RATING REPORT

Master Textile Mills Limited

REPORT DATE:
November 04, 2022

RATING ANALYST:

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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-1
Rating Outlook	Stable		Stable	
Rating Date	*November 04, 2022*		*September 01, 2021*	

COMPANY INFORMATION	
Incorporated in 1992	**External auditors:** M/s Grant Thornton Anjum Rahman
Public Unlisted Company	**CEO:** Mr. Najeeb Malik
Key Shareholders:	
N.M Enterprises – 27.6%	
Master Polymer Industries (Pvt) Ltd – 22.1%	
N.M Holding (Pvt) Ltd – 11.2%	
Najeeb Holding (Pvt) Ltd - 11.2%	
Mr. Nadeem Malik – 11.2%	
Mr. Shahzad Malik – 6.7%	

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

Master Textile Mills Ltd

OVERVIEW OF THE INSTITUTION	RATING RATIONALE

Master Textile Mills Ltd was incorporated in Pakistan in 1992. It is a vertically integrated composite unit comprising spinning, weaving, denim processing and apparel.

Master Textile Mills Ltd. (MTML) is a vertically integrated textile setup engaged in the manufacturing and sale of yarn, griege cloth, dyed fabric, denim fabric and stitched denim & non-denim garments (comprising mainly of bottoms for work-wear). The head office and factory is situated at Manga Mandi, Lahore, Pakistan. MTML is a part of 'Master Group of Industries' which has diversified presence across various business sectors including foam and spring mattresses, engineering, automobiles, chemicals and energy sectors.

<u>Key Rating Drivers</u>

Enhanced Capacities across all segments

Capex during FY22 was incurred to finance expansion across all segments- spinning, garments and dyeing units. The purpose of expansion within spinning and weaving was to eliminate the need to outsource fabric and steer towards complete in-house production of the key inputs. . The expansion is planned to be financed 63% by debt while the remaining (37%) through internal cash generation.

<u>Spinning and Weaving</u> – Total annual installed capacity of the spinning and weaving segments increased to 44,640 spindles and 173 looms, respectively in FY22. The additional 10,800 spindles installed are expected to be operational by November'22. As per management, the looms portfolio now consists of 133 single-sided ones and 40 double-sided looms. Capacity utilization for both yarn and weaving were reported at 95% (FY21: 96%) and 62% (FY21: 73%) during FY22.

<u>Dyeing</u> – The annual installed capacity of dyeing unit increased to 45.6m meters at end-FY22 reflecting an increase of 27% in relation to the prior year. Capacity utilization stood lower at 85% (FY21: 95%) during FY22.

<u>Garments</u> – The stitching plant's production capacity also increased to 11.4m pcs/annum in FY22 from 8.7m pcs/annum in FY21. Capacity utilization was reported lower at 84% (FY21: 94%) during FY22.

Capacity utilization witnessed a downtick across all the segments as actual production did not increase in the same proportion as installed capacity given enhanced capacities coming online in 4Q22. Therefore, the full year impact of the incremental capacity will be visible in FY23.

Business risk profile is supported by industry wide growth in exports over the last year; however, recent floods across the country have adversely affected the cotton crop. Consequently, margins of textile operators may be effected with projected elevated

cotton cost. Comfort may be drawn from higher likelihood of selling prices being adjusted against rising input costs largely through PKR devaluation.

Surge in textile exports has continued in FY22 as COVID-19 related restriction are lifted across the globe. Over the year, businesses in Pakistan earned $19.3b from the export of textile and apparel products, an increase of 21% year-on-year. Category wise, knitwear was the commodity that contributed the most, followed by ready-made garments and bed wear. The margins of textile companies have broadly depicted improvement despite the uptick in raw material costs, given that the same was offset by exchange rate movement.

However, floods in Sindh and Southern Punjab regions during the recent monsoon season have resulted in serious damage to the cotton crop. According to an estimate, around 45% of the crop has been washed bearing a total value of more than $2.5b. Consequently, price of cotton in the country also surged by more than 30%. The Government has communicated its decision to facilitate textile players in importing raw material to overcome the domestic shortfall. Nevertheless, in addition to having an impact on profit margins, higher raw material pricing is expected to increase the working capital requirements for the companies in the sector, which is likely to weigh negatively on the liquidity profile of textile operators.

