RATING REPORT

Gujranwala Food Industries (Pvt) Limited (GFIL)

REPORT DATE:
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RATING ANALYSTS:
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RATING DETAILS		
Rating Category	*Initial Rating*	
	Long-term	*Short-term*
Entity	BBB-	*A-3*
Rating Outlook	Stable	
Outlook Date	*December 10, 2018*	

COMPANY INFORMATION

Incorporated in 1984	External auditors: Iyaz Ahmad & Co. Chartered Accountants
Private Limited Company	Chairman/CEO: Mr. Abdul Haleem
Key Shareholders (with stake 5% or more) :	
Mr. Abdul Haleem – 33.87%	
Ms. Zubaida Kausar– 15.01%	
Mr. Muhammad Jamal – 5.27%	
Mr. Muhammad Suleman – 5.27%	

APPLICABLE METHODOLOGY(IES)

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

Gujranwala Food Industries (Pvt.) Limited

OVERVIEW OF THE INSTITUTION

Gujranwala Food Industries (Pvt.) Limited was established in 1984. The company is involved in producing Confectionary, Snacks, Wafers and Chocolate items.

Profile of Chairman/CEO:

Mr. Abdul Haleem and family has the controlling stake in the company. As the founding member, the CEO has been associated with the company since inception and he is a foreign graduate.

Financial Snapshot:

Total Equity: end-FY18: Rs. 368m; end-FY17: Rs. 333; end-FY16: Rs. 334m

Assets: end-FY18: Rs 1.1b; end-FY17: Rs. 1.0b; end-FY16: Rs. 0.9b

Profit After Tax: FY18: Rs. 35.0m; FY17: Rs. 28.5m; FY16: Rs. (2.2m)

RATING RATIONALE

The ratings assigned to Gujranwala Food Industries (Pvt.) Limited (GFIL) take into account its presence in cash rich and fast moving consumer goods industry whereby economic downturn and inflationary pressure has limited impact on the overall operational performance. The ratings draw strength from GFIL being a mid-tier player in the oligopolistic confectionery industry with reasonable market share. While the company operates on thin net margins, its business risk is considered moderate despite increasing competitive operating environment on the back of established market presence in relatively low priced products. The ratings also incorporate low gearing and adequate debt service coverage of the company. However, the ratings are constrained by the company's limited scale of operations, minimal growth in revenues on a timeline basis and high operating expenses, putting a drag on profitability and liquidity indicators.

Key Rating Drivers:

Competitive oligopolistic industry amidst encouraging consumer dynamics: The target market for confectionary products is mainly children; however growth opportunities are being reaped by tapping the youth and adult market segments as well. The revenue driven growth risk for the company is largely curtailed on account of general increase in population coupled with broader based population density with around 44.5% of country's total population falling in the less than twenty years bracket. In addition, growth in the urban middle class and enhancement in personal disposable income in metropolitan cities has steadily improved the consumption patterns for confectionary products. Demand driven price risk is on a higher side on account of high substitutability, modest brand loyalty and low involvement levels of end-consumers towards the product portfolio of the local confectionery producers. The aforementioned factors lead to higher price sensitivity making it unfeasible for GFIL to improve margins in a highly competitive market. In addition, the unorganized confectionary sector is also a major revenue risk for the company. Further, the presence and prominence of foreign brands among urban middle and upper class consumers' results in cannibalization of the local producers' market share to a certain extent. Imported products entailing higher brand recognition are generally associated with superior quality vis-à-vis local products; therefore, charge premium prices and reap higher margins. Moreover, owing to strong financial muscle and healthy cash flows, the international players are able to give better distributor margins leading to prominent display of their products which in turn leads to higher revenues. The company mitigates inventory risk by following make to order model whereby production is initiated after receiving the order.

Limited increase in revenues with nominal profitability and cash flows: The company recorded a compounded annual growth rate of 8.3% in revenues over the last three years; with range bound prices, the growth was largely a function of volumetric increase. The company sales mix remained dominated by local sales with export revenues, though increased, represented one-third of the total sales during FY18. In absolute terms, export sales exhibited positive trajectory on account of penetration in new export markets including Middle East and South Africa. Bubble gums and chew toffees are the major revenue drivers for the company representing four-fifths of the total sales. The company operates on stable gross margins; however, the same does not translate into the bottom line owing to relatively high operating expenses. Liquidity, in terms of cash flows, witnessed some volatility in recent years; Funds from Operations (FFO) was recorded lower during FY18 despite positive momentum in profitability owing to higher tax paid. Further, the current ratio is maintained over 1.1x over the last three years. Given around 80% of the company's local sales are made on cash basis, the cash conversion cycle remained sound. Further, FFO to total debt, albeit adequate, decreased during FY18. Ageing profile of trade debts is considered manageable with a limited amount of receivables overdue for over three months. Given that the company does not plan to mobilize any further long-term debt in the foreseeable future, coverages are projected to remain sufficient.

Low gearing levels due to conservative capital structure: The capital structure of the company remains conservative owing to minimal reliance on borrowings. Total equity increased on account of internal capital generation. Further, the total equity includes interest free long-term loan acquired from sponsors. The company mobilized long-term funding from commercial banks during FY17 to finance CAPEX requirements. Further, GFIL primarily uses export refinance facility to meet its short-term working capital requirements; meanwhile overdraft facility is also utilized on need basis. Given increase in trade payables and advances received from customers, debt leverage increased and is considered relatively high. Considering the business model of the company along with no immediate plan of equity injection by the sponsors, leverage indicators are likely to remain around current levels.

Experienced management team: Senior management team of the company comprises experienced resources having relevant experience in the industry. Going forward, the management plans to impart further emphasis on strengthening of brand positioning in the local market, higher automation and development of sustainable high-margin export base.

Gujranwala Food Industries (Pvt.) Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**June 30, 2016**	**June 30, 2017**	**June 30, 2018**
Non-Current Assets	278	385	363
Stock-in-Trade	274	239	334
Trade Debtors	70	86	52
Advances, Deposits & Prepayments	225	218	288
Cash & Bank Balances	55	47	70
Other Assets	9	3	2
Total Assets	911	978	1,109
Trade Payables	246	273	347
Short-Term Borrowings	51	60	71
Long-Term Borrowings *(Inc. current maturity)*	9	106	95
Advances Against Sales	220	152	166
Other Liabilities	51	54	62
Total Equity	334	333	368
INCOME STATEMENT	**June 30, 2016**	**June 30, 2017**	**June 30, 2018**
Net Sales	1,727	1,919	1,994
Gross Profit	393	436	451
Operating Profit	18	57	63
Profit After Tax	(2)	28	35
FFO	27	93	62
RATIO ANALYSIS	**June 30, 2016**	**June 30, 2017**	**June 30, 2018**
Gross Margin (%)	22.8	22.7	22.6
FFO to Long-Term Debt	2.97	0.87	0.66
FFO to Total Debt (%)	0.45	0.56	0.38
Debt Servicing Coverage Ratio (x)	3.76	7.36	7.51
ROAA (%)	-	3.0	3.4
ROAE (%)	-	8.5	10.0
Gearing (x)	0.18	0.50	0.45
Debt Leverage (x)	1.18	2.09	2.15

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix 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 — Appendix III

Name of Rated Entity	Gujranwala Food Industries (Pvt.) Limited
Sector	Consumer Goods
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see table below
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
10/12/2018	BBB-	A-3	Stable	Initial