A DILEMMA OF PRIVATIZATION: NATIONAL FIBRES LIMITED

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Abstract

This paper examines the case of National Fibres Limited; a public sector unit was financed by National Development Fianance Corporation (NDFC) and Islamic Development Bank (IDB), Jeddah. The unit was the first man made fibre plant of the country, and had various technical and marketing problems since inception i.e. 1981-82.

NDFC and IDB Jeddah revive the unit by providing technical and marketing inputs, and also converted their long term loans into equity so that the unit could service its loans, and have sufficient cash flow for operation. By the year 1992, the unit became healthy. Its pretax profit was RS.131.00 million, and was in the process of Balancing Modernization and Rehabilitation (BMR).

The unit was privatized and handed over to the Schon Group on February 02, 1992, despite the fact that the group only paid 50% of the bid price (Rs.735 million) and for the balance 50% it arranged a bank guarantee through HBL. After the takeover by the Schon Group, the NFL's financial health deteriorated. By the year 1996, the unit had a loss of Rs.285.000 million along with the accumulated liability of more than Rs.1.00 billion.

In view of the above, the minority equity holders and creditors through the High Court of Sindh took the control of the management of the company on December 05, 1997 with the objective of revival / rehabilitation. This was the first time in the history of the Pakistan that a unit was taken over by the minority-shared holders under section 292 of the company ordinance 1984. To receive the project, the new management lead by NDFC, prepared a comprehensive rehabilitation plan consisting of debt equity swap, rescheduling of existing debts and the provision of additional funds for Balancing, Modernizing and Rehabilitation (BMR). The rehabilitation plan of NFL is the focus of this study.

Keywords: *Public sector, Private sector, Privatization plan, stakes holders, Polyester fiber and polyester yarn.*

1. INTRODUCTION

National Fibres Limited (NFL) a public sector unit was financed by National Development Fianance Corporation (NDFC) and Islamic Development Bank (IDB), Jeddah. The unit was the first man made fibre plant of the country, and had various technical and marketing problems since inception in 1981-82. Some of the problems were (1) size of the project, (2) producing polyester fibre of 1.5 denier whose demand in last few years had reduced to 10% of its initially projected demand.

NDFC and IDB tried to revive the unit by providing technical and marketing inputs, and also converted their long-term loans into equity so that the unit could service its loans, and also have sufficient cash flows for operations. By the year 1992, the unit became healthy. Its pre-tax profit was Rs.131.00 million, and was in the process of Balancing, Modernization and Rehabilitation (BMR).

The unit was privatized and handed over to the Schon Group (a private sector business entity) on February 02, 1992, despite the fact that the group only paid 50% of the bid price (Rs.735 million) and for the balance 50% it arranged a bank guarantee through Habib Bank Ltd. (HBL) for which it pledged the shares of the NFL as a security. However, the Privatization Commission of Govt. of Pakistan could not invoke the bank guarantee as the Schon Group obtained a stay order from the Lahore High Court, Rawalpindi Bench.

After the takeover by the Schon Group, NFL's financial health deteriorated. By the year 1996, the unit had a loss of Rs.285.000 million along with the accumulated liability of more than Rs.1.00 billion.

In view of the above, the equity holders/creditors through the High Court of Sindh obtained the Management of the Company on December 05, 1997 with the objective of revival / rehabilitation. This was the first time in the history of the Pakistan that a unit was taken over by the minority-share holders and creditors under section 292 of the Companies Ordinance 1984.

The court appointed management prepared several rehabilitation packages for the approval of the government/ consortium members. However, the banks were not willing to make further investment in the unit. Finally the assets of the units were sold at the price of Rs.800 million. The funds however could not be distributed to the creditors as per statutory requirement as once again the Schon Group obtained a stay order against the decision of selling the assets of the company.

An analysis of the operations of National Fibers Ltd. demonstrated that the project was viable upto the point of its privatization. The new private sector management added a substantial debt burden on the project without enhancing the capacity in any meaningful manner. It was not possible for the project to sustain its accumulated debt burden. The technology base of the project was old and its size was small relative to its current competitors. However, if the debts were appropriately restructured and competent management was inducted, the project could have been successfully rehabilitated.

