RATING REPORT

Gadoon Textile Mills Limited

REPORT DATE:
November 30, 2021

RATING ANALYSTS:
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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 Date	*November 30, 2021*		*November 13,2020*	
Rating Outlook	Stable		Stable	

COMPANY INFORMATION

Incorporated in 1988	**External auditors:** M/s Yousuf Adil, Chartered Accountants
Public Listed Company	**Chairman:** Mr. M. Yunus Tabba
Key Shareholders:	**CEO:** Mr. M. Sohail Tabba
Y.B. Holdings (Private) Limited	

APPLICABLE METHODOLOGY(IES)

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

Gadoon Textile Mills Limited

OVERVIEW OF THE INSTITUTION

Gadoon Textile Mills Limited was incorporated in 1988 as part of Yunus Brothers Group (YBG). The principal business activity of the Company is to manufacture and sell yarn, knitted sheets, and production and sale of milk.

Profile of Chairman

Mr. Mohammad Yunus Tabba started his career over 59 years ago with YBG as one of its founding members and seen it progress and expand.

Profile of CEO

Mr. Muhammad Sohail Tabba is a seasoned businessman with extensive experience in manufacturing, energy, real estate and cement sectors. Mr. Sohail is a chairman of ICI Pakistan Limited, Yunus Energy Limited and NutriCo Morinaga (Private) Limited. Furthermore, he serves as a CEO of Lucky Energy (Private) Limited, Lucky Knits (Private) Limited and LuckyOne (Private) Limited.

RATING RATIONALE

Company Profile

Gadoon Textile Mills Limited (GTML) is engaged in the production and sale of yarn, knitted bedding products and production and sale of milk. GTML is part of Yunus Brothers Group, a reputable conglomerate with strong financial presence in diversified sectors including textile, building materials, real estate, power generation, chemicals, pharmaceuticals, food and automotive.

GTML Operations

GTML operates through two manufacturing facilities one located in Karachi (near super highway) and another one in District Swabi Province of KPK with over 345,000 spindles. Historically, the Company has been operating at high utilization levels, but remained under pressure in FY20 due to pandemic induced slow-down. However, given subsequent economic recovery post first wave of COVID -19 together with favorable Government measures, volumes along with capacity utilization recovered during FY21.

GTML Investments

Long-term investments stood higher at Rs. 3.5b (FY20: Rs. 3.1b) during FY21. Long term investments represent 11.4% of the total assets.

Table 1: Long-Term Investments

(Rs. in millions)	FY20	FY21
ICI Pakistan Limited	2,010.5	2,194.8
Yunus Energy Limited	1,138.2	1,374.3
Lucky Holdings Limited	1.8	1.5
Total	**3,150.5**	**3,570.6**

In addition, GTML has provided subordinated loans of Rs. 15.6m to Tricom Solar Power (Private) Limited and Yunus Wind Power Limited. These renewable power projects are in their initial stage and the Company plans to further invest in the project within the limit as approved by the Company's shareholders.

Key Rating Drivers

Positive growth momentum in textile sector post ease in COVID-19 led lockdowns lends support to the business of the Company. However, volatility in raw material prices and increasing freight costs continue to remain key business risk factors.

Textile exports of Pakistan recorded double digit growth of 23% for FY21 to stand at USD 15.4b, with the ambition of the government to enhance it further for FY22. Further growth of 27% was witnessed during Q1'FY22 vis-à-vis Q1'FY21. The increase in textile exports has been due to increase in demand for textile products with the opening up of countries post COVID-19 imposed lockdown and further supported by diversion of orders from neighboring countries facing comparatively severe COVID-19 disruption. Value-added segment contributed mostly towards the textile export growth. Meanwhile, the commodities that witnessed dull growth included raw cotton, cotton yarn and cotton cloth. Going forward, sector dynamics are considered sound as Pakistan continues to receive export orders, especially for value added textile products, from global economies. However, skyrocketing cotton prices and significant increase in freight cost continue to remain key business risk factors.

