720m (FY17: Rs. 992m; FY16: Rs. 180m) with the decreased in profits during FY18. The company's policy of meeting working capital requirements from internal cash generation reflects positively on the liquidity profile. However, given capex in new spinning unit, the cash & bank balance of the company stood lower at Rs. 56m by end-FY18 (FY17: Rs. 2.5b; FY16: Rs. 2.3b) and hence the company availed short-term borrowings of Rs. 1.9b to supports its higher working capital requirements. Consequently, FFO to long-term and FFO to total borrowing ratios weakened to 0.63x and 0.27x (FY17: 0.93x and 0.93x), respectively. Additionally, the debt service coverage ratio is likely to decrease, though is expected to remain sound, once debt repayments starts in 2019. Moreover, in line with its working capital strategy, RTML has retired its short-term credit lines during 5MFY19 and is carrying cash & bank balance of about Rs. 800m. The current ratio decreased to 2.6x (FY17: 8.1x), though remained sufficient. Meanwhile, inventory plus trade receivables to short-term borrowings improved to 8.3x (FY17: 4.2x), which also highlights healthy liquidity position of the company. Going forward, the cash flows position is expected to improve on the back of incremental income from spinning unit-III and recent uptrend in margins noted during 5MFY19.

Capitalization and Funding

Total equity base augmented to Rs. 8.2b by end-FY18 (FY17: Rs. 7.6b; FY16: Rs. 6.7b) with the accumulation of profits. During FY17 and FY18, the company has incurred capital expenditure worth Rs. 3.8b for spinning unit-III and modernization of some existing spindles. RTML has mobilized long-term borrowings of Rs. 1.4b over the same period while a major portion of CAPEX has been financed with internally available funds. The Long-term Finance Facility (LTFF) carries a markup rate of 2.0% plus a spread of 0.25%. The repayments will begin from May 13, 2019, whereas the final payment will be made on February 13, 2027. The gearing and debt leverage indicators were reported higher at 0.40x and 0.51x by end-FY18 (FY17: 0.16x and 0.24x) owing to increase in borrowings. As on now, the company has repaid short-term borrowings and has no plan to mobilize new long-term in the foreseeable future. Thereby, gearing indicators are expected to improve with the scheduled repayments of long-term borrowings and continued retention of profits, going forward.

Governance & Internal Audit

The Board of Directors of RTML comprises three members, all being representatives of the sponsoring family. The senior management team comprises experienced resources from the textile sector and has largely depicted stability.

Riaz Textile Mills (Pvt.) Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	FY16	FY17	FY18
Non-Current Assets	1,750	4,475	5,131
Stock-in-Trade	2,288	1,801	4,700
Trade Debts	278	271	831
Cash & Bank Balances	2,326	2,450	56
Loans and Advances	186	121	1,244
Other Assets	235	302	380
Total Assets	**7,063**	**9,420**	**12,342**
Trade and Other Payables	263	498	670
Short Term Borrowings	-	-	1,899
Long-Term Borrowings *(Inc. current matur)*	-	1,185	1,399
Provision for Taxation	71	106	148
Other Liabilities	32	48	72
Total Liabilities	366	1,837	4,188
Tier-1 Equity	6,696	7,583	8,154
Total Equity	6,696	7,583	8,154
INCOME STATEMENT	**FY16**	**FY17**	**FY18**
Net Sales	7,137	7,696	11,333
Gross Profit	536	1,348	1,034
Operating Profit	199	1,026	768
Profit After Tax	109	886	571
FFO	273	1,098	874
RATIO ANALYSIS	**FY16**	**FY17**	**FY18**
Gross Margin (%)	7.5	17.5	9.1
Net Working Capital	4,979	4,335	4,457
FFO to Long-Term Debt	-	0.93	0.63
FFO to Total Debt	-	0.93	0.27
Debt Servicing Coverage Ratio (x)	5	40	25
ROAA (%)	1.5	10.7	5.2
ROAE (%)	1.6	12.4	7.3
Gearing (x)	-	0.16	0.40
Debt Leverage (x)	0.05	0.24	0.51
Current Ratio	15.9	8.1	2.6
Inventory + Receivables/Short-term Borrowings (x)	9.8	4.2	8.3

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix II

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 III
Name of Rated Entity	Riaz Textile Mills (Pvt.) Limited				
Sector	Textile				
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				
	12/31/2018	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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