2. BACKGROUND

2.1 NFL in Public Sector (1981 to 1992)

National Fibers Limited (NFL) was the first man made fibre Unit of the country. The unit was commissioned in the year 1981-1982. The installed capacity of the unit was 12,000 tons of Polyester Fiber per annum. Additionally, the unit had a capacity of producing polyester yarn of various specifications. The unit was based on old batch technology, and faced problems since inception. It was originally envisaged that the product specification would be 90% and 10% for 1.5D and 1.2D of fiber. However, by the time the unit got commissioned the market demand had reversed. The market share for 1.5d of polyester was 10%, and for 1.5D was 90%. During this period ICI's fiber unit with the same capacity of 12,000 tons was commissioned. This unit was also based on the old batch technology and had the same capacity as NFL, but had the right product mix. NFL thus was not able to operate at the desired capacity level and continued to accumulate debts.

With the efforts of NDFC, the unit was finally revived. The revival package included conversion of a portion of long-term loans into equity. The equity pattern and summarized operating results of the units are presented below:

EQUITY	SHARES (Million)	PERCENT
FCC&CL	27.764	61%
IDB, JEDDAH	8.050	20%
NDFC	08.120	19%

a) The unit had a net profit of Rs.78.938 million in the year 1989, which increased to Rs.108.372 in the year 1992.

b) The net equity during the year 1989 was Rs.418.563 million, which increased to Rs.1.148 billion by the year 1992.

c) Total liability in the year 1989 was Rs.504.614 million, which decreased to Rs. 98.705 million by the year 1992.

2.2 Privatization of the Unit

The unit was privatization under the Government Privatization Program. The management was transferred to Schon Group, along with the majority shareholdings of the company as on February 02, 1992. The share holding pattern after the privatization was as follows:

EQUITY	SHARES (Million)	PERCENTAGE
FCC&CL	4.145	05%
IDB, Jeddah	17.932	21%
NDFC	17.112	20%
Schon	44.324	52%
Others	01.265	5%

After the takeover by the Schon Group, the NFL's financial health deteriorated. By the year 1996, the unit had a loss of Rs.285.000 million along with accumulated liability of more than Rs.1, 000 billion. The operating results are presented below:

a) The unit had a net profit of Rs.47.491 million in the year 1993, which converted to a loss of Rs.42.344 million by December 04, 1997, at the time of the take over by the court appointed management.

b) The net equity during the year 1993 was Rs.1.145 billion, which decreased to Rs.247.782 million by December 04, 1997.

c) The total liabilities during the year 1993 were Rs.457.07 million, which increased to Rs.1.274 billion by the year 1997.

2.3 NFL Under Court Appointed Management

It was the first time in the Pakistan's Banking history that the creditors took over the management of the unit. The equity holders/creditors filed the petition under section 292 of the company's ordinance 1985. While the petition was still in the High Court of Sindh, the court gave the Management of the Company to the petitioner on December 05, 1997 under section 290 of the companies' ordinance 1985. The company was under the operation of the court appointed management from December 05, 1997 to December 2006.

After the take over of the unit, two different sets of rehabilitation plans were developed. The first part was to make the unit operational with minimum possible finance. The second Rehabilitation plan was developed for the Task Committee formulated by the Government of Pakistan for the rehabilitation of the sick units in Pakistan. The purpose and objective of the task committee was to ascertain the marketing, technical, and financial viability of the units that were sick and revive those that had the potential to become competitive.

The performance under the new management is discussed below:

a) M/s. Rahman & Sarfraz and Co., Chartered Accountants worked out a detailed plan that envisaged a funding of Rs.235.00 million to make the plant operational. However, the NDFC was the only institution, which provided cash funding of Rs.80.00 million that was not sufficient to re-commission the entire plant. In view of the shortfall in the funds, the new management could only made the yarn sections operational and was operating these sections at about 90% capacity utilization. As the polymer and fiber sections, could not be made operational due to paucity of funds, the sales revenue dropped by 50% as against the projected sales target. In view of such a huge short fall in the revenues, the unit was unable to absorb all the fixed costs and therefore incurred loss.

