The Pakistan Credit Rating Agency Limited

Rating Report

Mughal Iron & Steel Industries Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
21-Oct-2022	A+	A1	Stable	Maintain	-
22-Oct-2021	A+	A1	Stable	Upgrade	-
23-Oct-2020	A	A2	Stable	Upgrade	-
24-Sep-2020	A-	A2	Positive	Maintain	-
24-Sep-2019	A-	A2	Positive	Maintain	-
25-Mar-2019	A-	A2	Positive	Maintain	-
18-Dec-2018	A-	A2	Positive	Maintain	-
27-Jan-2018	A-	A2	Positive	Initial	-

Rating Rationale and Key Rating Drivers

Mughal is a known name in the steel industry. The Company's business profile has sustained and improving, over the last few years. Governance framework is strengthened by presence of independent oversight on board. The Company has a diversified product slate as its operating both in ferrous & non-ferrous segments. The ferrous segment comprises Billets, Rebars & Girders while the non-ferrous segment comprises Copper ingots mainly. Furthermore, the establishment of strong brands like 'Mughal Supreme' gives a competitive edge to the Company. The ratings incorporate the essence of material advancement that Mughal has achieved in terms of further diversity in revenue streams. The highlighted achievement through geographical diversification in the revenue stream led to a significant contribution from exports of Copper Ingots to China (i-e; ~21% of revenue contribution) which not only contributed to the top line but also brought sustained profit stream, going forward. Mughal has attained a formidable market share by establishing the brand and earning trust with regard to quality. The company is currently working on automation of its non-ferrous plant which is expected to come online by end of current year and also plans to commence exports of Aluminium ingots. With regard to expansion of ferrous segment, the company enhanced its melting and grid load capacity and also carried out BMR of re-rolling mill. The reported profitability for Jun-22 showed significant growth from previous years primarily due to increase in sales prices as volumes in ferrous segment declined slightly. Margins witnessed slight decline as the impact of increase in raw material prices and other input costs was not completely transferred into sale prices.

The ratings are dependent upon the company's ability to sustain its healthy business profile amidst strong competition, herein, effective and prudent management of financial risk indicators remain important. Moreover, upholding of governance framework is vital.

Disclosure	
Name of Rated Entity	Mughal Iron & Steel Industries Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-22),Methodology | Correlation Between Long-term & Short-term Rating Scales(Jun-22),Methodology | Rating Modifiers(Jun-22)
Related Research	Sector Study | Steel(Sep-22)
Rating Analysts	Uswa Sikandar | uswa.sikandar@pacra.com | +92-42-35869504

Profile

Legal Structure Mughal Iron & Steel Industries Ltd. is a listed Company since March 2015. Its shares are traded on Pakistan Stock Exchange Limited (PSX). The Company's shares are quoted under the Engineering Sector.

Background Incepted in the early 1950s in the form of a proprietorship firm, the company was incorporated in 2010. The company operates through its registered head office located in Lahore while the factory is located at 17 KM's Sheikhupura Road with sales centers located at Badami Bagh Lahore. Its products are used in the housing sector in both rural and urban and hi-tech industrial complexes and infrastructural projects.

Operations Mughal Iron & Steel Industries Limited (Mughal) is primarily engaged in the manufacturing and sale of billets, girders, and rebars and has also recently diversified into non-ferrous segment through exports of copper.

Ownership

Ownership Structure Mughal's ownership structure has changed post listing. Presently, the company is majority (~76%) owned by Mughal family, followed by Financial Institutions, and general public.

Stability The ownership structure of the Company is seen as stable as no ownership changes are expected in near future. The majority stake will rest with Mughal family.

Business Acumen The sponsors – the Mughal family – carry over five decades of experience in steel and allied business.

Financial Strength The sponsors have demonstrated their commitment towards the company by injecting funds on as and when required basis. Given that Mughal is the flagship entity of sponsors, willingness to support the company in case need arises is considered high.

Governance

Board Structure The overall control of the Company vests in the nine members' board of directors, wherein six are from sponsoring family including the Chairman and the CEO, while three are independent members.

Members' Profile Mughal's Board Members carry requisite skills, competence, diversified knowledge background, and experiences, which is considered positive.

Board Effectiveness Two board committees in place, include (i) Audit, and (ii) Human Resource & Remuneration. Furthermore, presence of independent directors and good attendance in board meetings reflect on good governance framework of the company.

Financial Transparency M/s Fazal Mahmood & Company, Chartered Accountants, classified in category 'C' by SBP in 2017 and having a QCR rating, are the external auditors of the company. They have expressed an unqualified opinion for the Financial statements of end-Jun22. M/s Fazal Mahmood & Company is a member of prime global.

Management

Organizational Structure Mughal has a streamlined organizational structure with clearly demarcated roles and a high degree of delegation. The reporting lines are segregated between two executive directors and CEO which in turn report to the BoD. The current structure results in strong decision-making and brings operational efficiencies.

Management Team Mr. Khurram Javaid (CEO) has been instrumental in improving the overall HR quality of the company. He is supported by a team of experienced individuals equipped with the necessary technical skills and relevant industry experience.

