RATING REPORT

Best Exports (Pvt.) Limited (BEL)

REPORT DATE:
January 7, 2020

RATING ANALYSTS:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	BBB	A-2	BBB	A-2
Rating Date	*Dec 30, 2019*		*Nov 5th, 2018*	
Rating Outlook	Stable		Stable	

COMPANY INFORMATION	
Incorporated in 1996	External auditors: Deloitte Yousuf Adil Chartered Accountants
Private Limited Company	Chairman of the Board/CEO: Mr. Waqas Ali
Key Shareholders (with stake 5% or more):	
Mr. Waqas Ali – 99.98%	

APPLICABLE METHODOLOGY
VIS Entity Rating Criteria: Corporates (May 2019) ***https://www.vis.com.pk/kc-meth.aspx***

OVERVIEW OF THE INSTITUTION

Best Exports (Pvt.) Limited was established in 1996 under the Companies Act, 1984 (now Companies Act, 2017). The company is a small sized weaving unit that is primarily involved in manufacturing and export of grey, bleached, dyed and made ups consisting of bed sets, pillow covers, quilt covers, cotton bags, table covers and curtains.

Profile of the Chairman/CEO

Mr. Waqas Ali along with his father founded the company in 1996. Mr. Waqas has studied at Aitchison College, Lahore and has obtained Master's degree from Oxford University, UK.

Financial Snapshot

Core Equity: end-FY19: Rs. 1.6b; end-FY18: Rs. 1.4b

Assets: end-FY19: Rs. 4.5b; end-FY18: Rs. 4.2b

Profit After Tax: FY19: Rs. 86.5m; FY18: Rs. 130.4m

RATING RATIONALE

The ratings assigned to Best Exports (Pvt.) Limited (BEL) take into account its presence in export-oriented value-added textile segment. The management's focus on expanding current operations and growth in value-added products exports bodes well for the company. Adequate liquidity and coverages has provided comfort to the assigned ratings. However, the ratings remained constrained by relatively limited scale of operations. Further, maintenance of low leverage capital structure is considered a key rating factor.

Key Rating Drivers:

Textile sector, the largest export industry of Pakistan: According to the Pakistan Economic Survey 2018-19, Pakistan's largest export industry has been the textile industry. Overall export performance of the textile sector has been muted during the outgoing year despite significant rupee devaluation and notable measures undertaken by the Government of Pakistan (GoP) to uplift the textile sector; the latter included reduction in energy prices and regulatory duty on import of cotton. Non-value-added exports contracted by 20.6%/19.9% in terms of volume and value during FY19 while value-added exports depicted meager growth of 6.8%/3.0% in volume/value terms. Global demand of Pakistani yarn has experienced downward pressure, owing to shifting of spinning mills from China to Vietnam coupled with reduced export orders from China in light of the prevailing US-China trade tensions. On the flip side, volume led growth in value-added exports has enhanced local consumption of yarn resulting in limited export surplus for the same. Nevertheless, signing of FTA phase 2 (Free Trade Agreement) with China presents an opportunity for spinning mills to enhance exports to China.

Cost pressures for the industry are reflective of the global and local cotton production data which shows scaled down cultivation area and production at both ends. Resultantly, local cotton prices have gone up. With respect to spinning segment, dependence on imported cotton, particularly from India, had been on the higher side given its identical quality with the local cotton. However, sprained relations with India and significant rupee devaluation would further spike up raw material costs for the spinning segment. Margins and financial performance of the players in the industry have depicted volatility due to inherent cyclicality of crop levels and oscillations in cotton prices.

Expansion of operations: BEL has 445 Suzler looms installed, running at 88% (FY18: 84%) capacity utilization during FY19. The management intends to expand its weaving operations by adding 72 Airjet looms; total capex on the project is estimated to be around Rs. 1.4b, out of which Rs. 377m will be incurred on land & building, installation and local machinery. As per management, Rs. 450m will be mobilized through internal sources/equity injection. For the same purpose, advance paid against land (8-Acres) amounted to Rs. 36.2m and capital work in progress of Rs. 4.6m pertained to the civil work on land during FY19. For import of machinery costing Rs. 1.1b, the company plans to avail LTTF in FY21. The management expects the civil work to complete by end-FY21, while the project is projected to be completed by end-FY22. Further, the company has added 40 new stitching machines worth Rs. 4.5m during FY19, to increase production of made-ups.

The management's plan for downward integration of adding spinning unit of 31,680 spindles has been shelved, due to elevated revised cost for the project, an outcome of currency devaluation and higher mark-up rates.

