RATING REPORT

Chashma Sugar Mills Limited

REPORT DATE:
November 23, 2021

RATING ANALYST:
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RATING DETAILS				
	Latest Rating		Previous Rating	
Rating Category	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Outlook	*Stable*		*Stable*	
Rating Date	*Nov 23, 2021*		*Nov 10, 2020*	

COMPANY INFORMATION	
Incorporated in 1988	**External auditors:** M/s. A.F. Ferguson & Co. Chartered Accountants.
Public Limited Company	**Chairman of the Board:** Mr. Abbas Sarfaraz Khan
	Chief Executive Officer: Mr. Aziz Sarfaraz Khan
Key Shareholders (with stake 5% or more):	
The Premier Sugar Mills & Distillery Limited ~47.9%	
Other Group Companies ~18.7%	
Directors & Relatives ~14.0%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Industrial Corporates (August 2021) *https://docs.vis.com.pk/docs/CorporateMethodology202108.pdf*

Chashma Sugar Mills Limited

OVERVIEW OF THE INSTITUTION

CSML was incorporated in May 1988 as a public company, under the repealed Companies Ordinance 1984 (now the Companies Act, 2017). The company is engaged in production and sale of white crystalline sugar and other allied products. The head office of the company is situated in Islamabad, while manufacturing facilities are located at Dera Ismail Khan, KP.

Profile of CEO

Mr. Aziz S. Khan is Chairman BoD of Premier Sugar Mills & Distillery Co. Ltd. He is also a board member of The Frontier Sugar Mills & Distillery Ltd. and Arpak International Investments Ltd.

RATING RATIONALE

Chasma Sugar Mills Limited (CSML) is part of Premier Group. The group has presence in sugar, ethanol, high-grade polypropylene, real-estate and distribution of consumer goods and bulk storage of agriculture produce. CSML is principally engaged in manufacturing and sale of sugar and ethanol with over three decades of track record of operations. Headquartered in Islamabad, CSML has manufacturing facilities (2 units of sugar mills and 1 ethanol plant) located at Dera Ismail Khan, KP. Total staff strength stands at around 2K employees.

Regulatory Matter (Update on Penalty Imposed)

The ratings have incorporated the developments with regards to penalties imposed by CCP on certain sugar mills and legal proceedings for interim relief (stay) initiated by the subject company. However, in the meanwhile, uncertainty of the outcome would persist on the sector. The material impact of penalty imposed (amounting to Rs. 6.7b) on CSML will be sizeable and hence VIS will continue to monitor further development in this matter.

Long-term Investments

CSML holds 100% stake at Whole Foods (Pvt.) Limited, amounting to Rs. 219.9m at end-June'21. In addition, the company has also provided a sub-ordinated loan of Rs. 220.5m in MY21. WFL is establishing wheat silos in Layyah and Bhakkar, having storage capacity of 20,000 tons and intends to earn rental income from governmental contracts.

Capex & Efficiency Enhancement Plans

The company made a capex of Rs. 619.4m in fixed assets (MY20: Rs. 580.3m; MY19: Rs. 500.9m) during 9M'MY21, mainly to enhance production efficiencies. Since last review, effluent treatment plants, emission control systems (wet Scrubber for boilers) and FFE (Filing Film Evaporators) have been installed at both units of sugar mills. Furthermore, the management has planned a capex of Rs. 500m to install high pressure boiler and steam turbine of capacity 6MW; of which 60% will be utilized by ethanol plant and the remaining to support future business initiatives.

Operational Performance:

The production capacity of both sugar crushing units and distillery has remained unchanged at 18,000 tons per day (tpd) and 125,000 litres per day (lpd) respectively. As per management, there are no plans to enhance the capacities in the near future.

Sugar

During the outgoing year, the mill operated for 107 days (MY20: 107 days; MY19: 98 days; MY18: 129 days). CSML crushed 1.46m MT of sugarcane which is 3% higher than the previous year; however, overall sugar production was recorded lower at 146K MT (MY20: 151K MT) in MY21 due to a slight decline in recovery rate (owing to industry-wide early commencement of crushing activity). Previously, during the period (MY18-20), sucrose recovery registered an upward trajectory on account of continued provision of support to farmers including better usage of seed. Utilization levels have depicted some improvement in comparison to previous year, albeit remains on the lower side.

