RATING REPORT

H.A Fibres (Pvt.) Limited

REPORT DATE:
October 02, 2023

RATING ANALYST:
Asfia Amanullah
asfia.aziz@vis.com.pk

Sundus Qureshi
sundus.qureshi@vis.com.pk

RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook	*Stable*		*Positive*	
Rating Date	*October 02, 2023*		*June 23, 2022*	
Rating Action	*Maintained*		*Reaffirmed*	

COMPANY INFORMATION	
Incorporated in 2006	**External auditors:** BDO Ebrahim & Co. Chartered Accountants
Private Limited Company	**Chairperson/CEO:** Mrs. Sabeena Husnain
Key Shareholders (with stake 5% or more): Mrs. Sabeena Husnain—100%	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Corporates (May 2023): 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

H.A Fibres (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

H.A Fibres (Pvt.) Limited was incorporated as a private limited company in May 2006 under the Companies Ordinance 1984 (Now Companies Act 2017). Registered office of the company is situated at DHA Lahore while plant is located at Sujhan pura 6 km, Off Khanewal Road, Multan.

Profile of Chairperson of Board & CEO: Mrs. Sabeena Husnain serves as chairperson of the board and CEO of the Company. She has over 15 years of experience in textile sector. She is also the CEO of associated concern Husnain Textile Mills (Pvt.) Limited.

Financial Snapshot

Tier-1 Equity:end-9MFY23: Rs. 4.9b; end-FY22: Rs. 4.8b; end-FY21: Rs. 3.4b;

Assets:end-9MFY23: Rs. 9.0b; end-FY22: Rs. 7.3b; end-FY21: Rs. 4.7b;

Profit After Tax: 9MFY23: Rs. 78.1m; FY22: Rs. 1,461.1m; FY21: Rs. 1,143.9m;

RATING RATIONALE

H.A Fibres (Pvt.) Limited (HAFL) was incorporated as a private limited company in May 2006 under the Companies Ordinance 1984 (Now Companies Act 2017). HAFL is a spinning unit located at Multan. The company is a part of 'H.A group', other two group companies are Husnain Textile Mills (Pvt.) Limited (HTML) and Palm Villas, an Association of Persons in real estate sector. HAFL holds 30.21% equity in HTML classifying it as an associate Company; it is a spinning mill with an installed capacity of 77,700 spindles.

Capacity utilization & capital expenditure

	FY21	FY22	9MFY23
Number of spindles installed	41,844	47,060	47,060
Number of spindles shifts worked	3	3	3
Installed capacity @ 20/S count (Kgs) 360 days	18,076,608	20,172,445	15,129,334*
Actual production of all counts (Kgs)	10,712,807	12,892,128	9,669,096*
Actual production @ 20/S count (Kgs) 360 days	16,896,729	19,430,620	14,572,965*
Capacity Utilization on conversion (%)	93%	96%	96%*

**Numbers for the period 9MFY23*

During FY21, FY22 and 9MFY23, HAFL incurred capital expenditure of around Rs. 3.3 (Rs. 0.9b in FY21, Rs. 1.9b in FY22 and Rs. 487m in 9MFY23) to finance BMR initiatives and additional spindles. Out of the total capex, Rs. 1,174m was financed through debt facilities, four-fifth of which comprised concessionary rate TERF. The remaining was funded by internal cash resources. This capex has increased the spindle capacity from 41,844 spindles to 63,624 spindles and 3,520 rotors at end-July'23, however 20,904 spindles are under erection phase expected to commence operations by end-September'23.

Capacity utilization levels of the Company have remained on the higher side necessitating capacity expansion. Management expects stable growth in production levels supported by adequate demand which can be catered by additional capacity expected to be operational in HYFY24.

Key Rating Drivers

Business risk profile is constrained by current weak macroeconomic environment both globally and locally, high-interest rates, inflationary pressures, rising raw material costs, ongoing energy crisis in the country, and a global slump in demand. All these factors pose a challenge to the sector over the medium term in terms of margins sustainability and future growth.

Pakistan's export proceeds have oscillated in the range of USD 22-25b during the past decade (FY11-FY21), however, in FY22 exports broke the threshold, clocking in at USD 32.4b. Textile sector contributes nearly one-fourth to industrial value-added segment and provides employment to about 40% of the industrial labor force. Contributing around 8.5% to the country's GDP, with an estimated market size of around Rs. 4.0tr, textile sector has maintained an average share of about 60% in national exports over the years.