Augmentation in topline with largely stagnant export sales: Export sales have remained the major revenue driver, however its contribution in total sales mix decreased to 64% (FY18:

83%) during FY19. Exports sales including exchange gain stood at Rs. 2.1b (FY18: Rs. 2.2b), mainly included sales of made ups, which remained at prior year's level of Rs. 1.1b (FY18: Rs. 1.1b). Meanwhile, sale of grey cloth decreased to Rs. 278.0m (FY18: Rs. 397.4m) and export sale of dyed, printed cloth stood at Rs. 630.4m (FY18: Rs. 642.3m). As a result of local currency depreciation, exchange gain increased to Rs. 184.2m (FY18: Rs. 54.5m) during the review period. Export sales were largely targeted in Europe, with around 71% (FY18: 57%) share in revenue, followed by increased exposure in North America to 17% (FY18: 3%) and South America to 9% (FY18: 6%). Local sales comprising grey cloth, increased to Rs. 1.1b (FY18: Rs. 263.9m) during FY19. According to management, higher local sales were made to sustain production capacity, while increase in export sales of made-ups is expected during the ongoing year. Export sales during 5MFY20, amounted to Rs. 1.02b; 62% of which constituted export sales of made-ups. Client concentration, though improved, have remained moderate, as sales to top ten customers accounted for 33.5% (FY18: 48.4%) of the total sales during FY19.

Despite increase in average sale prices of all products as measured in terms of average price per meter, gross margins were reported lower at 9.1% (FY18: 12.7%), primarily on account of increase in proportion of relatively lower margin sales of greige fabric in local market and higher depreciation expense related to enhanced fixed assets. Cost of raw material consumed increased during FY19, however, its contribution to cost of goods manufactured has remained at 78.6% (FY19: 78.8%). Prices of locally procured yarn increased by 23% during FY19; average price of local yarn has increased to Rs. 15,140/bag (FY18: Rs. 12,358/bag), while average price of imported yarn, constituting 9.0% of the total procurement, increased to Rs. 12,904/bag (FY18: 5,448.8/bag); the difference in average rates is due to the type of yarn being imported. Stores and spares consumed increased to Rs. 142.3m (FY18: Rs. 123.8m) due to repair and maintenance of generators during the review period. Meanwhile, fuel and power expenses were recorded lower at Rs. 118.0m (FY18: Rs. 125.4m); higher expense during preceding year was the result of usage of diesel engines for some time in place of gas engines due to overhauling of the latter. Depreciation charge stood higher at Rs. 106.0m (FY18: Rs. 12.6m) owing to higher cost of revalued property, plant and equipment.

Selling and distribution expenses stood higher at Rs. 53.6m (FY18: Rs. 45.0m) mainly owing to increase in freight charges. Administrative expenses were higher mainly on account of increase in salary and benefits, an outcome of annual salary adjustments.

In conformity with higher mark-up rates, finance cost increased to Rs. 114.5m (FY18: Rs. 80.8m). Other expenses relating to worker's profit participation fund and worker's welfare fund, stood lower at Rs. 4.8m (FY18: Rs. 8.2m) and other income, majorly comprising profit on deposits, stood lower at Rs. 0.35m (FY19: Rs. 0.92m). Despite recognition of deferred tax asset, net profit was reported lower at Rs. 86.5m (FY18: Rs. 130.4m), mainly owing to lower gross profits, higher operating expenses and finance cost during FY19.

Intact liquidity position and adequate debt service ability: Albeit profit before taxation decreased during the review period, Funds from Operations (FFO) increased to Rs. 174.4m (FY18: Rs. 149.4m) primarily on account of higher non-cash adjustments during FY19. However, with increase in total debt *(comprising only short-term borrowings)* FFO to total debt remained unchanged at 0.14x (FY18: 0.14x) during FY19. Debt service coverage ratio (DSCR) decreased marginally to 2.54x (FY18: 2.77x).

Trade debts stood higher at Rs. 879.7m (FY18: Rs. 555.1m) by end-FY19 mainly on account of increase in local trade debts amounting Rs. 332.5m (FY18: Rs. 136.5m). Aging analysis of receivables showed that all are within 6 months' credit bracket. Current portion of long-term receivable related to amount due from Best Fibres (Pvt.) Limited (BFL) *(An associated concern)* for the sale of spinning unit, originally amounted to Rs. 542.1m, stood at Rs. 136.7m (FY18: Rs. 132.3m) by the end-FY19, following the receipt of first installment in the preceding year. It is an interest free receivable and was initially recognized at an amortized cost using prevailing market interest rate of 6.79% in FY18. Deferred expense of Rs. 44.1m (FY18: Rs. 88.9m) represented the difference between the carrying value and the fair value of this receivable is the benefit foregone from the interest free receivable.

