The Pakistan Credit Rating Agency Limited

Rating Report

Ghandhara Industries Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
12-Dec-2018	A+	A1	Stable	Maintain	-
30-Jun-2018	A+	A1	Stable	Maintain	-
29-Dec-2017	A+	A1	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Ghandhara Industries Limited (GIL) operates in the pickup, truck & buses segment of the automobile sector. The strength of the company is its alliance with ISUZU – a leading Japanese brand in the aforementioned segment. ISUZU has enabled the company to build a strong fortress in the competitive industry of Pakistan. The volumes have been steadily rising – boosting the relative market share of GIL. The company has improved its ranking in the market and has recently launched its pickup range by the name of Isuzu D-Max. The group has built synergies between the two companies operating in the same sector. The sponsoring group upholds good corporate governance standards. Their business acumen is further enriched by the group's stake in the country's leading tyre manufacturing company. GIL has enhanced its market share over the last couple of years. It is important to sustain the growth while managing the rising competition. Foreign players are also taking interest in the local market. The landscape of the industry is expected to change – although it is yet to be seen. The financial risk profile of GIL is strong. The working capital is supported by cash cum advances sale mechanism.

The ratings are dependent on upholding of the company's business as well as financial risk profile. Two key elements are company's stance on long term debt and working capital management. Moreover, management's ability to sustain its market share while benefiting from positive demand fundamentals is crucial.

Disclosure	
Name of Rated Entity	Ghandhara Industries Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-18),Methodology | Criteria | Rating Modifier(Jun-18),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study | Auto and Allied | Trucks & Buses(Dec-18)
Rating Analysts	Nadeem sheikh | nadeem.sheikh@pacra.com | +92-42-35869504

Profile

Legal Structure Ghandhara Industries Limited (hereinafter referred to as ‘‘the Company’’ or ‘‘Ghandhara’’) is a public listed entity. It is authorized assembler and dealer of ISUZU pickup, truck and buses in Pakistan. The corporate office of the company is in F-3, Hub Chawki Road, S.I.T.E.

Background The company was founded in 1953 by General Motors Overseas Distribution Company and was purchased in 1963 by Late Lt. General (R) Habibullah Khan Khattak. The company was later nationalized in 1972 and renamed as National Motors Limited. In 1992, Late Lt. General (R) Habibullah Khan Khattak reacquired the company from the Government and renamed it to Ghandhara Industries Limited.

Operations Ghandhara is primarily engaged in the assembly, body fabrication and sale of Isuzu pickup, truck and buses and is the exclusive distributor of ISUZU products in Pakistan. The company has outsourced the assembly of its pickup, truck and buses to Ghandhara Nissan Ltd (an associate).

Ownership

Ownership Structure Majority ownership of the company is held by Bibojee Group of Companies, whereas Bibojee Services (Private.) Limited directly owns ~39% shares, Ghandhara Nissan Limited has ~19% and Universal Insurance Company Limited holds ~6% shares of the company. Other shares are held by corporates, financial institutions and individual shareholders.

Stability Bibojee Group of Companies, represents a family with history of entrepreneurship spanning over four decades. The group operates through holding company “Bibojee Services (Private) Limited”. This provides a formal structure to the group and a platform for relatively smooth execution of succession matters amongst family members.

Business Acumen Bibojee is the parent company of Bibojee Group of companies under whose umbrella come automobile companies, textile, insurance, construction and tyre manufacturing concern. Bibojee's group understanding of the business is strong.

Financial Strength Financial strength of Ghandhara’s sponsors is deemed strong.

Governance

Board Structure The overall control of the company vests in seven members board of directors. The board structure comprises of one executive director, four non-executive directors and two independent directors.

Members’ Profile The Board members are professionals with experiences of managing business affairs in different sectors. Mr. Lt. Gen. (Retd.) Ali Kuli Khan Khattak is the Chairman of the Board having diverse experience in the Auto and Allied sector, which brings specialized and comprehensive experience and knowledge on the board

Board Effectiveness In line with the guidelines of Code of Corporate Governance, the Board has formed two sub-committees – (i) HR and Remuneration Committee and (ii) Audit Committee. Both committees are headed by an Independent director and consist of 5 and 4 members respectively. Attendance in meetings held during FY18 was good.

