RATING REPORT

Chakwal Textile Mills Limited (CTML)

REPORT DATE:
April 02, 2021

RATING ANALYSTS:

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RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	BBB-	A-2	BBB-	A-2
Rating Outlook	Stable		Rating Watch - Negative	
Rating Date	*April 02, 2021*		*April 27, 2020*	

COMPANY INFORMATION

Incorporated in 1979	**External auditors:** Horwath Hussain Chaudhury & Co. Chartered Accountants
Public Limited Company (Unlisted)	**Chairman of the Board:** Mrs. Sadaf Jawed
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mrs. Sadaf Jawed
Mrs. Sadaf Jawed – 63.48%	
Mrs. Andleeb Kausar – 36.52%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (May 2019)
https://www.vis.com.pk/kc-meth.aspx

Chakwal Textile Mills Limited (CTML)

OVERVIEW OF THE INSTITUTION

Chakwal Textile Mills Limited was incorporated on September 16, 1979 under the Companies Act, 1913 (now Companies Act, 2017). Registered office of the company is in Lahore while manufacturing unit is located in Chakwal.

Profile of Chairperson of the Board & CEO

Mrs. Sadaf Jawed has over 14 years' of experience in textile sector. She joined CTML as the CEO of the company in 2018 and is also serving as Chairperson on the Board of Directors.

RATING RATIONALE

Chakwal Textile Mills Limited (CTML) Public Limited (unlisted) Company primarily engaged in the business of textile spinning. The company produces different counts of polyester viscose yarn. The company has been providing PV yarn products mainly to local customers. The main raw material 'Polyester' is procured from the local market while other raw material 'viscose' is imported mainly from SABIC in Saudi Arabia. The cumulative power requirement of the unit is 2.5 MW which is met through WAPDA connection only.

Product Portfolio – focused on manufacturing of Coarse Count Polyester Viscose Yarn

CTML manufactures coarse count polyester viscose yarn of different ranges and is mainly used to produce wash & wear fabric for shalwar suits.

Spinning Products			
Yarn Type	**Count Range**	**Composition**	**End Use**
Coarse Count Polyester Viscose Yarn	26 PV	90% Polyester : 10% Viscose	Wash & Wear fabric
	36 PV	90% Polyester : 10% Viscose	
	45 PV	90% Polyester : 10% Viscose	
	65 PV	90% Polyester : 10% Viscose	
	18 PVB	80% Polyester : 20% Viscose	
	30 PVB	80% Polyester : 20% Viscose	
	20 MVS	65% Polyester : 35% Viscose	
	30 MVS	65% Polyester : 35% Viscose	

Operational Capabilities & Performance – Decrease in capacity utilization on account of production halt of 45 days due to imposition of Covid-19 lockdown

At end-FY20, CTML had 22,512 spindles with production capacity to produce 12.22m kg per annum of coarse count polyester viscose yarn at end-FY20. The company's capacity utilization went down to 68.72% (FY19: 92.5%) in FY20 on account of production halt of 45 days due to imposition of Covid-19 lockdown. The company did not carry out any CAPEX during FY20; however, Capex of Rs. 160.0m is planned in the ongoing year to finance BMR of the spinning facility *(Saurer and Murata Vortex Machinery*). The company follows the practice of keeping raw material inventory of polyester up to 15 days since it is readily available in the local market from suppliers like Ibrahim Fibers, Rupali Polyester, etc., while about 3 months inventory of viscose is carried by the company depicting exchange rate volatility risk.

Recovery in industry wide exports post ease in COVID-19 lockdown measures support business risk profile of the company.

With the objective of enhancing exports to support the economy, the Government of Pakistan (GoP), has provided incentives in the form of subsidized utility tariffs, low interest rates (EFS, LTFF and TERF) and sales tax refund to the textile industry. The textile policy 2020-25 has laid emphasis on fixed electricity and gas tariff for the next 5 years till 2025 at US cents 7.5 per KWh and USD 6.5 per MMBTU, respectively. Moreover, the limits of subsidized (LTFF) financing have been enhanced under this policy to facilitate exporters. Initiatives are also being undertaken in order to increase production and yield of cotton. However, the imposed sales tax has negatively impacted the textile industry. Even though impact of Covid-19's third wave remains elevated, we expect the order book for the industry to remain strong in the ongoing year, easing our business risk concerns.

Topline of the company fell by 27.7% during FY20 on account of lockdown imposed due to Covid19. Going forward, sales are expected to escalate on account of adequate orders in pipeline, reduction in imports due to currency devaluation and projected increase in average selling prices.

Sales revenue has decreased to Rs. 1.5b (FY19: Rs. 2.0b; FY18: Rs. 1.6b) during FY20 largely provided by a 28% decline in quantity sold on account of Covid19 in the outgoing year. Higher sales tax amounting to Rs. 260.7m (FY19: Rs. Nil) also impacted the reported revenue in FY20. Sales mix entirely comprises local sales with a diversified customer base. During 1HFY21, the company reported sales revenue to the tune of Rs. 987.5m depicting an uptick in order pipeline. Going forward, sales are expected to escalate on account of adequate orders in pipeline, projected reduction in imports due to currency devaluation and increase in average selling prices.

Overall profitability profile of the company was impacted by higher raw material prices led by currency devaluation and disrupted production cycle due to Covid19 during FY20. During 1HFY21, gross and net margins of the company improved to 11.7% and 8.7%, respectively and are projected to witness continued improvement going forward on the back of projected gradual increase in demand and average selling prices.

