

RATING REPORT

Adam Sugar Mills Limited

REPORT DATE:

21st May 2024

RATING ANALYSTS:

Muhammad Subhan
subhan@vis.com.pk

RATING DETAILS

Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Date	May 21, 2024		June 12, 2023	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION

Incorporated in 2008	External auditors: Rahman Sarfaraz Rahim Iqbal Rafiq Chartered Accountants
Public Listed Company	Chairman: Mr. Jawaid Ahmed
Key Shareholders (with stake 10% or more):	CEO: Mr. Ghulam Ahmed Adam
Adam Pakistan Limited – 20.3%	
Mrs. Sarah Adam – 18.0%	
Mrs. Humera Dewan – 14.1%	
Mr. Junaid G. Adam – 14.1%	
Mr. Muhammad Hussain – 5.0%	

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:

<https://docs.vis.com.pk/docs/VISRatingScales.pdf>

APPLICABLE METHODOLOGY(IES)

VIS Entity Rating Criteria: Industrial Corporates

<https://docs.vis.com.pk/docs/CorporateMethodology.pdf>

Adam Sugar Mills Limited

OVERVIEW OF THE INSTITUTION	RATING RATIONALE																																								
<p>Adam Sugar Mills Limited was incorporated in Pakistan on October, 1965 in the name of Bahawalnagar Sugar Mills Limited as a public limited company under the companies act, 1913 (repealed with Companies Ordinance, 1984 and subsequently Companies Act, 2017). In 1985, name of the Company was changed to Adam Sugar Mills Limited.</p>	<p>Corporate Profile:</p> <p>Adam Sugar Mills Limited (“ASML” or “the Company”) was incorporated in Pakistan on Oct, 1965 in the name of Bahawalnagar Sugar Mills Limited as a public limited company under the Companies’ act, 1913 (repealed with Companies Ordinance, 1984 and subsequently Companies Act, 2017). In 1985, name of the Company was changed to Adam Sugar Mills Limited.</p> <p>ASML is principally engaged in manufacturing and sale of sugar and by-products with operating track record of nearly six decades. The mills started with initial capacity of 1,500 TCD, which was gradually increased to 16,000 TCD. Major shareholding of the company is vested with the Adam family while members of the family are actively involved in management and supervision of operations. Headquartered in Karachi, ASML has the production unit located at District Bahawalnagar, Punjab.</p> <p>Operational Performance:</p> <table border="1" style="width: 100%; border-collapse: collapse; text-align: center;"> <thead> <tr style="background-color: #4F81BD; color: white;"> <th></th> <th><u>Units</u></th> <th><u>2024</u></th> <th><u>2023</u></th> <th><u>2022</u></th> </tr> </thead> <tbody> <tr> <td>Crushing Capacity per day</td> <td>Tons</td> <td>16,000</td> <td>16,000</td> <td>16,000</td> </tr> <tr> <td>Crushing Period in days</td> <td>Numbers</td> <td>104</td> <td>106</td> <td>142</td> </tr> <tr> <td>Cane Crushed</td> <td>Tons</td> <td>684,186</td> <td>590,048</td> <td>833,340</td> </tr> <tr> <td>Sugar Production</td> <td>Tons</td> <td>69,369</td> <td>57,790</td> <td>82,039</td> </tr> <tr> <td>Sucrose Recovery</td> <td>% age</td> <td>10.14%</td> <td>9.79%</td> <td>9.84%</td> </tr> <tr> <td>Molasses Produced</td> <td>Tons</td> <td>29,694</td> <td>27,805</td> <td>37,061</td> </tr> <tr> <td>Molasses Recovery</td> <td>% age</td> <td>4.34%</td> <td>4.71%</td> <td>4.45%</td> </tr> </tbody> </table> <p>The Company faced production challenges in terms of availability of sugarcane due to floods in MY23. This was in line with the fact the countrywide sugar production fell by 20% in MY23 due to low cultivation by farmers and floods affecting certain areas, however, the region where Adam Sugar Mills Limited is situated was not majorly affected by floods. Resultantly, a shortened crushing period was recorded at 106 days (MY22: 142 days). Cane crushed was also recorded lower in MY23 at 590,048 tons (MY22: 833,340 tons), which resulted in lower production of sugar, molasses and bagasse as compared to MY22. The Company carry out regular BMR activities in the mills on an annual basis, however, the existing process house need to be upgraded to meet the optimal sugar cane crushing.</p> <p>In addition, crushing period declined to 104 days (MY23: 106 days) in MY24 due to a shorter crushing season. In MY24, the cane crushed for the year is recorded at 684,186 tons (MY23: 590,048 tons) and sugar production increased to 69,369 tons (MY23: 57,790 tons) with increase in sucrose recovery to 10.14% (MY23: 9.79%).</p> <p>Key Rating Drivers:</p> <p>Medium business risk profile characterized by high cyclicity and moderate capital and competitive intensity</p> <p>VIS has assigned a medium business risk to the sugar industry given its moderate level of barriers of entry, technology risk, and capital-intensive nature. However, industry’s high cyclicity with the production of sugarcane possess a raw material availability risk.</p>		<u>Units</u>	<u>2024</u>	<u>2023</u>	<u>2022</u>	Crushing Capacity per day	Tons	16,000	16,000	16,000	Crushing Period in days	Numbers	104	106	142	Cane Crushed	Tons	684,186	590,048	833,340	Sugar Production	Tons	69,369	57,790	82,039	Sucrose Recovery	% age	10.14%	9.79%	9.84%	Molasses Produced	Tons	29,694	27,805	37,061	Molasses Recovery	% age	4.34%	4.71%	4.45%
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The industry faces an inelastic demand linked with the growing population in the country coupled with government's measure to allow exports further supporting its stable demand. However, unfavorable sugar prices due to surplus of carryover sugar stock expose the industry to lower revenue gains.

