RATING REPORT

Bhanero Textile Mills Limited

REPORT DATE:
April 22, 2020

RATING ANALYST:

Talha Iqbal
talha.iqbal@vis.com.pk

Asfia Aziz
asfia.aziz@vis.com.pk

RATING DETAILS				
	Latest Rating		**Previous Rating**	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A+	A-1	A+	A-1
Rating Date	*April 22, 2020*		*February 21, 2019*	
Rating Outlook	Rating Watch-Developing		Stable	
Rating Action	Maintained		Reaffirmed	

COMPANY INFORMATION	
Incorporated on March, 1980	**External auditors:** M/s Mushtaq & Co. Chartered Accountants
Public Limited Company	**Chairman:** Mr. Mohammad Shaheen
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Khurrum Salim
Admiral (Pvt) Ltd (16.7%)	
Mrs. Samia Bilal (11.1%)	
Mrs. Fatima Amin (5.7%)	
Mr. Muhammad Qasim (5.28%)	
Mr. Mohammad Amin (5.3%)	

APPLICABLE METHODOLOGY(IES)
Applicable Rating Criteria: Industrial Corporates (April 2019) https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Bhanero Textile Mills Limited

OVERVIEW OF THE INSTITUTION

BHAT is part of the Umer Group of companies and was established in 1980 as a public limited company under Companies Ordinance, 1984 and is quoted on Pakistan Stock Exchange Limited. BHAT started with a single spinning unit situated in Dadu district. Over the years BHAT has expanded with 2 spinning units and a weaving unit situated in Ferozewatan, Sheikupura.

Financial Statements of the company for FY19 were audited by Mushtaq & Co., Chartered Accountants. Auditors belong to category 'B' on the approved list of auditors published by the State Bank of Pakistan (SBP).

Profile of Chairman

Mr. Shaheen has over 38 years of top management experience in textile business. He completed the Director Education from Pakistan Institute of Corporate Governance in June, 2013.

Profile of CEO

Mr. Khurrum is serving the board of Umer Group of Companies for

RATING RATIONALE

Group Profile

Bhanero Textile Mills Limited (BHAT) is a part of the Umer group of industries having diversified presence in footwear, retail, leather, dairy, power generation and construction; however, its core strength lies in textile business. Umer group operates through 3 companies in the textile sector.

Within textile sector, the group has over three decades of experience and is primarily engaged in the business of manufacturing and trading of grey and dyed yarn and greige fabric. The group is recognized as a prominent player in spinning and weaving segment with annual turnover of around Rs. 35.7b during FY19. Umer Group has a strong presence in the export market with more than 50% of total sales comprising exports to China, Italy, Japan, Turkey and Belgium & other European countries. Around 60% of the total sales revenue of the Group has been generated through the spinning segment while the remaining comprises sales of greige fabric.

Umer Group of Companies (Rs. in m)				
	FY18	%	FY19	%
Sales	30,174		35,723	
Exports	15,075	50%	18,280	51%
Local	15,100	50%	17,445	49%
Yarn Sales	17,996	61%	21,035	61%
Fabric Sales	11,330	39%	13,576	39%
Spindles	186,960		186,960	
Looms	565		567	

Umer Group has a total installed capacity of 186,960 spindles and 567 looms at end-June'19. The group carries its operations through five spinning and three weaving units each producing a unique specialized product. Moreover, in order to ensure an uninterrupted power supply, the group has established its own captive power generation plants for each unit with a total capacity of 37 megawatt (MW).

Company and Operating Profile

BHAT is engaged in the business of manufacturing and trading of yarn and knitted fabric. The Company maintains two separate spinning units of which Unit-I consist of 27,840 spindles and Unit-II consist of 52,272 spindles. Both units are adequately equipped to produce cotton, rayon, ring spun & carded yarn. There is a separate facility for weaving operations installed with 162 air-jet looms. This unit produces mix ranges of fine woven greige cloths, from light to heavy, wider width, plain, textured, twills and luxurious satins. At end-FY19, BHAT operated with total 80,112 spindles and yarn capacity utilization was reported on the higher side at 83% (FY18: 77%). Utilization levels for 9MFY20 remained on the higher side till mid-March'20 and declined slightly for the remaining half of the month owing to partial closure of the facilities. All manufacturing units have resumed operations since then. Going forward, management envisages capacity utilization to decline amidst economic slowdown led by COVID-19; however the same is expected to remain at reasonable level given export orders in hand till June'20.

