RATING REPORT

Gohar Textile Mills (Pvt.) Limited

REPORT DATE:
March 29, 2019

RATING ANALYSTS:
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RATING DETAILS		
	Initial Rating	
Rating Category	**Long-term**	**Short-term**
Entity	A	A-1
Rating Date	*26th march'19*	
Rating Outlook	Stable	
Outlook Date	*26th march'19*	

COMPANY INFORMATION	
Incorporated in 1980	External Auditors: Azhar Zafar & Company
Private Limited Company	Chairman of the Board/CEO: Mr. Liaqat Ali
Key Shareholders (More than 5%):	
Mr. Liaqat Ali – 32.2%	
Mr. Gohar Mustafa – 35.8%	
Mr. Muhammad Aftab Gauhar – 15.8%	
Mr. Altaf Gohar – 13.7%	

APPLICABLE METHODOLOGY(IES)
JCR-VIS Entity Rating Criteria: Industrial Corporates (May 2016)
http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf

Gohar Textile Mills (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Gohar Textile Mills Limited (GTML) was established in 1980 in UK and an integrated operation was opened in Pakistan in 1990. The company is involved in the spinning, weaving and finished fabric.

Profile of the Chairman/CEO

Mr. Liaqat Ali serves as the Chairman of the Board and Chief Executive Officer. He has over 35 years of experience in the textile industry.

Financial Snapshot

Total Equity: end-FY18: Rs. 5.7b; end-FY17: Rs.5.05b; end-FY16: Rs. 4.47b

Assets: end-FY18: Rs. 9.49b; end-FY17: Rs. 7.82b; end-FY16: Rs. 6.47b

Profit After Tax: end-FY18: Rs. 654m; end-FY17: Rs. 577m; end-FY16: Rs. 430m

RATING RATIONALE

Rating Rationale

The ratings assigned to Gohar Textile Mills (Pvt.) Limited (GTML) take into account the company's presence in export oriented value-added textile segment, positive momentum in profitability on a timeline basis, sound liquidity and reasonable experience of management team in the relevant industry. The ratings derive strength from sustenance of healthy margins, low leverage indicators with minimal reliance on long-term borrowings and comfortable debt service coverages. GTML operates as a family owned business with the shareholding vested among individuals of the same family. The ratings remain constrained by overall high business risk related to inherent volatility in the textile sector. The ratings remain dependent on maintenance of margins and low leveraged capital structure, realization of projected targets, incremental cash flow generation from recent capital expenditure coupled with evolution of sector dynamics.

Competition from regional competitors on a higher side: The significance of textile sector is exemplified by the fact that this sector contributes more than half of Pakistan's total exports. On average, textile products accounted for 59% of the country's total exports during the last three years. The demand driven price risk is largely curtailed given the demand for textile apparel in the world was recorded around US$1.2 trillion during FY18 and it is projected to increase at a CAGR of 2% during the next four years. In line with positive demand outlook coupled with recent rupee devaluation, the sector has significant opportunity to earn foreign exchange through textile exports. However, potential revenue risk prevails on account of intense competition posed by regional competitors including India and Bangladesh in the international market. In addition, sell side risks involving sizeable energy costs shroud the actual potential of textile industry. Further, in the backdrop of increasing benchmark rates, the borrowing capacity of the local market players has been adversely impacted leading to liquidity stress. In addition, the resistance to change and inflexibility in built in the sector dynamics has hampered the capability of exporters to incorporate ever-changing consumer preferences in the product profile; the same has largely rendered exports uncompetitive in the past. In view of this, relaxation in governed policies, incentivisation of the local textile producers in terms of subsidies, conduction of trade fares and supply of uninterrupted power is likely to play a significant role in unlocking the budding potential of the segment.

Integrated manufacturing facility: The sponsors of GTML, started textile business in 1980 through a Registered Partnership Firm named as Gohar Enterprises; the same was later incorporated as GTML on 23rd October 1995. After recognition of a market gap in Pakistan, the company initiated integrated operations in Pakistan in 1990 with 40 weaving machines. Currently, the total headcount of the company is around 3,000. The Mill comprising Spinning, Weaving, Processing, Stitching and Wadding & Quilting units, is located at 3-KM, Chak Jhumra Road, Khurrianwala, Faisalabad and the company's head office is situated at 208 Chak Road, Zia Town, Faisalabad, Pakistan. GTML is a vertically integrated textile unit consisting of an in-house yarn manufacturing, weaving, fabric processing (dyeing, printing & finishing), CMT (cutting, Stitching & Packing), Quilting (Wadding and Quilt making) manufacturing facility.