The future outlook of the sugar industry appears challenging due to prevailing economic conditions of the country, SBP discount rate remaining elevated despite expectation of rate cut, which will maintain pressure on finance cost of the Company, and increase in sugarcane support prices by the provinces which increases the production cost of sugar with no adequate corresponding increase in the sugar prices.

Revenue affected in MY23 due to lower quantity sold while 1QMY24 witnessed significant improvement in the profitability due to higher sugar prices

In MY23, the Company exhibited stability in its revenue stream, maintaining sales at PKR 5.4 bln. Despite a decrease in the quantity sold to 56,179 tons (MY22: 65,217 tons) in FY23, a notable uptick in sugar prices to PKR 83 thousand/metric ton (MY22: PKR 71.5 thousand/metric ton) and export of 2,366 tons of sugar at average price of USD 605/ton (PKR 250/kg) provided a mitigating effect, maintaining the overall revenue performance. However, due to higher sugarcane procurement cost at PKR 7,849/ton (MY22: PKR 6,036/ton) in MY23 the Company's gross margin declined to 11.8% (MY22:12.5%). Amidst this scenario, the net margin displayed a contrasting trend, ascending to 3.9% (MY22: 2.6%) in FY23 on account of reduced tax incidence during the year.

In 1QMY24, the reported sales amounted to PKR 1.8 bln, translating into enhancement in the gross margin at 27.6%. This notable upswing in the gross margin during 1QMY24 is owing to inventory gains on already available stock coupled with steep escalation in the sugar prices by 66%. Concurrently, the net margin significantly improved at 13%.

Coverage profile depicted weakening in MY23, however 1QMY24 witnessed a rebound

ASML's coverage profile depicted weakening in MY23 with its debt service coverage ratio (DSCR) declining to 1.7x (MY22: 2.5x). This reduction in the DSCR is due to lower funds flow from operations (FFO) reporting at PKR 421 mln (MY22: PKR 550.2 mln), a result of lower profit before tax (PBT). However, the 1QMY24 witnessed significant improvement as the DSCR strengthened to 3.1x due to stronger FFO emanating from higher profitability.

Capital structure improved in MY23, while 1QMY24 showed weakening

The gearing ratio of the Company demonstrated improvement reporting at 0.7x (MY22: 1.0x) in MY23. This improvement in the gearing ratio, despite a drawdown of long-term debt, is on account of higher profit retention and repayment of short term debt during the year. However, despite the positive development in the equity base in MY23, the leverage marginally weakened at 2.2x (MY22: 2.1x) in MY23 due to higher trade payables coupled with increase in the long term debt.

