RATING REPORT

Master Motor Corporation (Private) Limited

REPORT DATE:
August 30, 2019

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-2	A-	A-2
Rating Outlook	Stable		Stable	
Rating Date	26th August, 2019		6th April 2018	

COMPANY INFORMATION	
Incorporated in 2002	**External auditors:** Kreston Hyder Bhimji & Co.
Private Limited Company	**Chairman of the Board:** Mr. Nadeem Malik
	Chief Executive Officer: Mr. Nadeem Malik

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria Methodology – Industrial Corporates (May 2019)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

Master Motor Corporation (Private) Limited

OVERVIEW OF THE INSTITUTION

Master Motor Corporation (Private) Limited (MMCL) was incorporated as a Public Limited Company in 2002. During 2010, the company's status was converted from being an unquoted public company to a private limited company. Financial Statements of the company for FY18 were audited by Kreston Hyder Bhimji & Co. Chartered Accountants.

Profile of Chairman & CEO:

Mr. Nadeem Malik has an extensive experience in automobile and foam products industry. Mr. Nadeem has been associated with Master Group from past 27 years. He holds a Bachelor's degree in Business Administration from the University of Southern California

RATING RATIONALE

Group Profile

Master Motor Corporation (Private) Limited (MMCL) is part of Master Group of Companies. Amongst others, the group has diversified presence in mattresses & upholstery, home fashion, textile, chemical, power, automobile and auto part sectors.

Master Group of Companies	Year of Incorporation
Master Enterprises (Private) Limited	1963
Procon Engineering (Private) Limited	1988
Master Textile Mills Limited	1992
Master Celeste (Private) Limited	1996
Master Foam (Private) Limited	1998
Master Offisys (Private) Limited	2000
Master Motor Corporation (Private) Limited	2002
Fuso Master Motors (Private) Limited	2013
Master Wind Energy Limited	2015
Master Motors Limited	2018

Product Portfolio

MMCL is involved in the assembly of trucks and buses at Port Qasim, Karachi. The company is ISO9001 certified for both its assembly plant & after sales services & marketing, hence meeting international quality standards. The company's product portfolio is as follows:

Product Portfolio	
Foton M280	Light Duty Trucks
Foton BJ1041	
M-400	
M600	Medium Duty Trucks
MP-600	
MP640 / M-640	
MP-900	Heavy Duty Trucks
Yutong Bus	Luxury Bus

The company sells trucks through both direct sales and 12 dealers across Pakistan. However, buses are sold directly to customers. MMCL has a marketing team of around 70 people overseeing marketing operations of MMCL and Fuso Master Motors (Private) Limited.

Investment and MoUs

MMCL has made investment in a subsidiary company Master Motors Limited (MML). MML is a joint venture between MMCL and Changan Automobile Investment (Shenzhen) Corporation Limited (Changan). MML has a design capacity to assemble/manufacture 10,000 units annually on a single shift basis. The company is still in its testing phase, and plans to build its presence in Light Commercial Vehicle and Passenger Vehicle segments with a formal launch expected in the ongoing calendar year. MMCL also expects to assemble IVECO (Italian Automotive Manufacturing Company) trucks in Pakistan. As per management, test marketing has been successful and the Company would focus on niche prime mover segment.

Production Capacity and Capacity Utilization

Trucks			
	FY17	**FY18**	**FY19**
Design Capacity (units)	4,500	4,500	4,500
Operational Capacity (units)	1,400	2,000	2,000
Actual Production	1,295	1,898	1,313
Capacity Utilization	92.5%	94.9%	65.7%
Buses			
	FY17	**FY18**	**FY19**
Design Capacity (units)	360	360	360
Operational Capacity (units)	160	300	300
Actual Production	139	261	268
Capacity Utilization	87.0%	87.0%	89.3%

MMCL has a design capacity of 4,500 units for trucks and 360 units for buses, respectively. However, operational capacity was lower and is calculated based on workforce employed given demand dynamics. During FY19, capacity utilization for the trucks segment witnessed a noticeable decline compared to preceding year due to slowdown in GDP growth. However, capacity utilization of the buses segment remained on the higher side due to stable demand on account of improved road connectivity and cheaper mode of travel vis-à-vis alternate modes. MMCL production capacity also includes the assembly of trucks and buses for Fuso Master Motors (Private) Limited.

Industry Dynamics[1]

The trucks and buses industry is oligopolistic with few large players dominating the market. Over the past 5 years, sales of trucks and buses by local assemblers' have grown at CAGR of 17.0% and 10.1%, respectively. However, truck sales witnessed a sharp decline of 37.5% compared to preceding year (FY19: 5,828 units; FY18: 9,331 units) during FY19. The decline is attributable to the following reasons:

[1] http://www.pama.org.pk/statistical-information/sales-production/monthly-sales-production

- Economic slowdown and sizeable increase in interest rate.
- Significant hike in truck prices has been witnessed due to rupee devaluation as localization levels are on the lower end.
- A decline of 10% in imports during FY19 vis-à-vis preceding year has reduced demand for trucks due to lower transportation requirements.
- Slowdown in ongoing CPEC project.

