The Pakistan Credit Rating Agency Limited

Rating Report

Masood Spinning Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
07-Apr-2021	BBB+	A2	Stable	Maintain	YES
12-May-2020	BBB+	A2	Stable	Initial	YES

Rating Rationale and Key Rating Drivers

Masood Spinning Mills Limited (‘Masood Spinning’ or ‘The Company’) is a public unlisted limited company. The Company is part of Mahmood Group, one of the leading textile conglomerates in the country. The Company is engaged in manufacturing 30 -40 count yarn (coarse yarn) and fine count yarn. The rating reflects a steady revenue base in recent years. The topline primarily consists of exports. The Company's margins have improved lately though remained below par when compared with peers. The financial risk matrix remains adequate with high leveraging and coverages. Merger improvement witnessed in 1HFY21 with an increase in coverage and healthy working capital. Organic growth in the equity base is positive. Going forward, the planned CAPEX is expected to bring in efficiency gains and improve margins.

The Company's association with Mahmood Group and vast experience of sponsors remain important rating factors. The ratings are dependent upon the management’s ability to improve margins, profitability, and financial profile of the Company. This includes keeping the debt levels manageable and improve the Company’s competitive position in the industry. Sponsor’s support and business acumen remain important for the ratings.

Disclosure

Name of Rated Entity	Masood Spinning Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Ratings(Jun-20),Methodology | Correlation Between Long-Term And Short-Term Rating Scale(Jun-20),Criteria | Rating Modifier(Jun-20)
Related Research	Sector Study | Spinning(Sep-20)
Rating Analysts	Sehar Fatima | sehar.fatima@pacra.com | +92-42-35869504

Profile

Legal Structure Masood Spinning Mills Limited ('Masood Spinning' or 'The Company') is a public unlisted limited concern. The Company has been operating since June 2000.

Background The Company is a part of Mahmood Group which started operations in 1935 and has since evolved into a diversified business empire. Masood Spinning Mills Limited was incorporated in 2000.

Operations The Company has three production units. Unit 1 and Unit 2 are located in Kabirwala in Khanewal district near the Company's head office in Multan. Unit 3 is located in Phool Nagar in Kasur district. All three units have a collective capacity of 82,272 spindles. The Company's total electricity requirement stands at 14.6 M.W which is met through captive generation. Additionally, the Company also has a backup line from LESCO and MEPCO to meet unforeseen energy needs.

Ownership

Ownership Structure Masood Spinning is 100% owned by Mehmood Group directly, through individuals and associated companies. Ownership is equally divided between four sons of Khawaja M. Masood (Late).

Stability The group has a clearly defined shareholding among four brothers. Clarity among brothers with regards to operations of the group companies bodes well with stability of the Group and Masood Spinning. However, documentation of the succession plans would bring further clarity to the stability of ownership.

Business Acumen All four brothers are equipped with well-rounded experience in the textile industry. Each has over forty years of experience in running the businesses of the group. The third generation of sponsors is already actively involved in running the operations of different group companies and possesses relevant knowledge and capabilities.

Financial Strength Mahmood Group maintains a strong financial profile with an equity base of PKR 21bln at end-Jun20, as well as, well-diversified businesses through its multiple group companies. The Company ratings comfort from sponsors' ability and willingness to support it, in case the need arises.

Governance

Board Structure Oversight of the Company lies with an eight-member board, which includes both the Chairman and the CEO.

Members' Profile Mr. Khawaja Muhammad Iqbal – a Chairman, has over four decades of textile experience. He has held key positions in various local corporate bodies of Pakistan. Other directors' expertise in various stages of textile value-chain leads to a good skill mix overall board.

Board Effectiveness Board meetings have full attendance of directors, boding well for the board's effectiveness. Meanwhile, minutes are recorded properly, although, there is still some room for improvement. There are two sub-committees in place: Audit Committee and Human Resource Committee.

Financial Transparency Deloitte Yousuf Adil Chartered Accountants are the external auditors of the Company. The auditor is listed in Category "A" of the State Bank's panel of auditors. They have expressed an unqualified opinion on the financial statements of the company for the year ended June 30th, 2020.

Management

Organizational Structure The Company essentially operates in two distinct divisions before delegating strategic decisions to one overseeing body. At this highest level, departments are as follows: (i) Audit, (ii) Taxation, (iii) HR and Admin, (iv) IT and ERP, (v) Export and Import, (vi) Purchase & Production, (vii) Corporate affairs, (viii) Marketing and (ix) Finance.