Table: Pakistan Export Statistics (in USD millions)

	FY20	FY21	FY22		11M'FY22	11M'FY23
Pakistan Total Exports	22,536	25,639	32,450		29,363	25,794
Textile Exports	12,851	14,492	18,525		16,722	15,513
PKR/USD Average rate	158.0	160.0	177.5		175.0	244.5

Source: SBP

The lingering effects of Covid-19 pandemic continue to shape the Pakistan's textile industry. Initially, as lockdowns lifted, the industry capitalized on opportunities, securing production contracts with Western countries. This redirection of substantial volumes to Pakistan, complemented by government import tax reductions and subsidized COVID-related financing programs such TERF, spurred robust export growth during FY20-22. However, a subsequent phase presented new challenges. Global interest rate hikes aimed at curbing post-pandemic inflation, coupled with geopolitical unrest such as the Ukraine conflict, led to supply chain disruptions and energy crisis. These factors led to a global demand slowdown in major textile economies, reflected in a ~15% year-on-year decline in Pakistan's textile exports in FY23, totaling USD 16.5b (FY22: USD 19.3b). Knitwear, Readymade, and Bed wear segments remain key contributors, making up over 60% of the textile exports.

Table: Textile Export Details (in USD millions)

	FY20	FY21	FY22	FY23	YoY FY23
High Value-Added Segment	**9,669**	**12,427**	**15,611**	**13,576**	**-13%**
- Knitwear	2,794	3,815	5,121	4,437	-13%
- Readymade Garments	2,552	3,033	3,905	3,492	-11%
- Bed wear	2,151	2,772	3,293	2,692	-18%
- Towels	711	938	1,111	1,000	-10%
- Made-up Articles	591	756	849	693	-18%
- Art, Silk & Synthetic Textile	315	370	460	412	-10%
- Others	555	743	872	851	-2%
Low to medium Value-Added Segment	**2,858**	**2,972**	**3,719**	**2,926**	**-21%**
- Cotton Cloth	1,830	1,921	2,438	2,022	-17%
- Cotton Yarn	984	1,017	1,207	844	-30%
- Others	43	34	74	60	-20%
Total	**12,527**	**15,399**	**19,330**	**16,502**	**-15%**

Source: PBS

Flash floods in Sindh and Southern Punjab from last year's monsoon wreaked havoc on the cotton crop, washing away roughly 45% worth over USD 2.5b. This catastrophe led to a historic low yield of 4 million bales in 2022, compared to a 12 million bales annual demand. Local cotton prices subsequently reached a 12-year high of over Rs. 22,000 per 40kg during the year, and imports rose by ~20% in USD terms for FY22, vis-à-vis preceding year. This situation heightened working capital needs, adversely affecting profit margins and liquidity profile for textile entities, particularly spinners, weavers, and dyeing companies. On a positive note, the production target for the current season is set at 12.7 million bales, supported by favorable weather and timely government intervention.

Table: Cotton Prices Trend (In Rs.)

	June'19	June'20	June'21	June'22	June'23
Per Maund	8,770	8,860	13,000	17,380	17,735
YoY % Change	26%	1%	32%	34%	*2%*

The industry faces medium-term risks due to the current weak macroeconomic environment both globally and locally, high-interest rates, inflationary pressures, rising raw material costs, ongoing energy crisis in the country, and a global slump in demand, primarily from North America and Europe. Additionally, the potential expiration of Pakistan's GSP plus status in December 2023 could be impactful. This status, allowing duty-free access to the EU for over 6,300 tariff lines, fosters beneficial trade. Its loss could lead to reduced trade revenues and create market uncertainties.

Previously, the sector also enjoyed incentives provided by the government through a five-year textile policy (2020-25), including preferential energy rates, low-interest financing schemes, and timely payments of various refunds, easing liquidity constraints for local players. However, the prevailing economic instability led to the reduction or withdrawal of many of these supports. This along with contractionary monetary policy and political uncertainties in the country are the key present business risk factors. In the long-run, improvement in value addition, investment in technology and optimization of energy cost would define the future prospects of textile exports.

High cyclicality and competitiveness in the spinning sector translate into high business risk profile.

Movement in cotton prices and cotton crop levels drives performance of spinning players in Pakistan. Given sizeable deficit in local cotton production compared to demand in recent years, cotton prices remained high. However, availability of imported yarn kept yarn prices competitive in the current fiscal year and thus resulting in weakening of profitability profile for spinning players.

Strong growth in revenue base during FY22 supported largely by higher average selling prices. Similar growth momentum was constrained in FY23 due to macroeconomic challenges on global and local front.

- Net sales of the Company witnessed a sizeable jump of 64% and were reported at Rs. 8.9b (FY21: Rs. 5.5b; FY20: Rs. 4.3b) in FY22 driven by 45% increase in prices.
- Sales mix predominantly comprised yarn which accounted for 98% (FY21: 98%) of net sales during FY22. Product mix also consists of a small proportion (2%) of waste material sold.
- Net sales of HAFL majorly comprises of indirect export sales representing 83% (FY21: 82%) of the sales mix during FY22. Remaining proportion of 2% and 15% of the revenue base consists of direct export sales to China and local sales, respectively. Local sales are directed towards customers based in Karachi, Faisalabad and Lahore regions.
- Customer concentration has improved on a timeline basis; however, the same is on a high scale with top 10 customers accounting for 64% of total sales during 9MFY23 (FY22: 68%; FY21: 74%). However, as per management, client concentration risk is partially eliminated due to long-term association with the existing clientele and specialized yarn produced by the Company.
- During 9MFY23, revenue of the Company was recorded at Rs.6.4b. The annualised decline in the outgoing year was a function of supressed demand and supply challenges due to unavailability of foreign reserves in the Country. While management expects revenues to report a stable growth in the ongoing year in view of gradual recovery of the overall economy on national and international fronts; materialization of the same will be critical.

