RATING REPORT

Mughal Iron & Steel Industries Limited

REPORT DATE:
September 25, 2020

RATING ANALYSTS:
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RATING DETAILS		
Rating Category	**Initial Rating**	
	Long-term	**Short-term**
Entity	A	A-2
Rating Outlook	Stable	
Rating Action	Initial	
Rating Date	*September 25, '20*	

COMPANY INFORMATION

Incorporated in 2010	External auditors: Fazal Mahmood & Company Chartered Accountants (Independent member firm of Prime Global)
Public Limited Company – Quoted	Chairman: Mirza Javed Iqbal CEO: Mr. Khurram Javaid
Key Shareholders (with stake 5% or more):	
Mr. Muhammad Mubeen Tariq Mughal – 13.56% Mr. Khurram Javaid – 10.84% Mr. Fahad Javaid – 10.84% Mr. Muhammad Mateen Jamshed – 10.55% Mr. Muhammad Sayyam – 10.55% Mr. Fazeel Bin Tariq – 7.01%	

APPLICABLE METHODOLOGY(IES)

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

Mughal Iron & Steel Industries Limited

OVERVIEW OF THE INSTITUTION

Mughal Iron & Steel Industries Limited (MISIL) was incorporated as a public limited company on February 16, 2010 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The principal business activity of the company is manufacturing and sale of long steel products. The manufacturing facility is located at 17-KM Sheikhupura Road, while head office is located at 31-A Shadman I, Lahore.

Profile of Chairman

Mirza Javed Iqbal is the Chairman of the Board of Directors. Mr. Javed joined the family business in 1976.

Profile of CEO

Mr. Khurram Javaid serves as the CEO MISIL. Mr. Khurram holds an MBA from the Coventry University, UK and a BSc. from the Lahore School of Economics, Pakistan.

Financial Snapshot

Total Equity: end-9MFY20: Rs. 8.2b; end-FY19: Rs. 7.5b; end-FY18: Rs. 7.5b.

Assets: end-9MFY20: Rs. 22.8b; end-FY19: Rs. 22.6b; end-FY18: Rs. 17.5b.

Net Profit: 9MFY20: Rs. 400m; Rs. FY19: Rs. 1.4b; FY18: Rs. 1.3b.

RATING RATIONALE

Company Profile

Mughal Iron & Steel Industries Limited (MISIL) was incorporated as a public limited company in February 2010 under the repealed Companies Ordinance, 1984 (now the Companies Act, 2017). The principal business activity of the company is manufacturing and sale of long steel products. The manufacturing facility is located at 17-KM Sheikhupura Road, while head office is located at 31-A Shadman I, Lahore.

Majority of the shareholding of the company is vested with the sponsoring family who owns 76.3% equity in MISIL. Sponsoring family's shareholding is equally divided among families of three brothers. Mirza Javed Iqbal (elder brother) serves as the chairman of the BoD while his son, Mr. Khurram Javaid serves, as the CEO. The BoD comprises 9 members, including 6 family members and 3 are independent directors.

Product Mix

MISIL is considered one of the major players in long steel sector of Pakistan. Product portfolio of the company principally comprises steel rebars, girders and t-iron. Steel rebars cater to both housing sector in urban areas and large infrastructure projects, while girders and t-iron are mainly used in the housing sector market in rural areas. Steel rebars and girders are the key revenue generating products, contributing 47% and 35%, respectively, towards overall volumetric sales in FY19. Billets accounted for 10% of volumes. Product-wise volume sales and average selling price are tabulated below;

	FY18		FY19		9MFY20	
	QTY - Tons	Price/Ton	QTY – Tons	Price/Ton	QTY - Tons	Price/Ton
MS Billet	2,615	71,700	29,184	82,344	7,783	79,325
Steel rebars	162,313	73,494	146,018	90,042	124,091	96,475
Girders	83,360	78,219	119,990	79,074	81,498	98,434
t-iron	-		3,428	75,720	4,578	84,798

Production Capacities

Production processes include melting and re-rolling. The company currently operates 7 induction furnaces including 1 new 12 mw furnace. Active melting capacity of the company currently stands at 342,900MT per annum. There is plan to add 4 new furnaces to further enhance melting capacity, going forward.