Management Team The Company CEO – Mr. Khawaja M. Younus – has over four decades of experience in the textile sector. He also sits on the board of various group companies. Mr. Younus is supported by a team of seasoned professionals. Mr. Anees s/o Mr. Khawaja Muhammad Younus and Mr. Meher s/o Mr. Khawaja Muhammad Ilyas look after day to day operations of Kabirwala (unit 1 & 2) and Phool Nagar (unit 3) facilities respectively.

Effectiveness Division of duties among the management is clearly defined. While there are no formal management committees, the Company maintains adequate IT infrastructure and related controls for smooth running of operations.

MIS Masood Spinning Mills Limited implemented an Oracle based ERP solution – Oracle EBS – in 2008 with multiple operational modules.

Control Environment The Company is following latest quality assurance standards for production and trade of yarn. On an operational level, samples of cotton and yarn are tested for quality under laboratories of each unit.

Business Risk

Industry Dynamics Textile Sector has depicted an overall growth of approximately 8% (USD value terms) in the exports in first six months of the fiscal year 2021 where knitwear, bed wear and towels segments recorded highest growth of 16.5%, 16.3% and 17.4% respectively. Knitwear, readymade garments, bed wear and cotton cloth segment combined have achieved almost 9% growth over the same period last year excluding cotton cloth which has experienced a decline. Towel and made-up articles both recorded growth of 17% each. In Pak Ruppee terms, the overall growth by textile exports has been recorded at around 13%. Covid-19 pandemic and related lock down imposed by the governments around the globe in FY20 had its ramifications however Pakistani textile exports have been seen rebounding in 1HFY21. Excluding knit wear and yarn, all other segments recorded incline in prices (USD terms) which is positive. The export outlook is likely to remain stable in the medium term as textile units have been operating at optimized capacity levels.

Relative Position Overall, Mahmood Group has a strong presence in the country's textile sector, while Masood Spinning Mills Limited with 82,272 spindles is also adequately positioned. Going Forward, the Company is planning to start a CAPEX, which will add 14,592 Spindles to existing capacity.

Revenues The Company manufactures and sells a wide range of yarn. During FY20, Masood Spinning's topline down by 7% to PKR 13,759mln (FY19: PKR 14,853mln) mainly because of lockdown in the last quarter of FY20. In FY20, exports of the Company stood at PKR 11,183mln (FY19: PKR 10,966mln), exports made up 81% (FY19: 74%) of total sales. In 1HFY21, the Company recorded a revenue of PKR 8,306mln (1HFY20: PKR 7,735mln), an increase of 7% period on period. During this period, exports constituted 27% of total sales at PKR 2,215mln.

Margins During FY20, the Company's gross margin decreased to 6.2% (FY19: 7.3%) on back of lower revenue led by the impact of lockdown due to Covid-19. Operating profit margin also decreased to 3.8% (FY18: 5.3%) due to higher operating expenses year-on-year, as the Company increased its selling and marketing expenses by 14% (FY20: PKR 162mln, FY19: PKR 142mln). Margins witnessed improvement in 1HFY21. Gross profit margin increased to 8.3% and operating profit margin to 6.0%, in line with increase in revenue fueled by better yarn prices, both locally and internationally.

Sustainability The Company will invest PKR 400mln in a number of projects such as; Solar System, AC Plant, and up-gradation of existing machinery during FY21. CAPEX will be incurred on the current spindle capacity; 14,592 spindles will be added and the cost incurred on this project is PKR 1.4bln. The Company also has planned to invest PKR 500mln in FY22 and PKR 420mln in FY23 to further upgrade the existing three production units.

Financial Risk

Working Capital During FY20, the Company's net working capital cycle days increased to 144days (FY19: 119days) because of increase in inventory days (FY20 109days; FY19: 96days). Short term trade leverage during FY20, improved to -7% (FY19: -24%) due to some increase in net trade assets and decrease in short term borrowings. Net working cycle decreased to 129days in 1HFY21.

Coverages During FY20, Masood Spinning's free cash flows (FCFO) down by ~46% to PKR 726mln (FY19: PKR 1,357mln) due to the loss. Due to the decrease in FCFO, the Company's interest coverage ratio also decreased to 0.8x (FY19: 1.6x) and debt coverage ratio 0.7x (FY19: 1.1x); also attributable to higher finance cost. FCFO in 1HFY20 increased to PKR 618mln (1HFY19: PKR 421mln) and the interest coverage ratio also witnessed improvement at 1.8x while the debt coverage ratio declined to 1.5x.