Expansion Plans

In view of long term growth strategy the company has planned capex to enhance efficiency in business operations through replacement 140 new looms; BMR has been deferred till improvement in overall sectoral outlook.

more than 20 years. He has been serving the position of CEO since 2011. He completed his bachelor's degree from Government College of Commerce Karachi and holds versatile experience in textile industry.

Key Rating Drivers:

Coronavirus outbreak is expected to result in uncertainty in textile sector dynamics due to prolonged lockdown, overall contraction in demand and challenging economic environment. It is expected that the entire value chain of the textile industry will be impacted these developments. However, comfort is drawn from export orders in hand, regulatory relaxations and relief measures provided by SBP including a moratorium on debt repayments.

Movement in cotton prices and cotton crop levels drives performance of spinning sector players. Historically, margins and financial performance of players have depicted variation. Moreover, competitive intensity is high due to commoditized nature of the product. As with other local producers in the spinning sector, reliance on China as the major export market translates into some country concentration risk. High country concentration risk and price volatility remains in the weaving sector as well with Bangladesh comprising the major fabric export market. Given the high degree of fragmentation specifically in the weaving segment; pricing power of companies operating in the segment remains limited. Business risk profile remains dependent on inherent cyclicality of prices, crop levels, and demand supply fluctuations. Over the years, management's strategy of cautiously building cotton inventory has resulted in margins oscillating in a narrow band of 11%-13.8%. However, sharp decline in cotton prices since the onset of the ongoing calendar year will result in inventory losses and pressure on margins. Timing and quantum of which will depend on average prices and quantity carried by different players.

Coronavirus outbreak is expected to result in uncertainty in textile sector dynamics due to prolonged lockdown, overall contraction in demand and challenging economic environment. It is expected that the entire value chain of the textile industry will be impacted these developments. However, players in the garment segment are expected to be impacted more while gradual opening up of Chinese market has allowed yarn exports. In general, exports are being impacted due to a number of countries being under partial or complete lockdown. Given the closure of large retail stores, risk of withheld shipment and future orders, delays or extension of payment timelines, and even cancelled orders remains. On the local market front, textile sales are being affected due to continued shut down which will impact revenues and may extend to Ramadan which constitutes a major sales period. A sizeable chunk of sales undertaken for prior months are on credit and delays in collections is expected to adversely impact cash flows. However, comfort is drawn from export orders in hand (up till June 2020) and regulatory relaxations and relief measures provided by SBP. Key measures announced by SBP include reduction in policy rates and allowance for deferral of principal payment for a period of one year. Both these measures will reduce financial burden on textile companies. Moreover, under the relief package announced by GoP, Rs. 30b have been allocated for textile exporters as payment of duty drawbacks providing liquidity support to textile exporters.

Healthy sales growth in FY19. Sales for FY20 are expected to be higher than FY19 given the orders in hand. Sales for FY21 will be impacted; quantum will depend on timing of opening of local and export markets and subsequent consumer behaviour.

Net sales of the company increased by 16% to Rs. 9.3b (FY18: Rs. 8.1b) during FY19. Historically, around two-third of topline has comprised local sales. Local sales increased by 19% to Rs. 6.2b (FY18: Rs. 5.2b) in FY19 while exports were higher by 10% to Rs. 3.2b (FY18: Rs. 2.9b) in FY19. Segment wise yarn continues to be the major contributor with 66% (FY18: 64%) share in total revenue. Moreover, yarn sales have gained foothold in the domestic market whereas weaving segment largely comprises exports. Sharp decline in cotton prices since Jan'20 may also put pressure on average selling prices of yarn and fabric.

Earning profile depicted improvement during FY19 largely on the back of currency devaluation yielding higher average selling prices and efficient raw material procurement. Profitability growth for FY20 may be impacted due to pressure on margins in the ongoing year.
Gross margins of the company have improved to 13.8% (FY18: 10.8%; FY17: 11.0%) during FY19 largely on the back of higher average selling prices led by sizeable currency devaluation. Overall operating expenses increased primarily due to higher distribution cost incurred. However, one-off gain from sale proceeds of assets along with higher interest income supported the bottom line, amounting to Rs. 832m (FY18: Rs. 482m) during FY19. Consequently, net margins also improved considerably to 8.9% (FY18: 6.0%) during the same period. During 1HFY20, gross margins of the company declined to 12.2% and are expected to further witness pressure due to sharp reduction in cotton prices causing inventory losses.

