RATING REPORT

Faran Sugar Mills Limited

REPORT DATE:
August 11, 2021

RATING ANALYSTS:

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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	Negative		Stable	
Rating Date	*August 11 , 2021*		*March 20 , 2020*	

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, 2019)
https://s3-us-west-2.amazonaws.com/backupsqlvis/docs/Corporate-Methodology-201904.pdf

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).

Profile of Chairman
Mr. Amin Bawany serves as Chairman of Faran Sugar Mills and is on the board of directors of FSML since 1984. He is also serving as chairman in the Faran Power Ltd and is the Chief Executive of B.F Modaraba. Also, is on the board of Reliance Insurance Company. Mr. Bawany holds associate degree from the American College of Switzerland.

Profile of CEO Mr. Ahmed Bawany is CEO of Faran Sugar Mills and is on the Board of Directors of FSML since 1995. Erstwhile, Mr. Ahmed served as Chairman of Pakistan Sugar Mills Association-Sindh Zone. He is also director in the associate company-Unicol and UniEnergy. And is on the board of Reliance Insurance Company. Also, Mr. Ahmed is the Chairman of B.F Modaraba and Uni-Food Industries. Mr. Ahmed holds a degree in entrepreneurship from University of Southern California.

RATING RATIONAL

Faran Sugar Mills Limited (FSML) was established in 1981 and is engaged in production and sale of white sugar. FSML is part of the Amin Bawany Group which has presence in sugar, ethanol, bakery products, insurance, modaraba and energy sectors. 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. 1.16b (MY20: Rs. 1.14), which represent around 18% of the total asset base. Equity accounted investments relate to Unicol Limited, Uni Energy Limited and Uni Food Industries (Pvt) Ltd. Unicol Ltd is primarily engaged in the production and sale of Ethanol. And has provided regular dividend income stream and support to profitability of Faran Sugar. Uni Energy Limited has not commenced its operations yet, whereas Uni Food Industries (Pvt) Ltd is currently in losses, and FSM will lend support in the form of increased investment. FSML's shareholding in Unicol, Uni Food Industries and Uni Energy stand at 33.3%, 34.7% and 20%, respectively.

Operating Performance

The company's installed sugar cane crushing capacity stands at 10,500 MT per day. Actual crushing capacity was 1.0m MT (MY20: 1.1m MT) as the mill operated for 98 days (MY20: 105 days) during MY21. Due to sugarcane shortage, the mill crushed 601,717 MT (MY20: 601,936) during MY21. Resultantly, the company produced 63,691 MT (MY20: 65,739 MT) of sugar during MY21. The recovery rate reduced to 10.6% (MY20: 10.9%) during MY21. Going forward, with the indication of a good crop size and attractive sugarcane prices available for the farmers, the production of sugar is likely to grow further during MY22.

	MY20	MY21
Installed cane crushing capacity per day (M.Tons)	10,500	10,500
No. of days Mill operated	105	98
Actual crushing (M.Tons)	601,936	601,717
Sugar Production (M.Tons)	65,739	63,691
Recovery Rate (%)	10.90%	10.59%

Business Risk

The business risk profile of sugar sector is considered high given inherent cyclicality in the crop levels and raw material prices. Moreover, distortion in pricing mechanism of raw material prices and refined sugar also creates challenge 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 5.62m 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. However, sector's risk profile draws support from diversification into distillery, power and other segments.

Profitability of the company under pressure amidst high raw material cost

Net Sales of the company was reported at Rs. 5.7b (MY19: Rs. 4.6b) during MY20. The increase in net sales by 24.5% is primarily associated with higher average selling price of sugar. The company was able to sell 83,476 MT (MY19: 81,566 MY) at an average price of 62,700/ MT (MY19: 51,554/ MT) during MY20. Also, the company sold 27,475 M.Tons (MY19: 31,459 M.Tons) of molasses at an average rate of Rs. 17,219 (MY19: 11,403) during MY20. Despite higher average selling prices, overall gross margins contracted to 4.7% (MY19: 6.1%) in MY20 due to higher prices of sugarcane procured. Along with decline in gross margins, the company witnessed significant decline in share of profits from associated companies (majorly owing to losses in UniFood Industries) and in the absence of one-off liability reversal (of Rs. 557.9m) resulted in Net Loss of Rs. 171.m in MY20 vis-à-vis Net Profit of Rs. 380.4m recorded in MY19.

Profitability in 9M'21 was depressed on account of sales strategy adopted in the beginning of the season whereby the company anticipated stability in sugar prices and offloaded stocks at lower price levels while sugar cane prices continued to surge. The government has fixed the sugar cane support price at Rs. 202/40kg (MY20: 192/40kg) in Sindh for the 2020-2021 crushing season. However, sugarcane was sold at a higher price across all regions than the minimum support price announced by the government due to shortage of sugarcane and quality issues. Hence, FSML procured sugarcane at a higher average rate of Rs. 320/maund (MY20: Rs. 268/maund) during MY21. Resultantly, with dip in margins losses continued in 9M'21 and stood at Rs. 285.6m (9M'20: loss of Rs. 72.3m). The company has around two-fourth of unsold inventory and is likely to incur inventory gains on account of higher prevailing prices of sugar. With improvement in selling prices in the last quarter, company expects Q4 to remain profitability and likely to offset some of the losses booked till date.

Ongoing capex likely to reduce operating cost and enhance by-product bagasse production as well

The company has obtained a long term financing facility of Rs. 700m out of which Rs. 43.8m has been disbursed. The company has replaced old plant and machinery with new and efficient one and is in process of installing 8MW turbines, Polyfill Evaporator and VKD that will reduce bagasse consumption curtailing power cost and ultimately enabling the company to enhance the bagasse sale.