Yarn manufacturing unit of the company has an installed capacity of 31,680 spindles with a production capacity of 685 tons of yarn/month. Out of the total yarn requirement, around one half is internally manufactured while the remaining is procured from other local and international yarn manufacturers. The capacity utilization of spinning unit stood at 97% (FY17: 95%) in FY18.

The company has an aggregate weaving capacity of 2,350,000 meters/month with 100 auto looms, 100 suzler looms and 216 airjet looms. The capacity utilization of the weaving unit was recorded higher at 95% during FY18 as compared to 92% in the preceding year. Processing function at GTML comprises fabric bleaching, dyeing, printing and finishing. Monthly fabrics processing capacity in linear meters is around 4,200,000 linear meters. The capacity utilization of the processing unit remained at 96% during FY18 as compared to 92% in preceding year. In bleaching overall capacity is around 230,000 meters/day. The company initially had 1 SAGA continuous bleaching plant; however, enhancement in the processing unit mainly pertained to addition of 1 more SAGA continuous bleaching plant with a capacity of 100,000/day during FY17.

The Printing Range includes rotaries, panel and digital printing with a combined printing capacity of 100,000 meters/day. The company has 2 Reggiani machines with 15 color printing options and a working width of 3.2 meters, 1 Reggiani flat bed and 1 MS digital printing machines. The rotary, flat bed and digital machines are capable of doing standard design repeats of 640mm, 820mm and 914mm. Moreover, quality assurance department involves strict quality control procedures with routine checkup for composition, thread count, piling, absorbency, whiteness, wet & dry washing and rubbing analysis to assure that fabric is properly inspected for relevant factors before being forwarded to the next stage of production.

In order to maintain the quality of processed fabrics, the company has a testing laboratory including abrasion tester, crease recovery tester, spray tester and multi-light meter to ensures all dyed fabric is properly checked for factors including shrinkage, color and thread quality. The company has a Stitching, Wadding and Quilting unit with 600 machines including lock stitch, over lock, multi needle, kaj button, ruffling, blind stitch, embroidery, threading and cutters etc. In atomization, the company also has multi needle quilting machines, direct filling, auto cutting, auto pillows making and embroidery machines .The latest Texpa line was introduced recently to automatically stitch duvet covers. Stitching unit has a capacity to stitch 3.5m pieces/month. During FY17, the capacity of stitching and quilting unit was enhanced on account of additions in cutting, quilting, embroidery, and stitching machines.

Performance lifted by exports: Product portfolio primarily includes plain dyed bedding, embroidered bed-sets, cushions, curtains, quilts, mattress protectors, blankets and pillows. Duvet cover sets and sheet sets are the main revenue drivers for the company constituting around 70% of the total sales mix. The breakdown of revenue mix in terms of product portfolio is presented in the table below:

Products	FY16	FY17	FY18
Sheet Sets	35.3%	33.3%	31.2%
Pillows, Pillow Covers, Pillow Ticks & Bolster	6.4%	10.1%	10.2%
Cushions & Cushion Covers	2.2%	1.8%	0.4%
Bed Sets	4.9%	3.7%	7.0%
Curtains	1.4%	1.2%	0.9%
Duvet Set & Duvet Cover Set	36.7%	39.9%	38.2%
Comforters	11.4%	8.4%	7.4%
Mattress Protector	1.1%	0.9%	1.3%
Gowns	0.4%	0.4%	0.6%

Blankets	0.0%	0.0%	2.6%
Mixed Made Ups	0.2%	0.3%	0.2%
Total	100%	100%	100%

The customers of the company include renowned international brands including K-Mart, ALDI, LIDL, Home choice, Next, Primark, Debenhams, Laura Ashley, Walmart/ASDA, Legend, Sainsbury's, Target, SIMBA and MEXOM. As a result of dealing with prominent wholesale clients, the client concentration was sizeable with top-10 customers representing 63% (FY17: 77%; FY16: 84%) of the total revenues during FY18. Europe is the main export market for GTML constituting for more than half of the total revenues. Going forward, the management plans to increase market penetration in USA to diversify its regional and customer concentration. Currently, sales in USA contribute around 1% of the total revenue. The regional breakup of revenue mix is tabulated below:

