RATING REPORT

Umar Spinning Mills (Pvt.) Ltd (USMPL)

REPORT DATE:
February 13th, 2019

RATING ANALYST:
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RATING DETAILS		
	Initial Rating	
Rating Category	**Long-term**	**Short-term**
Entity	BBB+	A-2
Rating Outlook	Stable	
Rating Date	February 13th, 2019	

COMPANY INFORMATION	
Incorporated on March 10, 1991	**External auditors:** M/s. Mushtaq & Company Chartered Accountants
Private Limited Company	**Chief Executive Officer:** Mr. Pervaiz Umar
Key Shareholders (with stake 5% or more):	
Pervaiz Umar 60%	
Mohammad Faisal Pervaiz 25%	
Shaheena Pervaiz 15%	

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

Umar Spinning Mills (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Umar Spinning Mills Private Limited (USMPL) was incorporated in1991 and became operational in 2003. Financial Statements of the company for FY18 were audited by Mushtaq & Company Chartered Accountants

Profile of CEO
Mr. Pervaiz Umar has been associated with the company since 1991. He is also associated with one of the largest clearing, forwarding and customs advisory house since 1968.

RATING RATIONALE

Umar Spinning Mills Private Limited (USMPL) is a part of Pervaiz Group of Companies which has presence in textile and clearing & forwarding business. USMPL is primarily engaged in the manufacturing and sale of yarn to both local and foreign markets.

Head office of the company is based in Karachi, while a representation office is based in Lahore. Production factory of USMPL is based in Raiwand, Lahore. At end-FY17, the company operated through 43,776 (FY16: 34,176) spindles.

Rating Drivers

Business Risk

Inherent cyclicality of cotton price and crop levels drives performance of players operating in the spinning sector. Historically, margins and financial performance of players have depicted seasonality. Moreover, competitive intensity is high due to commoditized nature of the product. Ability of the spinning companies to maintain their customer profiles along with product quality will be a key growth driver.

Production Capacity

	FY18	FY17	FY16
Number of spindles installed	43,776	43,776	34,176
Number of spindles worked	43,776	43,776	34,176
Number of working days	364	364	364
Number of shifts per day	3	3	3
Installed capacity of yarn (Lbs.)	20,816,137	15,288,000	15,288,000
Actual production of yarn (Lbs.)	20,541,522	15,099,285	14,310,553
Capacity utilization	98.7%	98.8%	93.6%

Sales Mix

USMPL's net sales have increased at a Compound Annual Growth Rate (CAGR) of 20.0% over the past three years (FY15-FY18). Net sales of the company in FY18 grew by 37.8% compared to preceding year (FY18: Rs. 3.5b; FY17: Rs. 2.6b). The increase in net sales can be associated with an increase in average selling price along with volumetric growth. Around two third of total sales of the company cater to domestic market (including indirect export sales). Concentration is witnessed in terms of client wise sales as two clients accounted for 45.2% (FY17: 45.2%; FY16: 35.0%) of gross sales in FY18. However, client concentration risk is partly mitigated by long term association with clients and customized products for clients. Country wise concentration is considered moderate as exports to one country constituted around 20% (FY17: 17.3%; FY16: 19.0%) of gross sales in FY18.

Going forward the company is planning to increase its market share in Europe and South Korea. The company engages with export through a third party agent in order to minimize its risk.

Profitability

Through product diversification the company has expanded its product portfolio, thereby selling greater proportion of higher count yarn to its customers. During the last three years, gross margins of the company have depicted an upward trend owing to favorable cotton procurement strategy. Gross margin was reported at 7.3% (FY17: 6.4%; FY16: 4.2%) in FY18. In HY19, gross margin depicted sizeable increase to 9.9% (HY18: 4.8%). As per management, the cotton was imported prior to the currency depreciation last year. With increase in cotton prices post currency devaluation, higher costs were passed to the customers in terms of higher yarn prices.

Improvement in gross margins has translated into higher net margins on timeline basis. Furthermore, finance cost of the company has trended upwards due to higher average short term borrowings to meet working capital requirements and increase in interest rates. Going forward, the management believes that the company will sustain gross margins on back of the currency depreciation and reduction in RLNG & electricity prices. Sustainability in margins in the given rating horizon would be an important rating determinant.

Capitalization and Funding

On a timeline basis, equity base of the company has depicted an increasing trend owing to profit retention. Equity base (excluding unrealized gains/losses on Available for Sale investments) of the company amounted to Rs. 1.8b (FY17: Rs. 1.7b; FY16: Rs. 1.6b) at end-FY18. Gearing and Leverage ratios increased to 1.0x (FY17: 0.8x; FY16: 0.2x) and 1.2x (FY17: 1.0x; FY16: 0.3x) respectively at end-FY18. The increase in the aforementioned ratios was associated with the increase in both short-term borrowing to meet the working capital requirements and long term borrowings to finance Capex.

Liquidity

Fund From Operations (FFO) has exhibited a rising trend owing to increase in company's profitability and depreciation. In FY18, FFO of the company increased by 59.5% (FY18: Rs. 288.4m; FY17: Rs. 180.8m; FY16: Rs. 64.3m). However, FFO as proportion of total debt has varied overtime. Debt Service Coverage Ratio is considered adequate and has depicted an improvement on account of increasing FFO. Current ratio has observed a downward trend owing to increase in short-term borrowing, however the same is considered satisfactory as it remains above 1.0x (FY18: 1.6x; FY17: 1.7x). Stock in trade and trade debts provide adequate coverage for short term borrowings.

Financial Summary (amounts in PKR millions)			**Appendix I**
	FY18	**FY17**	**FY16**
BALANCE SHEET			
Fixed Assets	1,500	1,599	1,096
Long term Deposits	4.3	4.4	4.4
Stock-in-Trade	1,019	955	497
Trade Debts	363	193	186
Cash & Bank Balances	36	26	36
Total Assets	3,876	3,210	2,159
Trade and Other Payables	315	229	172
Long Term Debt (including current maturity)	615	594	153
Short Term Debt	1,103	681	171
Total Debt	1,717	1,275	324
Total Liabilities	2,097	1,557	544
Total Equity (excluding unrealized gains/losses on Available for Sale investments)	1,781	1,659	1,585
INCOME STATEMENT			
Net Sales	3,548	2,576	2,261
Gross Profit	260	166	96
Operating Profit	124	52	-12
Profit After Tax	78	40	7
RATIO ANALYSIS			
Gross Margin (%)	7.3%	6.4%	4.2%
Net Profit Margin	2.2%	1.5%	0.3%
Net Working Capital	886	639	661
FFO to Total Debt (%)	16.8%	14.2%	19.9%
FFO to Long Term Debt (%)	46.9%	30.4%	42.0%
Debt Servicing Coverage Ratio (x)	3.41	3.36	-18.97
ROAA (%)	2.2%	1.5%	0.4%
ROAE (%)	4.6%	2.5%	0.5%
Gearing (x)	1.0	0.8	0.2
Leverage (x)	1.2	0.9	0.3

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	Umar Spinning Mills Private Limited				
Sector	Textiles				
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		
	13/02/2019	BBB+	A-2	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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