RATING REPORT

Master Textile Mills Limited

REPORT DATE:
July 8, 2019

RATING ANALYSTS:
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RATING DETAILS		
	Initial Rating	
Rating Category	Long-term	Short-term
Entity	A	A-1
Rating Date	*April 18, 2019*	
Rating Outlook	Stable	

COMPANY INFORMATION	
Incorporated in 1992	External Auditors: Grant Thornton Anjum Rahman, Chartered Accountants
Public Limited Company (Unquoted)	Chief Executive Officer: Mr. Najeeb Malik
Key Shareholders (More than 10%):	
NM Enterprises (Pvt.) Limited– 27.6%	
Master Polymer Industries Limited – 22.1%	
Mr. Nadeem Malik – 11.2%	
N M Holdings (Pvt.) Limited – 11.2%	
Najeeb Holdings (Pvt.) Limited– 11.2%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Corporates (May 2019)
https://www.vis.com.pk/kc-meth.aspx

OVERVIEW OF THE INSTITUTION

Master Textile Mills Limited was incorporated as a private limited company in 1992. It is a vertically integrated composite unit comprising spinning, weaving, denim, processing and apparel.

Profile of Chief Executive Officer (CEO)

Mr. Najeeb Malik specializes in textile industry and has been successfully running the business for the last 3 decades.

Financial Snapshot

Total Equity: end-HYFY19: 5.3b; end-FY18: Rs. 4.8b; end-FY17: Rs.4.8b; end-FY16: Rs. 4.1b

Assets: end-HYFY19: 15.3b; end-FY18: Rs. 13.3b; end-FY17: Rs. 11.9b; end-FY16: Rs. 10.1b

Profit After Tax: HYFY19: 457; FY18: Rs. 757m; FY17: Rs. 421m; FY16: Rs. 253m

RATING RATIONALE

Rating Rationale

Master Textile Mills Limited (MTML) operates as a family owned business with the shareholding vested among individuals of the sponsoring family and its associated concerns. The assigned ratings take into account MTML's association with the Master Group, having interest in mattress business, textiles, automobile, engineering, chemical and energy sectors. The ratings draw comfort from positive momentum in sales, margins and profitability indicators on a timeline basis and notable experience of senior management in the industry. Moreover, the company is comfortably placed in terms of coverages and liquidity indicators. However, the ratings remain constrained by inherent volatility in the textile sector.

Substantial revenue contributed by exports: The product portfolio largely includes yarn, grey and dyed cloth, denim and garments. Dyed & denim and garments have remained the major revenue driver, contributing around 83% of the total sales collectively.

MTML garment's division is associated with some of the well renowned brands which includes Aeropostal, Arcadia Group, Kiabi, Zara, Guess, Spring Field, Corte field, Road Runner and Tom Tailor. MTML has a highly diversified client concentration with top-10 customers representing 29% of total sales on average during the last three years. Although the company sale is diversified across different regions, sales in Asia and Europe constitute almost 83% of total sales revenue. Local sales constitute around 17% of the total revenue stream. The company has increased its exposure to Asia, whilst the same has been reduced for Europe and local regions. Going forward, the management plans to increase market penetration in Russia to further diversify its regional and customer concentration. The regional breakup of revenue mix is tabulated below:

	FY16 %	FY17 %	FY18 %
Top 10	29	29	29
Local Sales	22	24	17
Asia	36	32	47
Europe	41	43	35
South America	0.03	0.02	0
Middle East	0	0.04	0.12
Australia	0.03	0.02	0
North America	0.98	1.17	4.75
Africa	0	0.02	0.01

Investment in subsidiary and associate: MTML holds 100% shares in the Master Power (Pvt.) Limited (MPL) *(A subsidiary company)*, incorporated on February 4, 2015 under Companies Ordinance, 1984. Principal activity of the company is production and supply of power. MTML has investment amounting to Rs. 250m in its subsidiary. The directors have further injected equity amounting to Rs. 540m during FY18, in the form of unsecured interest free loan to support its operations. MPL has a total power generation capacity of 20MW, out of which 10-12 MW is required for MTML. However, the capex has been made to improve its operational performance. Furthermore, MTML has common directorship with its associate, Master Wind Energy Limited (MWEL), and holds 15% equity stake in the same. Profit after tax of MWEL, as reported in its audited financial statements at the end-

FY18 stood at Rs. 1.1b, meanwhile the top-line was recorded at Rs. 2.8b. In lieu of which, MTML has recorded dividend income from its associated company amounting to Rs. 121m in FY18, thus supplementing its net margins.