Figure: Sugar Mill (Capacity & Production)

	MY19	MY20	MY21

Sugarcane Crushing Capacity (TPD)	18,000	18,000	18,000
Total Cane Crushed (Ton)	1,562,413	1,432,075	1,468,505
Number of Crushing Days	98	107	107
Crushing Per Day (Ton)	15,943	13,384	13,724
Capacity Utilization	89%	74%	76%
Sugar Produced	166,252	151,013	145,987
Sucrose Recovery Rate	10.64%	10.55%	9.94%

Over the period of past five years, sugar production has declined by ~28% despite the improving trend in sucrose recovery. The management expects sugar production to increase in the ongoing year given the indication of higher crop coverage area, healthy crop size and attractive sugarcane prices available to farmers.

Ethanol

CSML's estimated market share (in terms of volume) in ethanol segment stands at around 4% with annual ethanol production of 44.1m liters (MY20: 43.5m liters) during MY21. The distillery remained operational for 353 days (MY20: 354 days) with few closure days on account of routine overhauling and cleaning shutdowns. The ethanol recovery rate has improved on a timeline basis. In line with higher cane crushing, molasses production during MY21 increased to 62,824 MT vis-à-vis 60,136 MT in the previous year.

Figure: Ethanol Distillery (Capacity & Production)

	MY19	MY20	MY21
Ethanol Capacity (LPD)	125,000	125,000	125,000
Number of Distillation Days	355	354	353
Total Ethanol Produced (Liter)	43,260,426	43,462,330	44,099,770
Ethanol Produced Per Day (Liter)	121,860	122,775	124,928
Ethanol Recovery Rate	18.07%	18.35%	18.66%
Capacity Utilization	97%	98%	99.9%

Key Rating Drivers:

Local demand supply dynamics of sugar sector are projected to depict some improvement in the ongoing year given the indication of higher crop coverage area.

The business risk profile of sugar sector is considered high given inherent cyclicality in crop levels and raw material prices. Moreover, distortion in pricing mechanism of raw material prices and refined sugar also create challenges for sugar mills. Typically, sugarcane production has a 3-5 year cycle, driven largely by government support for farmers and crop yield. Sugar cane production has increased by 22% to 81 MT on account of increase in area under cultivation and improvement in crop yield during MY21. Based on around 68% crushing and an average recovery rate of 10.2%, the sector has produced 5.6m MT (MY20: 4.8m MT) of sugar in MY21. Moreover, sugar demand is projected at 5.9m MT for the period. While narrow demand and supply dynamics may lead to high sugar prices, government plans to import sugar to keep the prices in check. Also, margins may also be curtailed due to increasing trend in sugarcane prices. During MY21, sugarcane procurement prices have been recorded as higher against the minimum support price of Rs. 202 per mound. However, sector's risk profile draws support from diversification into distillery, power and other segments.

Ethanol production is dependent on supply of molasses and decline in sugar cane crushing effected the growth in ethanol industry. Going forward,

ethanol growth is anticipated to remain subdued on the back of limited supply of molasses.

As per industry estimates, ethanol industry currently has an installed production capacity of over 1.1b liters per annum (3.3m liters per day) with around 20 distilleries operating in various provinces. Around 95% of ethanol produced locally is exported while at present, total exports (in terms of value) stand at USD 536m per annum. Top 5 players account for over 50% of total exports. Premier group is the largest player in the segment followed by Madina, Shakarganj, Shahmurad and Tandlianwala Sugar Mills. Major markets for ethanol exports include China, South Korea, EU and Philippines.

The shortages of molasses and reduction in sugarcane production are the key challenge faced by the sector. As a result, ethanol production is facing decline over the past three years. At present, total molasses requirement of ethanol sector is around 4.4m MT whereas the local sugar mills could only caters to around 50% to 65% of industry's requirement. Further, around 0.5 million MT of molasses is also being utilized by local animal feed industry.

