



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-2020	A	A1	Stable	Maintain	-
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 assigned ratings incorporate Gul Ahmed Textile Mills Limited's (Gul Ahmed) sound operating track record with strong presence in the broader textile value-chain; enabling the Company to manage volatility in textile business. Assigned ratings also reflect presence of seasoned senior management team which possesses considerable experience in the textile sector. Presence in retail with renowned brand "Ideas" in local market adds up to stronger business risk profile. 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 in addition to sustain quality would help manage the risk. During 3rd quarter of FY20, the revenues of all segments witnessed a decline due to the economic slowdown following lockdown to curb the spread of the Covid-19 pandemic. Subdued domestic demand and declining export demand due to lockdowns in global markets on account of Covid-19 come as a double blow for textile companies. While export demand revived in last two months of FY20. However, domestic demand would fairly depend on recoup of the Country's economy. Meanwhile, hefty branding activities and competition in the local market has kept net margins relatively strained. Liquidity profile of the Company is considered adequate with manageable working capital cycle and sufficient cash flows to meet outstanding obligations, while leveraging remains on the higher side.

The ratings are dependent on the Company's ability to sustain its business profile while maintaining its margins and strong. 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	Methodology Corporate Ratings(Jun-20),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria Rating Modifier(Jun-20)
Related Research	Sector Study Composite(Nov-19)
Rating Analysts	Muhammad Noor ul Haq noorulhaq@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 107 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 two directors from the sponsoring family while three are independent non-executive 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.

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 auditor expressed an unqualified opinion on the Company's financial statements for the period ended June 30th, 2019.

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 During 9MFY20, textile exports increased by 5% period on period. Currency devaluation and US-China trade war earlier in the year helped the country to increase its exports in value-added segments. Despite a decrease in per-unit prices, a factor of sharing currency devaluation benefits with buyers, exports of value-added segments increased by ~6%. Though the COVID-19 outbreak in early 2020 has affected the entire textile chain. Export orders have been postponed or delayed as major export destinations remain in lockdown to contain the virus. Several domestic players have shut down production or are partially operational. Recent government initiatives are expected to provide some relief. However, prevailing uncertainty due to global lockdown may have implications for the industry dynamics.

Relative Position With the improved operational efficiency, Gul Ahmed is among the largest vertically integrated textile unit in the country. Overall, it is among the largest exporters of the country, with a approximately share of 1.7% in Pakistan's total textile exports, while "Ideas by Gul Ahmed" is a leading textile retail brand.

Revenues Despite many economic challenges, the sales revenue of Gul Ahmed for the period under review has been increased by 11.8% from PKR 40.1bln to PKR 44.9bln as compared to the corresponding period. This double digit sales growth is led by volumetric increase in spinning segment owing to addition in capacity, PKR devaluation and enhancement of operational efficiencies. Moreover, in the quarter end-Mar20, the Company witnessed an adverse impact due to the economic slowdown and stoppage of production following lockdown to curb the spread of the COVID-19 pandemic. It is pertinent to mention that the Company's 63.5% (9MFY19: 54.6%) of revenues are being generated from export sales, hence it is susceptible to forex rate fluctuations. On the other hand, the Company faces high customer concentration risk, with over 25% of total revenue being generated from a single customer.

Margins The Company's gross margin dropped (9MFY20: 18.1%; 9MFY19: 23.4%) owing to higher input cost. Due to nature of operations, distribution and administration expenses of Gul Ahmed also remained on higher side as reflected in the operating margin (9MFY20: 4.7%; 9MFY19: 10.1%). Dependency on debt finance has forced the Company bear heavy finance cost (9MFY20: 1.2bln; 9MFY19: 0.8bln) which has eroded significant portion of net profit by (9MFY20: 0.7bln; 9MFY19: 2.7bln). Going forward, curtailed key interest rate will provide positive breathing space.

Sustainability The Company regularly undertakes BMR which has resulted in significantly enhanced capacity utilization and margins over the years. The Company incurred significant capex in the spinning segment during 9MFY20, including enhancements for value-addition as well as replacement of machinery. Lower demand and cancellation of export orders due to lockdown in USA & Europe will have a negative impact on the Company's performance. However, the Company has opted to avail relaxations introduced by SBP which will ease pressure on cash-flows. 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. Significant portion of the working capital cycle is inventory turnover period which stood at 138 days as at end-Mar20 owing to procurement of cotton while finished inventory levels remained high to cater to international orders and local retail demand. Therefore, net cash cycle remained stretched during 9MFY20 at 181 days (FY19: 170 days; FY18: 171 days).