2.4 Project Facilities

The total land of the unit was 42 acres. The covered area of the company was about 33,300 sq. meters. The premises which NFL was utilizing covered 17.269 acres; the balance of about 25 acres was surplus land with NFL.

The summary of constructed area is presented below:

Description	Covered area (Sq. Meter)	Description	Year of construction
Production Area	16,000	RCC & MS	1980
Workshop & others	10,000	RCC	1980
Ware House	6,000	RCC	1980, 90, 92
Office Building	1.300	RCC	1980, 92

a) A brief summary of the plant and machinery is presented below:

- The polymer section consisted of three production lines. The aggregate installed capacity of these three lines was 60 tons a day (based on old batch technology).
- There were two lines in the Fiber section. The installed capacity of this section was 40 tons per day
- There were two sections in yarn processing. Filament one was based on high speed spinning and nine texturising machines. Of these nine machines, only six machines were in operation. The rated capacity of these six texturizing machines was 9 tons per day. Filament two consisted of two lines of high-speed spinning units and five Zinser machines. The rated capacity of flat yarn (Zinser) was seven tons a day.
- The twister section consisted of 14 twister machines. The average capacity of this section was two tons per day.
- There were two generators of 3.2 MW each. Of this, one was operational and other was decommissioned.

2.5 Ownership Pattern & Related Issues

Schon Group was the majority shareholder of the company. The shareholding pattern of the company along with details such as shares pledged by the Schon Group against borrowing of NFL and its sister concerns is discussed below:

a) The Schon Group owned 44.324 million shares of NFL. Of this about 90% or 43.1 million shares were pledged by the Schon Group as a security for the liabilities created against several companies of the Schon Group. Of this total, 24 million shares were pledged by Schon Group against loan facilities of other companies of the Schon Group and 19.1 million shares pledged with various institutions on account of NFL.

2.6 Pending Litigation

The Schon Group had 52% shares of the company, therefore, were the majority shareholder. However, in order to protect the interest of the Equity holders/Creditors, the minority shareholders got the management of the company under section 290/292 of the Companies' Ordinance 1984. Since the takeover on December 5, 1997 it was being managed by the Court appointed management; the details of that and other litigation/legal status are discussed below:

The main petition i.e. J.M. 39/97 filed by the Equity-holders u/s 290 of the Companies Ordinance 1984 to protect the interest of Equity-holders and all the Creditors for the purpose of rehabilitation of the company, was still pending in the High Court of Sindh. However, an Interim Order dated December 4, 1997 allowed NDFC and others to take over the management of the Company.

Later on, the Schon Group filed a petition opposing the nomination of Mr. Riaz Niazi, praying that their objections on the nomination were not placed before the Hon'ble High Court. The High Court of Sindh after hearing their objection, in October 1998 appointed Mr. Khalid Mumtaz, a representative of Schon Group to coordinate and assist the Court appointed Chief Executive of the Company.

As the company was being run by the Court appointed management, therefore, CLA's statutory requirement such as, holding Board of Directors' Meetings, appointment of Auditors, and approval of Annual & Semi- Annual Accounts could not be undertaken. The Court appointed management therefore approached Corporate Law Authority/Securities Exchange Commission of Pakistan for waiver/postponement of the statutory requirement till the decision of JM-39 (Petition filed u/s 290 of the Companies Ordinance, 1984) by the High Court of Sindh.

3. REVIEW OF MARKET SITUATION IN 1999:

3.1 Existing Units of Polyester Fibre

In 1999 there were six polyester fibre units in the country. The total installed capacity of the units was about 393,000 tons. The details are presented below:

	Polyester Units	Location	Capacity (per annum)
1	Dewan	Hattar-NWFP	105,000
2	Dhan Fiber	Hattar-NWFP	90,000
3	ICI	Punjab	64,000
4	Ibrahim Fibre	Punjab	70,000
5	PSL	NWFP	28,000
6	Rupali Limited	Punjab	22,000
7	National Fibres	Karachi	14,000

Source: Filament Yarn Manufacturers Association

Dewan Salman was the largest unit followed by Dhan Fiber, ICI and Ibrahim Fiber. While PSL, Rupali and National Fibers were small units ranging between 28,000 tons to 14,000 tons per annum.