Sales revenue has registered a strong growth trend mainly driven by higher retail prices.

Topline of the company registered a double-digit annual growth rate for the second consecutive year and amounted to Rs. 15.9b (MY19: Rs. 12.4b; MY18: Rs. 10.4b) in MY20. The growth in sales was mainly driven by higher retail price of sugar along with a mix of volumetric and price increase in ethanol sales. The similar trend was noted during 9M'MY21 with the net sales amounting to Rs. 11.1b. Around three-fourth of total revenue is contributed by sugar segment while the remaining sales are associated with ethanol exports.

Sugar

The company managed to sell 104,313 MT (MY20: 176,473 MT) during 9M'MY21 at a significantly higher average selling price of Rs. 83,787 per ton (MY20: Rs. 75,237 per ton). However, due to a sizeable jump of ~20% in CSML's average sugarcane procurement cost (MY21: Rs. 252 per 40kg; MY20: Rs. 210 per 40kg), the margins in sugar segment have curtailed. Going forward, the margins are expected to remain under pressure over the rating horizon.

Figure: Sugar

	MY19	MY20	9M'MY21
Sugar Sold (MT)	175,296	176,473	104,313
Sugar Price (MT)	56,497	75,237	83,787
Net Sales (Less Sales tax & Others, Rs. in m)	9,208.2	11,442.1	7,701.9
Gross Profit (Rs. in m)	1,274.4	2,349.1	1,134.0
Gross Margin	13.8%	20.5%	14.7%

Ethanol

Ethanol volumetric sales were recorded at 29.3m liters during 9M'MY21 (MY20: 42.1m liters) with an average selling price of Rs. 113.9 per liter (MY20: Rs. 100.2 per liter). The ethanol is exported to foreign clients like Vitol and Mitsubishi on a 3 – 4 month supply contract.

Figure: Ethanol

	MY19	MY20	9M'MY21
Ethanol Sold (Million Liters)	45.5	42.1	29.3
Ethanol Price/Liter	73	100.2	113.9

Net Sales (Less Sales tax & Others, Rs. in m)	3,212.6	4,487.5	3,396.6
Gross Profit (Rs. in m)	962.7	540.1	548.8
Gross Margin	30.0%	12.0%	16.2%

Profitability margins have remained under pressure during the year given sizeable jump in average sugarcane and molasses procurement cost.
In MY20, overall profitability margins on gross and net basis have sustained at 18.1% (MY19: 18.0%) and 4.7% (MY19: 4.7%), respectively. However, the same remained under pressure during 9M'MY21 given sizeable jump in average sugarcane and molasses procurement cost.

On the cost front, increase in admin expenses during MY20 largely remained in line with inflation whereas the distribution cost doubled which was mainly associated with higher freight charges. Financial charges have witnessed an increasing trend on account of higher utilization of running finance and mobilization of long-term debt. Overall profitability profile was also supported by other income which mainly pertained to exports subsidy and exchange gain. Going forward, profitability indicators are likely to remain stressed given the increasing trend in prices of sugarcane and molasses.

Liquidity profile is considered manageable with adequate fund flow to support its outstanding financial obligations.
Funds from Operations (FFO) were reported at Rs. 1.1b (MY20: Rs. 1.2b; MY19: Rs. 1.4b) during 9M'MY21. In line with healthy cash flow generation, the debt servicing ability continues to remain strong as reflected by DSCR of 2.25x (MY19: 2.67x) in MY20. Current ratio of the company remains over 1.0x, while coverage of short-term borrowings in relation to stock in trade and trade debts stood at 0.89x at end-9M'MY21 indicating room for improvement.