Coverages During 9MFY20, cash flows (FCFO) of the Company dropped to PKR 4.3bln (FY19: PKR 6.6bln; FY18: PKR 4.8bln). Consequently, coverages showed YoY deterioration, with core coverage declining to 1.5x (FY19: 2.8x) and interest coverage dropped to 3.7x (FY19: 5.6x); remained strong. Moreover, the Company has opted to avail one-year deferral option of long term loan repayments by SBP due to COVID-19.

Capitalization Gul Ahmed has a highly leveraged capital structure (9MFY20: 72.4%, FY19: 65.4%), mainly comprising short-term borrowing (59.3%). Total borrowing has witnessed a significant increase (9MFY20: 39.8bln; FY19: ~PKR 29bln) to fulfill the commitment of expansion and increased working capital needs.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

Gul Ahmed Textile Mills Limited Composite	Mar-20 9M	Jun-19 12M	Jun-18 12M	Jun-17 12M
A BALANCE SHEET				
1 Non-Current Assets	27,069	19,472	16,369	16,280
2 Investments	70	-	-	-
3 Related Party Exposure	1,128	58	58	58
4 Current Assets	40,863	34,923	26,836	20,381
<i>a Inventories</i>	24,019	21,370	16,144	12,470
<i>b Trade Receivables</i>	6,816	7,071	5,399	3,345
5 Total Assets	69,130	54,454	43,263	36,719
6 Current Liabilities	14,039	9,963	7,202	5,722
<i>a Trade Payables</i>	4,736	3,330	2,458	1,956
7 Borrowings	39,785	28,999	23,354	19,760
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	165	158	87	322
10 Net Assets	15,142	15,334	12,621	10,914
11 Shareholders' Equity	15,142	15,333	12,621	10,914
B INCOME STATEMENT				
1 Sales	44,892	57,288	45,626	40,066
<i>a Cost of Good Sold</i>	(36,769)	(45,306)	(36,050)	(32,858)
2 Gross Profit	8,124	11,982	9,576	7,207
<i>a Operating Expenses</i>	(6,022)	(7,326)	(6,251)	(5,789)
3 Operating Profit	2,102	4,656	3,325	1,419
<i>a Non Operating Income</i>	425	825	(9)	268
4 Profit or (Loss) before Interest and Tax	2,527	5,482	3,315	1,686
<i>a Total Finance Cost</i>	(1,430)	(1,473)	(987)	(877)
<i>b Taxation</i>	(397)	(399)	(253)	10
6 Net Income Or (Loss)	700	3,609	2,075	818
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	4,350	6,583	4,774	2,274
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	2,929	5,234	3,823	1,422
<i>c Changes in Working Capital</i>	(1,470)	(5,074)	(4,907)	694
1 Net Cash provided by Operating Activities	1,459	160	(1,084)	2,116
2 Net Cash (Used in) or Available From Investing Activities	(7,228)	(4,899)	(1,956)	(5,320)
3 Net Cash (Used in) or Available From Financing Activities	6,239	4,761	3,240	3,166
4 Net Cash generated or (Used) during the period	470	22	200	(38)
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	4.5%	25.6%	13.9%	24.1%
<i>b Gross Profit Margin</i>	18.1%	20.9%	21.0%	18.0%
<i>c Net Profit Margin</i>	1.6%	6.3%	4.5%	2.0%
<i>d Cash Conversion Efficiency (EBITDA/Sales)</i>	10.9%	13.2%	11.6%	7.6%
<i>e Return on Equity (ROE)</i>	6.1%	25.8%	17.6%	8.3%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	181	159	149	146
<i>b Net Working Capital (Average Days)</i>	156	141	132	126
<i>c Current Ratio (Total Current Assets/Total Current Liabilities)</i>	2.9	3.5	3.7	3.6
3 Coverages				
<i>a EBITDA / Finance Cost</i>	4.2	6.4	6.3	4.2
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	1.5	2.8	2.2	1.6
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	3.8	1.9	2.1	5.1
4 Capital Structure (Total Debt/Total Debt+Equity)				
<i>a Total Borrowings / Total Borrowings+Equity</i>	72.4%	65.4%	64.9%	64.4%
<i>b Short-Term Borrowings / Total Borrowings</i>	0.6	0.7	0.6	0.6
<i>c Average Borrowing Rate</i>	4.6%	4.5%	3.9%	3.9%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 surveil 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):

<p>Entities</p> <ul style="list-style-type: none"> 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 	<p>Instruments</p> <ul style="list-style-type: none"> a) Basel III Compliant Debt Instrument Rating b) Debt Instrument Rating c) Sukuk Rating
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(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

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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.
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- (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)
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- (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)
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- (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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