

RATING REPORT

Lucky Textile Mills Limited

REPORT DATE:

November 22, 2019

RATING ANALYST:Narendar Shankar Lal
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RATING DETAILS

Rating Category	Initial Rating	
	Long-term	Short-term
Entity	AA-	A-1
Rating Outlook	Stable	
Rating Date	November 18, 2019	

COMPANY INFORMATION

Incorporated in December 2011	Internal auditors: EY Ford Rhodes, Chartered Accountants
	External auditors: Deloitte Yousuf Adil & Co., Chartered Accountants
Public Unlisted Company	Chairman: Mr. Muhammad Yunus Tabba
Key Shareholders (with stake 5% or more):	CEO: Mr. Jawed Yunus Tabba
Y.B. Holdings (Pvt) Ltd – 99.99%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria *Industrial Corporates (May 2016)*
<http://www.vis.com.pk/docs/Corporate-Methodology-201605.pdf>

Lucky Textile Mills Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE
<p><i>Lucky Textile Mills Limited (LTML) was incorporated in December 2011 as a Public Unlisted Company. The Company had taken over the assets and liabilities of Lucky Textile Mills which operated as a partnership firm registered in the year 1983 under the Partnership Act, 1932. Principal activity of the company includes manufacturing and export of fabric, home textile and apparel products.</i></p> <p>Profile of CEO <i>Mr. Javed Yunus Tabba has a rich experience in the Textile industry. He is also managing the Real Estate Project LuckyOne, which is the largest mall in Karachi. He is also extensively engaged in community welfare projects which include Aziz Tabba Foundation.</i></p>	<p>Lucky Textile Mills Limited (LTML) is a part of the Yunus Brother Group (YBG) being a wholly owned subsidiary of YB Holdings (Pvt.) Limited. LTML is a composite textile mill engaged in weaving, processing, and stitching of various kinds of textile products. Sales of the company can be classified into three categories: home textiles, garments and fabric.</p> <p>The company carries out its activities through its weaving, stitching and processing units.</p> <p>Weaving: The company has a mix of sulzer and airjet looms yielding installed capacity of 63 million meters per annum. The company is operating at almost full capacity in the weaving segment on account of sizeable increase in demand. In view of this scenario, the management plans to install additional 72 airjet looms in FY20.</p> <p>Processing: Processing unit of the company is located in Landhi area. Total installed capacity of this segment is 65m meters per annum. Further expansion is also planned in this segment going forward.</p> <p>Stitching: Total stitching capacity of LTML is 52.4m pieces per annum depending on the product mix. The management has already incurred capex in order to expand stitching capacities during the past few years</p> <p>Investments: Around 28% of the total asset base of the company comprises investments in various companies at end-FY19. LTML has investments in ICI Pakistan Limited, Lucky Holdings Limited, Yunus Energy Limited, KIA Lucky Motors Pakistan Limited, Feroze 1888 Mills Limited, Lucky Wind Power (Pvt.) Limited, Lucky Entertainment (Private) Limited, Lucky Textile Holdings (Pvt.) Limited and Interloop Limited. LTML will also acquire majority shareholding in a wind power project, which will be entirely funded through internal cash flows. Dividend income from investments and share of profit from associates has regularly supported overall profitability of LTML over the years. The management expects dividend income inflow to continue in future from its existing dividend paying investments because the companies are generating profits and are in mature stage of operations.</p> <p>Key Rating Drivers:</p> <p>Strong Sponsor Profile</p> <p>LTML is a group company of YBG, which is a reputable conglomerate with strong financial profile and has presence in diversified sectors including power generation, building materials, real estate, textile, chemicals, pharmaceuticals, food, entertainment and automotive sectors.</p>

Business risk profile supported by favourable industry dynamics and greater opportunities for growth

Figure 4: Pakistan Textile Exports (Source PBS)

