RATING REPORT

Mughal Iron & Steel Industries Limited

REPORT DATE:
December 28, 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-2
Rating Action	Upgrade		Initial	
Sukuk	A+		A+	
ICP-1	A-2		A-2	
Rating Outlook	Stable		Stable	
Rating Date	*December 28, 2021*		*June 30, 2021*	

COMPANY INFORMATION	
Incorporated in 2010	**External auditors:** Fazal Mahmood & Company Chartered Accountants (Independent member firm of Prime Global)
Public Limited Company – Quoted	**Chairman:** Mirza Javed Iqbal **CEO:** Mr. Khurram Javaid
Key Shareholders (with stake 5% or more):	
Mr. Muhammad Mubeen Tariq Mughal – 7.09% Mr. Khurram Javaid – 10.86% Mr. Fahad Javaid – 10.86% Mr. Muhammad Mateen Jamshed – 10.56% Mr. Muhammad Sayyam – 10.56% Mr. Fazeel Bin Tariq – 7.02% Mr. Waleed Bin Tariq – 7.02%	

APPLICABLE METHODOLOGY(IES)

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

Mughal Iron & Steel Industries Limited

RATING RATIONALE

The ratings assigned to Mughal Iron & Steel Industries Limited (MISIL) take into account the company's position amongst major players in the long steel sector of Pakistan. Product portfolio of the company comprises steel rebars, girders, billets, and copper ingot and coils. While steel rebars and girders are the key revenue drivers, trading of copper ingot and coils has also contributed well towards overall top-line growth and margins improvement over the past one and a half years. The assigned ratings take into account extensive experience of sponsoring family in the steel sector and established relations with the customers. The ratings draw comfort from sizeable scale of melting and re-rolling mill capacities, underpinned by installation of new furnaces and completion of balancing, modernization, and replacement (BMR) of bar re-rolling mill which attained commercial operations on June 01, 2021.

Key Rating Drivers:

Company Profile

MISIL was incorporated as a public limited company in February 2010 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The principal business activity of the company is manufacturing and sale of long steel products. During FY20, the company also started trading of non-ferrous metals such as copper ingot and coils, with China being the target market. The manufacturing facility is located at 17-KM Sheikhupura Road, Lahore, while registered office is at 31-A Shadman I, Lahore. Majority shareholding of the company is vested with the sponsoring family who owns 75.3% equity in MISIL. Sponsoring family's shareholding is equally divided among families of three brothers. Mirza Javed Iqbal (elder brother) serves as the chairman of the board of directors while his son, Mr. Khurram Javaid serves, as the CEO. The board comprises 9 members, including 6 family members and 3 independent directors.

Production capacities

MISIL is one of the largest players in long steel sector of Pakistan. Product portfolio of the company is categorized into ferrous and non-ferrous segments. Ferrous segment comprises long-rolled mild steel related products such as steel rebars, billets, and girders whereas non-ferrous segment mainly comprises copper ingot and related items. Within the ferrous segment, the company discontinued production of t-iron during the previous year due to lackluster business opportunities.

MISIL has increased its active melting capacity to 419,100MT per annum (FY20: 339,900MT per annum; FY19: 339,900MT per annum) with the addition of 2 new furnaces during June'21. The company has three more furnaces in the pipeline, out of which 1 furnace became operational in July'21 and remaining two are underway. MISIL previously had re-rolling capacity of 446,000MT per annum, of which 246,000MT per annum was dedicated to rebars and 200,000MT per annum to girders. Upon the completion of balancing, modernization, and replacement (BMR) of bar re-rolling mill in June'21, new dedicated bar-mill of 430,000MT per annum has replaced the aforementioned old bar-mill of 246,000MT per annum which has been leased out to a related party. Resultantly, active bar re-rolling capacity of the company has increased to 630,000MT per annum (FY20: 246,000MT per annum; FY19: 246,000MT per annum) during FY21. Since the new mill commenced commercial operations on June 01, 2021, the full impact of BMR on the top-line of the company is expected to materialize during the ongoing year. In addition, the company has also completed the upgradation of girder re-rolling mill on August 26, 2021, within four months of its initial announcement and capex of Rs. 620m. The company has also increased its copper ingot capacity to 10,000MT per annum (FY20: 3,000MT per annum) during FY21.

The company incurred capex of around Rs. 4.3b on the BMR of re-rolling mill, out which of Rs. 785m was funded through right share issue during FY18 and remaining cost was funded through bridge finance. Subsequently, the company raised new equity of Rs. 2.7b on April 29, 2021 via right share issue and utilized the proceeds to retire long-term loan of Rs. 2.4b and short-term loan of Rs.

