

RATING REPORT

Metco Textile (Pvt) Ltd

REPORT DATE:

April 16, 2020

RATING ANALYST:Muhammad Ibad Desmukh
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Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Date	Apr 16, 2020		Feb 8, 2019	
Rating Outlook	Rating Watch-Developing		Stable	

COMPANY INFORMATION

Incorporated in 2008	External auditors: M/s M. Saleem Associates
Private Limited Company	Chairman:
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Asad R. Premjee
Asad R. Premjee - 33.3%	
Miqdad Muhammad - 33.3%	
Bashir Parekh - 33.3%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria *Industrial Corporates (May 2019)*<http://vis.com.pk/kc-meth.aspx>

Metco Textile (Pvt) Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE																											
<p><i>Metco Textile (Private) Limited is a private limited company with equity distributed equally between three directors named (i) Asad R. Premjee (ii) Miqdad Muhammad (iii) Bashir Parekh.</i></p> <p>Profile of CEO: <i>Asad Premjee is associated with the company from 1994 and possesses 16 years of textile management business</i></p>	<p>Assigned ratings of Metco Textile (Private) Limited (MTL) take into account the company’s market position. Principal activity of MTL includes production of yarn to primarily cater to the requirements of the local market. Currently, there are three small-sized entities under the ambit of MTL; they belong to the ship breaking, commodity trading and steel sectors. MTL functions as a family owned business with the shareholding vested among three individuals. Similar to other private limited companies, governance and policy framework of the company depict significant room for improvement.</p> <p>Product line of the company includes yarn for both weaving and knitting segments namely slub, lycra and ring yarn along with spandex. The company operates three units; two units manufacture yarn for cloth and hosiery while the third produces yarn for towel manufacturers.</p> <p>Rating Drivers</p> <p>Cotton Procurement & Sales Procedure</p> <p>Given the lean structure of MTL, all business related decisions including pricing and choice of cotton variety are supervised by the CEO. Various samples from ginnerers are collected and sent to quality assurance lab. Once approved, ginnerers are selected based on domestic and international prices. Simultaneously, the CEO also approves the final selling rate of yarn along with payment terms offered to clients keeping in view prevailing market rates of varying counts and types of yarn.</p> <p>High cyclicity, volatility in cotton prices and competitive intensity in the spinning industry translate to moderate to high business risk profile</p> <p>Non-value added textile exports of Pakistan contracted by 20.6%/19.9% in terms of volume and value during FY19. Global demand of Pakistani yarn has experienced downward pressure, owing to reduced export orders from China in light of the prevailing US-China trade tensions. On the flip side, volume led growth in value added exports enhanced local consumption for yarn resulting in limited export surplus for the same.</p>																											
	<p>Figure 2: Pakistan non value added exports (Source: PBS)</p> <table border="1"> <thead> <tr> <th rowspan="2">(Mn Tons, USD Mn)</th> <th colspan="3">FY18</th> <th colspan="3">FY19</th> </tr> <tr> <th>Volume</th> <th>Value</th> <th>USD/Unit</th> <th>Volume</th> <th>Value</th> <th>USD/Unit</th> </tr> </thead> <tbody> <tr> <td>Raw Cotton</td> <td>35</td> <td>58</td> <td>1.66</td> <td>12</td> <td>20</td> <td>1.67</td> </tr> <tr> <td>Yarn</td> <td>518</td> <td>1,371</td> <td>2.65</td> <td>427</td> <td>1,125</td> <td>2.63</td> </tr> </tbody> </table>	(Mn Tons, USD Mn)	FY18			FY19			Volume	Value	USD/Unit	Volume	Value	USD/Unit	Raw Cotton	35	58	1.66	12	20	1.67	Yarn	518	1,371	2.65	427	1,125	2.63
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	<p>Figure 3: Cultivated Area (Source: USDA)</p> <table border="1"> <thead> <tr> <th>Area Under Cultivation (Mn Hectres)</th> <th>FY18</th> <th>FY19</th> <th>% Change</th> </tr> </thead> <tbody> <tr> <td>World</td> <td>33.7</td> <td>33.5</td> <td>-0.6%</td> </tr> <tr> <td>Pakistan</td> <td>2.7</td> <td>2.3</td> <td>-14.8%</td> </tr> <tr> <td>Production (Mn 480lb Bales)</td> <td></td> <td></td> <td></td> </tr> </tbody> </table>	Area Under Cultivation (Mn Hectres)	FY18	FY19	% Change	World	33.7	33.5	-0.6%	Pakistan	2.7	2.3	-14.8%	Production (Mn 480lb Bales)														
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Cost pressures for the industry are reflective of the global and local cotton production data which shows scaled down cultivation area and production. Reduction in cotton production coupled with an increase in demand from the local value added sector has resulted in an upward trend in the local cotton prices in FY19 and the ongoing year. International cotton prices have trended downwards during the same period despite decrease in production area due to weaker demand from China, which is a major consumer in the world.

Margins and financial performance of players in the spinning segment in Pakistan have depicted volatility due to inherent cyclicity of crop levels and oscillations in cotton prices. VIS expects prices to sustain increasing trend due to decline in cotton production. Waiver of all duties and taxes on imported cotton is expected to provide relief to the market players in the short term. Inherent cyclicity of cotton price and crop levels will continue to drive the performance of players operating in the spinning sector. Historically, margins and financial performance of players have depicted seasonality and the same trend is expected going forward. Business risk is considered to be on the higher side.

Sales & Profitability

Top line of the company has grown on the back of volumetric growth. However, increase in business has largely been a function of prices during the year ended June 2019. However, gross margin of the company has decreased. Volumetric growth in yarn is expected to remain sluggish on account of pressure on the demand side of the sector. Client concentration, in comparison to peers, is relatively lower given the competitive nature of the local industry. Ability to retain these clients over time will need to be monitored

Capitalization & Funding

Paid up capital of the company remained unchanged at end-June 2019. Adjusting for reserves, equity base increased at end-FY19 on account of profit retention. Short term borrowings increased in FY19 but leverage indicators remained manageable. The company finances its working capital requirement through internal cash generation and short term borrowing. Management anticipates no requirement for further borrowings given that there are no capex plans in the near horizon.

Liquidity & Cash Flows

Lower profitability has resulted in weakening cash flow generation. With higher utilization of borrowings, Funds from Operations (FFO) in relation to long-term debt multiples of MTL declined significantly. With no long term obligations on its books, MTL maintains a healthy cushion to repay any future obligations if they arise.

FINANCIAL SUMMARY (all amounts in PKR millions)			
BALANCE SHEET	30-Jun-17	30-Jun-18	30-Jun-19
Paid Up Capital	3.0	3.0	3.0
Total Equity	2,247.6	2,599.5	2,733.6
INCOME STATEMENT			
	30-Jun-17	30-Jun-18	30-Jun-19
Sales Revenue	4,173.3	4,828.6	5,311.9
(Loss)/Profit Before Tax	132.3	406.5	235.4
(Loss)/Profit After Tax	99.2	351.9	181.7
RATIO ANALYSIS			
	30-Jun-17	30-Jun-18	30-Jun-19
FFO	209.0	456.9	289.4
Gearing (x)	0.14	0.04	0.37
Current Ratio (x)	3.0	4.3	2.3

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	Metco Textile (Pvt) Limited				
Sector	Textile				
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				
	04/16/2020	A-	A-2	Rating Watch-Developing	Maintained
	02/08/2019	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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Due Diligence Meetings Conducted	Name		Designation		Date
	1	Mr. Farooq Ismail Bedi	Finance Manager		12-Mar-2020