RATING REPORT

Akram Cotton Mills Limited (ACML)

REPORT DATE:
February 27, 2024

RATING ANALYSTS:
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Rating Category	Initial Rating	
	Long-term	Short-term
Entity	BBB	A-2
Rating Outlook	Stable	
Rating Action	Initial	
Rating Date	*February 27, 2024*	

COMPANY INFORMATION

Incorporated in 1993	**External auditors:** Yousuf Adil Chartered Accountants
Public Limited Company (Unlisted)	**Chairman of the Board:** Mr. Ali Pervaiz
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Ali Pervaiz
Mr. Ali Pervaiz – 76.24%	
Mrs. Shaista Pervaiz – 21.96%	

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

Akram Cotton Mills Limited (ACML)

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Akram Cotton Mills Limited is a spinning mill engaged in the production of 100% carded and combed cotton yarn. The Company commenced operations in 1993 as (unlisted) Public Limited Company. Registered office of the Company is in Lahore while manufacturing unit is located in Pattoki, Punjab.

Profile of Chairperson of the Board & CEO

Mr.Ali Pervaiz is the Chairman of board and CEO of the company. He has been working as the CEO of the company for the last seventeen years. Previously he was engaged in the banking sector. He has also served as the Chairman of APTMA Punjab.

Corporate Profile

Akram Cotton Mills Limited ('ACML or 'the Company') is engaged in the business of manufacturing and sale of yarn. It specializes in the production of 100% carded and combed cotton yarn, with a count range of 20/1 to 30/1, mainly for hosiery purposes. The Company has also introduced combed cotton yarn to its product line.

Its Head Office is located in Block-M, Gulberg III, Lahore and the operational mill is situated in Pattoki, Punjab, at a distance of 90-km from Lahore on the Lahore-Multan National Highway. ACML has been providing yarn variants, under the brand name 'Anmol', 'Super Anmol' and 'Mahnoor,' mainly to local customers. The main raw material, cotton, is procured from the local market. Shareholding of the Company is held with sponsoring family, which is actively involved in the business operations.

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.

The spinning sector in Pakistan comprises ~407 spinning mills, which include both composite units and spinning units. This industry exhibits a competitive market structure with a large number of players producing a relatively homogenous product.

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. However, there is optimism as an anticipated bigger cotton crop in FY24 is expected to alleviate some pressure on input costs and margins.

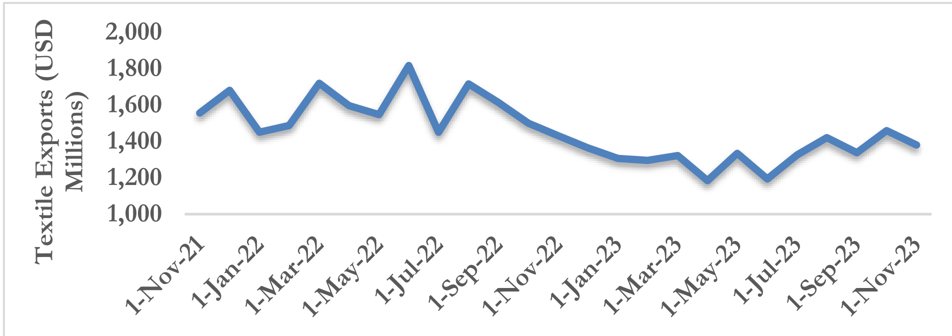

Figure 1: MoM Textile Exports (In USD' Millions)
Source: SBP

Operational Update

Slow demand led to a reduction in production levels in FY23

Table 1: Production Data

	FY21	FY22	FY23	1HFY24
No. of Spindles	23,220	23,220	23,220	23,220
Production Capacity mln Kgs 20/1	10.29	10.29	10.29	5.15
Actual Production mln Kgs 20/1	10.08	10.25	5.89	5.25
Capacity Utilization	***97.94%***	***99.59%***	***57.24%***	***101.94%***

Facing slow demand and unavailability of raw material in FY23 amid floods impact and import restrictions, the mill remained closed for 100 days during FY23, resulting in a fall in the actual production to 5.89 mln Kgs (FY22: 10.25 mln Kgs FY21: 10.08 mln Kgs). Consequently, the capacity utilization level stood at 57.24%, registering a decline of ~42.4% as compared to FY22.

During 1HFY24, the production reached to 5.25 mln Kgs, backed by demand recovery, while the available capacity was 5.15 mln Kgs, resulting in the capacity utilization to stand at 101.94%. Going ahead, the management expects operational efficiency to commensurate with historical benchmarks.

Key Rating Drivers

Reduced topline resulted in weak profitability and subdued margins in FY23

In FY23, the net revenue decreased to Rs. 2.99 bn (FY22: Rs. 4.45 bn), owing to a volumetric decline of ~42% in product sales leading to a fall in the gross profit to Rs. 176 mn (FY22: Rs. 643 mn). Resultantly, the gross margin contracted to 5.88% (FY22: 14.46%).

The profitability pressure further cascaded downward as evident from the drop in operating profit to Rs. 78.5 mn (FY22: 494.2 mn), despite the Company's endeavors to arrest fall in profitability through control on the selling, distribution, and administrative overheads. Rise in finance charges by ~66% to Rs. 190.5 mn (FY22: Rs. 114.6 mn) mainly owing to increased interest rates, further dented the profitability. Resultantly, the Company incurred a loss for the year of Rs. 66 mn.