(Mn Tons, USD Mn)	FY18			FY19		
	Volume	Value	USD/Unit	Volume	Value	USD/Unit
Raw Cotton	35	58	1.66	12	20	1.67
Yarn	518	1,371	2.65	427	1,125	2.63
Non-Value Added	553	1,429	2.58	439	1,145	2.61
Knitwear	117	2,733	23.36	133	2,909	21.9
Bedwear	359	2,261	6.30	376	2,262	6.02
Towels	189	788	4.17	194	786	4.05
Readymade Garments	40	2,581	64.53	50	2,657	53.14
Value Added	705	8,362	11.86	753	8,612	11.44

Total textile exports from Pakistan depicted strong growth during FY18 with increase being driven by the value added segment. While pace of growth has slowed down in FY19 with only 6.8%/3.0% growth registered in volume/value terms in value added textile exports, VIS expects double digit growth in textile exports over the medium term as impact of planned and ongoing capacity expansions and supportive government policies kicks in. Supportive government policies for the textile sector are evident from availability of electricity at competitive rates, sizeable rupee depreciation over the last 18 months, availability of funding lines at concessionary rates, continuation of drawback on local taxes and levies (DLTL) regime and commitment for timely release of outstanding refunds. Moreover, improving perception (opening of visa regimes) and law and order situation is facilitating buyers to visit the Country and place orders. Major buyers are also looking to diversify their procurement from China (ongoing trade war between USA and China and increasing cost of doing business in China), which is already resulting in gradual increase in orders to Pakistan. Nonetheless, key business risk factors include country's macro-economic challenges, slow-down in major markets, inability to pass on increase in input costs, increase in competition from other regional countries and local players and exit of a major customer. Recent 31% hike in gas prices by the government coupled with downward trend witnessed in prices in dollar terms may put pressure on the margins of textile companies in the short term.

Topline has registered healthy growth on timeline basis with growth momentum projected to continue over the rating horizon. While concentration risk is on the higher side, comfort is drawn from long-term association with major clients

Sales of the company primarily include export sales, which comprised 97% of gross revenues on average during the last 4 years. Net sales of the company have grown at a Compound Annual Growth Rate (CAGR) of 13.1% during the last three years. Growth in topline was achieved on the back of higher average selling price in FY19. In terms of product-wise break-up of sales mix, over three fourth of the sales revenue emanates from made-ups category primarily comprising bed sheets, comforters, pillow case and curtains. Apparels segment constitutes the second largest

proportion of overall sales of the company. Going forward, home textiles (madeups and knitted madeups) will continue to form the largest segment in overall sales but proportion of apparel segment is expected to increase on timeline basis due to greater competition from local players in the home textile segment.

Client concentration is considered to be on the higher side. However, the concentration risk is partly mitigated due to long term association with these clients. Going forward, topline will be driven primarily by volumetric growth due to increase in demand.

Profitability profile has strengthened during the ongoing year due to improved margins, and sizeable income from investments

After witnessing a decline in FY17, gross margins of the company have improved on a timeline basis in FY18 and FY19. Rupee devaluation was one of the key factors which contributed to improvement in margins during this period. Going forward, management expects gross margins to revert to sustainable level witnessed in FY18. Historically, overall expense base has remained within manageable levels with some increase in administrative expenses in the ongoing year in line with higher inflation. Profitability is also supported by dividend received from investments and share of profits from associate investments. Going forward, increase in profitability will be a function of volumetric growth in sales and sustained margins.

Liquidity profile is considered strong in light of healthy cash flows and sound debt coverage ratios. Despite debt draw down to fund expansion, cash flow coverages are projected to remain strong over the rating horizon.

Liquidity profile has improved in line with growth in profitability on timeline basis. Cash flow coverage metrics of the company are considered sound. Due to extended repayment period on existing and planned Long Term Finance Facility (LTFF) utilized by the company, financial flexibility is considered to be on the higher side over the rating horizon. Short term borrowings have been mobilized for working capital requirements and stood at Rs. 3.8b (FY18: Rs. 4.2b; FY17: Rs. 3.1b) at end-FY19. Stock in trade and trade debts are well in excess of short term borrowings while current ratio has remained consistently above 1(x) historically. Ageing profile of trade debts has remained manageable. Despite debt draw down to fund expansion, cash flow coverage ratios are projected to remain strong over the rating horizon.