OVERVIEW OF THE INSTITUTION

Mughal Iron & Steel Industries Limited (MISIL) was incorporated as a public limited company on February 16, 2010 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The principal business activity of the company is manufacturing and sale of long steel products. The manufacturing facility is located at 17-KM Sheikhupura Road, Lahore, while registered office is located at 31-A Shadman I, Lahore.

Profile of Chairman

Mirza Javed Iqbal is the Chairman of the Board of Directors. Mr. Javed joined the family business in 1976.

Profile of CEO

Mr. Khurram Javaid serves as the CEO MISIL. Mr. Khurram holds an MBA from the Coventry University, UK and a BSc. from the Lahore School of Economics, Pakistan.

Financial Snapshot

Total Equity: end-1QFY22: Rs. 18.2b; end-FY21: Rs. 16.5b; end-FY20: Rs. 8.16b.

Assets: end-1QFY22: Rs. 47.2b; end-FY21: Rs. 41.8b; end-FY20: Rs. 25.6b.

Net Profit: 1QFY22: Rs. 1.7b; Rs. FY21: Rs. 3.4b; FY20: Rs. 593m.

0.3b obtained on bridge financing basis for BMR of re-rolling mill.

Mughal Steel	FY19	FY20	FY21	1QFY22
Capacities - MT				
Melting	339,900	339,900	419,100	429,000
Re-rolling	446,000	446,000	630,000	630,000
Production - MT				
Melting	175,187	224,831	276,982	66,753
Re-rolling	343,407	259,990	307,945	91,959
Utilization - %				
Melting	52%	66%	66%	62%
Re-rolling	77%	46%	49%	58%

Sales and Profitability

MISIL has depicted sizeable growth in revenue and profits over the review period. Net sales of the company increased to Rs. 45.0b (FY20: Rs. 27.3b) during FY21, driven largely by growth in both ferrous and non-ferrous segments. Ferrous segment sales increased to Rs. 34.2b (FY20: Rs. 26.7b), accounting for 77% (FY20: 98%) of total sales during FY21. Growth in ferrous segment was mainly led by increase in rebar volumes to 183,974MT (FY20: 152,368MT) at a higher average selling price of Rs. 105,866/MT (FY20: 96,690/MT) and girder volumes of 123,320MT (FY20: 109,847MT) at a higher average selling price of Rs. 105,516/MT (FY20: Rs. 98,977/MT), due to sizeable investment in construction sector during FY21. Non-ferrous segment sales increased to Rs. 10.5b (FY20: Rs. 539m) during FY21, driven largely by increase in copper ingot exports to 5,800MT (FY20: 450MT) at a higher average selling price of Rs. 1,174,536/MT (FY20: Rs. 879,157/MT) owing to significant surge in international prices led by strong demand from China which accounts for nearly half of global copper consumption. International copper price increased from around USD 6,000/MT in July'20 to USD 9,400/MT in June'21.

Cost of sales increased at a slightly lower pace to Rs. 38.3b (FY20: Rs. 24.7b) during FY21, driven largely by higher production levels and increase in internal scrape prices. The company incurred average steel scrap price of Rs. 72,010/MT (FY20: Rs. 62,042/MT) during FY21. Steel scrape and other metals were the largest cost drivers accounting for 82% (FY20: 77%) of cost of goods sold, followed by fuel & power 13% (FY20: 14%), and salaries & wages 3% (FY20: 3%) during FY21. The company reported higher gross profit of Rs. 6.7b (FY20: Rs. 2.6b) with the improvement in gross margins of both ferrous and non-ferrous segments. Gross margin of ferrous segment improved steadily to 10.9% (FY20: 9.6%) during FY21 as favorable dynamics of construction sector allowed the company to fully pass on the impact of higher steel scrap prices while gross margin of non-ferrous segment increased to 28.1% (FY20: 10.4%) due to increase in international cooper prices supported by strong demand from China. Segment-wise breakdown of gross margins is tabulated below:

	Ferrous Segment			Non-Ferrous Segment		
Rs. Mn	**FY20**	**FY21**	**1QFY22**	**FY20**	**FY21**	**1QFY22**
Net Revenue	26,651	34,230	10,274	539	10,506	3,748
Gross Profit	2,548	3,724	1,439	56	2,950	1,310
Gross Margin	9.6%	10.9%	14.0%	10.4%	28.1%	34.9%

Sales and marketing expenses amounted to Rs. 254m (FY20: Rs. 144m) on account of increase in promotional spending and higher freight & handling costs due to growth in exports during FY21. Administrative expenses were recorded higher at Rs. 538m (FY20: Rs. 407m) due to inflationary adjustments in staff salaries & benefits. Increase in other expenses to Rs. 379m (FY20: Rs. 53m) was mainly led by higher workers' profit participation fund owing to sizeable growth in profits during the year. The company also recognized provision for export regulatory duty amounting to Rs. 54m. Other income amounted to Rs. 67m (FY20: Rs. 59m) which mainly comprised return on bank placements, foreign exchange gain, and rental income from a related party. Despite increased utilization of borrowings, finance cost decreased slightly to Rs. 1.4b (FY20: Rs. 1.5b) on account of lower interest rates during the year. Resultantly, the company reported higher net profit of Rs. 3.4b (FY20: Rs. 593m), translating into net margin of 7.6% (FY20: 2.2%) during FY21.