While margins have historically gather support from premium pricing of specialized yarn and share of profit of associates, the same were under pressure in FY23 due to currency devaluation and higher input & financial costs

- Gross margins of the Company followed a downward trend in 9MFY23 with the same reported at 9.3% (FY22: 18.9%; FY21: 22.7%) on account of increase in prices of imported raw material led by currency devaluation, higher local cotton prices and elevated fuel expense.
- In value terms, ~58% of raw materials including cotton and polyester are procured from the international market due to the product's specialized needs while the remaining proportion is procured locally. Management expects the imported proportion of raw material to remain on the higher side exposing the Company to exchange rate volatility risk.
- Finance charges stood higher at Rs. 279m (FY22: Rs. 264.9m; FY21: Rs. 181.4m; FY20: Rs. 246.5m) in 9MFY23 mainly due to higher benchmark rates and elevated total borrowing levels to finance costly working capital needs.
- Share of profit (9MFY23: Rs. 4.5m; FY22: Rs. 332.3m) from long-term investment in Husnain Textile Mills (Pvt.) Limited provided cushion to the profitability profile of the Company, barring 9MFY23.
- Due to the aforementioned along with absence of share of profit from associate in 9MFY23, net margins of the Company also significantly weakened to 1.2% (FY22: 16.3%, FY21: 21.0%).
- Given uncertain macroeconomic environment, improving margins will be critical from a ratings perspective.

Weakening noted in liquidity profile

- With lower profits in 9MFY23, Funds from Operation (FFO) of the Company decreased to Rs. 361.1m (FY22: Rs. 1,367.2m; FY21: Rs. 962.2m). In line with the subdued profitability profile and elevated quantum of debt, cash flow coverages against outstanding obligations have also witnessed weakening in the review period.
- FFO to Total Debt and FFO to Long-Term Debt declined to 17% (FY22: 80%; FY21: 102%) and 50% (FY22: 138%; FY21 134%) respectively during 9MFY23.
- While Debt Servicing ratio (DSCR) remain at adequate levels for the assigned ratings, the same reduced on a timeline basis to 1.47x (FY22: 3.97x; FY21: 4.61x) during 9MFY23.
- Current ratio as of end-Mar'23 stood at 1.39x, which is fairly above the minimum threshold level. Short-term borrowing coverage is deemed adequate at 202% at end-Mar'23.
- Aging profile of trade debts is considered fair with 90% of outstanding trade receivables due within five months.
- Ratings remain dependent on improvement of the liquidity indicators as per the benchmarks for the assigned ratings.

Sound capitalization profile for the assigned ratings

- Tier-I Equity base of the company accumulated to Rs. 4.9b (FY22: Rs. 4.8b; FY21: Rs. 3.4b) by end-Mar'23 through profit retention.
- The debt profile comprises a mix of long-term (33%) and short-term borrowings (67%) at end-Mar'23.
- Growth in long-term debt over the years was to finance spindle expansion and BMR initiatives.
- Short-term borrowings increased to Rs. 1,926.3m (FY22: Rs. 714.6m; FY21: Rs. 232.4m) at end-9MFY23 to meet higher working capital requirements in lieu of rising rising raw materials costs.
- With increase quantum of debt (9MFY23: Rs. 2.9b; FY22: Rs. 1.7b; FY21: Rs. 1.0b) being greater than profit retention in the review period due to increased cash conversion cycle, gearing and debt leverage ratios have depicted an uptick on a timeline basis.
- While capitalization levels have increased, gearing and leverage indicators remain at comfortable levels and were reported at 0.59x (FY22: 0.35x; FY21: 0.28x) and 0.84x (FY22: 0.50x; FY21: 0.38x) respectively, at end-9MFY23.
- Maintaining debt leverage at levels that commensurate with the benchmarks for the assigned ratings will be important.

REGULATORY DISCLOSURES Appendix I

Name of Rated Entity	H.A Fibres (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				
02/10/2023	A-	A-2	Stable	Maintained
23/06/2022	A-	A-2	Positive	Reaffirmed
06/07/2021	A-	A-2	Positive	Maintained
04/24/2020	A-	A-2	Rating-Watch Developing	Maintained
04/03/2019	A-	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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Due Diligence Meetings Conducted

	Name	Designation	Date
1.	Mr. Muhammad Ismail	Chief Financial Officer	24th July 2023
2.	Mr. Muhammad Naeem	Finance Manager	24th July 2023