RATING REPORT

Macter International Limited

REPORT DATE:

January 15, 2021

RATING ANALYST:

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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	A	A-2	A	A-2
Rating Date	*January 15' 21*		*September 17' 19*	
Rating Outlook	Stable		Stable	
Rating Action	*Reaffirmed*		*Downgrade*	

COMPANY INFORMATION

Incorporated in 1992	**External auditors:** EY Ford Rhodes, Chartered Accountants
Listed Public Limited Company	**Chairman of the Board:** Mr. Amanullah Kassim
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Asif Misbah
Misbah Family – 73.6%	
SAAS Enterprises (Private) Limited– 16.4%	
General Public – 10.0%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Industrial Corporates (April, 2019)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Macter International Limited (Macter)

OVERVIEW OF THE INSTITUTION

In 1992, Macter International Limited (Macter) was incorporated as a private limited company. Subsequently, it was converted into a public limited company in 2011. In 2017, Macter was listed on Pakistan Stock Exchange Limited. Registered office of the company is located in Karachi, Pakistan.

Profile of Chairman
Mr. Amanullah Kassim holds M.B.B.S degree from Sindh Medical College Karachi and possesses extensive experience in management of a private business group. He is also engaged with social charities and serves as the President of Kiran Patient Welfare Society & Zubaida Machiyara Trust.

Profile of Chief Executive Officer
Mr. Asif Misbah has been associated with Macter since 1994. He holds MBA degree from Institute of Business Administration, Karachi.

RATING RATIONALE

Macter International Limited is engaged in manufacturing and marketing of pharmaceutical products. The business activities of the company can be broadly segregated into two major segments - branded generics and contract manufacturing. Majority shareholding of the company is vested with Misbah Family, while the remaining shareholding is held by SAAS Enterprises (Private) Limited, other institutions and general public. Senior management of the company comprises experienced individuals having significant experience in the pharmaceutical sector.

The company has total annual capacity of ~89m units (on a single shift basis) for drug production in the form of tablets, capsules, syrups, suspensions, dry powder, injections, ointments, creams, drops and inhalers. The company has two production facilities located at SITE in Karachi. Macter is also involved in toll manufacturing for renowned multinational companies, which comprised 1.7% of the company's net sales in FY20.

Business risk of the sector is low due to non-cyclical nature of industry, growing demand and favourable population demographics

Given the non-cyclical nature of the sector with relatively stable (inelastic) demand, revenues and profitability of pharmaceutical industry are likely to remain unaffected by the economic downturns. Growing population, increase in income levels, high disease incidence coupled with emergence of new diseases and poor hygiene levels continue to support growth in demand for pharmaceutical products in the country. Hence, business risk is considered low in the long term. However, dependence on Drug Regulatory Authority of Pakistan (DRAP) for regulatory approvals pertaining to increase in prices and introduction of new products along with impact of rupee devaluation on margins continue to remain key risk factors. Recent amendments in the Drug Pricing Policy 2018 include introduction of a timeframe of 30 days for DRAP to review the increase in drug prices proposed by the manufacturers and reduction in timeline for decisions on hardship cases from 180 to 120 days.

Comprehensive product portfolio & therapeutic areas coverage but product wise concentration in sales is present

Macter is present across 39 therapeutic segments through its 92 products. Current portfolio composition indicates product wise concentration with top 5 products (including Cobolmin, Titan, Co-Amoxi, Salmicort and Maxima) accounting for approximately 45% of the company's revenues. Going forward, brand creation is a key component of the management's strategy. Management launched five new products in FY20 as a part of this strategy and further new products are in pipeline. Creation of new brands may help reduce the product wise concentration in sales. Ability of the firm to compete in its existing product segments and achievement of budgeted growth continue to remain important rating drivers.

Adequate Marketing, Sales and Distribution Network

The company maintains a comprehensive sales network covering ~ 15,000 physicians and 27,000 pharmacies. A separate team of 628 field force (FF) officers caters to specialist doctors to enhance the quantum of prescription business. Moreover, business intelligence tools to facilitate timely decision making are also used to enhance sales. Sales channels include street sales (over the counter and prescription medicines), institutional business (tender), toll manufacturing and export sales; majority of the sales of the company emanate from the street sales segment.

Supply chain disruptions and increase in raw material costs on account of COVID-19 coupled with higher finance costs resulted in lower profitability during FY20; however, with improvement in COVID-19 situation in the country, profitability is expected to recover provided that the impact of second wave of COVID 19 is not significant

During FY20, net sales of the company registered an increase of 35% (FY20: Rs. 5.5b; FY19: Rs. 4.1b). This increase was achieved primarily on account of significant growth in the institutional sales. Street (prescription) segment sales were impacted in the last quarter of FY20 due to the onset of COVID-19 which resulted in closure of out-patient departments in most hospitals and suspension of sales staff visits to doctors and clinics. Resultantly, on an overall basis, street sales increased by only 1.5% in FY20 vis-à-vis the preceding year. However, the company managed to win a large tender from DG Health Punjab, which more than doubled the overall institutional sales in comparison to the preceding year. Consequently, institutional sales formed a larger proportion of overall sales mix in FY20 (FY20: 29.1%; FY19: 12.8%).