Long-Term Investments in Associated Companies

The company recorded investment income from associates to the tune of Rs. 41m (MY19: Rs. 228m) during MY20. The decline observed in ethanol prices in the period under review contracted profitability of Unicol whereas loss posted by Uni Food Indsutries altogether reduced investment income in MY20 for FSML. Going forward, management expects healthy profits emanating from Unicol, given an increasing trend in Ethanol prices. However, UniFood is expected to post losses for next few years as the company will incur major expenses to expand existing line of production, launch new products, enhance distribution network and conduct extensive marketing campaigns across Pakistan to establish brand image and enhance its national reach.

FSML's Investment Income from Associates	MY18	MY19	MY20	H'MY21
Unicol Ltd	404.7	369.9	174.6	148.4
Uni Energy	-	-	-	-
Uni Food Industries	(109.0)	(142.4)	(133.7)	(71.4)
Total Investment income	**295.6**	**227.6**	**41.2**	**77.0**

Liquidity profile is considered weak due to limited cash flow coverage vis-à-vis outstanding debt obligations.

Liquidity profile remained on the lower side due to decline in cash generated from operations. Funds flow from operations has remained negative in line with the losses. In absolute terms, FFO stood negative at Rs. 128.3m (MY20: Rs. 42.1m; MY19: Rs. 46.5m) during 9M'MY21. Meanwhile, dividend income received from Unicol (9M'21: Rs. 162.5m: MY20: 276.2m) provided support to the bottom line to some extent. The debt service coverage ratio further declined to 0.11x (MY20: 0.9x) during 9M'MY20; it is pertinent to mention that the improvement in Debt Service coverage is necessary to reduce the sensitivity of the ratings at the assigned levels. Current ratio has remained below 1(x) (9M'MY21: 0.83x; MY20: 0.8x; MY19: 0.93x) over the last years and coverage of short-term borrowings vis-à-vis inventory and trade debts has remained on lower side and stood at 64% at end-9M'MY21. Going forward, funding requirement of investment in Uni Foods and limited cash flow operations are likely to keep liquidity profile under pressure.

Capitalization indicator to remain elevated

Equity base of the company exhibit declining trend on a timeline basis (9M'MY21: Rs. 1.84b; MY20: Rs. 2.12b; MY19: Rs. 2.32b) owing to losses booked during 9M'MY21 and MY20. Total debt of the company jumped significantly at end-Jun'21 to Rs. 3.8b (MY20: Rs. 1.6b). The increase in debt was primarily manifested in short term borrowing (9M'MY21: Rs. 3.5b; MY20: Rs.1.4b) to fund high stock levels. The company has obtained TERF of Rs. 700m having 10 year tenure including 2 years of grace period ending Nov'23 with a markup of SBP rate of 1% plus 1.75% spread. With greater increase in borrowings vis-à-vis equity, gearing and leverage ratios stood higher at 2.13x (MY20: 0.77x; MY19: 0.76x) and 2.98x (MY20: 1.15x; MY19: 1.43x), respectively as at end Mar'21. Improvement in liquidity and leverage indicators is considered important from a ratings perspective.

Financial Summary (amounts in PKR millions)
Appendix I

	MY18	MY19	MY20	9M'MY21
BALANCE SHEET				
Fixed Assets	1,730.4	1,874.6	1,884.9	1,948.9
Long term Investment	1,177.4	1,279.4	1,141.8	1,157.1
Stock-in-Trade	1,295.3	1,070.4	384.6	2,153.4
Trade Debts	190.4	128.1	183.3	69.4
Cash & Bank Balances	94.9	395.6	160.3	100.8
Total Assets	5,773.7	5,636.9	4,563.2	6,437.8
Trade and Other Payables	941.0	966.4	360.3	291.5
Long Term Debt (including current maturity)	309.3	242.9	247.6	340.2
Short Term Debt	1,933.3	1,522.5	1,394.0	3,489.7
Total Debt	2,242.6	1,765.3	1,641.6	3,829.9
Total Liabilities	3,736.2	3,316.8	2,438.7	4,598.7
Paid Up-Capital	250.1	250.1	250.1	250.1
Total Equity (without surplus revaluation)	2,037.5	2,320.1	2,124.5	1,839.1
INCOME STATEMENT				
Net Sales	6,291.2	4,619.1	5,751.4	3,526.1
Gross Profit	548.2	283.0	268.5	31.8
Profit Before Tax	624.4	521.2	(151.8)	(228.0)
Profit After Tax	442.4	380.4	(171.3)	(285.6)
RATIO ANALYSIS				
Gross Margin (%)	8.7%	6.1%	4.7%	0.9%
Net Profit Margin	7.0%	8.2%	-3.0%	-8.1%
Net Working Capital	(171.4)	(192.6)	(389.9)	(663.4)
FFO	368.8	32.4	46.5	(128.3)
FFO to Total Debt (%)	16.4%	1.8%	2.8%	
FFO to Long Term Debt (%)	119.2%	13.4%	18.8%	
Debt Servicing Coverage Ratio (x)	2.3	0.9	0.9	0.11*
ROAA (%)	8.1%	6.7%	-3.4%	-5.3%*
ROAE (%)	24.4%	17.5%	-7.7%	-20.0%*
Current Ratio	0.9	0.9	0.8	0.8
Gearing (x)	1.1	0.8	0.8	2.1
Leverage (x)	1.8	1.4	1.1	2.50
Inventory plus receivables/ST debt	77%	79%	41%	64%

**annualized ratios*

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
Rating History	see table below
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
08/11/2021	A-	Negative	A-2	Maintained
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	CFO	19/Jul/2021
2.	Mr. Atif Dhedhi	Manager Finance	19/Jul/2021