RATING REPORT

Rajby Industries

REPORT DATE:
June 22, 2023

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 Outlook	Stable		Stable	
Rating Action	Reaffirmed		Maintained	
Rating Date	*June 22, 2023*		*June 07, 2022*	

COMPANY INFORMATION	
Incorporated in 1990	**External Auditors:** Muniff Ziauddin & Co. Chartered Accountants
Partnership Firm	**Board Chairman:** Mr. Nafees Sultan
Key Shareholders (with stake 5% or more):	**CEO:** Mr. Mudassir Nafees
Mr. Nafees Sultan ~50%	
Mr. Mudassir Nafees ~10%	
Mr. Hamad Nafees ~10%	
Mr. Taha Nafees ~10%	
Ms. Zainab Salman ~10%	
Mrs. Shumaila Nafees ~10%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial 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*

Rajby Industries

OVERVIEW OF THE INSTITUTION

Rajby Industries (RI), the partnership firm was registered in Pakistan on November 15, 1990. The firm is principally engaged in manufacturing of readymade garments (mostly comprising denim) for exports.

RATING RATIONALE

Corporate Profile

Rajby Industries (RI), part of the Rajby Group, is a medium-sized partnership concern specializing in cutting, stitching, washing, finishing, quality control, and exporting denim garments for over 30 years. The product range includes trousers, shorts, skirts, dungarees, jackets, jeggings, vests, and more. The energy requirement of the manufacturing units is primarily met through gas-based generators.

Group Profile

Established in 1988, Rajby Group is a leading player in the textile sector, specializing in denim manufacturing. The group operates through RI and Rajby Textiles (Private) Limited. Formerly, Mr. Saleem Sultan and Mr. Nafees Sultan were co-owners of both entities, but their business partnership was dissolved in June'23. As a result, Mr. Saleem Sultan now majorly owns Rajby Textiles (Private) Limited, while Mr. Nafees Sultan retains his share of ownership in RI, with the remaining shares of both companies distributed among the family members.

Environmental, Social, & Governance (ESG) Initiatives

The company has taken several measures toward environment sustainability, including the installation of solar panels and obtaining LEED Certification for two operating facilities (Unit III & IV). Effluent Treatment Plants (ETPs) have also been implemented to minimize water and soil contamination. Additionally, there are plans to establish a Product Engineering Center in collaboration with a Spanish company, focusing on sustainable product development.

Operating Performance

Headquartered in Karachi, the company has six production units in various locations with a combined monthly capacity of 1.8m pieces. Post-pandemic, two units (I & V) were completely shut down by management due to reduced international market demand, resulting in a ~30% drop in installed capacity over the past two fiscal years. Production levels exhibited a contrasting trend, declining this fiscal year following an increase in FY22, attributed to a global demand slowdown. A similar trend is reflected in utilization ratios.

Figure: Capacity & Production Data (In millions)

	FY20	FY21	FY22	9M'FY23
Installed capacity – Pcs.	19.2	16.8	13.5	10.1
Actual production – Pcs.	13.9	11.2	12.2	6.5
Capacity Utilization	***72%***	***67%***	***90%***	***64%***

Key Rating Drivers

Business risk profile is constrained by current weak macroeconomic environment both globally and locally, demand slowdown, high interest rate situation, inflationary pressures and recent floods adversely affecting cotton crop while ongoing energy crisis in the country pose a challenge to 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 finally broke the threshold, coming in at USD 32.4b. Textile sector contributes nearly one-fourth to industrial value-added segment and

8.5% to the country's GDP, with an estimated market size of around Rs. 4.0tr. In addition, textile sector has maintained an average share of about 60% in national exports.

Figure: Pakistan Export Statistics (in USD millions)

	FY20	FY21	FY22		10M'FY22	10M'FY23
Pakistan Total Exports	22,536	25,639	32,450		26,858	23,211
Textile Exports	12,851	14,492	18,525		15,174	14,178
PKR/USD Average rate	158.0	160.0	177.5		174.4	245.4

Source: SBP

Export revenues from textile sector have noted sizeable growth over the years (FY22: $19.3b FY21: $15.4b; FY20: $12.5b; FY19: $13.6b). Knitwear, Readymade and Bed wear segments continue to contribute higher than other segments, with a cumulative contribution of more than 60% in textile exports. While the growth was primarily driven by volume (excluding knitwear and cotton yarn), higher prices also boosted exports.

Figure: Textile Export Details (in USD millions)

	FY20	FY21	FY22		10M'FY22	10M'FY23
High Value-Added Segment	**9,669**	**12,427**	**15,605**		**12,908**	**11,337**
- Knitwear	2,794	3,815	5,121		4,218	3,712
- Readymade Garments	2,552	3,033	3,905		3,214	2,905
- Bed wear	2,151	2,772	3,293		2,727	2,250
- Towels	711	938	1,111		928	825
- Made-up Articles	591	756	849		710	585
- Art, Silk & Synthetic Textile	315	370	460		385	343
- Others	555	743	866		725	718
Low to medium Value-Added Segment	**2,858**	**2,972**	**3,717**		**3,074**	**2,372**
- Cotton Cloth	1,830	1,921	2,438		2,006	1,685
- Cotton Yarn	984	1,017	1,207		1,006	637
- Others	43	34	72		62	51
Total	**12,527**	**15,399**	**19,332**		**15,982**	**13,709**

Source: PBS

Cotton prices rose to a new 12-year high of ~Rs. 22,935/maund as of Sept'22 driven by a scarcity of cotton resulting from the recent floods that impacted the local cotton production. Cotton imports were also up 19.8%, in USD terms, for FY22 vis-à-vis preceding year.

