RATING REPORT

Bhanero Textile Mills Limited

REPORT DATE:
May 27, 2021

RATING ANALYST:

Asfia Aziz
asfia.aziz@vis.com.pk

Sundus Qureshi
sundus.qureshi@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	*May 27, 2021*		*April 22, 2020*	
Rating Outlook	Stable		Rating Watch-Developing	
Rating Action	Maintained		Maintained	

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	RATING RATIONALE

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 and currently owns 2 spinning units and a weaving unit situated in Kotri and Ferozewatan, Sheikupura.

Financial Statements of the company for FY20 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

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. 41.9b and Rs. 23.5b during FY20 and 1HFY21, respectively. 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 56% 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)			
	FY19	FY20	1HFY21
Sales	41,036	41,921	23,524
Exports	20,148	22,216	10,792
Local	20,889	20,747	12,732
Yarn Sales	21,970	21,894	13,262
Fabric Sales	13,752	14,283	7,342
Spindles installed	186,956	186,956	186,956
Looms installed	568	568	568

Umer Group has a total installed capacity of 186,956 spindles and 568 looms at end-Dec'20. The group carries its operations through five spinning, three weaving units and one recently started finishing unit each producing a unique specialized product. Moreover, in order to ensure an uninterrupted power supply, the group has established Industrial power generation 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-FY20, BHAT operated with total 80,112 spindles with utilization levels of yarn reported lower at 72% (FY19: 83%). Utilization levels of the fabric segment were recorded on the higher side at 65% (FY19: 60%) at end-June'20. Going forward, management envisages capacity utilization to report at pre-COVID levels.

Expansion Plans

In view of long term growth strategy the company has planned to incur capital expenditure in the spinning segment. The plan involves adding another spinning unit encompassing around 19,584 spindles. The project is expected to come online by July'22. The total cost of the project has been estimated at Rs. 3.5b, out of which Rs. 2.2b will be financed through Temporary Economic Refinance Facility (TERF) debt with the remaining projected to be funded from internal cash generation. In addition to expansion, the company is also in the process of replacing 140 looms out of a total of 162 looms.

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:

Recovery in industry wide exports post ease in COVID-19 lockdown measures support business risk profile of the company.

With the objective of enhancing exports to support the economy, the Government of Pakistan (GoP), has provided incentives in the form of subsidized utility tariffs, low interest rates (Export Finance Scheme (EFS), Long Term Financing Facility (LTFF) and TERF) and sales tax refund to the textile industry. The textile policy 2020-25 has laid emphasis on fixed electricity and gas tariff for the next 5 years till 2025 at US cents 7.5 per KWh and USD 6.5 per MMBTU, respectively. Moreover, the limits of subsidized (LTFF) financing have been enhanced under this policy to facilitate exporters. Initiatives are also being undertaken in order to increase production and yield of cotton. However, the imposed sales tax has negatively impacted the textile industry. Even though impact of Covid-19's third wave remains elevated, we expect the order book for the industry to remain strong in the ongoing year, easing our business risk concerns.

Revenue for FY20 decreased due to the market slowdown caused by COVID-19. Going forward, sales are expected to escalate on account of adequate orders in pipeline along with expansion in the spinning segment.

Net sales of the company decreased by 5% to Rs. 8.9b (FY19: Rs. 9.3b) during FY20 due to COVID-19 led slowdown in the market and imposition of 17% GST on local sales. Local sales increased by 16% to Rs. 7.2b (FY19: Rs. 6.2b) in FY20 while exports were lower by 12.5% to Rs. 2.8b (FY19: Rs. 3.2b) in FY20. Consequently, proportion of local sales in the total sales revenue of the company increased to 72% (FY19: 66%) during FY20. Segment wise yarn continues to be the major contributor with 59% (FY19: 63%) share in gross revenue in FY20. Moreover, yarn sales have gained foothold in the domestic market whereas weaving segment largely comprises exports. During 9MFY21, the company reported sales revenue to the tune of Rs. 8.8b led by an uptick in volumetric sales and average selling prices. Going forward, in the medium term, sales are expected to escalate on account of adequate orders in pipeline along with expansion in the spinning segment.

Overall profitability profile of the company was impacted by higher cotton prices, currency devaluation on imported cotton and higher finance costs during FY20. During 9MFY21, gross margins of the company improved on account of inventory gains and are projected to normalize to historic levels once the low price inventory is used up by Jan'22.