Going forward, challenges on the global and domestic front will weigh on the business risk profile of textile operators; these include weakening demand dynamics internationally, and external account crisis on the domestic front. These may lead to competitive market pricing to the exporters.

Healthy revenue growth accounted by volumetric surge with shift in US market along with higher selling prices. Going forward, full year impact of enhanced capacities, rupee devaluation and focus towards sale of value-added products is expected to bode well for the topline of the company.

Net Sales revenue of the company posted double-digit growth of 49% in FY22 (FY22: Rs. 25.9b; FY21: Rs. 17.4b; FY20: Rs. 14.4b) with growth being a function of volumetric growth in sales volumes due to shift towards US market and higher average selling prices. MTML has diversified product range comprising yarn, denim fabric, griege cloth and stitched garments. In FY22, garments constituted around 48% of sales followed by dyed fabric at 40%. Export sales comprised ~86% (FY21: 84%) of the total topline of the company during the outgoing year.

Geographic sales mix of exports depicts high concentration in Europe with 45% share in FY22, however as a strategic move sales share emanating from US (FY22: 20%; FY21: 6%) rose to cater enhanced capacities. With Europe sales yielding higher margins and USA sales providing economies of scale due to greater volumetric demand, exports sales mix going forward is expected t be concentrated in these markets. Client wise concentration risk is considered moderate as the top ten overseas clients represented 37% (FY21: 37%) of the gross sales during FY22. Going forward, company aims to enhance focus on Non-Denim Wear which currently constitute 80% of sales mix to absorb value-added margins and reap expertise benefits (work-wear related garments). Going forward, full year impact of enhanced capacities, rupee devaluation and focus towards sale of value-added products is expected to bode well for the topline of the company.

Profitability profile of the company improved on the back of efficient inventory procurement, economies of scale through higher volumetric sales, rise in dollar based selling prices and enhanced focus on high margin value-added products..

Gross Margins of the company have increased on a timeline basis and were reported at 22.8% (FY21: 17.9%; FY20: 18.4) during FY22 attributable to efficient inventory procurement, economies of scale, rise in dollar based selling prices and enhanced focus on high margin value-added products. Distribution costs were reported higher at Rs. 1.6b (FY21: Rs. 0.9b; FY20: Rs. 0.8b) on the back of higher freight charges and greater travelling and conveyance expense; however they remain in conjunction with revenue growth. Finance cost increased to Rs. 512.6m (FY21: Rs. 398.0m; FY20: Rs. 427.9m) due to additional debt drawdown in FY22. Despite escalated finance costs and tax expense, higher net profit of Rs. 3.0b (FY21: Rs. 1.2b FY20: Rs. 0.7b) was achieved during FY22. Profitability of the company is also supported by dividend income from associate company- Master Wind Energy Limited (FY22: Rs. 120.3m; FY21: Rs. 60.5m). Going forward, management foresees net margins to sustain at current levels while growth in absolute profitability will be a function of volumetric increase in sales.

Long Term Investments to contribute to bottom line

MTML has long term investments worth Rs. 1.2b, representing 5% of the total asset base at end-FY22, in subsidiary and associate companies. Master Power Ltd (MPL) is a wholly-owned subsidiary with total coal-based power generation capacity of 20MW, out of which 10-12MW is consumed by MTML for its operations. Whereas associate companies include Master Wind Energy and Master Green Energy having equity ownership of 15% and 11.38%, respectively. MTML also has common directorship with both the associate companies. Master Wind Energy is a 50MW wind power project that commenced operations in Oct'2016 and Master Green Energy is another wind power project that commenced operations in FY22. MTML has recorded dividend income from its equity investments of Rs. 120.3m (FY21: Rs. 60.5m) in FY22. Going forward, growth in dividend income is expected over the next two-three years with the recent initiation of another wind power project.

Liquidity profile of the company is considered strong in light of healthy cash flows and sound debt coverage ratios.