Adequate liquidity profile and financial flexibility.
In absolute terms, Funds from Operations (FFO) amounted to Rs. 944m (FY18: Rs. 603m) depicting a sizeable increase on account of higher overall profitability during FY19. Debt Service Coverage Ratio (DSCR) and FFO/Long-Term Debt remain strong at 3.05x (FY19: 4.83x, FY18: 4.08x) and 65.8% (FY19: 74.8%, FY18: 62.4%) during 1HFY20, respectively. Inventory and trade debts provide strong coverage for short-term debt obligations while current ratio was reported at 3.1x at end-Dec'19. While cash flows for FY21 may be impacted, liquidity profile draws support from the company's plans to avail SBP's allowance for deferral of principal payment for a period of one year and no capital expenditure expected till cash flows improve. Maintaining working capital cycle and receivable days will also be important from a liquidity perspective.

Capitalization indicators supported by low leveraged capital structure and conservative financial policy.
On account of higher profit retention, net equity of the company was reported at Rs. 5b (FY19: Rs. 4.9b; FY18: Rs. 4.3b; FY17: Rs. 3.9b) at end-Dec'19. Dividend payout ratio was reported at 59% (FY19: 20%; FY18: 40%) during 1HFY20. Total debt carried on balance sheet amounted to Rs. 1.9b at end-Dec'19; around two-third of the total debt is long-term in nature with a major portion of the same being LTFF, acquired at considerably lower rate. With a larger equity base, leverage indictors have remained on lower side with gearing and debt leverage reported at 0.37x (FY19: 0.46) and 0.64x (FY19: 0.71) at end-1HFY20, respectively.

Bhanero Textile Mills Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**1HFY20***
Fixed Assets	2,085	2,826	3,193	3,187
Stock-in-Trade	2,713	2,347	3,569	3,395
Trade Debts	544	841	758	871
Cash & Bank Balances	40	68	144	72
Total Assets	5,895	6,646	8,406	8,186
Trade and Other Payables	488	772	726	816
Long Term Debt	506	967	1,262	1,251
Short Term Debt	677	220	993	604
Total Debt	1,183	1,187	2,255	1,856
Paid Up Capital	30	30	30	30
Total Equity	3,886	4,263	4,913	5,001
INCOME STATEMENT				
Net Sales	6,837	8,074	9,348	4,747
Gross Profit	754	868	1,294	580
Profit Before Tax	369	542	957	319
Profit After Tax	276	482	832	255
RATIO ANALYSIS				
Gross Margin (%)	11.0%	10.8%	13.8%	12.2%
Net Margin	4.0%	6.0%	8.9%	5.4%
Net Working Capital	2,527	2,701	3,286	3,359
Trade debts/Sales	8.0%	10.4%	8.1%	9.2%
FFO	511	603	944	412
FFO to Total Debt (%)	43.2%	50.8%	41.9%	44.4%
FFO to Long Term Debt (%)	101.0%	62.4%	74.8%	65.8%
Current Ratio (x)	3.01	3.48	2.73	3.09
Debt Servicing Coverage Ratio (x)	3.75	4.08	4.83	3.05
Gearing (x)	0.30	0.28	0.46	0.37
Leverage (x)	0.52	0.56	0.71	0.64
Long Term Debt to TD (%)	43%	81%	56%	67%
Short Term Debt to TD (%)	57%	19%	44%	33%
(Stock+ Trade Debts)/STD	482%	1446%	436%	706%
Dividend Payout	40%	40%	20%	59%
ROAA (%)	5%	8%	11%	6%
ROAE (%)	7%	12%	18%	10%

** Annualized numbers*

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix II

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	Appendix III
Name of Rated Entity	Bhanero Textile Mills Limited
Sector	Textile Industry
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see table below
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.
Disclaimer	Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. VIS is not an NRSRO and its ratings are not NRSRO credit ratings. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile. Copyright 2020 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
22/4/2020	A+	A-1	Rating Watch-Developing	Maintained
21/2/2019	A+	A-1	Stable	Reaffirmed
17/12/2018	A+	A-1	Stable	Initial

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Muhammad Salim	Executive Director	07-April-2020
2	Mr. Asim Mirza, ACMA, CPA(Aust), MBA	CFO	07-April-2020