

# RATING REPORT

## Al-Karam Towel Industries (Pvt.) Limited

### REPORT DATE:

September 10, 2024

### RATING ANALYSTS:

Zunain Arif

[zunain.arif@vis.com.pk](mailto:zunain.arif@vis.com.pk)

M. Amin Hamdani

[amin.hamdani@vis.com.pk](mailto:amin.hamdani@vis.com.pk)

### RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook / Rating Watch	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	
Rating Date	September 10, 2024		Aug 01, 2023	

### COMPANY INFORMATION

Incorporated in 2004	External Auditors: M/s. Rahman Sarfaraz Rahim Iqbal Rafiq Chartered Accountants
Private Limited Company	Chief Executive Officer: Mr. Hanif Bawa
Key Shareholders (with stake 5% or more):	
Mr. Rehan Mehtab Chavla ~25%	
Mr. Farrukh Mehtab ~25%	
Mr. Kashif Mehtab ~25%	
Mr. Noman Mehtab ~25%	

### APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial 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>

## Al-Karam Towel Industries (Private) Limited

OVERVIEW OF  
THE  
INSTITUTION

*Al-Karam Towel Industries (Private) Limited (AKTI) was incorporated as a private limited company in April 2004, under the companies' ordinance 1984 with its head office and production facilities based in Karachi, Pakistan.*

## RATING RATIONALE

**Corporate Profile**

Al-Karam Towel Industries (Private) Limited (“AKTI” or “the Company”) is a family-owned entity specializing in towel and terry product production and export. Recently, it has entered the domestic yarn market. With a 20-year history, the Company operates a vertically integrated textile mills including spinning, weaving, dyeing, bleaching, stitching, packing, and finishing facilities, supported by a workforce of over 2,900 employees. Product suite features terry towels, patterned bath and beach towels, bathrobes, kitchen towels, washcloths, hand towels, and shower wraps.

AKTI holds ISO certification and a range of other globally recognized accreditations, emphasizing its commitment to high-quality standards. IT infrastructure commensurate with scale of operations, utilizing an Oracle-based ERP system. The total energy requirement is ~16 Megawatt is met through a mix of in-house gas generators, a solar power plant, and the national grid, with diesel generators as backup. In the last two years, the Company has shifted the energy requirement of 10-12% to Solar power.

**Environmental, Social, & Governance (ESG) Initiatives**

AKTI is persistently committed to minimizing its environmental impact across all phases of operations and products - from design to end-of-life. Its eco-friendly initiatives encompass reducing carbon footprints, operating wastewater treatment facilities, and spearheading local tree-planting campaigns. Moreover, the company extends its emphasis on social responsibility by fostering equal opportunities, notably promoting women's empowerment, conducting health-centric campaigns such as blood testing and donations, and organizing breast cancer awareness sessions.

**Operational Performance**

The Company has registered Head Office at S.I.T.E Super Highway, Scheme 33, Karachi, Pakistan and have 12 factories with 6 located in Karachi and the rest in Nooriabad.

**Spinning** – During FY23, there was an increase in the installed capacity. The installed capacity of spinning increased by 121% from 19.67 million lbs in FY22 to 43.56 million lbs in FY23. This also led to a 113% improvement in the production during FY23. The yarn production improved from 19.67 million lbs in FY22 to 42 million lbs in FY23. The overall capacity utilization during FY23 was 96.3%. The capacity is expected to reach around 50 million lbs at year end FY24.

**Weaving** – During FY23, there was no change in the installed capacity. However, the fabric production declined by 25% from 53.53 million lbs in FY22 to 40 million lbs in FY23. The overall capacity utilization was 60.3% during FY23.

**Table: Capacity & Production Data (Units in millions)**

	FY20	FY21	FY22	FY23
<b>Spinning</b>				
Installed Capacity (lbs)	14.1	19.5	19.7	43.56
Actual Production (lbs)	6.3	18.4	19.7	41.95
<b>Capacity Utilization</b>	<b>44%</b>	<b>95%</b>	<b>100%</b>	<b>96%</b>
<b>Weaving</b>				
Installed Capacity (lbs)	44.0	44.0	66.3	66.3
Actual Production (lbs)	38.3	40.0	53.5	40
<b>Capacity Utilization</b>	<b>87%</b>	<b>91%</b>	<b>81%</b>	<b>60%</b>

**Sector Update**

The business risk profile of the textile sector in Pakistan is characterized by a high level of exposure to economic cyclicality and intense competition. This sector's performance is significantly influenced by the broader economic conditions in the country, making it inherently vulnerable to fluctuations in demand driven by economic factors.