Financial Transparency An effective Internal Audit department reporting to the Audit Committee is in place. M/s. Shine Wing Hameed Chaudhari & Co. along with M/s Junaidy Shoaib Asad have expressed an unqualified opinion on financial accounts of FY18.

Management

Organizational Structure The organizational structure of the company is divided broadly into various functional departments and all the department heads report to Deputy Chief Executive Officer. Major departments include (i) Finance, (ii) Human Resources and Admin (iii) Quality control (iv) Sales and Marketing (v) Material Management.

Management Team Management of the company comprises qualified and experienced professionals with a wide range of skills and diversified experience. Mr. Ahmad Kuli Khan Khattak is the CEO of the company Mr. Muhammad Kuli Khan Khattak is the Deputy Chief Executive Officer. He has an overall experience of over 11 years and he is assisted by able management team.

Effectiveness Every department head is responsible to manage the affairs of their departments. Clearly defined rules and responsibilities in organization add to the effectiveness of the organization structure.

MIS The company has implemented ERP-business software package designed to integrate all areas of a business. Strong MIS system is expected to add value to the company's operations going forward.

Control Environment The company has outsourced its assembly activity to Ghandhra Nissan Limited and ratained body fabrication of the trucks and buses in house.

Business Risk

Industry Dynamics Pakistan’s truck and bus industry is largely dominated by domestic players such as HinoPak, Ghandhara Industries, Master Trucks and Ghandhara Nissan. According to Pakistan Automotive Manufacturer Association a record 10,093 units of trucks and buses were sold in FY18 with 17% YOY growth. HinoPak was the top seller in FY18.

Relative Position Ghandhara a strong player in the industry, possessing 40% market share as at End June-18. Much of the trucks demand of the company is generated through commercial customers, such as oil marketing companies. The company sold 4,000 units of ISUZU trucks and buses during FY18. Due to strong relationship with its customers, the company is well poised to retain its market share.

Revenues Ghandhara’s revenue increased by 56% on YOY basis. The company posted a revenue of PKR 16,772mln during the FY18 due to strong demand for trucks. Revenue for 1QFY19, however remained stagnant on the backdrop of restricted demand.

Margins Gross profit margin of the company reduced to ~14% in 1QFY19 as compare to ~19% in FY18 mainly due to increase in cost of raw material. Decrease in gross profit margin led to decrease in operating margin in 1QFY19. Margin are expected to remain under pressure going forward as the recent devaluation of currency will make its impact.

Sustainability Sale of the company in coming periods is expected to increase after the resumption of orders from government institutes. Launch of D-Max pick-ups will also add to the revenues.

Financial Risk

Working Capital Average inventory days of the company increased to ~132 days at the end of 1QFY19 (~117 days FY18) due to launch of new product and less than expected demand. Net working capital days of the company also increased to ~116 days in 1QFY19 as compared to ~86 days in FY18.

Coverages Free cash flow from operations (FCFO) decreased by 169% on YOY basis in 1QFY19 clocking in at PKR~142 million (1QFY18: PKR~384.44 million). 1QFY19 witnessed a decline in FCFO on the backdrop of decreased profits. Decrease in FCFO led to decrease in interest coverage of the company during the period under review, interest coverage ratio decreased to 1.5x in 1QFY19 (FY18: 5.6x). Core and total coverage ratios in 1QFY19 also decreased to ~1.5x.

Capitalization The company has a leveraged capital structure. Total debt of the company in 1QFY19 clocked in at PKR~5,313 million as compared to PKR~3,675 million in FY18. Out of the total debt of PKR~5,313 million, PKR~5,274 million pertained to short term and PKR~39 million were long term liabilities. Gearing ratio is continuing its upward trend as it stand at ~51% in 1QFY19 (FY18: ~43.8%, FY17:~18%). Cautious management approach is necessitated. .

