



The Pakistan Credit Rating Agency Limited

Rating Report

MACPAC Films Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
08-Apr-2019	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan's packaging industry drives demand mainly from country's food sector, posting a growth of 10-15%. Packaging industry use variants of Polymer Resin to manufacture BOPET, BOPP and CPP films. During FY18, the packing film industry generated revenue around PKR 20bln. Major players in the packaging industry includes: Tri-Pack Films Limited, Macpac Films Limited, International Packaging Limited and Astro Films - Ismail Industries Limited.

The industry primarily operates in three segments: Biaxially Oriented Polyethylene (BOPET) Films, Biaxially Oriented Polypropylene (BOPP) Films and Cast Polypropylene (CPP) Films. All these segments are experiencing volumetric growth. Whereas, CPP film segment enjoys better margins by providing high sealability features. In the last few years, the food packaging companies have kept a high focus on better shelf life for their packaged products creating a strong demand for CPP films in market.

The ratings reflect Macpac Films established position in the packaging film (BOPP and CPP) industry. The Company has experienced a rising top-line owing to significant demand growth of packaging material. However, increasing competition, rising raw material prices and currency devaluation has led to an overall decline in the Company's margins. This is expected to improve, going forward, as CPP production increases. The Company has moderate leveraging and relatively weak coverages. The working capital requirements are expected to rationalize on the back of higher sales, going forward, from its current levels. The Company has strong governance framework.

The ratings are dependent on the management's ability to strengthen the relative positioning of the Company in the industry. Improvement in business margins and, in turn, profitability remains imperative. Any deterioration in the Company's coverages or sustained would have negative impact on the ratings.

Disclosure

Name of Rated Entity	MACPAC Films Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Packaging(Oct-18)
Rating Analysts	Adnan Dilawar adnan@pacra.com +92-42-35869504

Profile

Legal Structure Macpac Film Ltd. was incorporated as a Public Limited Company in 1993. The Company is listed on the Pakistan Stock Exchange.

Background Macpac Films started commercial production of Biaxially Oriented Polypropylene (BOPP) films in 1995 and began commercial production of Cast Polypropylene (CPP) films in 2003. In 2007, the Company had to halt the CPP films production due to a fire incident. In 2015, Metalizer plant for BOPP films became commercially operational. In 2017, the Company re-installed its CPP films manufacturing line; which became commercially operational in Feb-19.

Operations Macpac Films produces multiple grades of BOPP films variants at an installed capacity of 15,000 MT per annum. The Company's diverse portfolio also includes multi layered CPP films variants, manufactured at an installed capacity of 6,996 MT per annum. These films have applications in confectionery: biscuits, cookies, snacks, tea and baked products packaging. To minimized wastage, the Company opted to install Bruckner and SML manufacturing plants. Macpac Films production facility is located at Port Qasim, Karachi and the registered office is situated at Tipu Sultan Road, Karachi.

Ownership

Ownership Structure Macpac Films is primarily owned by Elahi family (51%), with major ownership residing with Mr. Maqbool Elahi (47%). Munshi family owns 15% stake in the Company. Employees Old Age Benefit holds 8% shares. The Company has a free float of 27%.

Stability Ownership of the business is seen as stable as the major ownership vests with Elahi family. The second generation has been inducted in the business.

Business Acumen Mr. Maqbool Elahi Sheikh introduced BOPP and CPP films in Pakistan and is considered a pioneer. The sponsors have been associated with the plastic packaging industry since 1983, after setting up Toyo Packaging (Pvt.) Limited.

Financial Strength Macpac Films is a stable business entity. The sponsoring family has made several investments in other sectors. The Company's sister concern, Toyo Packaging (Pvt.) Limited had a turnover of PKR 1.5bln in FY18.

Governance

Board Structure Macpac Films BoD comprises of four Non-Executive Directors, two Executive Directors and one Independent Director. The Company's second Independent Director recently resigned and will be appointed within 90 days. Elahi family has prominent presence on the Board. Following the Code of Corporate Governance, the Company has an apt Board size ensuring independent oversight.

Members' Profile The BoD members have diversified and relevant expertise. Board's Chairman, Mr. Naeem Munshi has been associated with the Company since inception. He holds the office of CEO at Hilal Foods (Pvt.) Limited and is a Board member of Hilal Care (Pvt.) Limited and Unique Food Service Co. (Pvt.) Limited.

Board Effectiveness The Board met five times during FY18, with majority attendance to discuss pertinent matters. Minutes of the BoD meetings were well documented. The Board has formed Audit Committee and Human Resource and Remuneration Committee. Each Committee comprises three members and met at least once every quarter during the year with majority attendance.