In FY23, the textile sector faced challenges due to various economic and environmental factors. These included damage to the cotton crop resulting from flooding in 1HFY23, escalating inflation, and import restrictions due to diminishing foreign exchange reserves.

During FY23, Pakistan's yarn production registered a substantial decline, primarily due to reduced availability of cotton, as a result of crop damage and import restrictions. The sector's profitability was constrained by factors such as higher production costs, increased raw material costs, and rising energy expenses, all of which constrained the sector's profit margin. The industry's performance is closely intertwined with the outlook of the cotton and textile industries, both of which were affected in FY23. Reduction in cotton supply, coupled with global economic slowdown and contractionary economic policies, led to a decrease in demand for textile products and, consequently, cotton yarn.

While the global outlook for cotton production is expected to rebound, local challenges persist. These challenges include high interest rates, increasing energy costs and inflationary pressures. Additionally, the sector's vulnerability to global market dynamics and the domestic economic landscape further contribute to its high business risk profile. The worrying trend has continued during the first quarter of FY25 as the cotton production has declined by 48% during the first 15 days of FY25. Several factors have contributed to this downturn. Climate change has altered weather patterns, resulting in irregular rainfall and increased temperatures that have negatively affected crop yields. Additionally, pest infestations, especially by the pink bollworm, have devastated cotton fields. Rising costs of inputs such as fertilizers, pesticides, electricity, and quality seeds have made cotton cultivation less profitable.

Addressing the decline in cotton production requires a multifaceted approach. Improved pest management practices, such as integrated pest management (IPM), can help control infestations more effectively. Education and training for farmers on IPM techniques are crucial. They need access to the latest research and pest-resistant cotton varieties. Investment in agricultural research and development is also essential. Developing drought-resistant and high-yield cotton varieties can mitigate the impacts of climate change.

**MONTH-WISE EXPORT DATA FOR TEXTILE SECTOR**

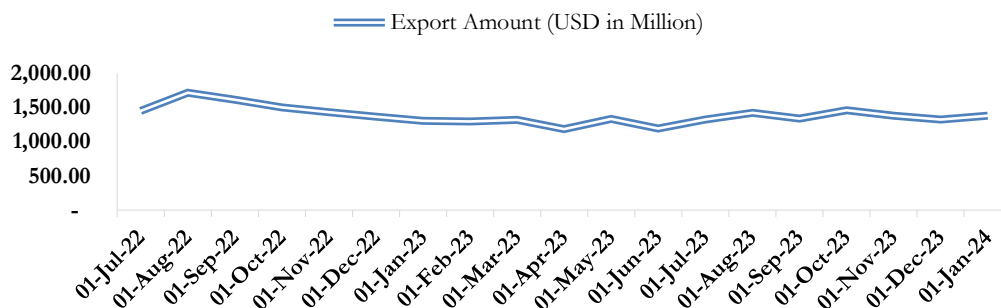


Figure 1: MoM Textile Exports (In USD' millions)  
Source: SBP

**Key Rating Drivers:**

**The increase in unit prices drives topline growth and boosts gross margin, while elevated finance cost negatively impacts net margin in FY23**

In FY23, the sales revenue increased by 20.4% Y/Y owing to rise in unit prices, though there was a contraction of 32.6% Y/Y in sales volumes. Consequently, gross margin rose to 26% (FY22: 22%) amid rupee depreciation. The finance cost incurred a ~3x increase to PKR 1.16b in FY23 (FY22: 373m) due to elevated interest rates. Consequently, the net margin declined to 6% in FY23 (FY22: 8%).

The topline is primarily supported by export sales contributing 93.6% to the total sales with major export made to USA and UK..

During 9MFY24, profitability indicators came under pressure with gross and net margins declining to 22% and 6% respectively (FY23: 26% and 8%) attributed to higher raw material prices, hike in fuel and power cost and elevated finance cost. Going forward, the Company's topline is expected to reach PKR 38bn in FY25 with the expansion in weaving segment.

**Liquidity and cashflow indicators remained adequate with strong debt service coverage**

During FY23, the Funds from Operations (FFO) increased to PKR 2.86 bn (FY22: 2.79 bn) due to higher profitability. This trend continued during 9MFY24 despite elevated financial cost. Consequently, the FFO to Long Term Debt improved to 0.56x in 9MFY24 (FY22: 0.55, FY23: 0.51). The current ratio of the Company also inched up to 1.42x in 9MFY24 (FY23: 1.21x, FY22: 1.32x).