However, with the recovery in net sales to Rs. 2.95 bn, during 1HFY24, both the gross profit and net profit improved to Rs. 285 mn and Rs. 75 mn, with corresponding increase in gross and net margins to 9.63% and 2.53%. The management expects the rebound in sales to continue for the rest of FY24 owing to higher demand, and margins to streamline driven by better procurement rates.

Higher short-term borrowings, necessitated by the need to meet working capital requirements, are influenced by high raw material prices amidst a shortage of crops. The same contributes to driving leverage indicators up

In FY23, the Company's short-term borrowings increased to Rs. 545.3 mn (FY22: 82.6 mn) to meet higher working capital requirements which were influenced by rising raw material costs amid shortage of crop and a prolonged cash conversion cycle of 104 days (FY22: 55 days). As a result, the total debt rose to Rs. 771 mn (FY22: 398.3 mn), pushing up both gearing and leverage ratios to 0.90x and 1.21x (FY22: 0.43x and 0.77x) respectively.

In 1HFY24, short-term borrowings increased further to Rs. 1.1 bn (FY23: Rs. 545.3 mn), as the Company built up raw cotton inventory in anticipation of unavailability of cotton. Higher borrowings further dented the gearing and leverage ratios to 1.38x and 1.89x respectively. Going ahead, improving the capital structure will be an important factor from the ratings perspective.

Cash flows deteriorate on account of profitability pressure

In FY23, the Funds from Operations (FFO) turned negative to Rs. 75.93 mn (FY22: Rs. 383 mn), primarily attributed to the Company incurring a net loss of Rs. 66 mn. This resulted in the Debt Service Coverage Ratio (DSCR) deteriorating to just 0.22x (FY22: 2.36x). The Company's liquidity profile was distressed as to make up for cash flow shortfall in FY23, ACML resorted to additional short-term borrowing of Rs. 463 mn, which was used to the extent of Rs. 209 mn for working capital purposes and the rest for debt servicing and other operational requirements. However, the current ratio of 1.52x (FY22: 2.63x) provided some comfort to the liquidity profile.

In 1HFY24, with the recovery in profitability, FFO turned positive, amounting to Rs. 120 mn (FY23: Rs. -75.93 mn). As a result, the DSCR improved to 1.47x (FY23: 0.22x), even though it is still lower as compared to historical levels (FY22: 2.36x FY21: 4.15x).

FINANCIAL SUMMARY					*(amounts in PKR millions)*
BALANCE SHEET	**Jun'20**	**Jun'21**	**Jun'22**	**Jun'23**	**Dec'23**
Fixed Assets	478	439	649	637	614
Stock-in-Trade	793	467	603	805	1,493
Trade Debts	84	187	287	289	385
Cash & Bank Balances	23	25	28	21	25
Total Assets	1,485	1,262	1,657	1,885	2,686
Trade and Other Payables	145	157	181	162	411
Long Term Debt	180	228	316	226	193
Short Term Borrowings	600	45	83	545	1,086
Total Debt	779	273	398	771	1,278
Total Equity (excluding surplus)	429	731	935	854	929
INCOME STATEMENT	**FY20**	**FY21**	**FY22**	**FY23**	**1HFY24**
Net Sales	2,184	3,331	4,445	2,999	2,957
Gross Profit	141	540	643	176	285
Operating Profit	63	417	475	78	209
Finance Cost	123	77	115	190	101
Profit (Loss) Before Tax	(60)	350	364	(112)	108
Profit (Loss) After Tax	(87)	303	239	(66)	75
RATIO ANALYSIS	**FY20**	**FY21**	**FY22**	**FY23**	**1HFY24**
Gross Margin (%)	6.5%	16.2%	14.5%	5.9%	9.6%
Net Margin (%)	-4.0%	9.1%	5.4%	-2.2%	2.5%
Net Working Capital	123	481	609	421	466
FFO	-24	366	383	-76	120
FFO to Long Term Debt (%)*	(0.13)	1.61	1.21	(0.34)	1.24
FFO to Total Debt (%)*	(0.03)	1.34	0.96	(0.10)	0.19
Debt Servicing Coverage Ratio (x)*	0.62	4.15	2.36	0.22	1.47
Gearing (x)	1.82	0.37	0.43	0.90	1.38
Leverage (x)	1.92	0.73	0.77	1.21	1.89
Current Ratio (x)	1.57	2.55	2.63	1.52	1.29
(Stock in Trade+ Trade Debts)/STD	1.50	14.39	10.77	2.01	1.73
ROAA (%)*	-6.6%	22.1%	16.3%	-3.7%	6.6%
ROAE (%)*	-18.1%	52.2%	28.6%	-7.4%	16.8%

**Annualized*

REGULATORY DISCLOSURES Appendix II

Name of Rated Entity	Akram Cotton Mills Limited
Sector	Textiles
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				
27 Feb, 2024	BBB	A-2	Stable	Initial
05 Jul, 2023	-	-	-	Withdrawn
17 Jun, 2022	BBB	A-2	Stable	Reaffirmed
29 Jun, 2021	BBB	A-2	Stable	Maintained
Apr 24, 2020	BBB	A-2	Rating Watch-Negative	Maintained
Dec 16, 2019	BBB	A-2	Stable	Upgrade
Jul 03, 2019	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.
Disclaimer	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. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Javed Ilyas	Manager Accounts and Internal Controls	24-January-2024