

RATING REPORT

Matco Foods Limited (MFL)

REPORT DATE:

December 11, 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	Positive		Stable	
Rating Date	December 10, 2019		November 15, 2018	

COMPANY INFORMATION

Incorporated in April 1990	External auditors: Grant Thornton Anjum Rahman Co. Chartered Accountants
Listed Public Limited Company	Chairman of the Board: Mr. Jawed Ali Ghori
Key Shareholders (with stake 5% or more):	Chief Executive Officer: Mr. Khalid Sarfaraz Ghori
Ghori Group – 60.02%	
International Finance Corporation – 15.0%	
General Public (Local)- 14.15%	

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates (May 2016)

<http://vis.com.pk/docs/Corporate-Methodology-201605.pdf>

Matco Foods Limited (MFL)

OVERVIEW OF THE INSTITUTION

RATING RATIONALE

Initially, Matco Foods Limited (MFL) was incorporated under the name of Mohammed Ali Trading Company (Matco) in 1964. However, the company was subsequently converted into a private limited company in 1990 as Matco Rice Processing (Private) Limited. With change in business strategy, the company was renamed to Matco Foods (Private) Limited. In 2017, the company was converted into a public limited company.

Profile of Chairman

Mr. Jawed Ali Ghori has over 40 years of experience pertaining to rice exports business, rice processing and development of rice industries. He also serves as Chairman to the Board of Directors at MFL.

Profile of CEO

With experience of over 30 years in the purchase and processing of rice, Mr. Khalid Ghori utilizes his vast experience in assessing the qualities of agri-products and oversees the procurement and production process. His insights into crop survey and harvest are aimed to help farmers and Matco to achieve procurement targets. Mr. Khalid Ghori graduated from University of Karachi in 1981 and pursued an article ship from ICAP (Institute of Chartered Accountants of Pakistan) Karachi between 1981 and 1984.

Matco Foods Limited ('MFL' or 'the Company') is in the business of processing and export of rice, rice glucose, rice protein and trade of biscuits, pink salt, bran oil, masala and kheer.

Business Update

As of end-FY19, MFL has completed procurement and installation of the Rice Glucose and Rice Protein plant having capacity of 20,000 MT and 2,000 MT respectively. Post completion of the Rice Glucose Project II, collective capacity of rice glucose and rice protein now stands at 30,000 MT and 3,000 MT respectively.

Furthermore, MFL has entered into a joint venture (JV) agreement with Barentz International B.V. (Barentz) to establish a joint venture company in Pakistan. The principal activities of the proposed JV company will be the import, sales and distribution of ingredients used in pharmaceutical, personal care, food and nutrition, and animal nutrition in the life science and food and nutrition sector. These activities are in line with MFL's existing rice glucose and rice protein business. In this regard, Barentz and MFL have paid their respective shares of Rs. 25.5m and Rs. 24.5m.

Industry and Business Risk

- In FY19, Pakistani Basmati rice exports registered 19.22% growth in terms of volumes and 9.87% growth in terms of value mainly attributable to increased share in European market while sharp rupee devaluation also gave some impetus to the value based growth achieved.
- The increased share in the European market is attributable to new pesticide residue regulations in the EU, which have affected Indian exports. It is expected that full compliance with EU pesticide regulations may take up to two crop cycles, subsequent to which the Indian rice will once again gain entry to the EU, thus translating in increased competition for Pakistani exporters over the medium to long term horizon.
- New export market of Saudi Arabia is expected to be added as the kingdom is set to follow the footsteps of EU for implementing pesticide residue regulations. With Indian rice constituting more than three-quarters of the Saudi market, the same presents the local producers with an advantage.
- Pakistan has also got access to the Qatar rice market, which was previously catered by India alone. Most recently, under the Pakistan-China Free Trade Agreement, the quota of Pakistani rice is to be further increased by 0.5m tonnes.

So far, in FY20, the rice exports have grown by 44% and 42% in terms of value and volume respectively. In view of the aforementioned developments, we expect industry growth to remain in double digits over the medium term horizon.