Stock in trade was recorded higher at Rs. 773.8m (FY18: Rs. 639.7m) mainly due to higher finished goods inventory and raw materials. It also includes stock of Rs. 127.8m (FY18: Rs. 639.7m) pledged as security with the bank. Stores, spares and loose tools stood higher at Rs. 108.5m (FY18: Rs. 77.1m) by end-FY19. Tax refunds due from government amounted to Rs. 207.9m (FY18: Rs. 218.4m). According to management, the government has started releasing sales tax refunds, which will provide support to liquidity to a certain extent. Advances and prepayments stood at Rs. 107.6m (FY18: Rs. 99.1m) and mainly comprised advances made to suppliers, advance income tax and advances made to CEO and director of the company. Other receivables primarily pertained to export rebate/duty drawback, stood at Rs. 96.6m (FY18: Rs. 93.7m) at end-FY19. Current ratio increased slightly to 1.8x (FY18: 1.7x) primarily on account of higher stock in trade and trade debts by end-FY19. Accordingly, stock in trade plus trade debts to short-term borrowing ratio increased to 1.3x (FY18: 1.2x) by end-FY19.

Conservative capital structure and comfortable capitalization indicators: Tier-1 equity stood higher mainly on back of profit retention on timeline basis to Rs. 1.6b (FY18: Rs. 1.4b). Revaluation reserve net of incremental depreciation on revalued assets, after adjustment of deferred tax assets, stood at Rs. 1.5b (FY18: Rs. 1.6b). BEL's debt profile comprised only short-term borrowings, which stood higher at Rs. 1.25b (FY18: Rs. 1.0b); the company has an access to total credit lines worth Rs. 1.5b. The short-term financing pertained to export refinance of Rs. 885.8m (FY18: Rs. 852.1m), running finances of Rs. 201.9m (FY19: Rs. 138.3m) and cash finances of Rs. 159.3m (FY18: Rs. 42.6m). These are secured against ranking charge over fixed assets and are subject to markup at the rates 1-3 months KIBOR plus 1-1.5% per annum and SBP rate plus 1% per annum. Further cash finances are secured against pledge of yarn and are subject to markup rate of 1 month KIBOR plus 1.25-1.50% per annum (FY18: 1 month KIBOR plus 1.5% per annum).

Despite higher tier-1 equity, gearing and leverage indicators increased slightly to 0.79x and 0.90x (FY18: 0.74x and 0.81x) respectively, at end-FY19, mainly on account of higher short-term borrowings. Equity base is projected to strengthen further on the back of profit retention, while gearing and leverage indicators are likely to increase mainly in FY21, when Rs. 1.1 will be mobilized for import of machinery.

BALANCE SHEET	FY17	FY18	FY19
Non-Current Assets	180	2,089	2,025
Long-Term Receivables *(including current portion)*	454	314	181
Store, Spares and Loose Tools	51	77	109
Stock-in-Trade	425	640	774
Trade Debts	971	555	880
Other Receivables	254	253	222
Tax Refunds Due from Government	326	218	208
Cash and Bank Balances	25	42	63
Total Assets	2,686	4,189	4,461
Trade and Other Payables	96	58	55
Long Term Debt *(including current maturity)*	-	-	-
Short Term Debt	1,226	1,033	1,247
Other Liabilities	92	52	123
Tier-1 Equity	1,272	1,403	1,585
Surplus on Revaluation of PP&E	-	1,643	1,451
Total Equity	1,272	3,046	3,036
Paid-up Capital	411	411	411
INCOME STATEMENT	FY17	FY18	FY19
Net Sales	-	2,593	3,220
Gross Profit	-	329	293
Profit Before Tax	-	156	75
Profit After Tax	-	130	87
Funds from Operations	-	149	174
RATIO ANALYSIS	FY17	FY18	FY19
Gross Margin (%)	-	12.7	9.1
Net Margins	-	5.0	2.7
Current Ratio (x)	-	1.7	1.8
Net Working Capital	-	774	1,069
FFO to Total Debt (x)	-	0.14	0.14
FFO to Long Term Debt (x)	-	-	-
Debt Leverage (x)	0.96	0.81	0.90
Gearing (x)	1.10	0.74	0.79
Debt Servicing Coverage Ratio (x)	-	2.8	2.5
ROAA (%)	-	3.8	2.0
ROAE (%)	-	9.7	5.8
(Stock in Trade+Trade Debt) to Short-Term Borrowing Ratio	1.1	1.2	1.3

ISSUE/ISSUER RATING SCALE & DEFINITIONS 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	Best Exports (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				
30-12-2019	BBB	A-2	Stable	Reaffirned
05-11-2018	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.
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