Gross margins of the company declined to 9.2% (FY19: 13.8%) during FY20 largely on the back of higher cotton prices and currency devaluation on imported raw material. Overall operating expenses decreased primarily due to lower distribution and other operating costs incurred. Finance charges increased to Rs. 181.4m (FY19: Rs. 166.3m) in FY20 due to higher rates until the last quarter of the outgoing year and elevated debt levels to meet working capital needs. Consequently, net margins also declined considerably to 3.7% (FY19: 8.9%) during the same period. During 9MFY21, gross and net margins of the company improved to 16.5% and 10.4%, respectively on the back of higher sales and inventory gains; the same are projected to normalize to historic levels once the low price inventory is used up by Jan'22.

Liquidity indicators weakened in FY20 due to subdued profitability; however the same improved in 9MFY21 and are expected to remain in line with projected increase in overall profitability, going forward.

In absolute terms, Funds from Operations (FFO) amounted to Rs. 525m (FY19: Rs. 944m) depicting a sizeable decrease on account of lower overall profitability during FY20. However, in line with improvement in profitability during 9MFY21, Debt Service Coverage Ratio (DSCR), FFO/Long-Term Debt, and FFO/ Total Debt were reported higher at 11.89x (FY20: 2.18x, FY19: 4.83x), 122.8% (FY20: 47.2%, FY19: 74.8%), and 122.8% (FY20: 19.6%, FY19: 41.9%) at end-Mar'21, respectively. Inventory and trade debts provide strong coverage for short-term debt obligations while current ratio was reported at 2.5x at end-June'20. However, cash flows for HYFY21 have improved and the liquidity profile draws support from the company's improved profitability in the ongoing year. 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 in the ongoing year and limitation on dividend payout under SBP's deferment terms, net equity of the company was reported higher at Rs. 5.8b (FY20: Rs. 4.9b; FY19: Rs. 4.9b) at end-Mar'21. Total debt carried on balance sheet amounted to Rs. 1.3b at end-Mar'21 comprising long term debt 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 0.22x (FY20: 0.55x; FY19: 0.46x) and 0.45x (FY20: 0.79x; FY19: 0.71x) at end-9MFY21, respectively. Given financing of capex plans through long term borrowings, capitalization indicators of the company are expected to increase going forward, however the same are projected to remain within manageable levels.

Bhanero Textile Mills Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*					
BALANCE SHEET	**FY17**	**FY18**	**FY19**	**FY20**	**9MFY21**
Fixed Assets	2,085	2,826	3,193	3,027	3,010
Stock-in-Trade	2,713	2,347	3,569	3,956	2,831
Trade Debts	544	841	758	957	1,184
Cash & Bank Balances	40	68	144	114	835
Total Assets	5,895	6,646	8,406	8,789	8,434
Trade and Other Payables	488	772	726	632	822
Long Term Debt	506	967	1,262	1,112	1,261
Short Term Debt	677	220	993	1,571	-
Total Debt	1,183	1,187	2,255	2,683	1,261
Paid Up Capital	30	30	30	30	30
Total Equity	3,886	4,263	4,913	4,919	5,832
INCOME STATEMENT					
Net Sales	6,837	8,074	9,348	8,924	8,814
Gross Profit	754	868	1,294	824	1,457
Profit Before Tax	369	542	957	456	1,038
Profit After Tax	276	482	832	329	913
RATIO ANALYSIS					
Gross Margin (%)	11.0%	10.8%	13.8%	9.2%	16.5%
Net Margin	4.0%	6.0%	8.9%	3.7%	10.4%
Net Working Capital	2,527	2,701	3,286	3,477	4,356
Trade debts/Sales	8.0%	10.4%	8.1%	10.7%	10.1%
FFO	511	603	944	525	1,162
FFO to Total Debt (%)	43.2%	50.8%	41.9%	19.6%	122.8%
FFO to Long Term Debt (%)	101.0%	62.4%	74.8%	47.2%	122.8%
Current Ratio (x)	3.01	3.48	2.73	2.54	5.19
Debt Servicing Coverage Ratio (x)	3.75	4.08	4.83	2.18	11.89
Gearing (x)	0.30	0.28	0.46	0.55	0.22
Leverage (x)	0.52	0.56	0.71	0.79	0.45
Long Term Debt to TD (%)	43%	81%	56%	41%	100%
Short Term Debt to TD (%)	57%	19%	44%	59%	0%
(Stock+Trade Debts)/STD	482%	1446%	436%	313%	N/A
ROAA (%)	5%	8%	11%	4%	14%
ROAE (%)	7%	12%	18%	7%	23%

** 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	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	27/5/21	A+	A-1	Stable	Maintained
	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
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 2021 VIS Credit Rating Company Limited. All rights reserved. Contents may be used by news media with credit to VIS.				
Due Diligence Meetings Conducted		**Name**	**Designation**	**Date**	
	1	Mr. Muhammad Salim	Executive Director	26-April-2021	
	2	Mr. Asim Mirza- FCMA	CFO	26-April-2021	