Net sales of the company increased to Rs. 14.0b (1QFY21: Rs. 7.7b), driven by continued growth in ferrous and non-ferrous segments during 1QFY22. Ferrous segment sales increased to Rs. 10.3b (1QFY21: Rs. 6.8b) as the company sold 48,440MT of rebars at higher average selling price of Rs. 139,404/MT and 24,798MT of girders at higher average selling price of Rs. 140,458/MT during the period. Non-ferrous segment sales also increased to Rs. 3.7b (1QFY21: Rs. 973m) as the company managed to export 1,913MT of copper ingot at a higher average selling price of Rs. 1,496,515/MT during 1QFY22. The company reported higher gross profit of Rs. 2.7b (1QFY21: Rs. 862m) on account of improvement in gross margin of ferrous segment to 14.0% (1QFY21: 6.0%) while gross margin of non-ferrous segment decreased 35% (1QFY21: 47.2%) on account of some correction in international copper price which declined from USD 9,300/MT in July'21 to USD 9,100 in Sept'21. Operating expenses increased to Rs. 366m (1QFY21: Rs. 176m) on account of higher promotional spending and workers' profit participation fund expense during 1QFY22. The company incurred finance cost of Rs. 446m (1QFY21: Rs. 312m) due to higher utilization of borrowings. Accounting for taxation, the company reported higher net profit of Rs. 1.7b (1QFY21: Rs. 352m), translating into net margin of 12.0% (1QFY21: 4.6%).

Liquidity

Liquidity profile of the company is supported by healthy cash flows generation. In line with the increase in profits, the company generated higher funds from operations (FFO) amounting to Rs. 3.9b during FY21 vis-à-vis a net outflow of Rs. 111m in the corresponding period. FFO of the company improved further to Rs. 2.1b during 1QFY22. Healthy cash flows generation underpins repayment capacity of the company, as reflected in the debt service coverage ratio (DSCR) of 1.37x (FY20: 0.68x) despite sizeable long-term debt repayment of Rs. 2.4b. DSCR was stood higher at 4.21x during 1QFY22 and is expected to improve further to 5.35x on account of projected increase in FFO to Rs. 4.8b during FY22. FFO-to-long-term debt and FFO-to-total debt ratios also improved to 1.89x (FY21: 0.83x) and 0.36x (FY21: 0.19x) by end-1QFY22. Current ratio is considered satisfactory and remained largely stable at 1.38x (FY21: 1.37x) at end-1QFY22. Inventory plus receivables to short-term borrowings ratio improved slightly to 1.30x (FY21: 1.25x) as the company has also mobilized long-term Sukuk to meet working capital requirements.

Capitalization

The company's paid-up capital inclusive of share premium stood at Rs. 5.7b at end-1QFY22; the same was increased to Rs. 5.7b (FY20: Rs. 3.0b) during FY21 with the issuance of right shares of Rs. 2.7b in order to finance the BMR of bar re-rolling mill by retiring various long-term and short-term facilities obtained on temporary bridge finance basis. Total liabilities increased to Rs. 29.0b (FY21: Rs. 25.3b) by end-1QFY22, mainly comprising borrowings, payables, and deferred taxation. Trade and other payables increased to Rs. 1.9b (FY21: Rs. 1.7b) and mainly included creditors, advances from customers, utilities payables, and workers' welfare and profit participation funds. Increase in deferred tax to Rs. 2.3b (FY21: Rs. 2.1b) by end-1QFY22 was due to revaluation of fixed assets over the review period. Utilization of short-term borrowings increased in line with the scale of operations and amounted to Rs. 19.5b (FY21: Rs. 16.1b) at end-1QFY22. Short-term borrowings include commercial paper (CP) of Rs. 1.827b for a tenor of 360 days and is due to be redeemed on July 28, 2022.

