RATING REPORT

Bhanero Textiles Mills Limited

REPORT DATE
August 15, 2022

RATING ANALYST:
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RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A+	A-1	A+	A-1
Rating Outlook	Stable		Stable	
Rating Date	*Aug 15, 2022*		*May 27, 2021*	
Rating Action	Reaffirmed		Maintained	

COMPANY INFORMATION	
Incorporated in 1980	**External Auditors:** M/s Mushtaq & Co. Chartered Accountants
Public Listed Company	**Chairman:** Mr. Mohammad Shaheen
Key Shareholding (more than 5%)	**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)
VIS Entity Rating Criteria: Industrial Corporates (August 2021) *https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf*

Bhanero Textiles Mills Limited

OVERVIEW OF THE INSTITUTION

Bhanero Textiles Mills Limited (BHAT), part of Umer Group of Companies, was incorporated as a public limited company in 1980, under the Companies Ordinance, 1984. BHAT is listed on Pakistan Stock Exchange (PSX) and registered office of the company is based in Karachi.

Financial Statements of the year FY21 were audited by 'Mushtaq & Co., Chartered Accountants', which belong to category 'B' on the approved list of auditors published by 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'13.

Profile of CEO:

Mr. Khurrum has been serving on the Board of Umer Group of Companies for more than 20 years. He has been serving as CEO since 2011. He completed his bachelor's degree from Government College of Commerce Karachi and holds versatile experience in textile industry.

RATING RATIONALE

Group profile

Umer Group of Companies, founded in 1982, is one of the Pakistan's leading textile groups, with an annual turnover of more than USD 350m. The group has a diverse business profile and investments in various other sectors as well such as power generation, footwear manufacturing/retail, leather, dairy and construction.

The group has an extensive experience of over 34 years in the textile sector and comprises 3 textile companies, which are cumulatively operating 5 spinning mills, 3 weaving mills and 1 recently established finishing unit. In addition, industrial power generation for each unit is present, with a total capacity of 44.5MW, ensuring uninterrupted power supply. Over the years, the group has managed to achieve a sizable market share in both domestic and export sales. Major export destinations include China, Italy, Japan, Turkey, Belgium, and other European countries.

Figure: Key Financial Figures – Umer Group (Rs. in m)

	FY19	FY20	FY21	6M'FY22
Sales	41,036	41,921	50,493	33,586
Exports	20,148	22,216	25,418	15,380
Local	20,889	20,747	25,738	18,206
Yarn Sales	21,970	21,894	28,555	18,700
Fabric Sales	13,752	14,283	15,083	11.993
Spindles installed	186,956	186,956	186,956	186,956
Looms installed	567	567	567	567

Corporate profile

Bhanero Textile Mills Limited (BHAT), headquartered in Karachi, operates 2 spinning and 1 weaving units in Kotri and Ferozewatan, Shiekhupura. For over four decades, BHAT has been manufacturing and trading yarn (cotton, rayon, ring spun & carded) and knitted fabric (mix ranges of fine woven greige cloths, from light to heavy, wider width, plain, textured, twills and luxurious satins) for both domestic and international markets. The sponsoring family is actively involved in business affairs, and there is a qualified senior management team in place with extensive experience. Total staff strength, including labor, has remained stable at 1,420 (2020: 1,416) employees.

Production capabilities

The installed capacity remains unchanged at 80,112 spindles (Unit I & II) and 162 air-jet looms (Unit III), with capacity utilization (for both spinning and weaving segments) depicting an increasing trend over the years. Power requirement of 14MW is met through a mix of 3 sources; gas-based generators, national grid and furnace oil captive power plant. In addition, a solar power plant is also recently deployed.

Figure: Capacity & Production Data

	FY19	FY20	FY21	6M'FY22
Spinning				
Installed capacity (kgs)	14.8m	14.8m	14.8m	7.4m
Actual Production (kgs)	12.4m	10.7m	12.2m	6.6m
Utilization	*77%*	*72%*	*83%*	*89%*
Weaving				
Installed capacity (mtrs)	26.6m	26.6m	26.6m	13.3m
Actual Production (mtrs)	15.9m	17.4m	21.1m	10.7m
*Utilization**	*60%*	*65%*	*79%*	*80%*

**utilization is reported on the lower side due to conversion of picks*

Capacity enhancement plans for both spinning and weaving divisions

In terms of capacity expansion initiatives, a new spinning unit with 19,584 spindles is currently under construction. Total revised project cost (including cost overruns due to recent currency depreciation) is Rs. 3.7b; of which Rs. 2.2b is for machinery, which is being financed through TERF and LTFF debt facility, while the remaining is funded through internal cash generation for construction of building. The production is scheduled to begin in Dec'22. In addition, the management has replaced 140 existing looms at a total capex of Rs. 1.780b for machinery, which is being financed through ILTFF debt financing for upgradation in the weaving unit.