Financial Transparency Macpac Film external auditors, M/s EY Ford Rhodes, have expressed an unqualified opinion on the financial reports for FY18. The firm is QCR rated by ICAP and is in the A Category of SBP's panel of auditors.

Management

Organizational Structure Macpac Films operates through six divisions; Plant, Sales and Marketing, Finance, Internal Audit, Human Resource and Information Technology. All Divisional Heads report to the Company's CEO, who reports to the Board. However, Head of Internal Audit and Human Resource reports administratively to the CEO and functionally to the Board Audit Committee and Human Resource and Remuneration Committee, respectively.

Management Team Macpac Film has professional management. Mr. Maqbool Elahi Sheikh, the founder of Macpac Films, has been working as CEO since inception. His overall work experience is above 50 years. Having an overall work experience of above 2 decades, Mr. Najam ul Hassan has been associated with the Company from past 2 years as the Chief Operating Officer.

Effectiveness Keeping in view the size and operations of the Company, improvement in operations can be achieved by establishing functional committees.

MIS Macpac Films manufacturing plant is in Port Qasim and Head Office are all connected through an ERP system. To facilitate the management, various reports are generated on daily and monthly basis. However, frequency of these reports may alter as per the managements requirement.

Control Environment The Company's internal audit function provides support, guidance and monitoring of the internally placed SOPs along with conducting Gap Analysis for evaluating already placed policies and procedures.

Business Risk

Industry Dynamics Pakistan's packaging industry drives demand mainly from country's food sector, posting a growth of 10-15%. Packaging industry use variants of Polymer Resin to manufacture BOPET, BOPP and CPP films. During FY18, the packing film industry generated revenue around PKR 20bln. Major players in the packaging industry includes: Tri-Pack Films Limited, Macpac Films Limited, International Packaging Limited and Astro Films - Ismail Industries Limited.

Relative Position Macpac Films holds a moderate market share of 11% in BOPP and CPP films segment.

Revenues The Company generates revenue by selling variants of BOPP films in the local market only. Direct sales are made to B2B customer with top ten customers generating 50% of the total sales. On geographical basis, revenue is concentrated in the South region of the country (56% of total sales). In FY18, the Company's topline showed a volumetric growth (40%) and clocked in at PKR 2.1bln (FY17: PKR 1.5bln). The Company was able to reap a revenue of PKR 1.1bln in 6MFY19. The impact of CPP film line on the Company's revenue will be visible in 3rd and 4th quarter of FY19.

Margins Macpac Films generates revenue from a relatively thin margin segment, BOPP films. Intense competition in the market keep the prices competitive. This along with difficulty in passing on the increased average import prices of raw materials deteriorated the Company's margins (gross: 6MFY19: 2.6%, FY18: 11%, FY17: 17% and operational: 6MFY19: -2.7%, FY18: 5.6%, FY17: 11%), resulting in losses in 6MFY19.

Sustainability Going forward, Macpac Film's CPP plant will increase the Company's overall production capacity by over 40%. Growth is anticipated in the demand of packaged milk in the unorganized markets, by 2020. The Company has an annual CAPEX requirement of PKR 70mln to maintain its operations in FY19.

Financial Risk

Working Capital In FY18, Macpac Films posted a stable net cash cycle of 80 days (FY17: 80 days), supported by significant improvement in the Company's inventory days (FY18: 80 days, FY17: 109 days). Stability was also witnessed in the Company's receivable days (FY18: 55 days, FY17: 57 days) due to increased production to cater the growing demand. The Company imports Resin payment upto 90 days. In 6MFY19, significant increase was witnessed in the receivable days (6MFY19: 63 days) leading to an increase in the Company's net cash cycle to 86 days. To improve the short term borrowing buffer, the Company intends to follow strict discipline in its working capital management.

Coverages During FY18, Macpac Films had modest coverages, indicated its ability to timely pay off the liabilities adequately. In 6MFY19, negative free cash flow of PKR 60mln stressed the financial profile of the Company. This significantly deteriorated the coverage ratio (6MFY19: -3x). The Company's core and total debt service cover dropped to less than 1 (6MFY19: -1x, FY18: 1x, FY17: 3x).

Capitalization Macpac Films has a moderately leveraged capital structure on the back of equity injection in FY18 (6MFY19: 46%, FY18: 12% and FY17: 34%). The leveraging increased in 6MFY19 on the back of higher borrowings. The Company intends to rationalize its borrowings, going forward, with no plans of further capacity expansion in near term.



