RATING REPORT

Indus Home Limited

REPORT DATE:
August 1, 2022

RATING ANALYSTS:
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RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Date	*August 1, 2022*		*May 25, 2021*	
Rating Outlook	Stable		Positive	
Rating Action	Maintained		Maintained	

COMPANY INFORMATION	
Incorporated in 2006	**External auditors:** M/s EY Ford Rhodes Chartered Accountants
Public Unlisted Company	**Chairman:** Mr. Mian Mohammad Ahmed
Key Shareholder (s):	**CEO:** Mr. Irfan Ahmed
Indus Dyeing and Manufacturing Company Limited ~ 99.99%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria Methodology – Industrial Corporates (August 2021) https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Indus Home Limited

OVERVIEW OF THE INSTITUTION

Indus Home Limited (IHL), a wholly owned subsidiary of Indus Dyeing and Manufacturing Company Limited (IDMC), was incorporated in Pakistan as a Public Unlisted Company on May, 2006. IHL is involved in the business of griege, terry towel and other home textile products.

Profile of Chairman

Mr. Mian Mohammad Ahmed laid the foundation of the Indus group of companies by setting up cotton ginning factories and later on establishing textile spinning. He is responsible for strategic and corporate planning.

Profile of CEO

Mr. Irfan Ahmed is the CEO of the company; possess BSC Textile Engineering Degree from USA and a vast knowledge of Terry Towel Industry with ten years' experience. He is a director in IDMC and Sunrays Textile Mills Limited.

RATING RATIONALE

IHL Operations & Sponsor Profile

Indus Home Limited (IHL), a wholly-owned subsidiary of Indus Dyeing and Manufacturing Company Limited (IDMC), is a part of Indus Group of Companies which is one of the well-established textile groups in the country with an annual turnover of over US$300m. The group has an extensive experience of more than six decades and operates through five different entities. Alongside, the group has also invested in a wind power project of 50MW. IDMC is the flagship company in the group.

Headquartered in Karachi, IHL is primarily engaged in the production and export of griege and finished terry cloth and other textile products. At present, the company's operations encompass spinning, weaving, dyeing and fabrication which are carried out through a towel manufacturing and finishing facility, located in Raiwind near Lahore. All production facilities are operating at high capacity utilization levels. Power requirement of 4.5MW is met through two sources; national grid and a gas-based captive power plant.

During FY21, the company invested in 1000 units of long-term TFC of HBL (Rs. 100m), acquired 24.18% shares of Indus Lyallpur Limited (Associated company) by investing Rs. 450m. Exposure in Indus Lyallpur Limited is planned to be sold to Indus Dyeing Company by FY23.

Continued BMR activities, including backward integration of operations expected to improve operational efficiency and lower the cost of production, going forward.

In the previous year, the company replaced existing looms with newer air-jet efficient ones. During the period under review, 10,000 kg capacity was added in the dyeing and processing segment with enhancement noted in the stitching capacity. More importantly, establishment of the spinning unit has commenced operations in the end of FY22. The facility having a total of 2880 rotors became operational in May'22, with a capacity to produce 510 bags of yarn on a daily basis. Around 50% of the yarn output will be utilized in-house, whereas the rest will be sold in the local market. This backward integration of operations is expected to help reduce cost of production and improve gross margins going forward. Overall capacity utilization of the plant is on the higher side on a timeline basis. Going forward, management plans to undertake routine BMR activities to enhance efficiency which is expected to be financed by internal cash generation.

	FY20	FY21	6MFY22
No of Looms Installed	132	132	132
No of Looms Worked	132	132	132
No of Working days	360	360	180
No of Shifts Per day	3	3	3
Installed Capacity of Towel (Lbs.)	28,258,008	28,253,465	14,126,733
Actual Production of Towel (Lbs.)	19,706,034	24,945,735	12,251,665
	70%	88%	87%

Key Rating Drivers

Business risk profile is supported by industry wide growth in exports over the last year

Surge in textile exports has continued in FY22 as COVID-19 related restriction are lifted across the globe. In the period July-April 2022, businesses in Pakistan earned $16.0b from the export of textile and apparel products, an increase of 26% year-on-year. Category wise, knitwear was the commodity that contributed the most, followed by ready-made garments and bed wear. With an investment plan of $3.5b in place for the sector, exports are projected to reach a figure of $21b for FY22, which will be a 40% increase over the last year.

The margins of textile companies have broadly depicted improvement despite the uptick in raw material costs, given that the same was offset by exchange rate movement. Nevertheless, higher raw material pricing has increased the working capital requirements for the companies in the sector, which is likely to weigh on the liquidity of textile players. Due to relatively high demand in comparison to the supply, cotton prices in Pakistan depicted a rise of around 80% in the first 11 months of FY22; however, a sharp decline has been observed since then. The order book for the industry is expected to remain adequate in the ongoing year easing our business risk concerns. However, risk of higher interest costs for highly leveraged companies is considered to be on the higher side.