	FY16	FY17	FY18
Top 10	84%	77%	67%
Europe	58%	55%	62%
Australia	20%	16%	21%
Africa	3%	5%	7%
Asia	17%	21%	9%
United States	2%	3%	1%

Almost 80% export sales are made on credit. The company has different payments terms with different buyers with credit period ranging between 15-90 days. Exports are made on four different bases of payments including Letter Of Credit (LC), Cash against Documents (CAD), Documents against Acceptance (DAA) and Telegraphic Transfer (TT) basis. On the other hand, yarn procurement from local market is done on cash while payment period for imported raw materials ranges between 10-90 days. GTML's total power requirement is around 10MW; the same has been arranged through various sources including 9.6MW from Water and Power Development Authority (WAPDA) and 10.7MW from the company's captive power. The power supply from WAPDA is currently relatively cheap; out of the total indigenous power production, 4MW is gas based while the remaining generation is based on furnace and diesel engine.

Profitability indicators supported by tax benefit: Over the last three years, sales of the company have grown at a CAGR of around 9%; moreover, the sales for 1H19 were recorded 40% than the corresponding period last year. The export sales remain the major revenue driver contributing around 96% to the sales mix. Net sales of the company remained largely stagnant during FY18; the slight increase was an outcome of higher selling prices of sheet sets, duvet sets and comforters. However, the impact of higher prices was offset by decline in volumetric sales of sheet sets, pillows, duvet sets and cushions. In addition, the result of higher output prices could not reflect in the gross margins owing to considerable increase in input cost, mainly related to fuel and power. The distribution cost increased slightly primarily as a result of higher freight expense owing to increase in cost of clearing and forwarding contracts. Further, administrative expenses increased on a timeline basis owing to inflationary pressure, leading to annual salary adjustments together with higher headcount reported during FY18. In the backdrop of increasing average benchmark interest rates coupled with higher average short-term borrowings and some additional long-term funding, finance cost of the company increased during FY18. Consequently with increase in operating expenses and finance cost together with slight dip in gross margins, GTML before tax profit was recorded lower during FY18 as compared to preceding year. Meanwhile, the bottom line was positively impacted by prior year tax adjustment related to tax credits received for investment in plant and machinery.

Strong liquidity profile as evident from healthy cash flows in relation to outstanding obligations and adequate debt service ability: Liquidity profile of the company is considered sound in view of sizable cash flows in relation to outstanding obligations and sound debt service capacity. Despite lower profit before taxation, Funds from Operations (FFO) exhibited an increasing trend in line with higher non-cash adjustments. Further, owing to significant increase in short-term funding, FFO to total debt decreased; however, FFO to long-term debt and debt service coverage remained sizeable in FY18. According to the management, cash flows are expected to improve on account of increase in sales supported by incremental revenue from installation of new looms in the weaving unit and cost saving from improving operational efficiencies from investment in wadding, bleaching and stitching unit. While trade receivables stood higher on account of relaxed payment terms offered to export clients and addition of new clients in FY18, other receivables also increased on a timeline basis mainly due to export rebate and duty drawback receivable from the government. The new clients included Shandong Textile Ltd China, Laura Ashley Ltd UK, Gerber LLC USA, Shanxi Qinchuan China and Lanificio Vasco. The aging of receivables is considered satisfactory since only 4.5% of the total receivables were due for more than three months. Further, stock in trade increased considerably on a timeline basis in line with sizeable quantum of imported raw material procured for meeting production orders received. The imported raw materials include chemicals, packaging material and polyester staple fiber. The current ratio is maintained at 1.4x over the last two years.