3.2 Demand And Supply Analysis of Polyester Fiber

The demand and supply situation of polyester fibre in the country during the period 1999 to 2004 is given below:

Year	Supply	Demand	Gap
1999	393,000	393,807	(807)
2000	393,000	433,1888	(40,188)
2001	449,000	476,506	(27,506)
2002	504,000	524,157	(20,157)
2003	517,000	576,573	(59,573)
2004	523,000	634,230	(111,230)
Source: NDFC's Estimates			

The above demand and supply situation estimated by NDFC in 1999 shows that there was a deficit of 807 tons in the year 1999, which was expected to increase by 40,108 in the year 2000. In subsequent two years, the deficit would have been in the range of 20,157 tons to 27,506 tons. Finally, in the year 2004, there was expected to be a deficit of 111,230 tons.

It may be noted that in the year 1999, there was a deficit of 807 tons. Comparatively, about 13000 tons of polyester fiber was expected to be imported. The reason for such a variation was that the above-developed schedule by NDFC was inclusive of the production by NFL, which was not producing Fiber.

3.3 Polyester Yarn (Existing Units in 1999)

In 1999, there were about 22 units of polyester yarn in the country, details of which are presented below:

	Name of the units	Location	Capacity in tons
1	Ms. Rupali Polyester	Shiekhupura	11,000
2	M/s Rupafil	Sharqpur	14,000
3	M/s. Gatron Industires Ltd-1	Hub-Balouchistan	13,000
4	Gatron Industries Limited-2	Hub Balouchistan	8.000
5	National fibre Limited	Karachi	5600
	Sub total based on PTA/MEG technology		51,600
6	Spintex	Azad Kashmir	10,000
7	S.G Fibers	Karachi	9000
8	Polyron	Hub Baluchistan	4000
9	Pak Fibre	Hub Baluchistan	2000
10	Progressive fibre	Hub Baluchistan	1400
11	Fayyaz Filament	Hub-Baluchistan	3000
12	Tilon Limited	Hub_baluchistan	700
13	Bengal Fibrer	Karachi	3000
14	Dilon Limited	Karachi	1000
15	Kohinoor Fibre	Faislabad	1,5000
16	Ahsan Industires	Faislabad	600
17	Ahmed Factory	Failsabad	600
18	Tristar Polyester	Karachi	3000
19	Sindh Star Industires	Karachi	500
20	Indus Polyester	Hattar-NWFP	2000
21	Tawwakkal Polyester	NWFP	1600
22	Papa Sierra Fibers	Hattar NWFP	2100
SUB TOTAL BASED ON CHIPS			**46,000**
GRAND TOTAL			**97,600**

Source: FYMA

The total installed capacity of these units was 97,000 tons per annum. Of the 22 local units, only five units had the capability of making polyester chips, a raw material for producing polyester yarn. The installed capacity of these units was about 51,600 tons per annum. The other 17 units were either purchasing the polyester chips from the local units or importing the same for making polyester yarn.

3.4 Shutdown Units of Polyester Yarn

Of the 22 units in the country, five units were not in production (shut down). The details of these units are presented below:

	Unit	Capacity in tons
1	Polyron	4000
2	Progressive fibre	1400
3	Fayyaz Filament	3000
4	Papaseira	2100
5	Pak Fiber	2000
	TOTAL	**12,500**

Source: FYMA

The actual production of the local yarn units was about 74,000 tons for the year 1999. If the capacity of the shut down units is excluded, the capacity utilization comes to 87%.

3.5 Demand And Supply Analysis Polyester Yarn

Following estimates of supply and demand were prepared by NDFC in 1999.It was assumed that the shutdown units will remain closed during the projected period.