Key Rating Drivers

Textile and clothing exports registered a sizeable growth given the surge in demand on account of rerouting of orders to Pakistan. The ongoing energy crisis in the country poses a challenge to future growth of the sector.

Textile sector contributes nearly one-fourth to industrial value-added segment and 8.5% to the country's GDP, with an estimated market size of Rs. 3.8tr (FY20: Rs. 3.3tr) in FY21. Barring seasonal and cyclical fluctuations, textiles products have maintained an average share of about 60% in national exports. Export revenues from textile sector have increased significantly over the years (FY22: $19.3b FY21: $15.4b; FY20: $12.5b; FY19: $13.6b). Knitwear, Readymade and Bed wear segments continue to contribute higher than other segments, with a cumulative contribution of more than 60% in textile exports. While the growth was primarily driven by volume (excluding knitwear and cotton yarn), higher prices also boosted exports.

Figure: Textile Exports (as per PBS)

Segments	Value (US$ millions)		
	FY20	FY21	FY22
Knitwear products	2,785	3,816	5,121
Readymade Garments	2,549	3,033	3,905
Bed wear	2,149	2,772	3,293
Cotton Cloth	1,830	1,921	2,438
Cotton Yarn	987	1,017	1,207
Towels	711	938	1,111
Made-up Articles	591	756	849
Art, silk and synthetic textile	314	370	461
Tents, canvas and tarpaulin	98	110	110
Others	487	667	835

Given the looming global recession, commodities super-cycle, rising inflation, and monetary tightening in major world economies, textile export orders growth in Pakistan is expected to slow down in the medium-term. This, combined with the country's ongoing energy crisis and rising production costs, poses a challenge to the sector's margin sustainability and future growth.

5-Year (2020-25) textile policy continues to support the industry.
With an aim to double textile exports in five years, GoP through a five-year textile policy (2020-25) has provided incentives in form of preferential energy rates, low interest rates financing schemes (such as EFS, LTFF and TERF) and timely payments of DLTL, Income tax & Sales tax refund which support liquidity constraints of local players. Initiatives have also been undertaken to increase production and yield of cotton to support the industry. However, imposition of 10% super tax would have a negative effect on profitability profile of textile players. In addition, contractionary monetary policy and political uncertainties in the country are the present major business risk factors. In the long run, improvement in value addition, investment in technology and optimization of energy cost would define the future of textile exports.

High cyclicality and competitiveness in the spinning sector translate into high business risk profile.
Movement in cotton prices and cotton crop levels drives performance of spinning players in Pakistan. Given sizeable deficit in local cotton production vis-à-vis demand in the recent years, cotton prices have remained elevated due to which inventory loss risk is considered limited. Business risk is supported by favorable government policies and healthy demand outlook.

Volumetric growth, primarily in domestic sales, combined with rising prices and rupee depreciation resulted in a strong increase in topline during the review period. Capacity expansion projects would drive further sales growth in the future.
Topline of the company has nearly doubled over the period of past five fiscal years, amounting to Rs. 12.2b (FY20: Rs. 8.9b) in FY21. The year-on-year uptick of ~36% was attributable to volumetric growth (primarily in local sales) and increasing prices coupled with rupee devaluation. With similar growth momentum, revenues amounted to Rs. 12.3b during 9M'FY22, increasing by ~40% vis-à-vis SPLY. As per management, sales revenues is targeted to cross the Rs.20b mark for the year FY23.

Segment wise, around two-third of sales revenue is generated from the spinning segment while weaving division accounts for the remainder. Yarn sales grew by ~54% in FY21, far outpacing the 13% increase in fabric segment. On a 3-year average basis, sales mix of local and export sales has been around 30:70, while in terms of growth, local sales increased by ~50%, vis-à-vis 9% growth in exports, during FY21; similar trend is noted in the outgoing fiscal year. Italy, Japan, Turkey, Portugal, Korea, and Bangladesh are among the major export destinations. Client-wise sale concentration risk (particularly in yarn and fabric exports) has remained elevated over time. Long-standing business relationships with major clients, on the other hand, provide comfort and ensure repeat business.

Inventory gains and efficient cotton procurement management significantly increased profitability margins.