Re-rolling capacity currently stands at 446,000MT per annum, of which 200,000MT per annum is dedicated to girders/t-iron and remaining 246,000MT per annum is rebar capacity. MISIL embarked on the balancing, modernization and replacement (BMR) project of re-rolling mill in FY18. Completion of the project was impacted by the outbreak of COVID-19; however, cold testing is in progress and commercial operations are expected in 4Q2020. Upon completion of the BMR project, new dedicated bar-mill of 430,000MT per annum will replace the aforementioned old bar-mill of 246,000MT per annum. Resultantly, active re-rolling capacity of the company will increase to 630,000MT per annum. Capacity and utilization of the company is tabulated below;

MT/PA	2015	2016	2017	2018	2019	9MFY20
Capacities - MT						
Melting	72,250	155,719	340,688	340,700	339,900	339,900
Re-rolling	229,688	326,563	446,224	446,000	446,000	446,000
Production - MT						
Melting	59,557	99,657	116,207	211,934	175,187	178,396
Re-rolling	180,230	245,675	241,773	251,590	343,407	205,735
Utilization - %						
Melting	82%	64%	34%	62%	52%	52%
Re-rolling	78%	75%	54%	56%	77%	46%

The company has incurred capex of around Rs. 4.3b on BMR of rolling-mill project, out of which Rs. 3.3b has been funded through syndicated long-term debt, Rs. 758m through right issue and remaining Rs. 242m through internal capital generation. Going forward, the company has no major capex plan. The company intends to issue Sukuk of Rs. 3.0b in FY21 primarily to manage projected elevated working capital requirements, going forward.

Asset Mix

Asset base of the company stood at Rs. 22.8b (FY19: Rs. 22.6b; FY18: Rs. 17.5b) at end-9MFY20. Increase in property, plant and machinery on a timeline basis to Rs. 9.3b (FY19: Rs. 8.6b; FY18: Rs. 6.3b) was mainly due to capex on in-house gas-fired power plant and BMR of existing re-rolling mill. Stock in trade stood higher at Rs. 7.8b (FY19: Rs. 5.6b; FY18: Rs. 5.9b) mainly on account of replenishment of raw material amounting Rs. 5.1b (FY19: Rs. 3.0b; FY18: Rs. 5.1b), partially offset by some decrease in finished goods inventory to Rs. 1.2b (FY19: Rs. 1.6b; FY18: Rs. 239m). Higher stores, spare and loose tools inventory of Rs. 1.5b (FY19: Rs. 969m; FY18: Rs. 597m) was due to BMR project.

Trade debts amounted to Rs. 2.1b (FY19: Rs. 3.3b; FY18: Rs. 1.3b). The company allows a credit of up to 15 days to its trustworthy customers while credit terms for development projects varies from client to client. Due from govt. against sales tax, advance income tax and export regulatory duty stood at Rs. 2.4b (FY19: Rs. 1.5b; FY18: Rs. 2.3b) at end-9MFY20; it is expected to decline over the next three years owing to expiry of tax credits. Cash and bank balance decreased to Rs. 611m (FY19: Rs. 3.2b; FY18: Rs. 1.3b) owing to increase liquidity requirements.

Sales and Profitability

Net revenue was reported at Rs. 21.3b (FY19: Rs. 30.8b; FY18: Rs. 22.2b) as the company managed to sell 124,091MT of steel rebars, 81,498MT of girders and 4,578MT of t-iron with higher selling prices during 9MFY20. Gross profit amounted to Rs. 2.0b (FY19: Rs. 3.2b; FY18: Rs. 2.8b) though margins decreased to 9.3% (FY19: 10.3%; FY18: 12.6%) as the company couldn't pass the full impact of higher raw material prices onto consumer due to change in tax regime. However, the recent uptrend in rebar prices along with the completion of BMR of existing re-rolling mill is expected to bode well for the margins to some extent due to energy and overheads efficiencies.

Operational expenses were curtailed at Rs. 440m (FY19: Rs. 692m; FY18: Rs. 673m) as the impact of increase in administrative expenses was more than offset by cut-back in selling & marketing and other expenses. However, financial charges increased significantly to Rs. 1.3b (FY19: Rs. 786m; FY18: Rs. 552m) due to increase in average borrowings and higher interest rates during the period. Going forward, financial charges are projected to remain largely stable as the higher utilization of debt financing would offset the impact of lower interest rates. Accounting for taxation, the company reported net profit of Rs. 400m (FY19: Rs. 1.4b; FY18: Rs. 1.3b) with lower margin of

1.9% (FY19: 4.5%; FY18: 5.8%) during 9MFY20.