Adequate capitalization levels; leverage indicators have improved on account of increase in equity base
Equity base (excluding revaluation surplus) of the company has grown to Rs. 3.8b (MY20: Rs. 3.5b; MY19: Rs. 2.6b) at end-9M'MY21. The company has been paying dividends for the past six years while dividend payout ratio stood at 19% (MY19: 7%). Debt profile of the company comprises a mix of short-term and long-term borrowings. Long-term debt financing (inclusive of current portion and related-parties loan) stood at Rs. 2.8b (MY20: Rs. 2.5b) at end-9M'MY21. Since last review, the management acquired long-term loan of Rs. 245m while further loan acquisition is expected on account of BMR activities. Due to notable growth in equity, gearing and debt leverage indicators have improved to 1.41x (MY19: 2.08x; MY18: 3.43x) and 2.08x (MY19: 2.76x; MY18: 4.48x), respectively at end-MY20.

Corporate governance is considered sound
Since last review, there has been no changes at board and senior management level. Presently, the board comprises nine members including two independent directors and three female directors. Overall corporate governance framework is supported by adequate board composition and oversight.

FINANCIAL SUMMARY *(amounts in PKR millions)*				Appendix I
BALANCE SHEET	**MY18**	**MY19**	**MY20**	**9M'MY21***
Property, Plant & Equipment	9,531.8	9,224.0	9,892.3	9,779.2
Long-term Investment	100.0	100.0	139.2	220.0
Stores, Spare & Loose Tools	342.7	469.7	502.3	404.0
Stock in Trade	2,242.6	1,724.8	1,242.0	5,149.9
Trade Debts	219.1	57.0	143.0	307.5
Loans, Advances & Tax Refund	331.7	1,392.9	1,619.5	1,261.9
Deposits, Prepayment & Others	812.0	338.9	311.1	313.7
Cash & Bank Balance	188.8	203.9	281.9	527.4
Total Assets	**13,815.7**	**13,526.3**	**14,890.0**	**18,865.2**
Trade & Other Payables	712.3	689.0	942.9	728.0
Deferred Taxation	1,154.8	1,056.9	1,341.6	1,443.6
Other Liabilities	8.0	8.7	10.5	10.5
Short-term Borrowings	3,796.2	3,100.9	2,419.7	6,119.0
Long-Term Borrowings *(Inc. current maturity)*	2,339.0	2,328.6	2,484.7	2,812.2
Total Liabilities	**8,010.2**	**7,204.9**	**7,199.4**	**11,115.2**
Paid-up Capital	286.9	286.9	286.9	286.9
Tier-1 Equity	1,786.5	2,608.0	3,467.5	3,765.3
Total Equity	**5,805.5**	**6,321.5**	**7,690.5**	**7,750.1**
INCOME STATEMENT				
Net Sales	10,383.8	12,420.7	15,929.7	11,098.5
Gross Profit	1,379.0	2,237.1	2,889.3	1,682.8
Operating Profit	737.5	1,386.0	1,646.6	893.7
Profit Before Tax	340.7	1,407.4	1,960.2	1,624.4
Profit After Tax	193.6	578.6	746.1	203.0
FFO	835.7	1,385.1	1,240.2	1,116.2
RATIO ANALYSIS				
Gross Margin (%)	13.3	18.0	18.1	15.2
Net Margin (%)	1.9	4.7	4.7	1.8
Net Working Capital	(1,014.6)	(344.9)	365.1	565.9
FFO to Long-Term Debt (x)	0.36	0.59	0.50	0.53
FFO to Total Debt (x)	0.14	0.26	0.25	0.17
Debt Servicing Coverage Ratio (x)	1.31	2.67	2.25	1.84
ROAA (%)	1.6	4.2	5.3	1.6
ROAE (%)	11.9	26.3	24.6	7.5
Gearing (x)	3.43	2.08	1.41	2.37
Debt Leverage (x)	4.48	2.76	2.08	2.95
Current Ratio	0.80	0.92	1.09	1.07
Inventory + Receivables to Short-term Borrowings (x)	0.65	0.57	0.57	0.89

**Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

VIS Credit Rating Company Limited

RATING SCALE & DEFINITIONS: ISSUES / ISSUERS

Medium to Long-Term

AAA
Highest credit quality; the risk factors are negligible, being only slightly more than for risk-free Government of Pakistan's debt.

AA+, AA, AA-
High credit quality; Protection factors are strong. Risk is modest but may vary slightly from time to time because of economic conditions.

