The Pakistan Credit Rating Agency Limited

Rating Report

Ghandhara Industries Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
22-Oct-2021	A+	A1	Stable	Upgrade	-
05-Nov-2020	A	A1	Stable	Maintain	-
13-Dec-2019	A	A1	Stable	Downgrade	-
13-Jun-2019	A+	A1	Stable	Maintain	-
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) has been one of the top leading automobile companies in Pakistan. Its product lines include trucks (light-duty, medium-duty & heavy-duty) buses, and D-MAX pick up. The strength of the company is its alliance with ISUZU – a leading Japanese brand in the country's trucks & buses segment. ISUZU has enabled the company to build a strong fortress in the competitive industry of Pakistan. FY21 has been a 'recovery period' for the auto sector. The buying interest among consumers revived after the reopening of markets in June 2020 as trucks sales soared by 20%, followed by 17% in buses, and 57% in pickups. Ghandhara Industries Limited has managed to translate the same in its top-line and achieve revenue growth of 27% in FY21. Further, the company's sales registered uptick as interest rates were supportive, hence strengthening auto financing. Bottom-line growth of the company is a resultant of improved gross margins for the period under review. Company's exposure to more advances has proved to be beneficial as business relies less on borrowed capital to fuel growth and other initiatives. There has been a considerable boost in company's cash flows from operations, thus bolstering coverages position. Over the years, company has been able to sustain its position in domestic automotive sector while managing uprising competition and secured high market share. The sponsoring group built synergies between the associated companies operating in the auto 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. During June 2021, finer working capital and reduced borrowings along with the low finance cost elevated the financial strength of the company. The capital structure remains moderately leveraged mainly comprising short-term borrowings.

The ratings are dependent on upholding of the company's business as well as financial risk profile. Improvement in margins and intact coverages are imperative. Key element is company's stance on working capital management. Moreover, management's ability to sustain its market share during the demand crunch is crucial.

Disclosure	
Name of Rated Entity	Ghandhara Industries Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21)
Related Research	Sector Study | Trucks & Buses(Dec-20)
Rating Analysts	Sohail Ahmed Qureshi | sohail.ahmed@pacra.com | +92-42-35869504

Profile

Legal Structure Ghandhara Industries Limited is a public listed entity. The corporate office of the company is in F-3, Hub Chawki Road, S.I.T.E, Karachi.

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 (outsourced), body fabrication and sale of Isuzu pickup, truck and buses and is the exclusive distributor and authorised assembler & dealer of ISUZU products in Pakistan. The company has outsourced the assembly of its pickup, truck and buses to Ghandhara Nissan Ltd.

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 (another associate company) holds ~6% shares. Other shares are held by corporates, financial institutions and individuals.

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 Bibojee Services (Private) Limited has strategic stakes in companies from different sectors including Textile, Insurance, Automobile and construction. Financial strength of the group is strong.

Governance

Board Structure The overall control of the company vests in seven members board of directors. The board structure comprises 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 4 and 3 members respectively. Attendance in meetings held during FY21 was good.

Financial Transparency An effective Internal Audit department reporting to the Audit Committee is in place. M/s. Shine Wing Hameed Chaudhari & Company, a QCR rated firm, has expressed an unqualified opinion on financial statements of FY21.

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 14 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 corporate structure of the company is diverged into various departments each having an effective Internal Control System. Robust MIS to assist reporting needs of management strengthens the control environment.

Business Risk

Industry Dynamics Pakistan's trucks and buses industry is dominated by domestic players such as Ghandhara Industries, Ghandhara Nissan, HinoPak and Master Trucks. Ghandhara Industries occupies the highest share in the industry followed by Master, HinoPak and Ghandhara Nissan. According to Pakistan Automotive Manufacturers Association, 4,347 units of trucks & Buses were sold during FY21 as compared to 3,647 units in FY20 representing a growth of ~19.19% as compared to decline of ~46% in FY20 which demonstrates that overall demand has revived after Global Pandemic Crisis. Positive macro indicators like lower interest rate, real-time recovery of related industries (OMCs, Steel, Construction) have shown good results, purchasing power has improved which further instigated the demand to rise.

Relative Position Ghandhara Industries - a strong player in the industry, possessing ~46% market share during FY 2021. Much of the trucks demand of the company is generated through commercial customers, such as oil marketing companies. The company sold 1,907 units of ISUZU trucks, 113 units of ISUZU buses, and 316 units of Isuzu D-Max Pickup during FY21 as compared to 1,582 units of trucks, 120 units of buses, and 656 units of D-Max Pickup in FY20. Due to strong relationship with its customers, the company is well poised to retain its market share.

Revenues During FY21, the negative impacts of COVID-19 started to reverse. Resultantly, automobile sector of Pakistan showed signs of springing back to life on back of resuming economic activities. Current volumes in truck and bus market in FY21 significantly improved, subsequently Company also managed to achieve revenue growth of 27% during FY21. Revenue of the company stands at PKR 14,999mln in FY21 (FY20: PKR 11,788mln).

Margins Consumption of economic activities and increasing volumes drive the increase in gross profit margin of the company. Gross margin ratio in FY20 was just ~6% on account of under-absorption of overheads due to contract assembly volumes. However, it has now improved to 13.8% during FY21. Increase in gross profit led to operating profit of PKR 1,151mln in FY21 as compared to loss of PKR 73mln in FY20. Accordingly, operating margins turned into positive 7.7% as compared to negative 0.6% in FY20. Recovery in Company's financial results is also due to decline in short term borrowings and reduction in finance cost.