Liquidity and Capitalization

Liquidity position of the company was under stress owing to significant decline in cash flows generation mainly as a result of higher finance cost and taxes paid. There was net outflow of funds from operations (FFO) amounting to Rs. 117m during 9MFY20 vis-à-vis positive FFO of Rs. 2.0b (FY18: Rs. 1.4b) during FY19. Resultantly, the debt service coverage ratio stood lower at 0.90x (FY19: 4.6x; FY18: 3.7x) during 9MFY20. FFO generation is expected to improve in FY21 beyond on account of higher projected profits along with a major tax benefit. However, coverages are projected to remain on the lower side (slightly above the minimum threshold of 1.0x) over the next three years as major debt repayments would fall in that period. Current ratio also decreased to 1.18x (FY19: 1.23x; FY18: 1.32x) by end-9MFY20 as the impact of largely stable current liabilities was more than offset by reduction in trade debts and cash balance. Inventory plus trade debts to short-term borrowings ratio stood at 1.08x (FY19: 0.97x; FY18: 0.95x). Going forward, current ratio is projected to remain above the minimum threshold of 1.0x.

Paid-up capital was unchanged at Rs. 2.5b at end-9MFY20. Equity base of the company stood at Rs. 8.2b (FY19: Rs. 7.5b; FY18: Rs. 7.5b) at end-9MFY20, including contribution from directors and their relatives. Debt profile of the company comprises a mix of short-term and long-term financing facilities. Working capital requirements are met through short-term borrowings which amounted to Rs. 9.4b (FY19: Rs. 10b; FY18: Rs. 7.8b) at end-9MFY20. Outstanding balance of long-term debt decreased slightly to Rs. 3.2b (FY19: Rs. 3.3b; FY18: Rs. 829m) on account of scheduled repayments. Resultantly, gearing and debt leverage stood 1.54x (FY19: 1.78x; FY18: 1.16x) and 1.75x (FY19: 1.91x; FY18: 1.30x). With the issuance of Sukuk instrument of Rs. 3.0 and higher short-term borrowings for working capital requirements, leverage indicators are projected to increase in FY21 and decrease subsequently.

Mughal Iron and Steel Industries Limited — Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**FY18**	**FY19**	**9MFY20**
Non-Current Assets	6,344	8,628	9,357
Stock in Trade	5,917	5,620	7,788
Trade Debts	1,263	3,304	2,087
Advances, Deposits & Prepayments	401	427	502
Due from Govt.	2,298	1,460	2,445
Cash & Bank Balance	1,251	3,202	611
Total Assets	**17,475**	**22,641**	**22,789**
Trade & Other Payables	463	496	782
Short-Term Borrowings	7,840	10,002	9,405
Long-Term Borrowings *(Inc. current matur)*	829	3,340	3,222
Deferred Tax	601	721	501
Other Liabilities	274	579	674
Total Liabilities	9,708	14,307	14,338
Tier-1 & Total Equity	**7,466**	**7,504**	**8,206**
Paid-up Capital	2,516	2,516	2,516
INCOME STATEMENT	**FY18**	**FY19**	**9MFY20**
Net Revenue	22,226	30,828	21,297
Gross Profit	2,794	3,189	1,988
Profit Before Tax	1,604	1,737	328
Profit After Tax	1,290	1,373	400
FFO	1,396	2,042	(117)
RATIO ANALYSIS	**FY18**	**FY19**	**9MFY20**
Gross Margin (%)	12.6	10.3	9.3
Net Margin (%)	5.8	4.5	1.9
Net Working Capital	2,722	2,657	2,064
Current Ratio (x)	1.32	1.23	1.18
FFO to Long-Term Debt (x)	1.68	0.61	n.m
FFO to Total Debt (x)	0.17	0.16	n.m
Debt Servicing Coverage Ratio (x)	3.48	4.61	0.69
Gearing (x)	1.16	1.78	1.54
Debt Leverage (x)	1.30	1.91	1.75

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	Mughal Iron & Steel Industries Limited
Sector	Steel Industry
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
25/10/2020	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
Mr. Zafar Iqbal	CFO	August 17, 2020
Mr. Fahad Hafeez	Company Secretary	August 17, 2020