Gross margins of the company declined to 3.9% (FY19: 5.6%; FY18: 2.7%) during FY20 largely on the back of higher raw material prices led by currency devaluation and disrupted production cycle due to Covid19. Overall operating expenses decreased due to lower loss allowance on receivables. Finance charges witnessed an increase to Rs. 2.3m (FY19: Rs. 1.8m; FY18: Rs. 4.1m) in FY20 due to higher rates until the last quarter of the outgoing year. Despite lower tax charge of Rs. 3.4m (FY19: Rs. 30.8m), net margins slightly declined to 1.1% (FY19: 1.8% FY18: 1.7%) during the same period. During 1HFY21, gross and net margins of the company improved to 11.7% and 8.7%, respectively and are projected to witness continued improvement going forward on the back of projected gradual increase in demand and average selling prices.

Liquidity profile of the company is considered adequate with satisfactory cash flow coverage of outstanding obligations. Liquidity indicators are expected to further strengthen in line with projected increase in overall profitability.

In absolute terms, Funds from Operations (FFO) decreased to Rs. 22.5m (FY19: Rs. 93.0m) on account of lower overall profitability during FY20. Debt Service Coverage Ratio (DSCR), FFO to total debt of the company are considered strong. Inventory and trade debts provide healthy coverage for short-term debt obligations while current ratio was reported above 1(x). Going forward, liquidity profile of the company is expected to further strengthen in line with projected increase in overall profitability.

In FY20, leverage indicators have trended downwards on account of smaller debt base. Given plans to drawdown debt to finance BMR, capitalization indicators are expected to trend upwards; however the same are projected to remain within manageable levels.

On account of higher profit retention, net equity of the company was reported higher at Rs. 384.1m (FY20: Rs. 302.4m; FY19: Rs. 299.2m) at end-December'20. Total debt carried on balance sheet amounted to Rs. 9.2m at end-Dec'20; where 100% of the total debt is short-term in nature. With a smaller debt base, leverage indictors have remained on lower side with gearing and debt leverage reported at 0.02x (FY20: 0.05x, FY19: Nil) and 0.57x (FY20: 0.82x, FY19: 0.91x) at end-1HFY21, respectively. Leverage indicators have trended downwards on account lower additional debt drawdown. Given plans to drawdown debt to finance BMR (estimating cost of Rs.160m); capitalization indicators are expected to trend upwards; however the same are projected to remain within manageable levels.

Corporate Governance depicts room for improvement.

The Board of Directors of CTML comprises three members; representatives of the sponsoring family. The senior management team of the company comprises resources from the textile sector having relevant experience. The company has Visual Basic based ERP system in place. CTML has no internal audit department while “Horwath Hussian Chaudhury & Co.” are the external auditors of the company.

Chakwal Textile Mills Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**1HFY21**
Fixed Assets	348.8	347.8	337.2	350.3
Stock-in-Trade	36.7	52.2	87.0	117.0
Trade Debts	6.4	35.9	6.5	11.6
Cash & Bank Balances	12.1	1.3	14.0	16.1
Total Assets	538.0	571.3	551.8	601.7
Trade and Other Payables	118.5	130.0	116.6	83.9
Long Term Debt	27.7	-	-	-
Short Term Debt	10.4	-	13.6	9.2
Total Debt	38.1	-	13.6	9.2
Total Equity	265.6	299.2	302.4	384.1
Total Liabilities	272.3	272.1	249.4	217.6
Paid Up Capital	135.0	135.0	135.0	135.0
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**1HFY21**
Net Sales	1,574.1	2,019.2	1,460.0	987.5
Gross Profit	41.8	112.8	57.6	115.1
Operating Profit	14.1	68.5	21.3	102.3
Profit Before Tax	10.0	66.6	19.0	100.5
Profit After Tax	27.2	35.8	15.6	85.6
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**	**1HFY21**
Gross Margin (%)	2.7%	5.6%	3.9%	11.7%
Net Margin (%)	1.7%	1.8%	1.1%	8.7%
Net Working Capital	8.4	45.9	58.7	139.7
Trade debts/Sales	0.4%	1.8%	0.4%	0.6%
FFO	26.7	93.0	22.5	96.1
FFO to Total Debt (%)	70.1%	-	165.1%	2082.3%
FFO to Long Term Debt (%)	96.4%	-	-	-
Debt Servicing Coverage Ratio (x)	1.3	3.3	260.8	51.73
Current Ratio (x)	1.0	1.3	1.4	2.3
Stock+Trade Debts/STD	414.4%	NA	687.2%	1392.6%
Gearing (x)	0.14	-	0.05	0.02
Leverage (x)	1.03	0.91	0.82	0.57
ROAA (%)	4.9%	6.5%	2.8%	29.7%
ROAE (%)	11.2%	12.7%	5.2%	49.9%

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	Chakwal Textile Mills Limited
Sector	Textiles
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings
Rating History	
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
April-02-21	BBB-	A-2	Stable	Maintained
April-27-20	BBB-	A-2	Rating Watch-Negative	Maintained
June-19-19	BBB-	A-2	Stable	Initial

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Khawaja Aman	Director	17-Mar-2021
Mr. Zahid Kiyani	CFO	17-Mar-2021