Sustainability Favourable business conditions coupled with better business opportunities for the Company including new institutional sales have started to steer the Company out of losses and it is expected that during the FY22, the Company will record growth both in terms of volumes and profitability.

Financial Risk

Working Capital Inventory days of the company decreased to ~170 days at the end of FY21 (~277 days: FY20) on back of decrease in company's inventory level. Receivable days have increased to ~15 days as compared to ~11 days in FY20 on account of revival in demand and increasing sales. Net working capital days of the company decreased to ~172 days in FY21 as compared to ~273 days in FY20.

Coverages Free cash flow from operations (FCFO) increased to PKR 1,160mln in FY21 from PKR -393mln in FY20. Increased cash flows led to improved interest coverage and core coverage ratio of the company. Going forward, strengthened cashflow streams are essential to keep the coverages intact.

Capitalization The company has a leveraged capital structure. Total debt of the company in FY21 clocked in at PKR~3,107mln as compared to PKR~6,614mln at FY20. Out of the total debt, PKR~2,853mln was short term and PKR~254ln was long term debt. Due to decrease in borrowings during the period, gearing ratio has improved, gearing ratio stands at ~35% at the end of FY21 (FY20: ~56.6%).

The Pakistan Credit Rating Agency Limited

Ghandhara Industries Limited Auto & Allied Trucks & Buses	Jun-21 12M	Mar-21 9M	Jun-20 12M	Jun-19 12M
A BALANCE SHEET				
1 Non-Current Assets	4,447	4,457	4,482	2,884
2 Investments	88	88	88	88
3 Related Party Exposure	1	1	1	1
4 Current Assets	10,368	11,003	14,358	12,949
a Inventories	*6,431*	*5,943*	*7,547*	*10,359*
b Trade Receivables	*581*	*1,071*	*639*	*88*
5 Total Assets	14,905	15,549	18,929	15,923
6 Current Liabilities	6,076	6,673	7,058	4,762
a Trade Payables	*616*	*424*	*452*	*517*
7 Borrowings	3,107	3,354	6,614	6,362
8 Related Party Exposure	-	-	146	118
9 Non-Current Liabilities	46	34	37	33
10 Net Assets	5,675	5,488	5,075	4,648
11 Shareholders' Equity	5,675	5,488	5,075	4,648
B INCOME STATEMENT				
1 Sales	14,999	10,603	11,788	13,910
a Cost of Good Sold	*(12,924)*	*(9,206)*	*(11,095)*	*(12,308)*
2 Gross Profit	2,075	1,397	693	1,602
a Operating Expenses	(924)	(654)	(766)	(803)
3 Operating Profit	1,151	743	(73)	799
a Non Operating Income or (Expense)	*53*	*120*	*32*	*91*
4 Profit or (Loss) before Interest and Tax	1,204	863	(41)	890
a Total Finance Cost	*(466)*	*(380)*	*(971)*	*(751)*
b Taxation	*(134)*	*(70)*	*(271)*	*(79)*
6 Net Income Or (Loss)	604	414	(1,283)	60
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,160*	*872*	*(393)*	*360*
b Net Cash from Operating Activities before Working Capital Changes	*575*	*395*	*(1,316)*	*(240)*
c Changes in Working Capital	*3,344*	*3,162*	*1,013*	*(1,899)*
1 Net Cash provided by Operating Activities	3,920	3,557	(302)	(2,138)
2 Net Cash (Used in) or Available From Investing Activities	32	2	(95)	(212)
3 Net Cash (Used in) or Available From Financing Activities	(3,561)	(3,268)	238	2,353
4 Net Cash generated or (Used) during the period	391	290	(160)	3
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	27.2%	19.9%	-15.3%	-17.1%
b Gross Profit Margin	13.8%	13.2%	5.9%	11.5%
c Net Profit Margin	4.0%	3.9%	-10.9%	0.4%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	30.0%	38.0%	5.3%	-11.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	9.4%	9.1%	-27.5%	1.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	185	196	288	229
b Net Working Capital (Average Days)	172	185	273	215
c Current Ratio (Current Assets / Current Liabilities)	1.7	1.6	2.0	2.7
3 Coverages				
a EBITDA / Finance Cost	3.4	2.7	0.2	1.5
b FCFO / Finance Cost+CMLTB+Excess STB	2.1	1.9	-0.4	0.5
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.3	0.4	-0.1	-0.2
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	35.4%	37.9%	56.6%	57.8%
b Interest or Markup Payable (Days)	88.4	94.0	90.0	99.5
c Entity Average Borrowing Rate	8.7%	8.9%	14.2%	11.0%

Credit Rating

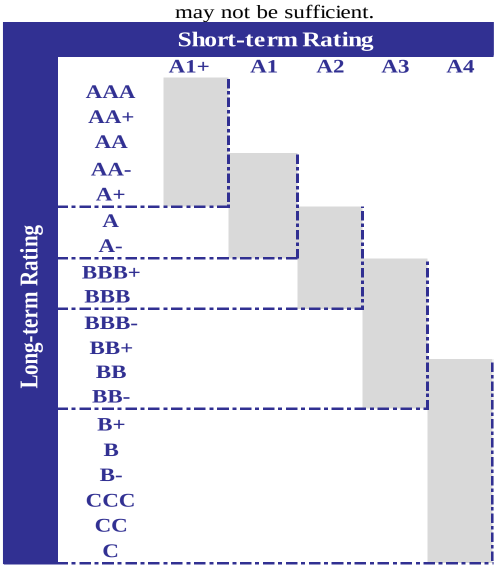
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 Rating

Scale	Definition
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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 some material identifiable event with indeterminable rating implications. 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 rating 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) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) 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.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities

a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments

a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

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