The Pakistan Credit Rating Agency Limited

RELIANCE WEAVING MILLS LIMITED

	INITIAL [NOV-16]
Entity	
Long Term	BBB-
Short Term	A3
Outlook	Stable

REPORT CONTENTS

NOVEMBER 2016

Profile & Ownership

- Reliance Weaving Mills Limited (RWML) – a Fatima Group company – commenced operations in 1990; listed on Pakistan Stock Exchange
- Engaged in manufacturing of yarn and fabric; currently operating with 61,920 spindles and 336 air-jet looms
- Majority owned by Fatima Group, through individuals (78%) and corporate (~3%)
- Fatima Group (FG) – a leading corporate group – has interests in fertilizer, textile, sugar, trading, and energy sectors

Governance

- Overall control of the company vests in seven-member board; Six directors are FG's family members, while one director is independent
- Apart from non-executive Chairman, three of the family directors are in executive roles, while two are directors' spouses

Management

- Mr. Fazal Ahmed Sh. is the designated CEO; however, Mr. Faisal Ahmed Mukhtar, Executive Director (ED), oversees operational matters while Mr. Fahd Mukhtar, the other ED, is mainly engaged in marketing
- Management team comprises experienced individuals

Operational Risk

- Deploys Oracle based ERP; comprehensive MIS reporting
- Captive power generation to meet power requirements (12.5MW)

Performance

- Sales mix has equal contribution from local and exports – previously skewed towards exports. Revenues dominated by weaving (65%), followed by spinning (35%)
- Since FY14, revenues have witnessed a declining trend; performance remained subdued. During FY16, the revenues (PKR 10bln) witnessed decline of ~8% on YoY basis – attributable to volumetric decrease in exports; however, increase in local spinning sales provided support
- Margins remained subdued in recent years; however in FY16 marginal improvement witnessed on account of lower YoY power costs – a factor of RLNG availability to the sector in last quarter
- Support from decline in finance cost (23% YoY) – a factor of lower benchmark rates – helped the company's bottomline turn green (FY16: profit: PKR 3mln; FY15: loss: PKR 98mln)
- RWML's investment portfolio (PKR 906mln at end-Jun16) constitutes ~33% of its equity base; with majority portion comprising strategic investments: Fatima energy (~88%), followed by equity stake (~10%) in Fatima Fertilizer. Dividend stream yet to build up
- Going forward, RWML is expected to hold its performance. Expected power cost saving (RLNG availability at lower rate) and recovery in fabric prices are likely to support margins. CAPEX (~PKR 400mln) planned in FY17 includes replacement of 63 looms; likely to bring efficiency gains

Financial Risk

- Stretched working capital cycle mainly attributable to high inventory days
- Asset-liability mismatch (PKR 525mln at end-Jun16) – continued to exist (though reduced on YoY basis). However, it is expected to reduce on account of expected re-profiling of balance sheet – ~PKR 1.5bln short-term loan will be converted into long-term
- Marginal improvement in coverages witnessed; though remained weak. Effective loan re-profiling will positively impact future coverages
- Highly leveraged capital structure (end-Jun16: ~69%); however, no major debt planned

RATING RATIONALE

The ratings reflect RWML's adequate business profile. Volumetric growth in local sales, on the back of recent capacity expansion, has provided support to revenues despite lower product prices. Overall gross margins further squeezed mainly due to spinning segment – a phenomenon largely observed industry wide. However, the management expects gradual improvement in margins in future given, (i) better cotton crop expectation for FY17 and rebound in international prices, and (ii) continuous energy supply at cheaper rates. The ratings are constrained by stretched financial profile. This is reflected in mismatch in short-term debt vis-à-vis self-liquidating current assets. Limited cashflows – a factor of lower profitability – constrained the coverages. Cognizant of these issues, the management is in process of re-profiling its balance sheet – converting short-term debt into long-term at lower rates. Decline in finance cost while supporting debt service coverages, has provided respite to financial risk profile lately. RWML's association with Fatima Group, a growing conglomerate, is a key rating factor.

KEY RATING DRIVERS

The ratings are dependent on the management's ability to prudently mange the liquidity and debt profile of the company, particularly working capital, while sustaining business margins. Significant deterioration in coverages will have negative implication for the ratings. Meanwhile, strengthening of governance framework for better oversight of strategic affairs is considered essential.

