The Pakistan Credit Rating Agency Limited

MICROTECH INDUSTRIES (PRIVATE) LIMITED

	NEW [MAR-17]	PREVIOUS [DEC-16]
Entity		
Long Term	BBB+	BBB+
Short Term	A2	A2
Outlook	Stable	Stable

REPORT CONTENTS

MARCH 2017

Profile & Ownership

- MicroTech Industries (Private) Limited (MicroTech), incorporated in 2003, manufactures digital and smart meters and also provides indigenous smart metering energy solutions; significant market share in smart metering
- Majority (55%) owned by Saeed family – key sponsors – followed by Siddiqi family (45%)

Governance

- Limited board size. Two members board, both are shareholders and hold executive positions
- No segregation in the role of CEO & Chairman
- Need for improvement in governance structure to bring independent oversight and guidance to management strategy

Management

- The CEO and key shareholder – Mr. Nauman Saeed – is engineer by profession and carries over two decades of experience in the field of technology
- Well-designed organization structure with a long associated professional and experienced management team
- In-house Research and Development function

Operational Risk

- Adequate technology infrastructure (internally developed ERP); MIS reporting needs improvement
- A state of the art in-house Surface-Mount Technology to produce electronic circuits
- Accredited with ISO and IEC certifications

Performance

- Business model comprises tender based sales; hence price sensitivity is high
- Key challenge include delays in implementation of projects due to bureaucratic procedural inefficiencies
- In 1HFY17, turnover recorded was PKR 590mln with composition tilted towards digital metering segment 91% (FY16: ~72%), while the remaining attributed to smart meters
- Per unit margins slashed owing to sale of digital meters to LESCO on reduced price; however, management positive about recovering margins in 2HFY17
- With the company's focus on reducing operational costs and decrease in finance cost, profit after taxation was recorded at PKR 29mln
- Upcoming smart metering ADB projects – first phase US$480mln – a likely opportunity for business expansion
- MicroTech plans to augment its revenue base through diversification in related businesses. In this regard installation of Injecting Molding plant has been achieved and it commenced production (Jan17)
- Furthermore, geographical diversification is on cards in medium term

Financial Risk

- Working capital requirements are a function of its receivables and inventory, for which the company relies on a mix of internal generation and STBs
- With the reduction in receivables as a percentage of sales; cash cycle improved (end-Dec16: 68days, end-Jun16: 91days)
- Coverages improved marginally on account of improved profitability (end-Dec16; interest coverage: 4x, core coverage: 3.2x)
- Low leveraged capital structure (end-Dec16: 25%, end-Jun16: 28%)

RATING RATIONALE

The ratings reflect MicroTech's adequate business profile characterized by healthy market share in energy meter manufacturing segment. The company's key strength lies in its indigenous Research and Development infrastructure and an able management team spearheading the company's operations. Single product and single buyer exposes the company to concentration risk. This at times lead to volatility in revenue and margins. At the same time, inherent risks of procedural delays in awarding contract and price sensitivity remains. However, comfort is drawn from the company's currently favorable competitive position in high margin smart metering business and sizeable business potential [particularly for smart meters] in local market, also unveiled by lately initiated foreign funded government projects focused towards infrastructure reforms. However, its translation in revenues may take time. MicroTech is eyeing revenues augmentation through, i) expansion in existing capacity, though small, and ii) diversification in related business; Injecting Molding plant installed and commenced production (Jan-17). The company's financial risk profile is adequate. The company's financial requirements emanate from its needs to fund its working capital (mainly receivables and tax refunds) and arranging requisite quantum of guarantees for soliciting business volumes. Current structure of bank limits provide reasonable support to the company's growth targets. However, participation in any new large project; expected to roll-out by the government over the medium-term, may require further capacities.

KEY RATING DRIVERS

The ratings are dependent on the company's ability to adapt to technological progression in its line of business to maintain its market position particularly in local industry. Proactive management of business affairs, thus sustaining margins, is imperative. Working Capital must be managed vigilantly due to receivable and tax refunds risk. Meanwhile, strengthening in governance structure is needed to improve independent oversight of board.

PKR mln

Microtech Industries (Private) Limited

BALANCE SHEET	31-Dec-16	30-Jun-16	30-Jun-15
	1H	Annual	Annual
Non-Current Assets	**462**	**446**	**381**
Investments (Incl. associates)	**17**	**-**	**50**
Equity	-	-	-
Debt	17	-	50
Current Assets	**826**	**723**	**887**
Inventory	255	173	197
Trade Receivables	171	303	499
Others	400	246	191
Total Assets	**1,305**	**1,169**	**1,318**
Debt	**151**	**179**	**263**
Short-term	104	146	234
Long-term (Inlc. Current Maturity of long-term debt)	47	32	29
Other Short-term liabilities	437	291	395
Other Long-term Liabilities	118	120	105
Shareholder's Equity	**599**	**579**	**555**
Total Liabilities & Equity	**1,305**	**1,169**	**1,318**
INCOME STATEMENT			
Turnover	**590**	**1,439**	**1,952**
Gross Profit	144	300	484
Other Income	(7)	(6)	(130)
Financial Charges	(15)	(37)	(89)
Net Income	**29**	**8**	**21**
Cashflow Statement			
Free Cashflow from Operations (FCFO)	60	66	305
Net Cash changes in Working Capital	54	86	47
Net Cash from Operating Activities	99	115	263
Net Cash from InvestingActivities	(65)	(30)	(133)
Net Cash from Financing Activities	(36)	(106)	(164)
Ratio Analysis			
Performance			
Turnover Growth	-59.0%	-26.3%	83.3%
Gross Margin	24.3%	20.8%	24.8%
Net Margin	4.9%	0.6%	1.1%
ROE	19.2%	1.3%	4.0%
Coverages			
Interest Coverage (FCFO/Gross Interest)	4.0	1.8	3.4
Core: (FCFO/Gross Interest+CMLTD+Uncovered Total STB)	3.2	1.5	3.1
Total: (TCF) / (Gross Interest+CMLTD+Uncovered Total STB)	3.2	1.5	3.1
Debt Payback (Total LT Debt Including UnCovered Total STBs) / (FCFO- Gross Interest)	1.0	1.1	0.1
Liquidity			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	67.9	91.2	85.0
Capital Structure (Total Debt/Total Debt+Equity)	25.2%	28.4%	39.3%

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

Rating	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 Ratings

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 conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

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 surveill the opinion due to lack of requisite information