Spinning sector characterized by high cyclicality and stiff competition

Movement in cotton prices and cotton crop yield drives the performance of the spinning segment. Cotton production declined to 6.98mn bales in 2020-21 from 9.18mn bales in 2019-20, mainly due to harvest area decline in Punjab and thin profit margin for growers. Hence, sizable decline in cotton production led to sharp rise in cotton prices which in turn escalated prices of yarn and added to the margins of the spinning business during FY21. For FY22, rough estimates put cotton production between 8.5 and 9 million bales against the official target of 10.5 million bales. On the other hand, higher cotton prices are likely to ease to some extent production concerns due to comparatively attractive prices available to farmers for cotton crop cultivation. However, volatility in cotton prices (both on local and international level) poses a challenging environment for spinners.

Capital expenditure to contribute towards improved operational efficiencies and capacity expansion

GTML is currently undertaking CAPEX involving purchase of new technological advanced machinery and replacing it with the old obsolete machinery for achieving higher operational efficiencies and improving competitive position in the market. Further, given the upbeat demand for its knitted bedding products, the Company aims to enhance its knitting capacity in the medium term. Expansion of its dairy segment is also in the pipeline. Company has so far incurred CAPEX amounting to Rs. 1.2b during FY21 and plans to invest further during the ongoing year. Almost entire CAPEX will be met through concessionary loans offered by the SBP.

Topline has registered strong growth in the outgoing year coupled with increase in gross margins

GTML recorded hefty rise in revenue during FY21 at Rs. 41.0b (FY20: Rs. 28.9b), reflecting impressive growth of 41.4%. Increase in demand post ease in COVID-19 crisis across the world and significant rise in yarn prices contributed to increase in sales. Exports (direct and indirect) continue to represent more than two-fourth of the sales mix at 58.3% (FY20: 61.8%) during FY21. The direct export sales of yarn exhibited decline on account of COVID-19 led weakening albeit sales witnessed increase in third and fourth quarter of the outgoing year. Geographic concentration in exports is on the higher side as major bulk of sales is directed to China. Management is looking forward to diversify its clientele by exploring and building its presence in other countries especially in USA.

Spinning segment continued to be the main revenue contributor followed by knitted bedding products and dairy. Significant growth of 90.5% was seen in the sale of knitting bedding products in line with overall rise in demand for bedding products. Going forward, management foresees higher demand for its knitting segment.

in Rs. Mn	FY20	% contribution in revenue	FY21	% contribution in revenue
Spinning	27,528	95.0%	**38,276**	93.3%
Knitting	1,265	4.3%	**2,411**	5.9%
Dairy	194	0.7%	**323**	0.8%
Total Sales	**28,987**		**41,010**	

Gross margins of the Company increased to 12.1% (FY20: 7.7%) during FY21. Margin expansion has been a function of increase in yarn prices, efficient cotton procurement and enhanced fabric demand in export markets.

The Company realized exchange gain of Rs. 62.2m in FY21 as against the exchange loss of Rs. 889.4m in the prior year contributing to a significant jump in net margins at 8.6% (FY20 : 0.2%) relative to last year. Margin improvement was further supported by low finance cost due to lower interest rate environment. Overall profitability is further supported through recognition of share of profit from associates (namely ICI Pakistan, Yunus Energy and Lucky Holdings) amounting to Rs. 677.5m (FY20: Rs. 492.5m) under the equity method, although the same has no cash flow impact and dividend income from these investments stood at Rs. 230.5m (FY20: Rs. 230.4m) during FY21. Margins, going forward, will remain subject to cotton price dynamics and rupee devaluation.