The capitalization metrics in 1QMY24 witnessed weakening with gearing and leverage ratio reporting at 1.6x and 3.0x, respectively. This decline in the capitalization metrics is due to a larger drawdown of short-term debt in the quarter to meet the working capital needs of the Company.

Adequate liquidity profile

Historically, the Company has maintained a 5-year average current ratio of 0.9x. In MY23, ASML's current ratio reported slight improvement at 1.1x (MY22: 1.0x), remaining same in the 1QMY24. The short-term debt (STD) coverage improved in the MY23 reaching 2.8x (MY22: 1.5x), attributed to increased sugar inventory and payments towards short-term borrowings. However, in the 1QMY24, the STD coverage declined to 1.5x due to higher drawdown of short-term debt.

Pending Litigation

The developments in relation to penalties imposed by Competition Commission of Pakistan (CCP) on Pakistan Sugar Mills Association (PSMA) along with majority of the sugar mills and the subsequent legal proceedings initiated by the subject company is still pending. The impact of the imposed penalty amounting PKR 278 mln on ASML would be significant. However, The Company has filed an appeal before the Competition Appellate Tribunal against the order of CCP, along with other sugar mills in Punjab zone. The Appellate Tribunal has restrained the CCP from adopting any coercive measures against The Company for recovery of the fine. The Company also challenged the same order of CCP before the Lahore High Court (LHC) in a writ petition, along with other sugar mills in the Punjab zone. The operation of the said order has been suspended and CCP has been restrained from recovering penalty imposed in terms of the order of the LHC dated Oct 18, 2021. The matter is pending adjudication before the LHC. Given uncertainty and materiality of the outcome, VIS will continue to monitor further developments in this matter.

Adam Sugar Mills Limited
Annexure I

Financial Summary								
Balance Sheet (PKR Millions)	MY19A	MY20A	MY21A	MY22A	MY23A	3MMY24A	MY24P	MY25P
Property, plant and equipment	5,115.4	4,939.0	4,840.7	4,966.6	6,532.7	6,479.7	6,449.7	6,376.4
Stock-in-trade	928.9	204.9	278.8	1,229.3	1,827.8	3,001.4	2,535.6	3,383.4
Trade debts	28.0	244.7	410.0	317.7	98.4	255.3	177.1	222.5
Cash & Bank Balances	70.1	100.0	191.8	64.8	35.2	558.9	490.9	641.2
Total Assets	6,432.6	5,856.6	6,077.3	6,890.9	8,811.3	10,673.9	9,994.9	10,996.2
Trade and Other Payables	734.1	521.8	361.9	780.2	1,090.9	1,159.1	917.8	1,175.5
Long-term Debt (incl. current portion)	305.2	200.9	294.3	242.2	429.4	420.8	227.5	125.1
Short-Term Borrowings	1,194.2	592.2	770.6	963.2	664.8	2,281.3	1,871.9	2,427.7
Total Debt	1,499.4	793.0	1,065.0	1,205.4	1,094.2	2,702.1	2,099.4	2,552.8
Total Liabilities	3,116.8	2,212.2	2,308.4	2,875.5	3,327.7	5,016.2	4,562.5	5,292.9
Paid up Capital	172.9	172.9	172.9	172.9	172.9	172.9	172.9	172.9
Equity (excl. Revaluation Surplus)	448.1	881.8	1,105.8	1,353.2	1,510.7	1,695.9	1,459.5	1,730.4
Income Statement (PKR Millions)	MY19A	MY20A	MY21A	MY22A	MY23A	3MMY24A	MY24P	MY25P
Net Sales	2,314.6	3,554.0	2,880.6	5,422.5	5,426.4	1,801.7	7,655.4	9,587.0
Gross Profit	18.8	708.0	410.3	709.8	641.1	497.5	1,158.5	1,263.1
Operating Profit	-87.0	601.4	278.1	488.1	434.9	445.6	935.8	1,028.9
Finance Costs	228.5	185.6	103.2	164.8	278.5	41.7	491.8	445.3
Profit Before Tax	-315.5	415.8	174.8	323.3	156.3	379.3	417.2	547.2
Profit After Tax	-254.1	318.6	195.7	158.4	101.3	234.8	142.0	314.1
Ratio Analysis	MY19A	MY20A	MY21A	MY22A	MY23A	3MMY24A	MY24P	MY25P
Gross Margin (%)	0.8%	19.9%	14.2%	13.1%	11.8%	27.6%	15.1%	13.2%
Operating Margin (%)	-3.8%	16.9%	9.7%	9.0%	8.0%	24.7%	12.2%	10.7%
Net Margin (%)	-11.0%	9.0%	6.8%	2.9%	1.9%	13.0%	1.9%	3.3%
Funds from Operation (FFO) (PKR Millions)	-180.8	627.6	389.6	550.2	420.5	286.2	586.8	624.8
FFO to Total Debt* (%)	-12.1%	79.1%	36.6%	45.6%	38.4%	42.4%	28.0%	24.5%
FFO to Long Term Debt* (%)	-59.3%	312.5%	132.4%	227.2%	97.9%	272.1%	257.9%	499.3%
Gearing (x)	3.3	0.9	1.0	0.9	0.7	1.6	1.4	1.5
Leverage (x)	7.0	2.5	2.1	2.1	2.2	3.0	3.1	3.1
Debt Servicing Coverage Ratio* (x)	0.1	2.9	2.5	2.5	1.7	3.1	2.2	2.4
Current Ratio (x)	0.6	0.7	0.9	0.9	1.1	1.1	1.1	1.1
(Stock in trade + trade debts) / STD (x)	0.8	0.8	0.9	1.5	2.8	1.5	1.6	1.6
Return on Average Assets* (%)	-5.0%	5.2%	3.3%	2.4%	1.3%	10.7%	1.4%	3.0%
Return on Average Equity* (%)	-44.5%	47.9%	19.7%	12.9%	7.1%	61.8%	9.1%	19.3%
Cash Conversion Cycle (days)	80.2	28.6	43.3	19.2	36.7	43.1	84.0	78.6
<i>*Annualized, if required</i>								
A - Actual Accounts								
P - Projected Accounts								
M - Management Accounts								