Table 1: Pakistan Rice Exports (TDAP)

Variety	Pakistan (TDAP)					
	Jul-18 to Jun-19		Jul-17 to Jun-18		% Change	
	Qty (MT)	Value "000" \$	Qty (MT)	Value "000" \$	Qty MT	Value "000" \$
Rice (Basmati)	668,763	639,250	560,959	581,847	19.22%	9.87%
Rice (Other)	3,436,220	1,430,366	3,535,487	1,453,744	-2.81%	-1.61%
Total Sales	4,104,983	2,069,616	4,096,446	2,035,591	0.21%	1.67%

Sales and Profitability

In FY19, MFL reported topline revenue of Rs.7.9b, 17% higher than in FY18 (Rs. 6.7b). Exports and local sales breakup has largely remained similar this year as well (Exports: 71.9%; Local: 28.1%). Growth in topline can mainly be attributed to better value terms, owing to the significant rupee devaluation. Besides this, induction of new export and local markets for the Rice Glucose Division (RGD) has also contributed to the overall growth in topline. Sales of RGD grew by 8.3 times, the segment as a proportion of topline grew from 0.9% to 6.4%. Given the expansion of the rice glucose facility, management has envisaged the segment's contribution to the topline to increase beyond 10% within the ongoing year.

Table 2: Sales Breakup

	FY18			FY19		
	Qty (MT)	Rs./MT	Value (Rs. Mn)	Qty (MT)	Rs./Unit	Value (Rs. Mn)
Rice						
Basmati (Exports)	38,716	123,153	4,768	40,135	135,966	5,457
Basmati (Local)	5,158	131,059	676	6,482	131,287	851
Irri (Export)	2,920	54,795	160	2,284	72,680	166
Total	46,794	119,759	5,604	48,901	132,390	6,474
Rice Glucose/Protein						
Rice Protein	328	79,268	26	1,216	98,684	120
Rice Glucose (Export)	91	109,890	10	810	133,333	108
Rice Glucose (Local)	401	64,838	26	4,924	58,692	289
Total	820	75,610	62	6,950	74,388	517
Other Items						
Export (NPD)	N/A	N/A	3.9	N/A	N/A	9.1
Local (NPD)	N/A	N/A	16.0	N/A	N/A	20.7
By- Product	30,898	38,805	1,199	31,213	33,223	1,037
Total	30,898	39,453	1,219	31,213	34,179	1,066
Total Sales	78,512	87,694	6,885	87,064	92,551	8,057

Gross margins (Adjusted for exchange gains) have relatively remained stable during the year vis-à-vis preceding year (FY19: 13.3%; FY18: 13.7%) while higher employee related costs have slightly compressed operating margins of the company (FY19: 6.4%; FY18: 7.6%). Despite adverse interest rate movement, MFL's cost of debt posted a marginal uptick, which is mainly attributable to MFL's debt profile, of which 65% pertains to subsidized financing facilities under Export Refinance Scheme (ERF) and Long Term Financing Facility (LTFF). Given a one off gain on sale of the building property (Rs. 73.3m) MFL's bottom line profitability for FY19 was higher by 34%.

Going forward, as the added sales from the high margin rice glucose division materialize, we expect business margins to improve, while volumetric growth will depend on the company's ability to capturing the market space created by the pesticide residue regulations.

Liquidity

Liquidity profile draws support from more than sufficient coverage of short term borrowings by way of inventory and receivables and healthy cash flow generation. Following the realization of a major tax benefit (granted on listing at the PSX and undertaking capital expenditure), which kept the tax charge lower in preceding year, the effective tax charge normalized in FY19, thereby compressing the FFO by 10% vis-à-vis prior year (FY19: Rs. 350m; FY18: Rs. 390m). Following the dip in FFO, debt servicing ability slightly declined with DSCR recorded at 1.71x (FY18: 1.84x) With borrowings primarily short term in nature (91%) against a sizeable amount of inventory, the company's ability to retire debt in a timely manner is considered adequate

Capitalization

Equity base (excluding surplus on revaluation of assets) has grown by 13.4% by virtue of high profit retention (FY19: 79%; FY18: 86%; FY17: 87%) and issuance of bonus shares during the year. Resultantly leverage and gearing indicators have also improved to 1.25x and 1.12x in FY19 (FY18: 1.37x; 1.24x). There are no plans of further long term leveraging; however given the additional procurement required for rice glucose production, short term financing requirements are expected to rise. Overall, the gearing and leverage indicators are projected to drop below 1.1x and 1.2x respectively.