Double-digit growth in topline post-COVID-19 contributed by higher average selling prices and volumes. With plans on adding new retail clientele and current order pipeline, sales revenue is expected to sustain this growth momentum, going forward.

During FY21, revenue of the company recorded a double digit growth of 29% year-on-year. The uptick was mainly attributable to volumetric growth in sales coupled with higher average selling price due to dollar devaluation. Sales revenue further grew in 11MFY22 registering an annualized growth of 39% year-on-year primarily attributed to local currency devaluation. More than 95% of sales revenue comprises direct exports. Product portfolio primarily consisted of different types of towels, which accounted for more than 95% of total revenue. Around 15% of the sales revenue is catered towards institutional clients (hospitals and hotels) with the remaining 85% catered to retail clients.

Over time, IHL has established its presence in around 35 countries across Europe, North America, and Asia, which has helped to achieve geographic diversification. Major concentration is in the European market (83% of total sales revenue in FY21) followed by USA (17% of sales in FY21). Customer concentration remained a bit on the higher side with top 5 export customers contributing 64% of the total revenue in FY21. These customers include Cleland Mciver Limited (UK), Westpoint Home LLC (USA), Desipro Pte Ltd (Singapore), Pem America Inc (USA), and Kaufland (Germany). Comfort of client concentration is drawn from long-term relationships with these clients. Going forward, management envisages sales growth through existing clients as well as plans to add new retail clients in Europe and USA such as Lidl, Aldi etc. As per management, sales revenue may slowdown in the short term as major retailers want to off-load its current inventory and then place orders.

Profitability indicators have trended downwards on a timeline basis due to elevated input costs. Improving the same is considered important from a ratings perspective.

Although sales revenue depicted growth on a timeline basis, gross margins of the company have been impacted by rising input costs. There has been a substantial increase in the prices of raw cotton, yarn and fuel prices over time. In the case of imported raw material, currency depreciation has further increased cost of production. Furthermore, with the company locking prices with customers in America for three months and locking prices for European markets for a season, price adjustments are not in tandem with cost escalations. Consequently, gross margins of IHL decreased and were reported at 10.0% for 11MFY22 (FY21: 10.4%, FY20: 17.7%). Overall profitability profile was supported by higher other income from exchange gain and lower other operating expenses owing to absence of compensation against license agreement. With elevated debt levels to finance backward integration and to fund working capital needs, higher interest costs may cause a drag on the overall thin net margins of 1.5% (FY21: 4.9%, FY20: 7.5%) in 11MFY22. Profit levels were lower in 11MFY22 due to higher finance charges and lower other income.

As per management, backward integration of operations is likely to offer better control over input costs and consequently improve margins going forward. Materialization of the same is considered important from a ratings perspective.

Stressed liquidity profile.

Due to a fall in profit earned for the year and a substantial increase in the quantum of debt, cash flow coverages of the entity have fell at end-FY21. However, some recovery was observed during 11MFY22. At end-11MFY22 FFO to Total Debt, FFO to Long Term Debt, and Debt Servicing Coverage were reported at 5.9% (FY21: 4.5%, FY20: 20.5%), 14.1% (FY21: 11.0%, FY20: 43.9%), and 2.0x (FY21: 2.55x, FY20: 3.74x), respectively. Stock in trade and trade debts also provide borderline coverage against short-term borrowings at 126% (FY21: 104%) at end-May'22. Even though inventory level was reported a bit on the higher side, comfort is drawn from the fact that orders equivalent to 75-80% of the capacity are booked for the next three months. Stress in liquidity profile is also visible through liquidation of short-term investments in FY22. Some comfort from sale of exposure in Indus Lyallpur may be seen in the ongoing year. Going forward, achieving higher cash flows on the back of improved projected profitability will be important to maintain the ratings at current levels.

Leverage indicators have increased over time to finance backward integration and working capital needs.

To finance BMR projects and backward integration in the spinning segment, the company withdrew significant amount of long-term loan over the period July'20-May'22. Furthermore, the quantum of short-term debt also increased to meet additional working capital needs. As a result of the same, at end-11MFY22, leverage and gearing ratios were reported at 2.1x (FY21: 1.6x, FY20: 0.8x) and 1.9x (FY21: 1.3x, FY20: 0.6x) respectively. Going forward, further drawdown of short-term debt is expected, for which the management is planning to expand the quantum of available borrowing lines. Improving gearing and leverage levels over the rating horizon through meeting projected profit levels and retaining the same is considered important from a ratings perspective.

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	Indus Home 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				
	8/1/2022	A-	A-2	Stable	Maintained
	5/25/2021	A-	A-2	Positive	Maintained
	4/29/2020	A-	A-2	Rating Watch - Developing	Maintained
	5/8/2019	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 Meeting Conducted	**Name**	**Designation**	**Date**		
	Mr. Ahmed Fraz	CFO	June 20, 2022		
	Mr. Gohar Mubahsir	GM Marketing	June 20, 2022		