YEAR	SUPPLY	DEMAND	GAP
1999(Base year)	85100	82400	2700
2000	85100	84872	228
2001	85100	87418	(2318)
2002	85100	90041	(4941)
2003	85100	92742	(7642)
2004	85100	95524	(10424)

Source: NDFC's Estimates

The above analysis indicates that there was a surplus supply of 2700 tons in the year 1999. This would change to a deficit supply of 2318 tons in the year 2001, which would have further increased to a deficit of 10, 424 tons by the year 2004.

It may be noted that although there was an excess supply in the year 1999 there were imports of 7000 tons in the same year. The reason for such a glut in the market was that, the polyester companies of the developed countries were dumping the yarn at throwaway prices in the local market. As a consequence, the local units could not operate at optimum level.

4 REHABILITATION PLAN OF NDFC

NDFC once again took the lead to develop a comprehensive rehabilitation plan. The plan along with details of the basic assumptions on which the plan was based is discussed in subsequent section.

The following section of the case study has deliberately been written in present tense rather than past tense to give one the feel of the plan as developed by the NDFC team.

4.1 NFL's Market Position

Considering the market environment given above, the NFL position will be as follows:

4.1.1 Polyester Fibre

The installed capacity of the NFL polyester fiber is 14000 tons per annum. Conversely, the deficit supply in the projected period is as low as 20,157 tons in 2002 and as high as 11,230 tons in the year 2004. In view of that, the NFL will not have any problem in marketing its fiber.

a) The quality of NFL's fiber is not the same as the modern plants based on continuous process (the NFL technology is based on old technology of batch process).

b) In view of the low quality of NFL's fiber, and the fact that NFL does not offer credit sales, transport facilities, and insurance, the prices of NFL fiber will therefore be lower than the market rate.

c) In view of the low prices and the quality of NFL polyester fiber, the NFL clients are generally old spinning mills producing lower count yarn. The NFL's fiber is more compatible to the old spinning mills, therefore they will remain NFL's clients.

4.1.2 Filament Yarn

The above discussed demand and supply position suggests that there will be excess supply of 228 tons in the year 2000. However, in subsequent years, the deficit will be 2318 tons which is expected to increase to 10424 tons by the year 2004. It may be noted that the supply schedule developed and discussed above is inclusive of NFL's capacity. Thus, in view of the deficit situation, NFL may not face any problem in marketing its filament yarn. The quality of NFL filament yarn is competitive to the market. However, as in the case of fiber, NFL does not give credit, transport, and insurance coverage; therefore, its prices are expected to be comparatively lower than the competitors.

4.2 The Restructuring Plan

The NFL has accumulated liabilities of more than 1.5 billion. Considering the prevailing market conditions and the size of project, which is based on old technology it could not service all the accumulated liabilities, efficiently. Therefore, the restructuring is required to be based on the debt servicing capability of the unit after rehabilitation. The parameters of the restructuring plan are discussed below:

1. Debt equity swaps amounting to Rs.191.000 million.
2. Capital injection of Rs. 125.000 million.
3. Restructuring of existing loans.
4. Capital generation of Rs.150.000 million by selling surplus land.

4.2.1 Debt Equity Swap

Presently, the Schon group with 53% share holding, is the majority shareholder of the company. Any restructuring of loans will neither be acceptable to the

IDB, Jeddah nor to the other equity holders such as NDFC and FCC&CL. Therefore, a debt equity swap has been suggested, so that the equity holder and creditors are able to reconstitute a Board for running the unit.

The Schon Group has 44.324 million shares. Against this, the Schon Group has pledged 43.030 million shares at various Banks and DFI as a security against the loans taken for the sister concerns of the Schon Group. This is inclusive of 19.11 million shares pledged by the Schon Group against the loans for NFL.

