RATING REPORT

Faran Sugar Mills Limited

REPORT DATE:
March 20, 2020

RATING ANALYSTS:

Talha Iqbal
talha.iqbal@vis.com.pk

Madeeh Ahmed
madeeh.ahmed@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 Outlook	Stable		Stable	
Rating Date	*March 20 , 2020*		*February 15, 2019*	

COMPANY INFORMATION

Incorporated in 1981	**External auditors:** M/s Rahman Sarfaraz Rahim Iqbal Rafiq Chartered Accountants
Public Listed Company	**Chairman:** Muhammad Omar Amin Bawany
Key Shareholders :	**Chief Executive Officer:** Ahmed Ali Bawany
Ahmed Ali Bawany - 16.10%	
Rukhsana Omar - 8.52%	
National Investment Unit Trust - 8.48%	
Shahdia Amin - 8.15%	
Ayesha Amin - 7.02%	
Gulshanara Amin - 5.94%	
Roshan Ara Mohd Amin - 5.50%	

APPLICABLE METHODOLOGY(IES)

Applicable Rating Criteria: Corporates (May, 2016)
https://www.vis.com.pk/kc-meth.aspx

Faran Sugar Mills Limited

OVERVIEW OF THE INSTITUTION

Faran Sugar Mills Limited (FSML) is a public limited company and is listed on Pakistan Stock Exchange (PSX).

The company operates under the umbrella of Amin Bawany Group.

RATING RATIONAL

Faran Sugar Mills Limited (FSML) was incorporated in 1981 and is engaged in production and sale of white sugar. FSML operates under the umbrella of Amin Bawany Group that has presence in sugar, ethanol, bakery products, insurance, modaraba and energy. Head office of the company is based in Karachi, while production factory is based in Sheikh Bhirkio, District Tando Mohammad Khan, Sindh.

The company has Long term investments of Rs 1.3b (MY18: Rs. 1.2b), which constitutes around 22.7% (MY18: 20.4%) of the total assets. Equity-accounted investments relate to Unicol Limited, Uni Energy Limited and Uni Food Industries (Private) Limited. Unicol Limited is primarily engaged in the production and sale of Ethanol and has provided regular dividend income stream to Faran Sugar over the last few years. Uni Energy Limited has not commenced its operations yet, whereas Uni Food Industries (Private) Limited is currently in losses, and is being financially supported by the parent company.

Faran Sugar Shareholding		
	MY18	**MY19**
Unicol Limited	33.3%	33.3%
Uni Energy Limited	20.0%	20.0%
Uni Food Industries (Private) Limited	34.7%	34.7%

Capacity Utilization:

FSML installed cane crushing capacity stands at around 10,500 MT per day. Actual sugar production decline by 30% during MY19 vis-à-vis MY18 due to shortage of sugar cane. However, recovery rate marginally improved to 11.005% (MY18: 11.01%) during MY19 and is on the higher side vis-à-vis average industry recovery rate. Going forward, sugar production for MY20 is expected to decline further given the severe shortage of sugar cane in the ongoing year. Nevertheless, VIS expects sugar cultivation and production to increase in MY21 given the significant recent upsurge in prices of sugar cane.

	MY18	**MY19**
Installed cane crushing capacity per day (M.Tons)	10,500	10,500
No. of days Mill operated	142	89
Total crushing capacity on basis of no. of days mills operated (M.Tons)	1,491,000	934,500
Actual crushing (M.Tons)	959,378	670,581
Capacity utilization	64.3%	71.8%
Sugar Production (M.Tons)	105,633	73,696
Recovery (%)	11.01%	11.005%

Business risk

Business risk profile of the sugar sector is considered high given the inherent cyclicality in crop levels and raw material prices. Moreover, distortion in pricing mechanism of raw material prices and refined sugar also creates challenges for sugar mills. Given the decline in area under cultivation in MY19 and the ongoing year and the resultant decline in sugar production, average sugar prices have increased by 19% in MY19 and 16% in the ongoing year. However, increase in profitability is expected to be limited (barring those players that have sizeable carryover stock) due to significant jump in sugar cane prices and decline in recovery ratio (Tiddi Dal pest attack) in the ongoing year. While demand and supply dynamics are expected to result in an increase in sugar prices, significant politicization of sugar prices may cap increase in sugar prices. Recent decline in international sugar prices ($355.6/ton as of 9th March vis-à-vis average price of $413.9/ton in the month of February) is also expected to cap increase in sugar prices given the threat of imports. Business risk profile of FSML draws support from recurring dividend income from investment in Unicol Limited which has consistently contributed to profitability over the last few years. Dividend income from Unicol Limited is expected to decline in the ongoing year given sizeable increase in prices of molasses in the ongoing year.