Liquidity profile of the company is considered sound with sufficient cash flows in relation to outstanding debt obligations. In absolute terms, Funds From Operation-FFO amounted significantly higher at Rs. 3.4b (FY21: Rs. 1.62; FY20: Rs. 1.13b) in line with improvement in profitability. However, higher current portion of debt profile resulted in Debt Servicing Coverage (DSCR) being reported lower at 3.47x (FY21: 3.76x; FY20: 2.44x) during FY22. Inventory and Trade Debts provide strong coverage for short-term debt obligations while current ratio has remained above 1x on a timeline basis. Trade debts ageing remains within manageable levels. Liquidity indicators are expected to improve on back of higher projected revenue and further escalation in profitability.

Capitalization indicators are expected to remain at comfortable levels

Equity base of the company has increased on a timeline basis reported at Rs. 10.6b (FY21: Rs. 7.7b; FY20: Rs. 6.5b) at end-June'22 on account of retained earnings. Total debt of the company was reported higher at Rs. 11.9b (FY21: Rs. 8.2b; FY20: Rs. 7.1b) at end-FY22 primarily being a function of higher long term borrowings acquired to fund expansion in capacity. Consequently, leverage and gearing ratios stood higher at 1.38x (FY21: 1.36x; FY20: 1.42x) and 1.12x (FY21: 1.07x; FY20: 1.10x), respectively at end-FY22. Going forward, given no sizeable debt planned (minimal debt is generally incurred every year for routine BMR), capitalization profile is expected to remain sound over the rating horizon.

Master Textile Mills Ltd — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**FY19**	**FY20**	**FY21**	**FY22**
Fixed Assets	4,211.0	4,338.9	4,666.1	8,523.6
Investment in Subsidiary	250.0	250.0	250.0	250.0
Investment in Associates	506.0	1,003.4	986.1	986.1
Stock-in-Trade	4,078.3	4,868.4	5,344.3	7,807.7
Trade Debts	2,384.7	2,346.1	2,901.8	3,179.4
Cash & Bank Balances	110.1	225.0	215.1	112.1
Total Assets	14,019.4	15,740.8	18,043.9	25,350.2
Trade and Other Payables	2,034.1	2,041.8	2,126.5	2,643.5
Long Term Debt (including current maturity)	1,076.0	1,458.2	2,068.6	4,047.5
Short Term Debt	5,099.1	5,674.7	6,103.9	7,870.7
Total Debt	6,175.2	7,132.9	8,172.4	11,918.2
Paid up Capital	316.0	316.0	316.0	316.0
Total Liabilities	8,291.2	9,247.6	10,388.8	14,703.6
Total Equity (Without surplus revaluation)	5,728.2	6,493.2	7,655.1	10,646.6
INCOME STATEMENT	**FY19**	**FY20**	**FY21**	**FY22**
Net Sales	13,830.2	14,386.0	17,362.2	25,856.2
Gross Profit	2,213.2	2,646.7	3,113.5	5,886.1
Profit Before Tax	1,059.3	909.7	1,344.0	3,217.4
Profit After Tax	930.4	765.0	1,162.0	2,991.4
RATIO ANALYSIS	**FY19**	**FY20**	**FY21**	**FY22**
Gross Margin (%)	16.0%	18.4%	17.9%	22.8%
Net Margin	6.7%	5.3%	6.7%	11.6%
FFO	1,334	1,131	1,622	3,379
FFO to Total Debt (%)	21.6%	15.9%	19.9%	28.3%
FFO to Long Term Debt (%)	124.0%	77.6%	78.4%	83.5%
Current Ratio (x)	1.22	1.28	1.36	1.42
(Stock+ Trade Debts)/ Short-term Debt	127%	127%	135%	140%
Debt Servicing Coverage Ratio (x)	2.94	2.44	3.76	3.47
Gearing (x)	1.08	1.10	1.07	1.12
Leverage (x)	1.45	1.42	1.36	1.38
ROAA (%)	6.8%	5.1%	6.9%	13.8%
ROAE (%)	17.7%	12.5%	16.4%	32.7%

ISSUE/ISSUER RATING SCALE &DEFINITIONS Appendix 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	**Appendix III**
Name of Rated Entity	Master Textile Mills Limited
Sector	Textiles
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		
04-Nov-2022	A	A-1	Stable	Reaffirmed
01-Sep-2021	A	A-1	Stable	Maintained
28-Apr-2020	A	A-1	Rating Watch – Developing	Maintained
18-Apr-2019	A	A-1	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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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Masood Ur Rehman	Chief Financial Officer (CFO)	9th September, 2022