Macpac Films Limited

Listed Public Limited

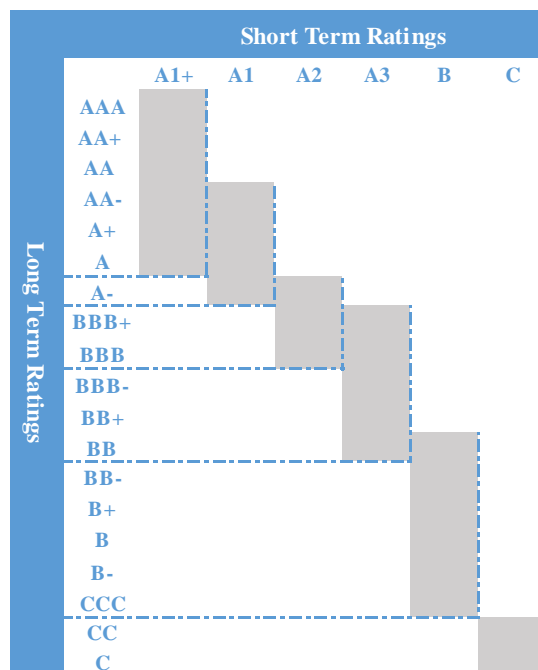
A BALANCE SHEET	Dec-18 6M	Jun-18 12M	Jun-17 12M	Jun-16 12M
1 Non-Current Assets	1,348	1,188	819	811
2 Investments	-	-	-	-
a Equity Instruments	-	-	-	-
b Debt Instruments	-	-	-	-
3 Current Assets	1,083	1,044	741	746
a Inventory	406	491	444	465
b Trade Receivables	361	398	240	233
c Others	317	154	58	47
4 Total Assets	2,431	2,232	1,561	1,557
5 Borrowings	694	125	308	261
a Short-Term	317	108	110	-
b Long-Term (Incl. CMLTB)	377	17	198	261
6 Other Short-Term Liabilities	811	1,056	508	596
7 Other Long-Term Liabilities	114	146	151	145
8 Shareholder's Equity	811	905	593	554
9 Total Liabilities & Equity	2,431	2,232	1,561	1,557
B INCOME STATEMENT				
1 Sales	1,096	2,125	1,516	1,310
2 Gross Profit	28	223	253	229
3 Non Operating Income	(44)	(31)	(6)	(11)
4 Total Finance Cost	(34)	(22)	(27)	(23)
5 Net Income	(82)	55	78	86
C CASH FLOW STATEMENT				
1 Free Cash Flow from Operations (FCFO)	(60)	130	190	180
2 Total Cashflows (TCF)	(60)	130	190	180
3 Net Cash changes in Working Capital	(56)	288	(94)	(42)
4 Net Cash from Operating Activities	(150)	398	71	121
5 Net Cash from Investing Activities	(101)	(443)	(79)	(4)
6 Net Cash from Financing Activities	312	75	(9)	(119)
7 Net Cash generated during the period	61	30	(18)	(1)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	3%	40%	16%	-2%
b Gross Profit Margin	3%	10%	17%	18%
c Net Profit Margin	-7%	3%	5%	7%
d Return of Equity	-19%	7%	14%	16%
2 Working Capital Management				
a Gross Working Capital (Inventory Days + Receivable Days)	137.9	135.1	166.4	212.4
b Net Working Capital (Inventory Days + Receivable Days - Payable Days)	86.1	79.9	79.8	93.0
3 Coverages				
a Debt Service Coverage (FCFO / Finance Cost+CMLTB+Excess STB)	-0.7	0.9	3.3	2.1
b Interest Coverage (FCFO / Finance Cost)	-2.6	8.8	9.2	11.9
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	-2.6	1.2	1.2	1.6
4 Capital Structure (Total Debt/Total Debt+Equity)				
a Capital Structure (Current Borrowings / Total Borrowings)	59%	97%	48%	27%
b Capital Structure (Total Borrowings / Total Borrowings+Equity)	46%	12%	34%	32%

Mar-19

Credit Rating Scale & Definitions

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 Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
AA		A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.
AA-		A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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.	B	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
A		C	An inadequate capacity to ensure timely repayment.
A-			
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.		
BBB			
BBB-			
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.		
BB			
BB-			
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.		
B			
B-			
CCC	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.		
CC			
C			
D	Obligations are currently in default.		



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

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

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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

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- (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.
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- (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)

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- (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)

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- (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)

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