It is recommended that the 19.11 million shares pledged by the Schon Group against the liabilities of the NFL may be converted to equity at a par value of Rs. 10 per share. In view of this debt equity swap, the Creditors' forum would have the majority share holding of 70%, and thus would be able to form its own Board. With the suggested debt equity swap, the equity holding pattern will be revised as follows:

	Before Debt Equity Swap		Debt Equity Swap	After Debt Equity Swap	
Schon	443.24	52%	(191.11)	252.13	29.74%
NDFC	171.12	20.18%		171.12	20.18%
IDB	179.32	21.15%		179.32	21.15%
FCCCL	41.45	4.89%		41.45	4.89%
OTHERS	12.65	1.49%		12.65	1.49%
HBL LEASING	0	0	191.11	191.11	22.54%

The principal outstanding of Bank / DFIs as on June 30,1999 is Rs.900.39 million. With the proposed debt equity swap of Rs. 191.110 million, the principal outstanding amount will decrease to Rs.709.28 million.

4.2.2 Capital Induction

An amount of Rs.125.00 million will be inducted into NFL, which will be utilized for operating the unit at optimum level, by re-commissioning the polyester fiber and polymer sections and carrying out other repair and maintenance related to the yarn sections.

The proposed funds will be mainly utilized for the following:

	Rs. In Million
● Utility (Generator)	30.000
● Agitator	10.000
● Chiller (Fiber)	05.000
● Compressor (Fiber)	05.000
● BMR (Yarn)	25.000
● Working Capital	50.000
	125.000

4.2.3 Restructuring of Loans

- The servicing including repayment of principal of the freshly inducted loan of Rs.125.00 million for rehabilitation purposes will start from the first year of operation, after rehabilitation.
- NDFC had provided Rs.50.000 million bridge loan and Rs.30.000 million for working capital. The total outstanding liability as on June 30, 1999 against the above loans is RS.96.98 million.
- The total to liabilities of Rs.96.68 million towards NDFC will be frozen and will be liquidated in four years starting from the second year of operation, after rehabilitation.
- Allied Bank had created a forced financing PAD of Rs.9.14 million against NFL, by retiring the LC documents from their own resources. The total outstanding amount against this facility as on June 30, 1999 is Rs.10.080 million
- This amount will be frozen and will be liquidated in four years, starting from the second year of operation, after rehabilitation. The spares and raw material against this facility are in the possession of the Allied Bank, which the ABL shall release under the rehabilitation program.
- Out standing principal of Banks and DFI as on June 30, 1999 is Rs.557.52 million and mark-up is

Rs.295.64 million. Total out standing liability thus is Rs.853.16 million. These liabilities will be frozen.

- NFL's shares amounting to Rs.19.11 million are pledged with the HBL and others. Based on the debt equity swap at Rs.10/ share, the principal amount will be reduced to Rs.441.52 million, which will be liquidated in ten years, starting from the third year of operations.
- The mark-up on above amounting to Rs.295.64 million will be liquidated in 12 years, starting from the fifth year of operation, after rehabilitation.
- The total principal outstanding of lease facility as on June 30, 1999 is Rs.256.39 million. Outstanding mark-up as on June 30, 1999 is 96.71 million, and penal interest is Rs.87.73 million. Thus, the total outstanding liabilities against the leasing companies as on June 30, 1999 are Rs.440.38 million. The total outstanding dues against the leasing companies will be frozen.
- With the suggested debt equity swap of 7.511 million shares at the par value of Rs.10/shares, the leasing company's principal amount of Rs.256.39 million will be reduced to Rs.181.27 million, to be liquidated in ten years in equal instalments starting from the third year of operations, after rehabilitation.
- The mark-up amount of Rs.184.44 million will be liquidated in 12 years, starting from the fifth year of operation.

4.2.4. Sale of Surplus Land

The National Fibers Limited has a surplus land of 25 acres, of which 17 acre can be carved out and sold out. The sale of surplus land is expected to generate Rs.150.000 million. This can be utilized for:

o Liquidating the fresh borrowing under the rehabilitation, or

o Carrying out diversification such as color fiber and yarn. This is highly value added product line and can generate additional revenue Rs.150.000 million per annum.