Effectiveness Mughal has no formal management committees in place. All departments have their own meetings and their heads review key performance areas of the department and report to respective executive directors.

MIS MIS reports are customized as per the requirements of the management on a daily, weekly, and monthly basis. Some of the reports generated include re-ordering sheets, financial facilities status, etc.

Control Environment The Company has an ERP system deployed which is currently being used for reporting purposes.

Business Risk

Industry Dynamics Pakistan Steel Sector is largely fragmented with over ~170 player registered with The Pakistan Steel Re-Rolling Mills Association. Key players in the industry are, however, less than 20 in number, yet account for over ~40-50 production capacity of the sector. Out of these, 12 players are listed on the PSX. Domestic steel industry has undergone through recent expansion phase. According to the PSX data of listed companies in the long steel sector, the net margins of the steel sector shrunk during the last five years, and leading players declared losses during FY 2019-2020. The steel sector came out of crisis during the years 2020-21 and 2021-22 for a brief span of time. However, the steel sector has once again landed into crisis after the drastic increase in interest rates during the first half of FY 2022 by the SBP, high scrap prices in international markets and increase in energy cost, rupee depreciation, slash in PSDP and dip in demand due to havoc created by recent floods tragedy.

Relative Position Mughal is a known name in the steel industry. The company has diversity in its product slate and its profiling has significantly improved post listing on PSX. The expansion projects related to 'Additional power and melting capacity' and 'Replacement of Re-Rolling Bar Mill' have enabled Mughal to further strengthen its market positioning.

Revenues During FY22, topline witnessed a growth of ~47% on YoY basis and recorded at PKR 66.153 billion (FY21: PKR 45bln; FY20: PKR 27.3bln) primarily due to increase in selling price and sales volume. The sale of Copper Ingots & Scrap contributed heavily towards the reported volumetric growth. Gross Profit has also reported significant growth in line to the growth in sales (FY22: PKR 10.13bln; FY21: PKR 6.7bln; FY20: PKR 2.6bln). During the period under consideration, finance cost reported increase over the previous quarters owing to increased policy rates and short-term borrowings (FY22: PKR 2.54bln; FY21: PKR 1.3bln; FY20: PKR 1.3bln). Net profit for FY22 has increased to PKR 5.4bln (FY21: PKR 3.4bln; FY20: PKR 0.593bln).

Margins During FY22, Mughal's gross and operating margins witnessed growth as per reported figures (Gross: FY22: 15.3%; FY21: 14.9%; FY20: 9.6%), (Operating: FY22: 13.9%; FY21: 13.1%; FY20: 7.6%). Mughal's improved margins are affected from the diversified product slate, increased sales volumes and prices, and effective cost management.

Sustainability The company has been taking many steps to lead ferrous as well as non- ferrous segments. In respect of ferrous segment, it has recently expanded its melting and grid load capacity and has also carried out BMR of re-rolling mill. As a part of diversification strategy and to increase global footprints, it has also announced expansion in non-ferrous segment in order to increase copper exports and to commence exports of Aluminium ingots .

Financial Risk

Working Capital During FY22, Mughal's working capital requirements, represented by net cash cycle (net working capital days) increased to 119days (end-Jun 21: 106days; end-Jun20: 106days). This is due to slight increase in inventory days to 94 (Inventory days: FY21: 81days; FY19: 76days), primarily due to increase in sales and prices. The company manages its working capital requirements through mix of internal generation and short-term borrowings. As at end-Jun22, STB have increased significantly to PKR 20.6 billion (FY21: PKR 16 billion; FY20: PKR 11.6 billion) while FCFO's were recorded at PKR 8.7 billion (FY21: PKR 5.6 billion; FY20: PKR 1.4 billion). Due to increase in short term borrowings, the company's liquidity profile has dipped with current ratio recorded at 11.0 x in FY22 (FY21: 13.0x; FY20: 10.1x).

Coverages During FY22, on account of higher YoY profitability, FCFO increased to PKR 8.73 billion (FY21: PKR 5.6 billion; FY20: PKR 1.4 billion). Due to upwelling in debt levels and increased key policy rates, finance cost increased to PKR 2.54 billion (FY21: PKR 1.3 billion; FY20: PKR 1.3 billion). Resultantly dip has been witnessed in Interest coverage ratio which was recorded at 3.4x in FY22 (FY21: 4.2x; FY20: 1x).

Capitalization Mughal's D/E ratio stood at ~55.5% end-Jun22 (end-Jun21: ~56%, end-Jun20: 65%). The overall debt of the company has been witnessing an increasing trend on account of ongoing expansions and supplementary cushion for the shortcomings of working capital, due to which short-term borrowing contributed a significant portion to the total debt (STB: end-Jun22: 79.4%; end-Jun21: 77%). However, comfort can be drawn from strong equity base of PKR 20.8 billion driven by healthy profits (FY21: PKR 16.5 billion; FY20: PKR 8.2 billion).