Corporate Governance

Board composition is line with best practices. Board of Directors comprises 9 members including 4 independent directors, 2 non-executive director and 3 executive directors. The board also consists of 2 female directors (Non-executive and Independent director) which further reaffirms sound governance framework.

Matco Foods Limited
Appendix I

FINANCIAL SUMMARY			
	<i>(amounts in PKR millions)</i>		
	30-Jun-17	30-Jun-18	30-Jun-19
<u>BALANCE SHEET</u>			
Non-Current Assets	2,175.9	2,212.7	2,744.6
Stock-in-Trade	5,240.5	5,139.0	5,204.9
Trade Debts	541.5	674.5	941.1
Short Term Loans & Advances	58.2	83.7	355.3
Cash & Bank Balances	111.1	823.1	78.4
Total Assets	8,235.2	9,048.4	9,574.9
Trade and Other Payables	332.6	225.9	248.1
Short Term Borrowings	3,886.8	4,081.8	4,139.2
Long Term Debt (Inc Current Maturity)	444.7	372.1	409.8
Total Interest Bearing Debt	4,331.5	4,453.9	4,549.0
Total Liabilities	5,092.0	4,919.7	5,068.0
Paid Up Capital	874.3	1,165.7	1,224.0
Total Equity (Exc Revaluation Surplus)	2,571.5	3,581.9	4,061.8
<u>INCOME STATEMENT</u>	30-Jun-17	30-Jun-18	30-Jun-19
Net Sales	6,134.4	6,722.7	7,863.1
Cost of Sales	5,169.1	5,862.0	6,948.5
Gross Profit	965.4	860.7	914.0
Distribution Expenses	291.9	153.5	167.1
Administrative Expenses	175.2	198.1	240.3
Other Income	36.6	17.8	106.7
Finance Cost	211.9	239.7	275.5
Profit before Tax	342.0	337.8	460.5
Taxation	73.1	29.5	46.7
Profit After Tax	269.0	308.3	413.8
<u>RATIO ANALYSIS</u>	30-Jun-17	30-Jun-18	30-Jun-19
Gross Margin (%)	15.7%	12.8%	11.6%
PBT Margin (%)	5.6%	5.02%	5.86%
Net Margin (%)	4.4%	4.59%	5.26%
Current Ratio (x)	1.32	1.52	1.48
Working Capital Cycle	353.3	340.1	298.0
Gearing (x)	1.68	1.24	1.12
Debt Leverage (x)	1.98	1.37	1.25
FFO	416.1	390.3	349.8
FFO to Total Debt (%)	10%	8.8%	7.7%
Debt Servicing Coverage Ratio (x)	2.27	1.84	1.71
ROAA (%)	3.6%	3.57%	4.44%
ROAE (%)	11.08%	10.02%	10.83%

ISSUE/ISSUER RATING SCALE & DEFINITIONS

Appendix II

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	Matco Foods Limited				
Sector	Food				
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				
	10-Dec-19	A-	A-2	Positive	Maintained
	15-Nov-18	A-	A-2	Stable	Reaffirmed
	01-Jan-18	A-	A-2	Stable	Reaffirmed
	4-Apr-17	A-	A-2	Stable	Reaffirmed
	28-Dec-15	A-	A-2	Stable	Reaffirmed
	29-Dec-14	A-	A-2	Stable	Reaffirmed
	15-Jun-12	A-	A-2	Stable	Reaffirmed
	12-Jun-12	A-	A-2	Stable	Upgrade
	27-May-11	BBB+	A-3	Stable	Upgrade
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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