



RATING (OCTOBER 2009)

Prosperity Weaving Mills Limited (PWML)

ENTITY	NEW
Long Term	BBB+
Short Term	A2

FINANCIAL DATA

PKR (mln)

	30-Jun-09	30-Jun-08
Total Assets	1,547.8	1,557.3
Pure Equity	347.5	290.5
Adj. Equity*	411.6	334.3
Turnover	3,634.6	2,766.9
Net Income/(Loss)	83.9	(65.1)
Net Debt/Equity (%)	225.0	326.2
Gross Margin (%)	10.1	5.6
RoE (%)	22.5	(16.4)

*Including revaluation surplus on land

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RATING RATIONALE AND KEY DRIVERS

- The ratings reflect PWML's improved business risk profile, emanating from a combination of factors including demand supply equilibrium in key markets of the company. Moreover, the company is taking significant steps on both production and marketing fronts to consolidate, indeed further fortify, its market position in these markets. Meanwhile, PWML's financial profile is expected to remain manageable.
- The ratings are dependent on the management's ability to sustain its competitive position among its peers without compromising its margins. Meanwhile, any adverse changes in the socio-economic environment deteriorating its margins and putting its cashflows and coverages under significant pressure would have negative implications for the ratings.

ASSESSMENT

- During FY09, PWML experienced substantial growth in its turnover. This was mainly attributable to better pricing of the company's products. Another factor leading to this was devaluation in the domestic currency. As a result, there was sizeable improvement in PWML's gross margins. The company also earned a net profit of PKR 23mln from sale of surplus electricity to LESCO. The company's operating expenses escalated mainly on account of export sales (freight and commission). Meanwhile, PWML incurred a small loss on forward contracts, which was set off by revaluation surplus on the investments. Despite high finance cost due to high interest rates, the company registered considerable increase in its profitability on a comparative basis. The company has continued the improving performance trend during 1QFY10.
- Going forward, PWML intends to fortify its position in its key markets. Global downturn has created room for less expensive, but reasonable quality products, to penetrate into a new class of customers. Meanwhile, changing socio-economic dynamics in the competing economies has also well placed the Pakistani textile industry in the export market. PWML, to capitalize on the growth opportunity, plans to add value to existing production capacity rather than expansion. In this regard, the company intends to introduce multiple fibre fabric, leveraging the group's capacity and experience in the spinning industry. Moreover, the company would be outsourcing processing of greige fabrics produced by PWML while employing inhouse knowledge of processed fabrics. Meanwhile, significant expansion in the marketing team is underway for the benefit of all group companies. In addition, power sale to LESCO is also expected to provide a constant income stream, supporting PWML's profitability.
- The latest increase in PWML's investment book (PKR ~158mln) is an outcome of excess liquidity. The company, as a policy, invests only in mutual funds having limited exposure in TFCs and equities. PWML, in the recent AGM, has decided to place surplus funds in its associates (PKR 75mln each in Nagina Cotton and Ellcot Spinning) to help them through tight liquidity environment. The interest to be charged will not be less than the borrowing costs of the company.
- PWML's working capital requirements are mainly a function of its inventory levels. The company, with improved turnover, depleted a sizeable portion of its finished goods during FY09. This coupled with higher gross margins enabled the company to register substantial improvement in its operating cashflows. Resultantly, the company's coverages improved on YoY basis. Going forward, the company is likely to continue with the existing trend.
- PWML has a leveraged capital structure. The recent improved profitability is not likely to fully augment PWML's capital structure as the company has announced 20% cash dividend. However, comfort can be drawn from a sizeable unrecognised revaluation surplus available on its plant, improving its reported equity base. Moreover, the management does not plan any major capex over the medium term. Hence, no drag on the capital structure of the company is expected.

PROFILE

- Prosperity Weaving Mills Limited (PWML), incorporated in Nov 1991, is primarily engaged in the production of apparel and home furnishing greige fabric and dyed yarn fabric (capacity: 324 air jet looms). The company is listed on Karachi and Lahore Stock Exchanges. Nagina Group (NG), founded by Mr. Enam Ellahi Shaikh, owns PWML, through group companies (53%) and key sponsoring individuals (35%). The group also owns Nagina Cotton Mills Limited and Ellcot Spinning Mills Limited having 46,428 and 54,528 spindles respectively.
- PWML's board of directors, comprising seven members including the CEO, is dominated by key sponsoring individuals. The company's CEO and son of NG's founder, Mr. Shaukat Ellahi Shaikh, is a graduate of Columbia University and has been associated with PWML since long.