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ıcial Summary
PKR mln

Mughal Iron & Steel Industries Limited	Jun-22	Jun-21	Jun-20	Jun-19
Steel	12M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	16,533	15,859	9,966	8,628
2 Investments	-	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	36,553	25,941	15,640	14,013
a Inventories	*21,043*	*13,181*	*6,732*	*4,651*
b Trade Receivables	*5,574*	*5,259*	*2,182*	*3,304*
5 Total Assets	53,085	41,800	25,606	22,641
6 Current Liabilities	3,314	1,992	1,553	823
a Trade Payables	*1,357*	*455*	*684*	*379*
7 Borrowings	25,941	20,809	15,045	12,511
8 Related Party Exposure	25	-	55	830
9 Non-Current Liabilities	2,959	2,494	795	973
10 Net Assets	20,847	16,505	8,158	7,504
11 Shareholders' Equity	20,847	16,505	8,158	7,504
B INCOME STATEMENT				
1 Sales	66,153	44,972	27,305	30,828
a Cost of Good Sold	*(56,025)*	*(38,280)*	*(24,688)*	*(27,639)*
2 Gross Profit	10,128	6,691	2,617	3,189
a Operating Expenses	(951)	(792)	(551)	(568)
3 Operating Profit	9,177	5,899	2,067	2,621
a Non Operating Income or (Expense)	*(353)*	*(367)*	*(169)*	*(100)*
4 Profit or (Loss) before Interest and Tax	8,824	5,532	1,897	2,521
a Total Finance Cost	*(2,622)*	*(1,370)*	*(1,344)*	*(783)*
b Taxation	*(791)*	*(732)*	*39*	*(364)*
6 Net Income Or (Loss)	5,411	3,429	593	1,373
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*8,726*	*5,564*	*1,370*	*2,567*
b Net Cash from Operating Activities before Working Capital Changes	*6,233*	*3,885*	*(111)*	*2,000*
c Changes in Working Capital	*(6,247)*	*(9,982)*	*(1,050)*	*(989)*
1 Net Cash provided by Operating Activities	(15)	(6,097)	(1,161)	1,011
2 Net Cash (Used in) or Available From Investing Activities	(1,171)	(1,263)	(1,470)	(2,424)
3 Net Cash (Used in) or Available From Financing Activities	4,126	7,235	1,908	3,363
4 Net Cash generated or (Used) during the period	2,941	(125)	(722)	1,951
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	47.1%	64.7%	-11.4%	38.7%
b Gross Profit Margin	15.3%	14.9%	9.6%	10.3%
c Net Profit Margin	8.2%	7.6%	2.2%	4.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	3.7%	-9.8%	1.2%	5.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh*	29.0%	27.8%	7.6%	18.3%
2 Working Capital Management				
a Gross Working Capital (Average Days)	124	111	113	97
b Net Working Capital (Average Days)	119	106	106	95
c Current Ratio (Current Assets / Current Liabilities)	11.0	13.0	10.1	17.0
3 Coverages				
a EBITDA / Finance Cost	3.8	4.6	1.8	3.7
b FCFO / Finance Cost+CMLTB+Excess STB	2.3	2.6	0.6	2.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	0.9	1.1	88.7	2.3
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	55.5%	55.8%	64.9%	64.0%
b Interest or Markup Payable (Days)	54.5	69.1	0.0	0.0
c Entity Average Borrowing Rate	10.1%	7.0%	9.4%	7.3%

Credit Rating

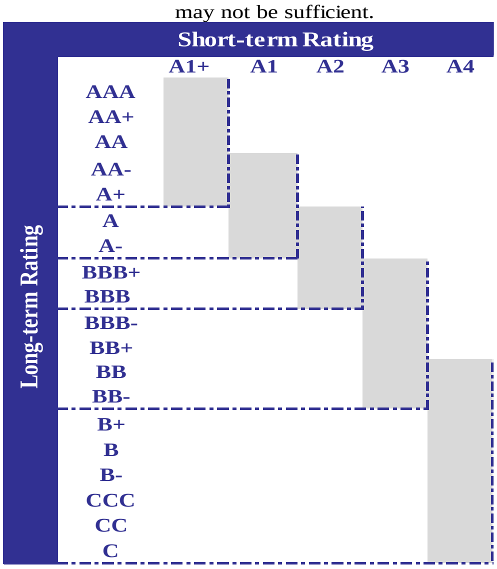
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
AA+ AA AA-	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ A A-	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ BBB BBB-	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances and in economic conditions are more likely to impair this capacity.
BB+ BB BB-	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ B B-	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business and economic environment.
CCC CC C	**Very high credit risk.** Substantial credit risk "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short-term Rating

Scale	Definition
A1+	The highest capacity for timely repayment.
A1	A strong capacity for timely repayment.
A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

Outlook (Stable, Positive, Negative, Developing) Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business/financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

Suspension It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities
a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

Rating Team Statements

(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**

i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)

ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)

iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term “family members” shall include only those family members who are dependent on the analyst and members of the rating committee

Restrictions

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)

(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)

(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business

(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)

(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report | Clause 11-(A)(p).

(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)

(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)

(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)

(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

Independence & Conflict of interest

(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity

(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers’ associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)

(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)

(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)

(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst’s area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)

(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review

(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)

(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)

(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)

(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)

Probability of Default

(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)

Proprietary Information