REGULATORY DISCLOSURES		Appendix II																									
Name of Rated Entity	Adam Sugar Mills Limited																										
Sector	Sugar																										
Type of Relationship	Solicited																										
Purpose of Rating	Entity Ratings																										
Rating History	<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 15%;">Rating Date</th> <th style="width: 25%;">Medium to Long Term</th> <th style="width: 15%;">Short Term</th> <th style="width: 20%;">Rating Outlook</th> <th style="width: 25%;">Rating Action</th> </tr> </thead> <tbody> <tr> <td colspan="5" style="text-align: center;">RATING TYPE: ENTITY</td> </tr> <tr> <td>21/05/2024</td> <td>A-</td> <td>A-2</td> <td>Stable</td> <td>Reaffirmed</td> </tr> <tr> <td>12/06/2023</td> <td>A-</td> <td>A-2</td> <td>Stable</td> <td>Reaffirmed</td> </tr> <tr> <td>17/05/2022</td> <td>A-</td> <td>A-2</td> <td>Stable</td> <td>Initial</td> </tr> </tbody> </table>		Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action	RATING TYPE: ENTITY					21/05/2024	A-	A-2	Stable	Reaffirmed	12/06/2023	A-	A-2	Stable	Reaffirmed	17/05/2022	A-	A-2	Stable	Initial
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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	<table border="1" style="width: 100%; border-collapse: collapse;"> <thead> <tr> <th style="width: 40%;">Name</th> <th style="width: 30%;">Designation</th> <th style="width: 30%;">Date</th> </tr> </thead> <tbody> <tr> <td>Mr. Omar G. Adam</td> <td>Managing Director</td> <td rowspan="2" style="text-align: center; vertical-align: middle;">08th May 2024</td> </tr> <tr> <td>Mr. Faisal Habib</td> <td>Chief Financial Officer</td> </tr> </tbody> </table>		Name	Designation	Date	Mr. Omar G. Adam	Managing Director	08 th May 2024	Mr. Faisal Habib	Chief Financial Officer																	
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