RATING REPORT

Gujranwala Food Industries (Pvt.) Limited

REPORT DATE:
January 10, 2022

RATING ANALYSTS:
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RATING DETAILS

Rating Category	Initial Rating	
	Long-term	**Short-term**
Entity	BBB	A-2
Rating Outlook	Stable	
Rating Action	Initial	
Rating Date	*January 10, 2022*	

COMPANY INFORMATION

Incorporated in 1984	**External auditors:** Iyaz Ahmad & Co. Chartered Accountants
Private Limited Company	**Chairman/CEO:** Mr. Abdul Haleem
Key Shareholders (with stake 5% or more):	
Mr. Abdul Haleem – 33.87% Ms. Zubaida Kausar – 15.01% Mr. Muhammad Jamal – 5.27% Mr. Muhammad Suleman – 5.27%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (August 2021)
https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf

Gujranwala Food Industries (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Gujranwala Food Industries (Pvt.) Limited was established in 1984 as a private limited company. The company is involved in production of confectioneries, snacks, wafers, and chocolate items.

Profile of Chairman/CEO

Mr. Abdul Haleem and family has the controlling stake in the company. As the founding member, he has been associated with the company since inception. He is a foreign graduate.

RATING RATIONALE

The assigned ratings take into account the company's presence in fast-moving consumer goods industry whereby economic downturn and inflationary pressure has limited impact on the overall operational performance. The ratings factor in the company being a mid-tier player in the oligopolistic confectionery industry with reasonable market share. The business risk profile is considered moderate on the back of established market presence in relatively low-priced products and increasing diversification into export markets. The company operates on largely stable gross margins; however, the same does not fully translate into the bottom-line owing to relatively high operating costs. The ratings also incorporate low gearing and adequate debt service coverage. However, the ratings are constrained by the company's limited scale of operations and high operating expenses, putting a drag on profitability and liquidity indicators.

Key Rating Drivers

Company Profile

Gujranwala Food Industries (Pvt.) Limited (GFIL) was established in 1984 as a private limited company. The principal activities of the company include manufacturing, export, import, trade, and supply of bubble gums, chewing gums, snacks, candies, chocolates, jellies, etc. Shareholding of the company is vested with Mr. Abdul Haleem & family. The board of directors comprises five members, all being from the sponsoring family. The senior management comprises experienced resources and has depicted stability over the years. The company has implemented SAP-based ERP platform with integrated modules for real-time monitoring and reporting. Internal audit function is present with four resources and focuses on both pre-and-post audit of transactions.

Competitive oligopolistic industry

The target market for confectionary products is mainly children and youth segments. The business risk profile draws comfort from increasing population, with around 44.5% of country's total population falling in the less than twenty years bracket. Growth in the urban middle class also bodes well for the confectionary products. Price sensitivity is high due to modest brand loyalty, strong competition amongst local and foreign players for the market share, and availability of a wide range of substitutes especially from the unorganized confectionary sector. Imported products entailing higher brand recognition are generally associated with superior quality vis-à-vis local products; therefore, charge premium prices and reap higher margins. Moreover, owing to strong financial profile and healthy cash flows, the international players are able to give better distributor margins, leading to prominent display of their products which in turn leads to higher revenues.

Sales and profitability

Revenue stream of the company is generated from local and exports channels. Production for local channels is based on market dynamics while production for exports channels is based on customer orders. In order to accelerate top-line growth, the company has increased its focus on export channels over the past few years. Revenue of the company increased at a higher growth rate during FY21, with growth mainly emanating from increased penetration in the U.S., the U.K., and Middle East. Local sales remained largely stable as the impact of geographic expansion via opening of new outlets in shopping malls was offset by coronavirus pandemic related issues and increased competition. Resultantly, contribution of exports in overall revenue mix increased further to 39% during FY21. Going forward, the company is targeting further growth in export revenue during FY22, partially due to penetration into new geographies such as Russia.

In line with the increased sales, the company reported higher gross profit despite marginal decrease in gross margins due to inputs inflation, especially sizeable increase in sugar prices, and strong competition. Selling and distribution expenses increased due to higher carriage outward & other clearing charges during the year. Administrative expenses also increased on account of inflationary adjustments in all the key components. Despite some increase in debt utilization, financial charges decreased slightly on account of lower interest rates during FY21. Recent increase in interest rates is expected to result in higher finance cost, going forward. Accounting for tax expense, the company reported improved net profit while net margin remained largely stable during FY21.

Liquidity

In line with the uptick in profits, the company generated slightly higher funds from operations (FFO) during FY21. The cash flows generation provides adequate coverage against the financial obligations of the company as reflected in the debt service coverage ratio of 4.42x (FY20: 6.20x; FY19: 7.23x) and largely stable FFO-to-total-debt ratio of 0.52x (FY20: 0.52x; FY19: 0.50x) during FY21. Current ratio improved slightly to 1.15x (FY20: 1.06x; FY19: 1.08x) mainly on account of higher trade receivables and cash & bank balance at end-FY21. Comfort is drawn from inventory-plus-receivables to short-term borrowings ratio which despite some decline continues to remain on the higher side at 2.06x (FY20: 2.14x; FY19: 2.27x) as the company also utilizes customer advances and supplier credit to manage working capital requirements. Net working capital cycle of the company has improved to 19 days (FY20: 33 days; FY19: 22 days) during FY21.

Capitalization

Increase in equity base was led by profits retention during FY21; however, the same is still considered modest. Debt profile of the company comprises a mix of short-term and loan-term borrowings. Due to higher working capital requirements, some increase in short-term borrowings was noted end-FY21 as the company made advance payments to secure sugar supplies in order to timely deliver export orders. Outstanding long-term loans decreased with the scheduled repayments during the year. The capital structure of the company remains conservative owing to minimal reliance on borrowings, resulting in low gearing ratio of 0.54x (FY20: 0.59x; FY19: 0.60x) at end-FY21. However, since the company utilizes supplier credit and customer advances to manage working capital requirements, debt leverage was recorded relatively higher at 1.91x (FY20: 2.07x; FY19: 2.07x) despite some improvement during FY21. Considering the business model of the company along with no immediate plan of equity injection by the sponsors, leverage indicators are likely to remain around current levels as the mobilization of lease finance and short-term borrowings may offset the impact of internal capital generation, going forward.

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure I

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES	Annexure II
Name of Rated Entity	Gujranwala Food Industries (Pvt.) Limited
Sector	Consumer Goods
Type of Relationship	Solicited
Purpose of Rating	Entity & Instrument Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
10.01.2022	BBB	A-2	Stable	Initial

Instrument Structure	N/A
Statement by the Rating Team	VIS, the analysts involved in the rating process and members of its rating committee do not have any conflict of interest relating to the credit rating(s) mentioned herein. This rating is an opinion on credit quality only and is not a recommendation to buy or sell any securities.
Probability of Default	VIS' ratings opinions express ordinal ranking of risk, from strongest to weakest, within a universe of credit risk. Ratings are not intended as guarantees of credit quality or as exact measures of the probability that a particular issuer or particular debt issue will default.
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Due Diligence Meetings Conducted	

Name	Designation	Date
Mr. Zahid Latif	CFO	December 17, 2021