Margins supported by a subtle increase in sales along with rationalized increase in cost of sales: Net sales of the company have grown at a CAGR of 9% during the last three business cycles. Increase in sales is mainly attributed to rise in export sales, which stood higher at end-FY18 and contributes around 77% to the total sales. Dyed & denim and garments constitute the highest proportion of total sales mix. The sale revenues augmented by volumetric increase in sales as well as per unit increase in price of garments, however, sale of dyed & denim exhibited an increase in only volume, coupled with a marginal decline in price. Moreover, other major component of sales mix, grey cloth showcased an increase on both price and volume basis, thus contributing to increase in margins. Furthermore, raw material consumed as a proportion of total sales declined due to favorable procurement rates and efficient inventory management. In the backdrop of increasing average benchmark interest rates coupled with higher average short-term borrowings and some additional long-term funding, finance cost of the company increased during FY18. Income from other sources, primarily emanating from foreign currency translation differences amounted to Rs. 68m in FY18 and dividend income from investment in associated company, Master Wind Power (Pvt.) Limited, amounted to Rs. 113m and has provided impetus to the profitability. Subsequently, with rationalized increase in operating and administrative cost, along with increase in sales revenue and other income, MTML reported significant higher net profit during FY18 as compared to preceding year.

Strong liquidity profile as evident from healthy cash flows in relation to outstanding obligations and adequate debt service ability: Liquidity profile of the company has remained sound in view of sizable cash flows in relation to outstanding obligations and sound debt service capacity. Funds from operations exhibited an increasing trend on timeline basis on back of notable increase in profitability. FFO stood higher by the end-FY18. Further, FFO to total debt, though improved marginally, remained weak, owing to significant increase in short term borrowings. However, FFO to long term debt and debt service coverage remained sizeable in FY18, on account of lower reliance on long term debt. Debt service coverage ratio increased to 4.2x in FY18. According to the management, cash flows are expected to improve further on back of augmentation in sales supported by incremental revenue from proposed capex in each segment of the company.

Leveraged capital structure with short term borrowing constituting the major proportion of debt profile: The equity base of the company has steadily strengthened on the back of profit retention. Moreover, Loan from directors was repaid during the year under review. MTML has total available short term credit lines of Rs. 10b out which Rs. 3.1b of availed credit is from State Bank of Pakistan (SBP) refinances and Rs. 1.8b pertains to short term running finance. Total short term borrowings stood higher at Rs. 5.7b, which includes murabaha financing of Rs. 606m. Mark-up on such loans ranges between of SBP rate plus 0.75% to 1% and 3 months KIBOR plus 0.4% to 2%. Resultantly, total debt levels of the company have increased on account of long-term borrowing obtained coupled with higher utilization of short-term credit facilities to meet increased working capital requirements. Given higher short-term borrowings carried on the balance sheet, gearing and leverage indicators have witnessed an increasing trend on a timeline basis.

Financial Summary *(amounts in PKR millions)*

BALANCE SHEET	June 30, 2016	June 30, 2017	June 30, 2018	December 31, 2018
Non-Current Assets	4,761	5,445	5,183	5,102
Stock-in-Trade	2,801	3,735	3,270	5,257
Stores, Spares and Loose Tools	102	92	110	116
Trade Debts	610	706	2,564	2,101
Loans and Advances	646	376	431	770
Tax Refunds Due from Govt.	1,059	1,482	1,617	1,776
Cash & Bank Balances	95	36	64	91
Other Assets	**48**	**43**	**43**	**76**
Total Assets	**10,122**	**11,915**	**13,282**	**15,289**
Trade and Other Payables	1,556	1,517	1,473	2,064
Short Term Borrowings	3,367	4,338	5,716	6,640
Long-Term Borrowings *(Inc. current maturity)*	712	1,229	1,223	1,243
Other Liabilities	37.5	63.4	73.1	87
Tier-1 Equity	**4,419**	**4,768**	**4,798**	**5,255**
Total Equity	4,451	4,768	4,798	5,225

INCOME STATEMENT	June 30, 2016	June 30, 2017	June 30, 2018	December 31, 2018
Net Sales	9,150	10,203	12,610	6,303
Gross Profit	1,112	1,364	1,943	1,245
Operating Profit	532	666	1,065	733
Profit After Tax	253	421	757	457
FFO	448	680	1,193	704

RATIO ANALYSIS	June 30, 2016	June 30, 2017	June 30, 2018	December 31, 2018
Gross Margin (%)	12.6	13.37	15.41	19.75
Net Margin (%)	2.77	4.13	6.0	7.25
Net Working Capital	317	413	692	1,271
Current Ratio (x)	1.06	1.07	1.09	1.14
FFO to Long-Term Debt	0.63	0.55	0.98	1.13*
FFO to Total Debt	0.11	0.12	0.17	0.18*
Debt Servicing Coverage Ratio (x)	1.29	2.80	4.19	-
ROAA (%)	2.64	3.82	6.01	6.4*
ROAE (%)	6.49	9.44	15.83	18.2*
Gearing (x)	0.98	1.17	1.45	1.50
Debt Leverage (x)	1.37	1.50	1.77	1.91
(Stock in trade+ Trade receivable) to Short-term borrowing ratio	1.01	1.02	1.02	1.11

**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	Master Textile Mills Limited
Sector	Textile
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.
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
April 18, 2019	A	A-1	Stable	Initial