Conservative capital structure with gearing levels expected to improve further: The equity base of the company has steadily strengthened on the back of profit retention. GMTL procured long-term debt during FY17 to finance capex in plant and machinery; the company carried out balancing, modernization and replacement (BMR) in spinning (Rs. 84m), weaving (Rs.126m) and processing units (Rs. 90m). Further during FY18, the company made an additional capex of Rs. 1.6b mainly for purchase of new looms related to weaving unit (Rs. 748m), capacity enhancement of wadding plant for layered quilts (Rs. 102), installation of bleaching plant (Rs. 106m), procurement on new texpa machine (Rs. 85m) and procurement of coal fired steam boiler (Rs. 59m). Subsequently, total debt levels of the company have increased on account of long-term borrowing obtained coupled with higher utilization of short-term credit facilities to meet increased working capital requirements. According to the management, the increase in short-term credit is temporary in nature, mainly pertaining to financing of stock inventory to process orders of new clients booked. The long-term finances include LTFF loans from commercial banks with markup ranging between 3.5% and 5.0%. The loan is secured against first equitable mortgage charge over fixed assets amounting to Rs. 1.1b at end-FY18. Given higher short-term borrowings carried on the balance sheet, gearing and leverage indicators have witnessed an increasing trend on a timeline basis; however, both are relatively on a lower side than industry averages.

Information Technology and Internal Audit function: GTML is using Oracle-based ERP software comprising four modules including Financial Management, Sales and Invoicing (both export and local), Purchase Management, Production Management (Spinning, Weaving, Processing, and Folding), Human Resources Management, Inventories Management, Taxation, Gate In/Out, Employees Provident Fund and Design Studio. Majority of the computerized machines are integrated with ERP platform which provides real time data on production. The internal audit team is comprises six members who conduct post and pre-audit of all the transactions.

Steady growth projected going forward with no sizable long-term funding planned to be procured: Going forward, the management projects sales to grow at a CAGR of 10.0% to 15.0% over the next six years with gross margins expected to be maintained around 16.0%. The profitability is projected to exhibit positive momentum on account of decline in finance cost with contractual yearly debt repayments and rationalization of operating expenses. Asset base is likely to augment on the back of further capex in fixed assets. The company has projected capex of Rs. 259m in FY19 pertaining to purchase of freehold land for setting up a separate weaving unit along with modest enhancement in electric installments of factory and office equipment. Capex is projected to be financed through a new long-term loan amounting to Rs. 47m to be procured during FY19; the capex subsequent to FY19 is projected to be financed through the company's internally generated funds. Debt leverage is projected to decline in line higher equity base.

Gohar Textile Mills (Pvt.) Limited Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	June 30, 2016	June 30, 2017	June 30, 2018
Non-Current Assets	3,472	4,635	4,874
Stock-in-Trade	1,507	1,871	2,641
Trade Debts	870	581	956
Other Receivables	431	514	581
Cash & Bank Balances	51	38	43
Other Assets	143	183	390
Total Assets	**6,474**	**7,822**	**9,485**
Trade and Other Payables	482	556	664
Short Term Borrowings	1,513	1,606	2,464
Long-Term Borrowings *(Inc. current maturity)*	-	590	622
Other Liabilities	10	23	34
Tier-1 Equity	**3,293**	**3,966**	**4,705**
Total Equity	4,469	5,047	5,701
INCOME STATEMENT	**June 30, 2016**	**June 30, 2017**	**June 30, 2018**
Net Sales	6,576	7,790	7,842
Gross Profit	972	1,196	1,178
Operating Profit	581	744	698
Profit After Tax	430	577	654
FFO	625	903	914
RATIO ANALYSIS	**June 30, 2016**	**June 30, 2017**	**June 30, 2018**
Gross Margin (%)	14.8	15.3	15.0
Net Working Capital	997	872	1282
FFO to Long-Term Debt	-	1.53	1.47
FFO to Total Debt	0.41	0.41	0.30
Debt Servicing Coverage Ratio (x)	8.0	6.9	3.9
ROAA (%)	7.8	8.1	7.6
ROAE (%)	11.6	12.1	12.2
Gearing (x)	0.46	0.55	0.66
Debt Leverage (x)	0.61	0.70	0.80

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure II

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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 III
Name of Rated Entity	Gohar Textile Mills (Pvt.) 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				
03-26-2019	A	A-1	Stable	Initial

Instrument Structure	N/A
Statement by the Rating Team	JCR-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.
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