Low leverage indicators and conservative financial policy depict strong capitalization indicators

Equity base (excluding unrealized gain on investments) of the company has grown at a CAGR of 16.9% during the last three years on account of profit retention. Quantum of dividend paid during three years has remained consistent; however, dividend payout ratio has witnessed a declining trend due to increase in bottom-line of the company. Long term debt mobilized amounted to Rs. 2.2b (FY18: Rs. 1.5b; FY17: Rs. 2.0b) at end-FY19 and comprises SBP's Long Term Finance Facility (LTFF) to fund expansion. The repayment period of this debt is 10 years. Going forward, further

draw down of LTFF facility is planned to fund expansion. The company also utilizes short term borrowings for working capital requirements. Total short term borrowings amounted to Rs. 3.8b (FY18: Rs. 4.2b; FY17: Rs. 3.1b) and primarily comprises export refinance facility. Gearing and leverage ratios of the company stood at 0.32x (FY18: 0.37x; FY17: 0.38x) and 0.57x (FY18: 0.61x; FY17: 0.60x) at end-FY19. Despite further debt drawdown, gearing and leverage ratios are projected to improve over the rating horizon due to growth in equity base.

Sound IT infrastructure

LTML has deployed Oracle E-Business Suite, which is an integrated set of business applications for automating customer relationship management (CRM), enterprise resource planning (ERP) and supply chain management (SCM) processes within organizations. With the help of this IT infrastructure, the management can track live data of production from the head office. IT infrastructure is considered sound with respect to the business requirements.

Internal controls are also considered sound but corporate governance framework depicts room for improvement; strong Health, Safety and Environment (HSE) practices and various accreditations from international organizations remain a strength of the company which may help in attracting international clients

LTML has established an internal audit department at the head office and each production unit. Furthermore, the company has also appointed EY Ford Rhodes, Chartered Accountants as an internal auditor to get an independent opinion on internal controls environment. LTML places a lot of emphasis on HSE practices by ensuring implementation of sound and consistent protocols across each production facility. Various accreditations by international institutions are a testament to company's quality control at each stage of production. Both of these factors may help in attracting more export clientele in future.

Lucky Textile Mills Limited

Appendix I

FINANCIAL SUMMARY				
<i>(amounts in PKR millions)</i>				
<u>BALANCE SHEET</u>	FY16	FY17	FY18	FY19
Long Term Debt	967.6	1,966.6	1,509.9	2,226.2
Short Term Debt	2,794.0	3,050.3	4,215.6	3,801.0
Issued, subscribed and paid up capital	2,000.0	2,000.0	2,000.0	2,000.0
Total Equity (excluding unrealized gain on investments)	11,618.9	13,136.8	15,354.4	18,579.4
Total Equity (including unrealized gain on investments)	14,265.7	14,000.9	15,784.0	19,129.1
<u>INCOME STATEMENT</u>	FY16	FY17	FY18	FY19
Net Sales	12,946.9	13,496.1	15,689.8	18,706.1
Profit Before Tax	1,732.0	2,014.6	2,857.9	3,825.6
Profit After Tax	1,619.2	1,968.7	2,610.6	3,597.9
<u>RATIO ANALYSIS</u>	FY16	FY17	FY18	FY19
Adjusted FFO	2,100.0	2,194.8	3,467.5	4,174.7
Adjusted FFO to Total Debt (%)	55.8%	43.7%	60.6%	69.3%
Adjusted FFO to Long Term Debt (%)	217.0%	111.6%	229.7%	187.5%
Debt Servicing Coverage Ratio (x)	26.2	19.2	14.8	19.2
Gearing (x)	0.32	0.38	0.37	0.32
Leverage (x)	0.54	0.60	0.61	0.57
Current Ratio (x)	1.34	1.36	1.45	1.70

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	Lucky Textile Mills 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
	<u>RATING TYPE: ENTITY</u>				
	Nov 18, 2019	AA-	A-1	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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