Debt service coverage ratio (DSCR) registered a drop with rise in financial charges, however remained satisfactory from the assigned ratings perspective. DSCR came in at 2.68x in 9MFY24 (FY23: 2.30x, FY22: 3.26x). Short term debt coverage from inventory and receivables remained stable at adequate levels of 1.23x in 9MFY24 (FY23: 1.33x, FY22: 1.27x).

The Company's cash conversion cycle improved to 147 days during 9MFY24 (FY23:179 days) due to better terms with clients and efficient inventory management

**Equity growth surpassing the increase in debt levels. Capitalization metrics improve marginally during the review period**

The Equity of the Company increased by 39% over the past 21 months, at 9MFY24. This growth is attributed to retention of profits. There was an increase in the long term debt and short-term debt during the period from FY22 to 9MFY24. Long term debt grew by 18% primarily due to additional borrowing to fund the solar power and spinning and weaving units expansion projects. Short term debt increased by 32% at end-9MFY24 to meet the higher working capital requirements arising from growth in business volumes. Despite these increases, gearing marginally improved to 1.54x (FY22:1.576x) in FY23 supported by higher equity base. Gearing further improved to 1.34x in 9MFY24 on the back of higher profit retention. Leverage however marginally deteriorated in FY 23 to 1.93x (FY22: 1.89x) with increase in trade related liabilities, however, improved to 1.55x in 9MFY24 owing to higher equity base. Going forward, maintaining capitalization profile will remain important for the assigned ratings.

**Al-Karam Towel Industries (Private) Limited**
**Appendix I**

Financial Summary (PKR in millions)	FY19	FY20	FY21	FY22	FY23	9MFY24
<b><u>Ratio Analysis</u></b>						
Gross Margin	17.5%	20.7%	18.3%	22.1%	25.9%	22.1%
Net Margin	7.9%	9.6%	8.2%	8.6%	8.1%	6.3%
Net Working Capital	1400	2126	2321	3351	2710	4890
Current Ratio	1.37	1.38	1.35	1.32	1.21	1.42
FFO	1,250	917	1,643	2,793	2,855	2894*
FFO to Total Debt	30%	13%	17%	22%	19%	19%*
FFO to Long Term Debt	93%	30%	32%	55%	51%	56%*
Debt Servicing Coverage Ratio	5.19	4.35	2.30	3.26	2.30	<b>2.68*</b>
(Trade Debts + Inventory)/Short term Borrowings	1.18	1.08	1.23	1.27	1.33	1.23
Gearing	0.95	1.29	1.45	1.57	1.54	1.35
Leverage	1.16	1.64	1.71	1.89	1.93	1.55
ROAA	11.3%	8.8%	8.5%	7.7%	7.2%	7%
ROAE	23.3%	21.5%	22.7%	21.6%	20.8%	19.1%
DSO	36	46	34	42	45	33
DIO	74	101	91	140	178	138
DPO	32	47	34	37	44	24
CCC	78	100	90	145	179	149

\*Annualized

REGULATORY DISCLOSURES						Appendix II
<b>Name of Rated Entity</b>	Al-Karam Towel Industries (Private) Limited					
<b>Sector</b>	Textile					
<b>Type of Relationship</b>	Solicited					
<b>Purpose of Rating</b>	Entity Ratings					
<b>Rating History</b>	<b>Rating Date</b>	<b>Medium to Long Term</b>	<b>Short Term</b>	<b>Rating Outlook</b>	<b>Rating Action</b>	
	10/09/2024	A-	A-2	Stable	Reaffirmed	
	01/08/2023	A-	A-2	Stable	Reaffirmed	
	05/25/2022	A-	A-2	Stable	Reaffirmed	
	04/20/2021	A-	A-2	Stable	Maintained	
	04/23/2020	A-	A-2	Rating Watch-Developing	Maintained	
	03/03/2022	A-	A-2	Stable	Reaffirmed	
12/17/2018	A-	A-2	Stable	Initial		
<b>Instrument Structure</b>	N/A					
<b>Statement by the Rating Team</b>	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.					
<b>Probability of Default</b>	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.					
<b>Disclaimer</b>	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. Copyright 2024 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.					
<b>Due Diligence Meeting Conducted</b>	<b>Name</b>	<b>Designation</b>		<b>Date</b>		
	Mr. Kamran Anwer	CFO		Aug 19, 2024		
	Mr. Waqar Khan	DGM -Finance				
Mr. Fahad Shaukat	DGM -Accounts					