4.3 Prospects after Rehabilitation

With the induction of Rs.125.000 million and proposed rehabilitation the plant can be operated at optimum level. At the optimum level the unit can produce;

ITEM	TONS / ANNUM
• Polyester fiber	14,000 tons per annum
• Polyester yarn	5600 tons per annum
• Polyester chips	21000 tons per annum (an intermediate raw material)

The projected operating results of the rehabilitated project are discussed below:

4.3.1 Projected Income Statement:

For the projected income statements see Appendix A

- The net annual sales will be about Rs.1.177 billion per annum.
- Total variable cost will be 81% of revenue throughout the projected period
- There will be a net profit of Rs.6.52 million in the first year of operation, which has an increasing trend. By the sixth year of operation it will increase to Rs.69.87 and by the tenth year of operation it will increase to Rs.90.68 million.
- The marginal contribution will be Rs.215.51 million per annum; This indicates that the unit will be able to absorb all the variable cost and total fixed cost, including the debt servicing and repayment of principal of the fresh loans amounting to Rs.125.000 million, and a portion of old liabilities.

4.3.2 Projected Cash Flow

The projected cash flow with detailed assumptions is enclosed as Appendix B and summarized working is presented below:

- The above projected cash flow suggests that the unit after rehabilitation will absorb all its fixed and variable cost, including payments of interest and debt servicing of proposed funds of Rs.125.000 million, and a portion of old loans. In fact, the unit will have surplus of Rs.6.51 million in the first year of operation, which has an increasing trend. By the sixth year of operation, the accumulated surplus position will increase to Rs.157.39 million. The accumulated surplus in tenth year of operation will be about Rs.259.53 million.

4.3.3 Breakeven

The commercial breakeven, in the first year of operations will be 96.97%, which will decline to 67.58% by the sixth year of operations. In the tenth year it will further reduce to 57.92%.

The cash break even in the projected period is as low as 61.02% first year and as high as 113% fifth year. From the sixth year of operation the cash breakeven is 88.12 % in the rest of the projected period. The reasons for such a fluctuation are that the unit will be servicing the interest and repayments of old loans as well. It may be noted that although in the cash break-even in the fifth year of operation is as high as 113%, the unit may not require borrowing of additional funds as the cash surplus carried forward from the previous year is about 161.000 million.

4.3.4 Sensitivity Analysis

1) Decrease of Sale Price by 5%
- Profit will decrease from Rs.59.77 million to Rs.35.62 million.
- Commercial breakeven will increase from 72.27% to 81.37%.
- Cash breakeven will increase from 113.67% to 128.03%.
- It may be pointed out that the above adverse position due to decrease in price of yarn of 5%, is also due to the fact that the unit is servicing substantial portion of old liabilities. Moreover, the unit has sufficient accumulated cash surplus to absorb such a high cash breakeven/commercial breakeven.
- Marginal contribution will decline from Rs.215.51 million per annum to Rs.191.24 million.
- Accumulated cash available will decrease from Rs.131.46 million to Rs.10.71 million.

2) Sale Prices Remain Constant & 90% Cu
- Profit will decrease from Rs.59.77 million to Rs.36.87 million.
- Commercial breakeven will increase from 72.27% to 80.80%.
- Cash breakeven will increase from 113.67% to 127.27%.
- Marginal contribution will decrease from Rs.215.51 million per annum to Rs.192.03 million.
- Accumulated cash available will decrease from Rs.131.46 million to Rs.16.96 million.

The above analyses indicate that in case of the above variations, the company will be able to absorb all the fixed and variable cost including the repayments of principal and markup of the current borrowing of Rs.125.000 million and a portion of old loans. Moreover, the unit will have sufficient accumulated cash surplus to absorb such a high cash breakeven/commercial breakeven.

5. RECOMMENDATIONS

In order to give effect to the rehabilitation plan, it will be necessary for the following actions to take place:

I. A new Board of Directors will be appointed by the Federal Government to take complete management and control of NFL.

II. The rehabilitation plan as proposed in the subject report will also be notified by the government. The proposed debt equity swap will be implemented, immediately. The new equity holders will enter into a joint venture agreement amongst themselves with respect to their rights and obligations as the new sponsors of NFL. The agreement will also specify the conditions on which the shares may be dis-invested. The agreement will be structured, binding and effective.