During FY19, the bus segment posted a growth of 22.7% compared to preceding year. The reason behind this growth is associated with introduction of new variants by various players and improved road connectivity particularly on highways. Overall local assemblers continue to enjoy an advantage over imports given the 15% duty benefit vis-à-vis imports and 100% cash margin requirements for completely built units. While imposition of axle load restrictions in the recent budget is expected to bode well for truck sales, effective implementation of the same remains to be seen. Going forward, VIS expects industry off-take to remain under pressure given slowdown in GDP growth.

Sales Mix[2]

Sales of the company grew by over 20% in FY19. The increase in net sales was a function of increase in average selling price while company's overall volumes depicted a decline due to dip in truck sales. While truck segment comprises bulk of volumetric sales, the buses segment represents the major portion of revenues given the higher unit prices. Around two third of the sales revenue emanated from Yutong Buses (Luxury buses) where the Company enjoys market leadership. The second largest contributor to revenue included sale of Light Duty Trucks.

Profitability[2]

Gross margin of MMCL depicted a decline vis-à-vis the preceding year. The decline in margins is attributable to increase in input cost due to currency devaluation. Moreover, absence of one-off capital gain from sale of land & building, jump in operating expenses owing to higher employee related cost and increase in finance cost due to higher quantum of borrowing and hike in interest rate has contributed to lower profitability during FY19. Going forward, continued focus on product diversification, focused management of margins and rationalization of expenses through various efficient initiatives is planned to maintain profitability profile given the challenging macroeconomic outlook.

Capitalization and Funding[2]

Equity base (including interest free loan from directors and associates) of the company increased on a timeline basis at end-FY19. Debt profile of the company is entirely short-term in nature. Short term borrowing has witnessed a significant increase due to increasing working capital requirements primarily on account of currency devaluation and also investment in new models. With increase in total debt, gearing ratio of the company trended upwards (FY19: 0.7x, FY18: 0.4x). However, leverage ratio witnessed a decline on account of reduction in trade payables (FY19: 1.5x; FY18: 2.0x).

[2] *FY19 Financial Statements are un-audited*

Liquidity[2]

Funds From Operations (FFO) remained around prior year level in FY19. However with an increase in outstanding debt, cash flow coverage of outstanding total debt has weakened during the outgoing year. Ageing profile of trade debts remains within manageable level. Current ratio is considered satisfactory as it remains above 1.0x (FY19: 1.3x; FY18: 1.1x). With no long-term debt outstanding, debt servicing coverage is satisfactory while stock in trade and trade debt represented 2x the outstanding short-term borrowing at end-FY19.

[2] *FY19 Financial Statements are un-audited*

Financial Summary (amounts in PKR millions)			Appendix I
	FY16	FY17	FY18
BALANCE SHEET			
Fixed Assets	652.0	801.9	789.8
Long term Investment and Deposits	2.2	2.3	554.4
Stock-in-Trade	559.9	1,255.7	2,102.4
Trade Debts	166.4	165.5	468.0
Cash & Bank Balances	12.6	8.6	24.8
Total Assets	1,636.0	2,604.5	4,411.5
Trade and Other Payables	336.8	1,356.3	2,344.9
Long Term Debt (including current maturity)	-	-	-
Short Term Debt	329.2	145.0	557.3
Total Debt	329.2	145.0	557.3
Total Liabilities	712.0	1,539.9	2,940.5
Total Equity	923.9	1,064.6	1,471.0
INCOME STATEMENT			
Net Sales	1,613.9	3,001.9	5,807.6
Gross Profit	241.8	420.7	787.0
Operating Profit	88.1	169.9	825.5
Profit After Tax	45.4	110.5	686.8
RATIO ANALYSIS			
Gross Margin (%)	15.0%	13.9%	13.6%
Net Profit Margin	2.8%	3.7%	11.8%
Net Working Capital	291.1	289.0	158.8
FFO to Total Debt (%)	9.7%	32.4%	43.5%
FFO to Long Term Debt (%)	N/A	N/A	N/A
Debt Servicing Coverage Ratio (x)	2.1	2.9	5.6
ROAA (%)	4.6%	5.3%	19.6%
ROAE (%)	5.9%	11.4%	54.2%
Gearing (x)	0.4	0.1	0.4
Leverage (x)	0.8	1.4	2.0

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: 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	Master Motor Corporation (Pvt) Limited				
Sector	Automobile				
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				
	26-Aug-19	A-	A-2	Stable	Re-affirmed
	06-Apr-18	A-	A-2	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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