Financial Profile

Sales Mix

Net Sales of the company was reported Rs. 4.6b (MY18: Rs. 6.3b) during MY19. The decline in net sales by 26.6% can be primarily associated with decline in volumetric sales due to lower production. During MY19, a major proportion of the sugar was sold in the local market, unlike MY18 where a major proportion was exported. Molasses by-product of sugarcane is sold to Unicol Limited at market rate for Ethanol production. While higher average selling prices vis-à-vis corresponding period will support revenue growth, overall revenues are expected to be under pressure given the expected decline in sugar production. Moreover, export sales are also expected to be limited due to recent imposition of ban on sugar exports in February 2020.

Profitability

GP Margin of the company has trended downwards during the outgoing year to 6.1% (MY18: 8.7%). The decline in GP Margin can be associated with the rising cost of sugarcane which was higher than the minimum support price announced by the Sindh Government. Alongwith decline in GP margins, profitability of the Company was also impacted by significant jump in finance cost which almost doubled during the outgoing year. Overall profitability was supported by a one-off reversal of excess cane cost provision.

Going forward, significant increase in cost of production is expected to exert pressure on profitability unless sugar prices increase significantly from current levels. While demand and supply dynamics are expected to result in an increase in sugar prices, significant politicization of sugar prices and active monitoring by the government may cap increase in sugar prices.

Liquidity

Liquidity profile weakened in the outgoing year due to decline in cash generated from operation (before working capital changes and adjusted for reversal of excess cane cost provision). Cash flows were supported by dividend income from investment in Unicol Limited which amounted to Rs. 226.7m. While funds flow from operations depicted a noticeable decline, cash flow generated from operations during MY19 was higher due to sizeable realization of freight subsidy. Current ratio has remained below 1(x) (MY19: 0.93x; MY18: 0.94x) over the last years while coverage of short-term borrowings vis-à-vis inventory and trade debts has remained modest and stood at 78.7% at end-MY19. Incorporating freight subsidy receivable, coverage of short-term borrowings stood at 108%. Going forward, decline in dividend income from Unicol Limited (due to sharp rise in molasses prices), funding requirement of investment in Uni Foods and limited cash flow operations are expected to keep liquidity profile under pressure.

Capitalization

Equity base of the company amounted to Rs. 2.39b (MY19: Rs. 2.32b; MY18: Rs. 2.0b) at end-1Q20. Equity base of the company increased significantly in MY19 primarily on account of profit retention. Total debt of the company was reported at Rs. 0.9b (MY19: 1.8b; MY18: Rs. 2.2b) at end-1Q20. Short term borrowing has witnessed a significant decrease due to declining stock levels resultantly reducing working capital requirement. Resultantly, gearing and leverage ratios reduced to 0.4x (MY19: 0.8x; MY18: 1.1x) and 0.9x (MY19: 1.4x; MY18: 1.8x) respectively at end-1Q20.

Financial Summary (amounts in PKR millions)			Appendix I
	MY17	**MY18**	**MY19**
BALANCE SHEET			
Fixed Assets	1,570.4	1,730.4	1,874.6
Long term Investment	968.4	1,177.4	1,279.4
Stock-in-Trade	2,003.8	1,295.3	1,070.4
Trade Debts	82.0	190.4	128.1
Cash & Bank Balances	70.3	94.9	395.6
Total Assets	5,153.6	5,773.7	5,636.9
Trade and Other Payables	832.3	941.0	966.4
Long Term Debt (including current maturity)	204.2	309.3	242.9
Short Term Debt	2,089.0	1,933.3	1,522.5
Total Debt	2,293.2	2,242.6	1,765.3
Total Liabilities	3,558.3	3,736.2	3,316.8
Paid Up-Capital	250.1	250.1	250.1
Total Equity (without surplus revaluation)	1,595.3	2,037.5	2,320.1
INCOME STATEMENT			
Net Sales	4,435.7	6,291.2	4,619.1
Gross Profit	(97.0)	548.2	283.0
Profit Before Tax	(178.6)	624.4	521.2
Profit After Tax	(184.0)	442.4	380.4
RATIO ANALYSIS			
Gross Margin (%)	-2.2%	8.7%	6.1%
Net Profit Margin	-4.1%	7.0%	8.2%
Current Ratio (x)	0.86	0.94	0.93
Net Working Capital	(433.9)	(171.4)	(192.6)
FFO	(179.6)	368.8	13.5
FFO to Total Debt (%)	-7.8%	16.4%	0.8%
FFO to Long Term Debt (%)	-87.9%	119.2%	5.6%
Debt Servicing Coverage Ratio (x)	(0.4)	2.3	0.8
ROAA (%)	2.0%	5.4%	4.0%
ROAE (%)	5.2%	16.3%	10.4%
Gearing (x)	1.4	1.1	0.8
Leverage (x)	2.2	1.8	1.4

ISSUE/ISSUER RATING SCALE & DEFINITIONS Appendix II

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	Faran Sugar Mills Limited
Sector	Sugar
Type of Relationship	Solicited
Purpose of Rating	Entity Rating
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.
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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
03/20/2020	A-	Stable	A-2	Reaffirmed
02/15/2019	A-	Stable	A-2	Initial

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Muhammad Ayub Warind	CFO	02/20/2020