Ghandhara Industries Ltd

BALANCE SHEET	30-Sep-18	30-Jun-18	30-Jun-17	30-Jun-16
	3MFY19	FY18	FY17	FY16
Non-Current Assets	**2,576**	**2,481**	**2,058**	**1,956**
Investments (Incl. Associates)	**90**	**90**	**90**	**90**
Current Assets	**10,861**	**9,463**	**6,446**	**3,114**
Inventory	7,850	6,888	3,779	1,624
Trade Receivables	371	95	485	260
Others	2,639	2,480	2,181	1,231
Total Assets	**13,526**	**12,034**	**8,595**	**5,160**
Debt	**5,282**	**3,640**	**792**	**194**
Short-term	5,274	3,632	792	194
Long-term (Incl. Current Maturity of Long-Term Debt)	8	8	-	-
Other Short-term Liabilities	3,091	3,544	4,047	1,732
Other Long-term Liabilities	126	127	66	126
Shareholder's Equity	**5,027**	**4,723**	**3,689**	**3,109**
Total Liabilities & Equity	**13,526**	**12,034**	**8,595**	**5,160**

INCOME STATEMENT				
Turnover	**4,384**	**16,772**	**10,741**	**5,826**
Gross Profit	623	3,111	2,203	1,547
Other Income	(16)	6	(222)	(4)
Financial Charges	(93)	(222)	(225)	(113)
Net Income	**304**	**1,362**	**796**	**746**

Cashflow Statement				
Free Cashflow from Operations (FCFO)	142	1,236	1,090	979
Net Cash changes in Working Capital	(2,062)	(3,413)	(932)	(285)
Net Cash from Operating Activities	(1,971)	(2,373)	(66)	589
Net Cash from InvestingActivities	(71)	(472)	(110)	(73)
Net Cash from Financing Activities	(5)	(303)	(203)	(58)
Net Cash generated during the period	(2,047)	(3,148)	(379)	457

Ratio Analysis				
Performance				
Turnover Growth	10%	56%	84%	77%
Gross Margin	14%	19%	21%	27%
Net Margin	7%	8%	7%	13%
ROE	17%	21%	17%	18%
Coverages				
Debt Service Coverage (x) (FCFO/Gross Interest+CMLTD+Uncovered STE	1	5	5	9
Interest Coverage (x) (FCFO/Gross Interest)	2	6	5	9
Debt Payback (Years) (Total Lt.Debt (excluding Covered Short Term Borrowings) / FCFO)	0.2	0.0	0.0	0.0
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	115	86	82	79
Capital Structure (Total Debt/Total Debt+Equity)	51%	44%	18%	7%

Rating Scale

Credit Rating Scale & Definitions

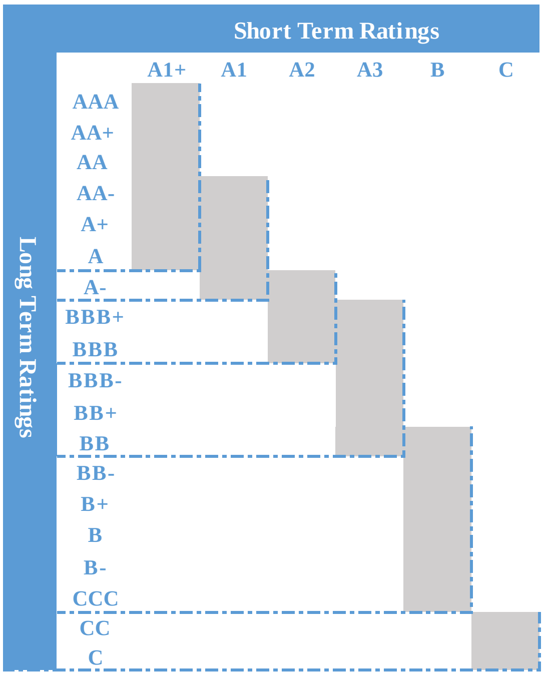
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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-**	**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+ **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.
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.

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.



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 surveill the opinion due to lack of requisite information.

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

Regulatory and Supplementary Disclosure
(Credit Rating Companies Regulations,2016)

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)
Proprietary Information