Figure: Cotton Prices Trend (In Rs.)

	FY19	FY20	FY21	FY22	10M'FY23
Per Maund	8,770	8,860	13,000	17,380	20,235
YoY % Change	26%	1%	32%	34%	*n/a*

Floods in Sindh and Southern Punjab during recent monsoon season have caused significant damage to the cotton crop. According to industry estimates, ~45% of the crop has been washed, worth more than $2.5b, resulting in significant price increases. The government has announced facilitation for raw materials imports to compensate for domestic shortages. Nonetheless, in addition to affecting profit margins, higher raw material pricing is expected to increase the working capital requirements, which is likely to have a negative impact on the liquidity profile of textile operators, particularly spinners, weavers and dying companies.

Global and domestic challenges, such as slowdown in export demand (primarily from North America and the EU, which has begun to materialize in Pakistan's monthly export proceeds) due to recessionary trend, industrial gas load shedding expected in the country, and rising production costs due to inflation, will weigh on the business risk profile going forward. These factors may result in competitive market pricing for exporters.

FY22 witnessed a strong revenue recovery fueled by rupee devaluation, higher dollar prices, and increased volume, while current year faced a significant impact from demand slowdown.

Net sales, after a two-year consecutive decline, have rebounded with a strong double-digit annual growth in FY22. This growth can be explained by ~12% rupee devaluation impact, ~10% higher prices in dollar terms and ~4% volumetric uptick. However, the recent demand slowdown due to the economic downturn in major world economies led to a sizeable dip in volumes and impacted growth in the current fiscal year, with revenues marginally declining by 1% in 9M'FY23 compared to 9M'FY22. Despite significant support from consistent rupee depreciation, management projects full-year revenue for FY23 to decline by approximately 6% compared to FY22.

Almost the entire revenue emanates from exports, with only wastages being sold locally. Product-wise, trousers and shorts drive the majority of revenues accounting for more than ~90% of total exports on a timeline, while the rest is shared by dungarees, skirts, shirts, jackets, vests, dresses, jeggings, chinos, and others. The geographical sales mix is well-diversified, with the US representing one-quarter of total sales, followed by Spain, Germany, Canada, Netherlands, and the UK. Client concentration risk remains high, with the top ten clients contributing over 80% of total sales; however, comfort is drawn from established long-term relationships with these clients including some of the top global brands.

Gross margins slightly improved, and net profitability increased through effective cost control and limited financial charges.

Despite lower revenues, gross margins improved slightly in the current year due to factors like rupee devaluation and limited reliance on imported raw materials. Average denim fabric procurement cost has nearly doubled in the past 21 months, with a significant dip in procured volumes. Adequate stock levels are maintained to fulfill confirmed sales orders. Half of the denim fabric needs are sourced from an associate company, RTPL, while the rest is acquired from the open market based on client specifications.

In FY22, overhead expenses grew with revenue but decreased this fiscal year due to a sizeable drop in freight charges. Financial charges slightly rose with higher benchmark rates, while debt utilization declined. Net margins consistently improved on a timeline through effective control of operating overheads.

Debt coverage metrics have improved with declining debt levels and positive trend in cash flows.

In FY22, despite improved profitability, funds flow from operations (FFO) remained comparable due to lower depreciation and amortization along with gains from fixed asset sales. However, cash flows improved considerably this fiscal year, and a consistent decline in debt levels resulted in improved debt coverage metrics, aligning with industry peers.

Liquidity profile is satisfactory, supported by consistent improvement in the current ratio and sound coverage of short-term debt in relation to inventory and trade debts. The cash conversion cycle increased to 35 days in 9M'FY23, up from 23 days in FY21, but remains lower compared to peers. The aging profile of trade debts is adequate, as ~90% are settled within 6 months, and no bad debt has been reported.

Leverage ratios have improved, showing a slight favorable comparison to similar rated peers.
Supported by improved bottom-line and healthy retention, the equity base grew by ~32% in the last 21 months at end-9M'FY23, despite significant drawings by the partners.

Debt profile is a mix of short-term and long-term debt, with total interest-bearing liabilities increasing at end-9M'FY23; ~79% constituted short-term debt. Aggregated running finance lines amount are majorly allocated to concessionary IERS/IERF schemes. In addition, an interest-free loan from an associate company, RTPL remains the same at end-9M'FY23 compared to FY22. Leverage ratios have improved significantly with declining debt levels, showing a slightly favorable position compared to similar-rated peers.

Room for improvement exists in terms of corporate governance framework.
Ratings are constrained by the current corporate infrastructure as a partnership entity, but the company maintains adherence to international compliance protocols, has experienced senior management, and utilizes 'Oracle EBS' and cloud technology for operational efficiency. Room for improvement exists in terms of enhancing board composition, strengthening oversight, and documenting a succession plan.

REGULATORY DISCLOSURES — Appendix I

Name of Rated Entity	Rajby Industries
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				
22-06-2023	A-	A-2	Stable	Reaffirmed
07-06-2022	A-	A-2	Stable	Maintained
03-06-2021	A-	A-2	Negative	Maintained
23-04-2020	A-	A-2	Rating Watch - Negative	Maintained
29-11-2019	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.
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Due Diligence Meeting Conducted

Name	Designation	Date
Mr. Tauseef Karim	Director Finance	June 09, 2023
Mr. Muhammad Ilyas	General Manager Accounts	