



The Pakistan Credit Rating Agency Limited

Rating Report

Gul Ahmed Textile Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
03-Sep-2019	A	A1	Stable	Maintain	-
05-Mar-2019	A	A1	Stable	Maintain	-
05-Sep-2018	A	A1	Stable	Maintain	-
05-Mar-2018	A	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect Gul Ahmed Textile Mills Limited's (Gul Ahmed) established business profile with strong presence in the broader textile value-chain; enabling the Company to manage volatility in textile business. Presence in retail with renowned brand "Ideas" in local market adds up to stronger business risk. The entity has achieved a sizable revenue base, while focus on value added products brings higher gross margins. This emanates from export market orientation, targeting established niche of quality-conscious institutional buyers. Nevertheless, this has led to customer concentration; longevity of relationship with big-name clients in addition to sustained quality would help manage the risk. The currency devaluation has boded well for the Company's export-oriented topline while recurrent BMR has improved efficiency, depicted in improved gross margins. Meanwhile, hefty branding activities and competition in the local market has kept net margins relatively strained. Gul Ahmed's financial risk profile remains strong, characterized by robust cash flows, supporting improved working capital management and strong debt-servicing ability. While leveraging remains on the higher side, financing at concessionary rates by the SBP shields the Company against recent interest rate hikes.

The ratings are dependent on the Company's ability to sustain its business profile while maintaining strong margins and coverages. At the same time, prudent management of working capital needs and meeting financial obligations remain critical.

Disclosure

Name of Rated Entity	Gul Ahmed Textile Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	PACRA_Methodology_Corporate_FY19(Jun-19),PACRA_Criteria_LT ST Relationship_FY19(Jun-19),PACRA_Criteria_Rating Modifiers_FY19(Jun-19)
Related Research	Sector Study Textile(Oct-18)
Rating Analysts	Muhammad Hassan muhammad.hassan@pacra.com +92-42-35869504

Profile

Legal Structure Gul Ahmed Textile Mills Limited (Gul Ahmed) is a listed, public limited concern, incorporated in 1953.

Background Gul Ahmed is the flagship company of Gul Ahmed Group, which commenced spinning and weaving operations in 1953 as a private limited company and became listed in 1955. The Company is now a fully integrated composite textile unit with its own retail brand "Ideas by Gul Ahmed" with an extensive chain of over 100 retail stores across Pakistan.

Operations Gul Ahmed's operations are broadly divided into four main segments: Spinning, Weaving, Processing & Home Textile and Retail, with all segments operating as separate profit centers. The Company also has captive power generation with a capacity exceeding its in-house requirements.

Ownership

Ownership Structure The majority stake (~67%) in Gul Ahmed is held by the Gul Ahmed Group through two corporates: Gul Ahmed Holdings (Pvt.) Limited (~67%) and Swisstex Chemicals (Pvt.) Limited (~3%), while the remaining stake lies with financial institutions and the general public.

Stability Gul Ahmed Holdings, the Group's holding company, is formed solely for the purpose of investment in subsidiaries of Gul Ahmed and is owned by the Bashir Family. Presence of the holding company bodes well for the stability of Gul Ahmed.

Business Acumen The Bashir Family has over five decades of experience in the textile industry. In addition to textile, the Family has interests in chemicals and IT through other group companies. The sponsors of the Company carry significant industrial experience and are actively involved in their respective roles.

Financial Strength The Bashir Family has demonstrated commitment and support for Gul Ahmed, in the years of expansion, injecting cash in the form of right issue. The family also holds a sizable investment portfolio of properties and has demonstrated willingness and ability to support the Company in case the need arises.

Governance

Board Structure The overall control of the Company vests in a seven-member Board of Directors including the Chairman – Mr. Mohamed Bashir – and Vice Chairman – Mr. Zain Bashir. The remaining members comprise three directors from the sponsoring family while two are independent directors.

Members' Profile Mr. Mohamed Bashir – Chairman of the Group – is a business veteran and has been entrusted with various honorary consular positions by Government of Pakistan. He also serves on the Board of various other companies. The other Board members also possess diversified experience and have reasonably long association with the Company.

Board Effectiveness Although the Board is dominated by the sponsoring family, due challenge is brought in by independent directors, enhancing the governance profile of the Company. Furthermore, attendance of Board members remains satisfactory and board meeting minutes are properly documented while two subcommittees exist to assist on relevant matters.

Financial Transparency The Company has outsourced its internal audit function to M/s Grant Thornton Anjum Rahman Chartered Accountants while M/s. Kreston Hyder Bhimji & Co. Chartered Accountants is the external auditor of the Company. Both auditors are listed in "A" category of the State Bank's panel of auditors. The external audit for the period ended June 30th, 2019, is in process.

Management

Organizational Structure Gul Ahmed has a lean organizational structure with a large number of individuals reporting directly to the CEO.

Management Team Mr. Mohamed Bashir is entrusted with overall oversight of the Company while his youngest son, Mr. Zaki Bashir, is CEO. Mr. Zaki Bashir has been on the Board of Gul Ahmed since 2008 and also serves on the Board of various other Group companies. The family members have structured themselves well in terms of roles and responsibilities with defined management roles.