Over the review period, gross margins increased significantly (9M'FY22: 21.8%; FY21: 22.5%; FY20: 9.2%; FY19: 13.8%) due to better absorption of per unit fixed costs, efficient cotton procurement, and favorable cotton price differential, which is consistent with the industry trend. Furthermore, more than half of cotton is purchased from international market. Financial charges have decreased over time due to lower debt utilization levels, while distribution and administrative overheads have increased largely in line with inflation. Given sizeable growth in revenues and margins, bottom-line noted a nearly six-fold increase in FY21 and increased further during 9M'FY22. Given that cotton procurement is covered till Dec'23, management expects margins to sustain in the current fiscal year FY23.

Liquidity profile is strong, with sizeable cash flow generation in line with improvement in profitability.

In line with improving profitability, Funds from Operations (FFO) increased significantly to Rs. 2.2b (FY21: Rs. 2.3b; FY20: Rs. 0.5b) at end-9M'FY22. As a result, FFO to total debt and FFO to long-term debt also increased considerably to 0.93x (FY21: 1.77x; FY20: 0.20x) and 0.93x (FY21: 1.77x; FY20: 0.47x), respectively. Healthy cash flow generation has positively impacted debt coverage metrics as reflected by strong growth in DSCR to 10.06x (FY21: 17.11x; FY20: 2.18x). Current ratio is reported at above 4.0x while inventory and trade debts provide strong coverage for short-term debt obligations. Aging profile of trade debts remains within manageable levels.

Capitalization levels are supported by strong growth in earnings, low-leveraged capital structure and overall group's conservative financial policy.

Equity base grew by ~74% over the last 18 months, reaching to Rs. 8.6b (FY21: Rs. 6.8b) at end-9M'FY22. The dividend payout ratio stood at 12% (FY20: 46%) in FY21. As at end-9M'FY22, total debt increased to Rs. 3.1b (FY21: Rs. 1.3b); entirely long-term in nature. Though gearing ratio has improved over time, it nearly doubled during 9M'FY22 (compared to FY21) as additional debt was mobilized during the year to fund expansion. Going forward, leverage indicators are expected to remain within manageable levels on account of projected profitability.

Bhanero Textiles Mills Limited Appendix I

FINANCIAL SUMMARY					*(amounts in PKR millions)*
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**FY21**	**9M'FY22**
Non-Current Assets	2,855	3,222	3,055	3,121	6,480
Stores, Spares. And Loose Tools	68	112	122	108	169
Stock-in-Trade	2,347	3,569	3,956	2,659	4,333
Trade Debts	841	758	957	1,628	2,184
Advances, Deposits and Other Receivables	466	601	584	238	689
Cash and Bank Balance	68	144	114	1,739	459
Total Assets	**6,646**	**8,406**	**8,789**	**9,493**	**14,315**
Trade and Other Payables	772	726	632	862	1,278
Long-Term Borrowings *(Inc. current maturity)*	967	1,262	1,112	1,289	3,083
Short-Term Borrowings	220	993	1,571	-	0
Total Liabilities	**2,383**	**3,493**	**3,870**	**2,730**	**5,742**
Paid-up Capital	30	30	30	30	30
Total Equity	**4,263**	**4,913**	**4,919**	**6,763**	**8,572**
INCOME STATEMENT					
Net Sales	8,074	9,348	8,924	12,158	12,312
Gross Profit	868	1,294	824	2,732	2,687
Profit Before Tax	542	957	456	2,161	2,205
Profit After Tax	482	832	329	1,851	2,024
RATIO ANALYSIS					
Gross Margin (%)	10.8%	13.8%	9.2%	22.5%	21.8%
Net Margin (%)	6.0%	8.9%	3.7%	15.2%	16.4%
Net Working Capital	2,701	3,286	3,477	5,290	6,162
Current Ratio	3.48	2.73	2.54	5.89	4.68
FFO to Long-Term Debt	0.62	0.75	0.47	1.77	0.93
FFO to Total Debt	0.51	0.42	0.20	1.77	0.93
DSCR (x)	4.08	4.83	2.18	17.1	10.1
Gearing (x)	0.28	0.46	0.55	0.19	0.36
Debt Leverage (x)	0.56	0.71	0.79	0.40	0.67
Inventory + Receivable/Short-term Borrowings (x)	14.5	4.4	3.1	*n/a*	*n/a*

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 Textiles Mills Limited					
Sector	Textile					
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					
	15/Aug/2022	A+	A-1	Stable	Reaffirmed	
	27/May/2021	A+	A-1	Stable	Maintained	
	22/Apr/2020	A+	A-1	Rating Watch-Developing	Maintained	
	21/Feb/2019	A+	A-1	Stable	Reaffirmed	
	17/Dec/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.					
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Due Diligence Meeting Conducted	**Name**	**Designation**	**Date**			
	Mr. Mohammad Shaheen	Chairman	July 21, 2022			