Outstanding balance of long-term loans decreased to Rs. 4.5b (FY21: Rs. 4.7b) by end-1QFY22 due to principal repayment of Rs. 175m and no new mobilization during the quarter. During FY21, the company mobilized total long-term loans of Rs. 3.6b including Sukuk instrument of Rs. 3.0b for working capital, the SBP's salaries & wages loan of Rs. 136m, and remaining Rs. 450m for capex requirements, and also made principal repayment of Rs. 2.4b. Sukuk has been issued for a period of 5 years including 1-year grace period and is repayable in 16 equal quarterly installments, with last installment due in April 2025. The company has paid 3rd profit installment on due date of December 02, 2021. Gearing and debt leverage ratios remained manageable at 1.62x (FY21: 1.59x) and 1.96x (FY21: 1.93x) at end-1QFY22. Going forward, gearing and leverage indicators are projected to improve steadily to 1.46x and 1.76x, respectively, on account of internal capital generation despite slight increase in total debt to Rs. 24.3b by end-FY22.

Mughal Iron and Steel Industries Limited — Annexure I

FINANCIAL SUMMARY (*amounts in PKR millions*)				
BALANCE SHEET	**FY19**	**FY20**	**FY21**	**1QFY22**
Non-Current Assets	8,628	9,966	15,859	15,927
Stock in Trade	5,620	8,120	14,868	19,592
Trade Debts	3,304	2,182	5,259	5,744
Advances, Deposits & Prepayments	427	335	1,068	389
Due from Govt.	1,460	2,626	2,529	2,701
Cash & Bank Balance	3,202	2,377	2,217	2,809
Total Assets	**22,641**	**25,606**	**41,800**	**47,162**
Trade & Other Payables	496	1,191	1,732	1,932
Short-Term Borrowings	10,002	11,639	16,111	19,523
Long-Term Borrowings *(Inc. current matur)*	3,340	3,461	4,677	4,508
Deferred Tax	721	490	2,051	2,264
Other Liabilities	579	668	724	743
Total Liabilities	15,137	17,449	25,295	28,969
Tier-1 Equity	**7,504**	**8,158**	**13,103**	**14,811**
Paid-up Capital	2,516	2,516	3,402	3,382
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**1QFY22**
Net Revenue	30,828	27,305	44,972	14,023
Gross Profit	3,189	2,617	6,691	2,749
Finance Cost	786	1,515	1,370	446
Profit Before Tax	1,737	554	4,161	2,006
Profit After Tax	1,373	593	3,429	1,688
FFO	2,042	(111)	3,885	2,135
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**1QFY22**
Gross Margin (%)	10.3	9.6	14.9	19.6
Net Margin (%)	4.5	2.2	7.6	12.0
Net Working Capital	2,657	1,631	7,051	8,586
Current Ratio (x)	1.23	1.12	1.37	1.38
FFO to Long-Term Debt (x)	0.61	n.m	0.89	1.89*
FFO to Total Debt (x)	0.16	n.m	0.19	0.36*
Debt Servicing Coverage Ratio (x)	4.61	0.68	1.27	4.21
Gearing (x)	1.78	1.85	1.59	1.62
Debt Leverage (x)	1.91	2.13	1.93	1.96
Inventory Plus Receivables/STD	0.97	0.89	1.25	1.30

* *Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure 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 — Annexure III

Name of Rated Entity	Mughal Iron & Steel Industries Limited
Sector	Steel Industry
Type of Relationship	Solicited
Purpose of Rating	Entity & Instrument Ratings
Rating History	

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
28/12/2021	A+	A-1	Stable	Upgrade
25/09/2020	A	A-2	Stable	Initial
RATING TYPE: Sukuk				
28/12/2021	A+		Stable	Reaffirmed
05/10/2020	A+		Stable	Preliminary
RATING TYPE: ICP-1				
28/12/2021		A-2		Reaffirmed
06/30/2021		A-2		Preliminary

Instrument Structure

MISIL has issued rated, listed, secured and privately placed long-term Sukuk of amount upto Rs. 3b (inclusive of a green shoe option of Rs. 1b). Tenor of the Sukuk will be 5 years including 1-year grace period. The instrument will be redeemed in 16 equal quarterly payments starting from 15th month from the date of issuance. Besides conventional security structure, a debt payment account (DPA) will be maintained with the agent bank which will be build up with one-third of the installment (principal plus profit) each month by the 25th day such that the entire upcoming installment is deposited in the DPA by the 15th day of 3rd month.

MISIL has also issued rated, unlisted, Islamic Commercial Paper (ICP) of amount Rs. 1.827b for meeting working capital requirements. Tenor of the ICP will be 12 months (360 days) and will be redeemed at face value after adjustment of profit/loss.

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.

Disclaimer

Information herein was obtained from sources believed to be accurate and reliable; however, VIS does not guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. For conducting this assignment, analyst did not deem necessary to contact external auditors or creditors given the unqualified nature of audited accounts and diversified creditor profile.

Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Zafar Iqbal	CFO	November 23, 2021
Mr. Fahad Hafeez	Company Secretary	November 23, 2021