Effectiveness While no formal management committees are in place, informal management committees are formed from time to time on need basis. Further, weekly one to one meetings are held with all departmental heads where performance of each department is discussed at length.

MIS The Company has deployed Oracle EBS 12.1 and Microsoft Dynamics as ERP solutions, which integrates the business functions of the Company and help the management in timely decision making. Meanwhile, Microsoft Dynamics Cloud has also been successfully implemented in the retail segment.

Control Environment The Company's monthly MIS comprises comprehensive segment and unit wise performance reports review frequently by the senior management. Gul Ahmed is also accredited with International certifications for compliance including ISO 9001.

Business Risk

Industry Dynamics In FY19, Pakistan's textile sector exports displayed negative YoY growth of ~1% in dollar terms. Even though leading textile categories including ready-made garments, knitwear and cotton cloth displayed double-digit volumetric growth, the hit to unit prices on account of exporters having to share the benefit of the currency depreciation with buyers, curbed overall growth. Meanwhile, cotton yarn exports fell by ~18% YoY, mainly driven by volumetric decline owing to the US-China trade war. Amidst rising interest rate environment, the recent removal of zero-rated status of the textile sector in the FY19-20 budget may pose a challenge to the liquidity of exporters if refunds are not timely disbursed by the government.

Relative Position Gul Ahmed is among the largest vertically integrated textile units in Pakistan. Overall, it is among the largest exporters of the country, with a share of ~2% in the Country's total textile exports, while "Ideas by Gul Ahmed" is a leading textile retail brand.

Revenues Gul Ahmed maintains a balanced sales mix, slightly tilted toward exports (~55%) comprising apparel and home textile while yarn, fabric and retail clothing is sold locally. During 9MFY19, revenues witnessed ~25% YoY growth driven mainly by: i) currency devaluation during the period, ii) increase in yarn revenues led by volumetric growth following addition in spinning capacity during the previous year as well as favorable yarn price trend and iii) strong demand in the retail and home textile segments. Meanwhile, the Company's customer concentration remains high, with over 25% of total revenue being generated from a single customer.

Margins The Company's gross margin has shown YoY improvement (9MFY19: ~23%, 9MFY18: ~21%), driven by a combination of: i) impact of the currency devaluation, ii) timely procurement of raw material and iii) upgradation of machinery in the spinning and weaving segments. Operating margin also showed significant improvement (9MFY19: ~10%, 9MFY18: ~7%) as the Company continues to control selling expenses through consolidation of revenues from existing retail stores. Despite a ~44% increase in finance cost over the period on account of higher borrowing to finance working capital management and BMR, profitability remained robust, with net profit amounting to ~PKR 2,697m (9MFY18: ~PKR 1,255) while net margin amounted to ~7% (9MFY18: ~4%).

Sustainability The Company regularly undertakes BMR which has resulted in significantly enhanced capacity utilization and margins over the years, particularly in the spinning and home textile segments. The Company incurred significant capex in the weaving segment during 3QFY20, including enhancements for value-addition as well as replacement of old looms. These measures are expected to help sustain margins, going forward.

Financial Risk

Working Capital Gul Ahmed's working capital requirements are a function of its inventory and receivables for which the Company relies on a mix of internal generation and short-term borrowing. The Company maintains a sizable borrowing cushion, at trade assets level, on account of strong cash flows. The Company's net cash cycle remains stretched, increasing YoY to ~150 days (9MFY18: ~134 days). This is mainly due to increased procurement of cotton to cater to additional spinning capacity while finished inventory levels remained seasonally high to cater to international orders and local retail demand.

Coverages During 9MFY19, free cashflows surged by ~50%, driven by strong profitability. Thus, coverages showed YoY improvement, with interest coverage clocking in at ~5.8x (9MFY18: ~5.7x) while core coverage increased to ~2.7x (9MFY18: ~2.1x). Predominant portion of borrowing availed at the State Bank's concessionary rates has kept the Company's interest rate exposure amidst the rising interest rate environment quite low.

Capitalization Gul Ahmed has a highly leveraged capital structure (9MFY19: ~67%, 9MFY18: ~65%), mainly comprising short-term borrowing (~67%). Total borrowing has witnessed a significant YoY increase (9MFY19: ~PKR 30bn, 9MFY18: ~PKR 22bn) to support increased working capital needs as well as capex including BMR and recent expansionary activities.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

Gul Ahmed Textile Mills Limited Textile Composite	Mar-19 9M	Jun-18 12M	Jun-17 12M	Jun-16 12M
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A BALANCE SHEET

1 Non-Current Assets	18,500	16,369	16,280	12,241
2 Investments	-	-	-	-
3 Related Party Exposure	58	58	58	58
4 Current Assets	35,764	26,836	20,381	19,870
<i>a Inventories</i>	23,103	16,144	12,470	13,854
<i>b Trade Receivables</i>	5,713	5,399	3,345	2,364
5 Total Assets	54,322	43,263	36,719	32,169
6 Current Liabilities	10,001	7,202	5,722	5,121
<i>a Trade Payables</i>	3,413	2,458	1,956	2,512
7 Borrowings	29,814	23,354	19,760	17,984
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	80	87	322	345
10 Net Assets	14,427	12,621	10,914	8,718
11 Shareholders' Equity	14,427	12,621	10,914	8,718