Strong profitability growth led to improvement in cash flow coverage indicators

Liquidity profile of the Company is considered strong with healthy cash flows in line with improved profitability. In absolute terms, Funds from Operations (FFO) increased considerably to Rs. 4,122.9m (FY20: Rs. 703.0m) in FY21. Consequently, FFO to total debt, coupled with significant reduction in short-term borrowings, was reported higher at 41.7% (FY20: 4.4%). Debt Service Coverage Ratio improved to 6.57x (FY20: 1.57x) during FY21 in line with higher profit. Current ratio of the company has improved on a timeline basis and was recorded at 1.31x. Trade debts and stock in trade are more than sufficient to cover short term borrowings. Aging profile of trade debts remain within manageable levels.

Sound capitalization indicators

Equity base augmented to Rs. 12.6b (FY20: Rs. 9.1b) on account of retained earnings. The long term loan of the Company increased to Rs. 4.8b (FY20: Rs. 3.6b) in FY21 to fund CAPEX. On the other hand, reduction in quantum of short term borrowings (FY21: Rs. 5.0b; FY20: Rs. 12.4b) on account of higher operating cash flows resulting from improved profitability contributed towards lower total debt at Rs. 9.9b (FY20: Rs. 16.0b) in FY21. As a result, gearing and leverage improved to 0.78x (FY20: 1.76x) and 1.48x (FY20: 2.39x), respectively during FY21. Despite projected increase in debt levels to finance CAPEX, gearing and leverage indicators are expected to remain at comfortable levels owing to high equity base.

Gadoon Textile Mills Limited **Appendix I**

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY18**	**FY19**	**FY20**	**FY21**
Fixed Assets	7,791.9	9,870.4	10,165.0	10,253.6
LT Investments	2,686.9	2,890.6	3,150.6	3,570.6
Stock-in-Trade	7,469.6	8,407.4	12,914.4	10,877.3
Trade Debts	2,464.2	3,517.7	2,333.0	4,038.4
Cash & Bank Balances	188.9	112.5	86.1	143.2
Total Assets	23,142.5	27,305.5	30,833.4	31,226.2
Trade and Other Payables	3,088.5	3,700.8	4,181.7	7,101.9
Long Term Debt (including current maturity)	594.3	2,675.1	3,594.8	4,839.5
Short Term Debt	9,864.9	9,926.7	12,362.1	5,038.8
Total Debt	10,459.2	12,601.8	15,956.9	9,878.3
Paid up Capital	280.3	280.3	280.3	280.3
Total Equity	8,213.5	9,209.4	9,084.4	12,610.1
INCOME STATEMENT	**FY18**	**FY19**	**FY20**	**FY21**
Net Sales	27,554.7	31,217.5	28,986.8	41,009.8
Gross Profit	1,944.9	2,892.7	2,241.3	4,975.6
Profit Before Tax	1,473.6	1,668.5	337.7	4,026.1
Profit After Tax	1,185.3	1,186.1	45.5	3,534.1
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**	**FY21**
Gross Margin (%)	7.1%	9.3%	7.7%	12.1%
Net Margin	4.3%	3.8%	0.2%	8.6%
FFO	1,602.9	2,360.3	703.0	4,122.9
Current Ratio (x)	0.96	1.02	1.03	1.31
(Stock+ Trade Debts)/ Short-term Debt	1.01	1.20	1.23	2.96
Debt Servicing Coverage Ratio (x)	4.01	3.59	1.57	6.57
Gearing (x)	1.27	1.37	1.76	0.78
Leverage (x)	1.82	1.97	2.39	1.48
ROAA (%)	5.5%	4.7%	0.2%	11.4%
ROAE (%)	15.2%	13.6%	0.5%	32.6%

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	Gadoon Textile Mills Limited
Sector	Textiles
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				
Nov-30-21	A+	A-1	Stable	Maintained
Nov-13-20	A+	A-1	Stable	Maintained
Apr-24-20	A+	A-1	Rating Watch - Developing	Maintained
Dec-13-19	A+	A-1	Stable	Reaffirmed
Oct-29-18	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. Imran Moten	CFO	Oct 04th, 2021
Mr. Muhammad Umair	Financial Controller	
Mr. Abdul Jabbar Raja	GM Finance	