PKR mln

Reliance Weaving Mills Limited

BALANCE SHEET	30-Jun-16	30-Jun-15	30-Jun-14
	Annual	Annual	Annual
Non-Current Assets	**5,238**	**5,462**	**4,619**
Investments (Incl. associates)	**906**	**936**	**426**
Equity	906	936	426
Debt			
Current Assets	**4,007**	**3,738**	**4,644**
Inventory	2,346	1,576	2,384
Trade Receivables	528	954	1,029
Others	1,132	1,208	1,232
Total Assets	**10,151**	**10,137**	**9,690**
Debt	**6,250**	**6,396**	**5,848**
Short-term	3,560	3,564	3,747
Long-term (Inlc. Current Maturity of long-term debt)	2,691	2,832	2,101
Other shortterm liabilities	972	826	850
Other Longterm Liabilities	155	170	96
Shareholder's Equity	**2,774**	**2,744**	**2,895**
Total Liabilities & Equity	**10,151**	**10,137**	**9,690**
INCOME STATEMENT			
Turnover	**10,049**	**10,878**	**11,412**
Gross Profit	887	842	1,122
Other Income	(4)	10	97
Financial Charges	(523)	(682)	(598)
Net Income	**3**	**(98)**	**219**
Cashflow Statement			
Free Cashflow from Operations (FCFO)	809	699	907
Net Cash changes in Working Capital	(70)	926	(232)
Net Cash from Operating Activities	213	931	197
Net Cash from InvestingActivities	(11)	(1,515)	(1,135)
Net Cash from Financing Activities	(196)	540	980
Ratio Analysis			
Performance			
Turnover Growth	-7.6%	-4.7%	19.9%
Gross Margin	8.8%	7.7%	9.8%
Net Margin	0.0%	-0.9%	1.9%
ROE	0.1%	-3.7%	8.2%
Coverages			
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STB)	0.5	0.3	0.9
Interest Coverage (x) (FCFO/Gross Interest)	1.5	1.0	1.5
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCF(	11.2	206.6	6.8
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	46.7	47.6	64.3
Capital Structure (Total Debt/Total Debt+Equity)	69.3%	70.0%	66.9%

The Pakistan Credit Rating Agency Limited

STANDARD RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments. This capacity is highly unlikely to be adversely affected by foreseeable events.
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Speculative.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic change over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**Highly speculative.** Significant credit risk. A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**High default risk**. Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short Term Ratings

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved with in foreseeable future, but may continue if underlying circumstances are not settled.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.

Name of Issuer	Reliance Weaving Mills Limited
Sector	Textile
Type of Relationship	Solicited
Purpose of the Rating	Independent Risk Assessment

Rating History

Date	Long Term	Short Term	Outlook	Action
11-Nov-16	BBB-	A3	Stable	Initial

Related Criteria and Research

Rating Methodology	Corporate Rating Methodology
Sector Research	Textile Sector - Viewpoint | Sep-16

Rating Analysts

Saira Rizwan
saira.rizwan@pacra.com
(92-42-35869504)

Rating Team Statement

Rating Procedure
Rating is an opinion on relative credit worthiness of an entity or debt instrument. It does not constitute recommendation to buy, hold or sell any security. The rating team for this assignment does not have any beneficial interest, direct or indirect in the rated entity/instrument.

Disclaimer

Rating Shopping
PACRA maintains principle of integrity in seeking rating business.
PACRA has used due care in preparation of this document. Our information has been obtained directly from the underlying entity and public sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA shall owe no liability whatsoever to any loss or damage caused by or resulting from any error in such information.

Conflict of Interest
PACRA, 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 done by them
The analysts involved in the rating process do not have any interest in a credit rating or any of its family members has any such interest
The analysts and members of the rating committees including the external members have disclosed all the conflict of interest, including those of their family members, if any, to the Compliance Officer PACRA
The analysts or any of its family members do not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This is, however, not applicable on investment in securities through collective investment schemes. PACRA has established appropriate policies governing investments and trading in securities by its employees
PACRA may provide consultancy/advisory services or other services to any of its clients or to any of its clients' associated companies and associated undertakings that is being rated or has been rated by it. In such cases, PACRA has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities
PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA's opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and ii) fee mandate - signed with the payer, which can be different from the entity
PACRA ensures that the credit rating assigned to an entity or instrument should not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship

Surveillance
PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the rated entity/ issuer, the security arrangement, the industry etc, is disseminated to the market, in a timely and effective manner, after appropriate consultation with the entity/issuer
PACRA reviews all the outstanding ratings on annual basis or as and when required by any stakeholder (including creditor) or upon the occurrence of such an event which requires to do so
PACRA initiates immediate review of the outstanding rating(s) upon becoming aware of any information that may be reasonable be expected to result in any change (including downgrade) in the rating

Reporting of Misconduct
PACRA has framed and implemented whistle-blower policy encouraging all employees to intimate the compliance officer any unethical practice or misconduct relating to the credit rating by another employees of the company that came to his/her knowledge. The Compliance Officer reports to the BoD and SECP

Confidentiality
PACRA has framed a confidentiality policy to prevent abuse of the non-public information by its employees and other persons involved in the rating process, sharing and dissemination of the non-public information by such persons to outside parties
Where feasible and appropriate, prior to issuing or revising a rating, PACRA informs the issuer of the critical information and principal considerations upon which a rating will be based and provide the opportunity to clarify any likely factual misperception or other matter that PACRA would wish to be made aware of in order to produce a fair rating. PACRA duly evaluates the response. Where in a particular circumstance PACRA has not informed the entity/issuer prior to issuing or revising a rating, it informs the entity/issuer as soon as practical thereafter

Prohibition
None of the information in this document may be copied or otherwise reproduced, stored or disseminated in whole or in part in any form or by any means whatsoever by any person without PACRA's written consent. PACRA reports and ratings constitute opinions, not recommendations to buy or to sell

Probability of Default (PD)

PACRA's Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA's transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA's Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past