Capitalization At end-Jun20, the Company had a highly leveraged capital structure with a leveraging ratio of 78% (FY19: 75%). Leveraging ratio increased year-on-year as the Company's borrowings increased to PKR 9,142mln (FY19: PKR 8,257mln) mainly due to rise in long term borrowings. Majority portion of debt comprised short-term borrowings (78%) from various commercial banks. Leveraging ratio almost remained stagnant at ~78% in 1HFY21.

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Financial Summary
PKR mln

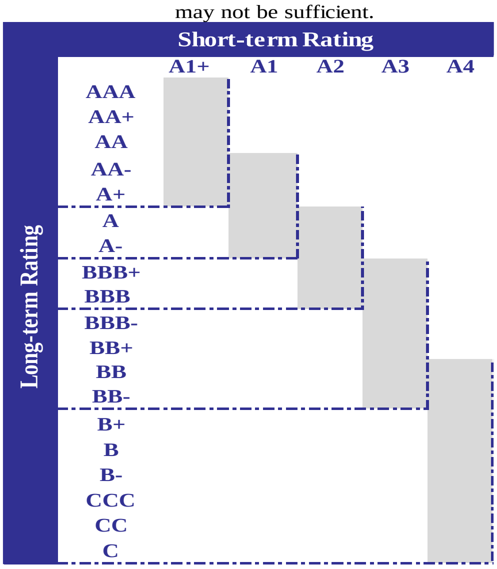
Masood Spinning Mills Limited	Dec-20	Jun-20	Jun-19	Jun-18
Textile	6M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	3,956	3,694	3,982	3,490
2 Investments	1,151	1,120	1,424	2,068
3 Related Party Exposure	303	303	283	190
4 Current Assets	7,527	7,203	5,981	5,756
a Inventories	*3,958*	*4,025*	*4,172*	*3,614*
b Trade Receivables	*1,681*	*2,113*	*828*	*1,312*
5 Total Assets	12,936	12,320	11,671	11,504
6 Current Liabilities	706	659	612	481
a Trade Payables	*156*	*125*	*129*	*80*
7 Borrowings	9,596	9,142	8,257	8,704
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	3	3	-	-
10 Net Assets	2,631	2,516	2,801	2,320
11 Shareholders' Equity	2,631	2,516	2,801	2,320
B INCOME STATEMENT				
1 Sales	8,306	13,759	14,853	11,867
a Cost of Good Sold	*(7,619)*	*(12,910)*	*(13,770)*	*(11,104)*
2 Gross Profit	688	848	1,083	763
a Operating Expenses	(192)	(328)	(295)	(302)
3 Operating Profit	496	520	788	461
a Non Operating Income or (Expense)	*54*	*256*	*114*	*221*
4 Profit or (Loss) before Interest and Tax	549	776	902	681
a Total Finance Cost	*(351)*	*(926)*	*(877)*	*(574)*
b Taxation	*(84)*	*(129)*	*136*	*(51)*
6 Net Income Or (Loss)	115	(280)	161	57
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*618*	*726*	*1,357*	*948*
b Net Cash from Operating Activities before Working Capital Changes	*280*	*(218)*	*536*	*389*
c Changes in Working Capital	*(348)*	*(1,115)*	*(232)*	*(702)*
1 Net Cash provided by Operating Activities	(68)	(1,333)	304	(313)
2 Net Cash (Used in) or Available From Investing Activities	(397)	473	146	(853)
3 Net Cash (Used in) or Available From Financing Activities	454	894	(446)	1,178
4 Net Cash generated or (Used) during the period	(11)	33	4	12
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	20.7%	-7.4%	25.2%	29.3%
b Gross Profit Margin	8.3%	6.2%	7.3%	6.4%
c Net Profit Margin	1.4%	-2.0%	1.1%	0.5%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	3.2%	-2.8%	7.6%	2.1%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareholders' Equity)]*	8.9%	-11.4%	5.8%	2.6%
2 Working Capital Management				
a Gross Working Capital (Average Days)	129	148	122	156
b Net Working Capital (Average Days)	126	144	119	153
c Current Ratio (Current Assets / Current Liabilities)	10.7	10.9	9.8	12.0
3 Coverages				
a EBITDA / Finance Cost	1.9	1.0	1.7	2.0
b FCFO / Finance Cost+CMLTB+Excess STB	1.5	0.7	1.1	1.1
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	4.8	-14.5	3.5	4.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	78.5%	78.4%	74.7%	79.0%
b Interest or Markup Payable (Days)	96.0	67.2	78.8	85.3
c Entity Average Borrowing Rate	7.4%	10.8%	9.8%	6.4%

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.

(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