A+, A, A-
Good credit quality; Protection factors are adequate. Risk factors may vary with possible changes in the economy.

BBB+, BBB, BBB-
Adequate credit quality; Protection factors are reasonable and sufficient. Risk factors are considered variable if changes occur in the economy.

BB+, BB, BB-
Obligations deemed likely to be met. Protection factors are capable of weakening if changes occur in the economy. Overall quality may move up or down frequently within this category.

B+, B, B-
Obligations deemed less likely to be met. Protection factors are capable of fluctuating widely if changes occur in the economy. Overall quality may move up or down frequently within this category or into higher or lower rating grade.

CCC
Considerable uncertainty exists towards meeting the obligations. Protection factors are scarce and risk may be substantial.

CC
A high default risk

C
A very high default risk

D
Defaulted obligations

Short-Term

A-1+
Highest certainty of timely payment; Short-term liquidity, including internal operating factors and /or access to alternative sources of funds, is outstanding and safety is just below risk free Government of Pakistan's short-term obligations.

A-1
High certainty of timely payment; Liquidity factors are excellent and supported by good fundamental protection factors. Risk factors are minor.

A-2
Good certainty of timely payment. Liquidity factors and company fundamentals are sound. Access to capital markets is good. Risk factors are small.

A-3
Satisfactory liquidity and other protection factors qualify entities / issues as to investment grade. Risk factors are larger and subject to more variation. Nevertheless, timely payment is expected.

B
Speculative investment characteristics; Liquidity may not be sufficient to ensure timely payment of obligations.

C
Capacity for timely payment of obligations is doubtful.

Rating Watch: VIS places entities and issues on 'Rating Watch' when it deems that there are conditions present that necessitate re-evaluation of the assigned rating(s). Refer to our 'Criteria for Rating Watch' for details. www.vis.com.pk/images/criteria_watch.pdf

Rating Outlooks: The three outlooks 'Positive', 'Stable' and 'Negative' qualify the potential direction of the assigned rating(s). An outlook is not necessarily a precursor of a rating change. Refer to our 'Criteria for Rating Outlook' for details.www.vis.com.pk/images/criteria_outlook.pdf

(SO) Rating: A suffix (SO) is added to the ratings of 'structured' securities where the servicing of debt and related obligations is backed by some sort of financial assets and/or credit support from a third party to the transaction. The suffix (SO), abbreviated for 'structured obligation', denotes that the rating has been achieved on grounds of the structure backing the transaction that enhanced the credit quality of the securities and not on the basis of the credit quality of the issuing entity alone.

(blr) Rating: A suffix (blr) is added to the ratings of a particular banking facility obtained by the borrower from a financial institution. The suffix (blr), abbreviated for 'bank loan rating' denotes that the rating is based on the credit quality of the entity and security structure of the facility.

'p' Rating: A 'p' rating is assigned to entities, where the management has not requested a rating, however, agrees to provide informational support. A 'p' rating is shown with a 'p' subscript and is publicly disclosed. It is not modified by a plus (+) or a minus (-) sign which indicates relative standing within a rating category. Outlook is not assigned to these ratings. Refer to our 'Policy for Private Ratings' for details. www.vis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when VIS believes that the ratee has selectively defaulted on a specific issue or obligation but it will continue to meet its payment obligations on other issues or obligations in a timely manner.

REGULATORY DISCLOSURES						Appendix III
Name of Rated Entity	Chashma Sugar Mills Limited					
Sector	Sugar					
Type of Relationship	Solicited					
Purpose of Rating	Entity Rating					
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**	
	RATING TYPE: ENTITY					
	11/23/2021	A-	A-2	Stable	Reaffirmed	
	11/10/2020	A-	A-2	Stable	Reaffirmed	
	10/18/2019	A-	A-2	Stable	Upgrade	
	11/15/2018	BBB+	A-2	Stable	Initial	
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	**Name**	**Designation**	**Date**			
	Mr. Wajahat Qamar Butt	Deputy General Manager Tax & Finance	Oct 12, 2021			