Although institutional sales supported the top-line of the company, overall gross margins of the company were reported lower at 36.9% (FY19: 42.5%) as average margins in institutional sales are less than half of those witnessed in case of prescription sales. Moreover, increase in the prices of raw materials and disruption in supply chain of imported active pharmaceutical ingredients due to COVID-19 also contributed to lower gross margins. Gross profit was reported at Rs. 2.0b (FY19: Rs. 1.7b) in FY20. Higher utilization of borrowings due to increased working capital requirements resulted in significant increase in the finance costs. Consequently, both net margins and net profit of the company were reported lower at 0.3% (FY19: 2.6%) and Rs. 14.9m (FY19: Rs. 106.4m), respectively.

The company has posted net sales and net profit of Rs. 1.3b (Q1'FY20: Rs. 1.1b) and Rs. 29.3m (Q1'FY20: Loss of Rs. 52.0m) in Q1'FY21. Profitability metrics are expected to recover on account of cost rationalization initiatives undertaken by the management and further improvement in street sales provided that the impact of second wave of COVID 19 in the country is not significant. Improvement in profitability is considered important from ratings perspective.

Capitalization indicators and liquidity profile depict room for improvement

In FY20, the company incurred capex to the tune of Rs. 154m to conduct upgrades to existing facility. This capex was funded through increase in long term borrowings. Working capital requirements also increased due to maintenance of larger inventories and higher number of days' receivables in case of institutional orders. Higher working capital requirements were funded through increase in both short and long term borrowings. As equity base remained at approximately similar level due to low profits and payment of dividend pertaining to FY19, adjusted gearing and leverage ratios were reported higher at 1.49x (FY19: 1.16x) and 2.39x (FY19: 1.69x). The company has not paid any dividends during FY20. With decrease in profitability, FFO in relation to long term debt and debt service coverage ratio has also declined on timeline basis.

With recovery in profitability, cash flows witnessed improvement in Q1'FY21. Nevertheless, leverage and gearing indicators remained at approximately similar levels. Leverage indicators are on the higher side vis-à-vis peers. In the absence of any significant capex plans in the short to medium term and efforts to reduce the reliance on debt, management is projecting improvement in leverage indicators going forward. Materialization of projected improvement in capitalization and cash flow indicators is considered important from ratings perspective.

Macter International Limited **Appendix I**

FINANCIAL SUMMARY			*(in Rs. millions)*
BALANCE SHEET	**FY18**	**FY19**	**FY20**
Property, plant and equipment	1,182.3	1,232.8	1,332.9
Stock-in-Trade	878.7	773.2	1,038.1
Trade Debts	561.4	580.7	762.6
Cash & Bank Balances	47.0	142.6	129.7
Total Assets	3,044.1	3,210.6	3,957.7
Trade and Other Payables	712.6	625.2	979.5
Adjusted Long Term Debt	607.8	596.0	854.4
Short Term Debt	622.9	790.7	883.5
Adjusted Total Debt	1,230.8	1,386.8	1,737.9
Paid up Capital	391.4	391.4	391.4
Total Equity	1,167.5	1,193.9	1,167.7
INCOME STATEMENT	**FY18**	**FY19**	**FY20**
Net Sales	4,053.2	4,081.8	5,528.1
Gross Profit	1,822.4	1,732.9	2,037.4
Administrative Expenses	198.8	221.9	226.4
Distribution Costs	1,235.4	1,277.7	1,523.1
Profit Before Tax	320.6	122.6	62.5
Profit After Tax	246.3	106.4	14.9
RATIO ANALYSIS	**FY18**	**FY19**	**FY20**
Gross Margin (%)	45.0%	42.5%	36.9%
Net Margin (%)	6.1%	2.6%	0.3%
FFO to Adjusted Total Debt (%)	26.4%	10.9%	6.9%
FFO to Adjusted Long Term Debt (%)	53.4%	25.3%	13.9%
Adjusted Gearing (x)	1.1	1.2	1.5
Adjusted Leverage (x)	1.8	1.9	2.5
Adjusted Debt Servicing Coverage Ratio (x)	1.7	0.8	0.5
Current Ratio	1.2	1.2	1.1
(Stock in trade + trade debts) / Adjusted Short Term borrowings (%)	231.2%	171.2%	203.8%
Return on Average Assets (ROAA) (%)	8.5%	3.4%	0.4%
Return on Average Equity (ROAE) (%)	21.3%	9.0%	1.3%

*Adjusted for commitments for Ijarah rentals in respect of plant & machinery, motor vehicles and equipment

RATING SCALE & DEFINITION 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: 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	Macter International Limited
Sector	Pharmaceutical
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
Rating History	see table below
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.
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Due Diligence Meetings Conducted	see table below

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
15-Jan-21	A	A-2	Stable	Reaffirmed
17-Sep-19	A	A-2	Stable	Downgrade
1-June-18	A	A-1	Stable	Initial

Due Diligence Meetings Conducted

S. No	Name	Designation	Date
1	Syed Khalid Noor	Chief Financial Officer	October 28, 2020