III. The articles and memorandum will be amended to ensure that the Schon Group or any of their nominees cease to have any voting rights in terms of the annual general meeting, and any rights vis-à-vis the management of the company.

IV. Action can still be taken for misappropriation and ultra vires action u/s 296 of the Companies Ordinance, 1984 to recover liabilities from the personal assets of the Schon Group nominees.

V. The JM.39/97 could be withdrawn. However, there will be no possible representation by the Schon Group, since they cease to be shareholders/members and thus their role as Respondents in the JM 39/97 also becomes infractuous. This will save NFL from any further possible litigation and aid them in the smooth running of the affairs of NFL, unhampered.

VI. In order to maintain the continuity of operations, it is necessary that Rs.25.000 million as an interim arrangement may be immediately inducted in to NFL.

6. AFTERWARDS

Forced liquidation, generally, results in scrapping of the plant and machinery and selling the land to real estate builders. Filing the petition under section 292 of the Companies Ordinance 1984 was a "test case" which was undertaken with the following vision.

a) NDFC's vision was to takeover the sick units, revive and rehabilitate them and then sell them to the potential buyers. This would have ensured that the projects continued running and contributing towards the economic development.

b) NDFC and the banks were fully aware of the fact that running, takeover units, and selling them to the potential buyers was not their forte. Had the test case of NDFC's takeover been successful, the NDFC/Banks would have developed a team or "expert working group" who, on behalf of the NDFC/Banks, would have run, rehabilitated, and sold the taken over units to the potential buyers.

c) One of the key reasons for the failure of the test case was extra ordinary delay by the court in giving the verdict on the main petition. Banks, generally, are reluctant to make investment in the units that are still in litigation, therefore, they did not participate in the rehabilitation of NFL.

APPENDIX-A

PROJECTED INCOME STATEMENT

	1st yr	2nd yr	3rd yr	4th yr	5th yr	6th yr
Sales	1177.48	11177.48	11177.48	1177.48	1177.48	1177.48
Raw material and packaging	711.15	711.15	711.15	711.15	711.15	711.15
Other variables	250.82	250.82	250.82	250.82	250.82	250.82
Total variable cost	961.97	961.97	961.97	961.97	961.97	961.97
Total fixed cost	166.49	156.24	147.02	138.71	131.24	124.52
Cost of sales	1128.45	1118.21	1108.98	1100.68	1093.21	1086.48
Gross profit/(loss)	49.03	59.27	68.50	76.80	84.27	90.99
Total operating cost	36.62	32.12	27.62	23.12	18.62	15.24
Other income Profit/(loss) before income tax	12.41	27.16	40.88	53.68	65.66	75.75
Turn over tax	5.89	5.89	5.89	5.89	5.89	5.89
profit/(loss) after tax	6.52	21.27	35.00	47.80	59.77	69.87

APPENDIX-B

PROJECTED CASH FLOW

	1ST YR	2ND YR	3RD YR	4TH YR	5TH YR	6TH YR
Inflow						
Net profit/(loss) after tax	6.52	21.27	35.00	47.80	59.77	69.87
Depreciation add back	102.49	92.24	83.02	74.71	67.24	60.52
Financial charges (add back)	21.38	16.88	12.38	7.88	3.38	0
Working capital	125.000					
Total inflows	255.39	130.39	130.39	130.39	130.39	130.39
Out flow						
Principle repayment	25.00	25.00	25.00	25.00	25.00	0
Repayment of mark up	21.38	16.88	12.38	7.88	3.38	0
repayment of old loans/mark up	0	26.69	88.97	88.97	131.46	104.77
Capital cost bmr	75					
Working capital/inventory	50.00	0.00	0.00	0.00	0.00	0.00
Total out flow	171.38	68.57	126.34	121.84	159.84	104.77
Surplus/(deficit)	84.01	61.82	4.04	8.54	(29.45)	25.61
Closing balance	86.51	148.33	152.37	160.91	131.46	157.07