B INCOME STATEMENT

1 Sales	40,524	45,626	40,066	32,275
<i>a Cost of Good Sold</i>	(31,047)	(36,050)	(32,858)	(24,968)
2 Gross Profit	9,476	9,576	7,207	7,306
<i>a Operating Expenses</i>	(5,403)	(6,251)	(5,789)	(5,076)
3 Operating Profit	4,074	3,325	1,419	2,230
<i>a Non Operating Income</i>	(109)	(9)	268	15
4 Profit or (Loss) before Interest and Tax	3,965	3,315	1,686	2,245
<i>a Total Finance Cost</i>	(985)	(987)	(877)	(910)
<i>b Taxation</i>	(283)	(253)	10	(193)
6 Net Income Or (Loss)	2,697	2,075	818	1,141

C CASH FLOW STATEMENT

<i>a Free Cash Flows from Operations (FCFO)</i>	4,824	4,774	2,274	3,009
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	3,918	3,823	1,422	2,007
<i>c Changes in Working Capital</i>	(5,819)	(4,907)	694	(4,092)
1 Net Cash provided by Operating Activities	(1,900)	(1,084)	2,116	(2,085)
2 Net Cash (Used in) or Available From Investing Activities	(3,504)	(1,956)	(5,320)	(4,159)
3 Net Cash (Used in) or Available From Financing Activities	5,576	3,240	3,166	6,435
4 Net Cash generated or (Used) during the period	172	200	(38)	190

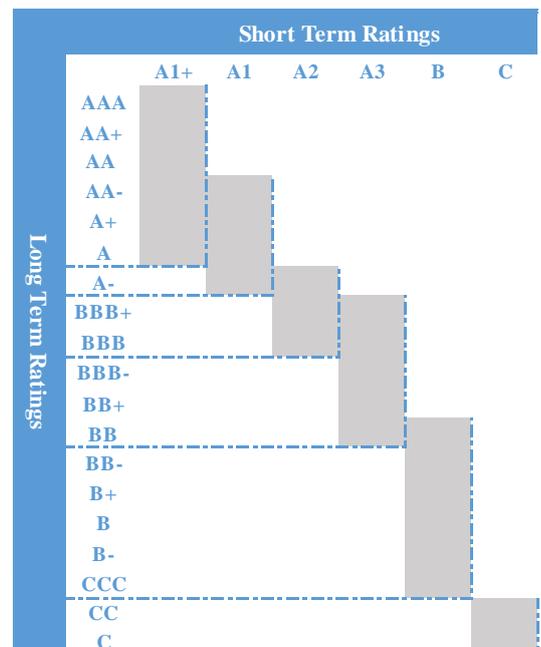
D RATIO ANALYSIS

1 Performance				
<i>a Sales Growth (for the period)</i>	18.4%	13.9%	24.1%	-3.2%
<i>b Gross Profit Margin</i>	23.4%	21.0%	18.0%	22.6%
<i>c Net Profit Margin</i>	6.7%	4.5%	2.0%	3.5%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	13.5%	11.6%	7.6%	10.7%
<i>e Return on Equity (ROE)</i>	26.6%	17.6%	8.3%	14.4%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	170	149	146	281
<i>b Net Working Capital (Average Days)</i>	150	132	126	246
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	3.6	3.7	3.6	3.9
3 Coverages				
<i>a EBITDA / Finance Cost</i>	6.5	6.3	4.2	4.3
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	2.7	2.2	1.6	2.3
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	1.9	2.1	5.1	2.3
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	67.4%	64.9%	64.4%	67.4%
<i>b Short-Term Borrowings / Total Borrowings</i>	67%	65%	60%	72%
<i>c Average Borrowing Rate</i>	4.2%	3.9%	3.9%	5.4%

Credit 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		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
BB+ BB BB-	Moderate risk. Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
B+ B B-	High 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.	C	An inadequate capacity to ensure timely repayment.
CCC CC C	Very high credit 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.		



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’.

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. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating Watch may accompany Outlook of the respective opinion.

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, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Disclaimer: PACRA’s ratings are an assessment of the credit standing of entities/issue in Pakistan. They do not take into account the potential transfer / convertibility risk that may exist for foreign currency creditors. PACRA’s opinion is not a recommendation to purchase, sell or hold a security, in as much as it does not comment on the security’s market price or suitability for a particular investor.

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) Conflict of Interest

- i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
- ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
- iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

- (3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)
- (4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
- (5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

- (6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
- (7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
- (8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)
- (9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
- (10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
- (11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

- (12) 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 fee mandate - signed with the payer, which can be different from the entity
- (13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
- (14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
- (15) PACRA ensures that the rating assigned to an entity or instrument is 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 | Chapter III; 12-2-(i)
- (16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
- (17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

- (18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
- (19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
- (20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
- (21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) 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 | Chapter III | 14-(F-VII)

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