RATING REPORT

FARAN SUGAR MILLS LIMITED

REPORT DATE:
October 31, 2022

RATING ANALYST:

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RATING DETAILS				
Rating Category	Latest Ratings		Previous Ratings	
	Long-term	Short-term	Long-term	Short-term
Entity	A-	A-2	A-	A-2
Rating Date	*October 31, 2022*		*August 11, 2021*	
Rating Action	Reaffirmed		Maintained	
Rating Outlook	Negative		Negative	

COMPANY INFORMATION	
Incorporated in 1981	**External auditors:** Rahman Serfaraz Rahim Iqbal Rafiq Chartered Accountants
Unquoted Public Limited Company	**Chairman of the Board:** Muhammad Omar Amin Bawany
Key Shareholding	**Chief Executive Officer:** Ahmed Ali Bawany
Ahmed Ali Bawany - 16.10%	
Shahdia Amin – 10.25%	
Gulshanara Amin – 9.19%	
Ayesha Amin – 9.14%	
Rukhsana Omar - 8.52%	
National Investment Unit Trust - 8.48%	
Roshan Ara Mohd Amin - 5.85%	

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

FARAN SUGAR MILLS LIMITED

OVERVIEW OF THE INSTITUTION

Faran Sugar Mills Limited (FSML) was incorporated in November 3, 1981 and commenced commercial operations on November 25, 1981. The principal business activity of the company is manufacturing and selling of White Refined Sugar.

Profile of the Chairman

Muhammad Omar Amin Bawany is the Chairman of Board of Director at FSML. He went to American College of Switzerland to obtain Associate Degree. He is also on the board of Reliance Insurance Company, Unicol Limited and Uni Foods Industries Ltd.

Profile of the CEO

Mr. Ahmed Ali Bawany has been serving FSML as the Chief Executive since 1995. He has a Degree in Business Entrepreneurship from University of South California. He previously held directorship in Reliance Insurance Company, Unicol Limited and Uni Foods Industries Ltd

RATING RATIONALE

Incorporated in 1981, Faran Sugar Mills Limited ('FSML' or 'the Company') commenced commercial operations in 1981. The principal business of the Company is manufacture and sale of white refined sugar. The registered office of the Company is located in Karachi, Sindh and manufacturing unit is located at Shaikh Bhirkio District Tando M. Khan.

Sector Update

Table 1: Area Under Cultivation and Sugarcane Production

	Area Under Cultivation (Hect)			Production (Tonnes)		
	2018-19	**2019-20**	**2020-21**	**2018-19**	**2019-20**	**2020-21**
Punjab	710,610	643,430	776,980	44,906,310	43,346,580	57,000,000
Sindh	279,472	286,090	279,694	16,691,323	17,233,832	18,335,533
KPK	110,991	109,359	107,438	5,532,012	5,753,957	5,627,545
Baluchistan	N/A	N/A	N/A	N/A	N/A	N/A
Total	1,101,073	1,038,879	1,164,112	67,129,645	66,334,369	80,963,078

Source - PSMA

- Pakistan is the 6th largest sugar producer and 8th largest sugar consumer in the world. Sugar production is the second largest agricultural industry in Pakistan after textile. Pakistan's sugarcane production stood at ~81m MTs in MY21, up 22% YoY given expansion in area under cultivation following assurances from Government of Pakistan (GoP) of affixing Minimum Support Price (MSP) for sugarcane and higher retail price for sugar.
- Punjab has the highest sugarcane production, comprising two-third of the aggregate sugarcane output in MY21, followed by Sindh (25%), KPK (8%) and Baluchistan (<1%).

Table 2: Domestic Production, Supply and Demand of Sugar

In MT '000s	MY20	MY21	MY22*
Beginning Stocks	1920	1,685	2,752
Total Sugar Production	5,400	6,505	7,160
Total Imports	40	312	-
Total Supply	7,360	8,502	9,912
Total Exports	75	-	-
Human Domestic Consumption	5,600	5,750	5,900
Total Use	5,600	5,750	5,900
Ending Stocks	1,685	2,752	3,512

Source- USDA
*Provisional

- Refined sugar production increased by 20% in MY21, given further expansion in area under cultivation. Given the sugar shortfall in MY20, the GoP banned export of sugar in February 2020 on recommendations of Sugar Advisory Board (SAB) to arrest the pricing uptick. As such, there is no restriction on the import of sugar, though prior permission is required from the Economic Coordination Committee (ECC) to control its inflow. Sugar imports was minimal during MY22, due to the high sugar production, which has consistently translated in an increase in carry-over stock.
- Sugar prices in Pakistan have depicted volatility historically, given demand/supply gap and market inefficiencies. The provincial government sets the MSP for the sugarcane, incorporating cost of production of farmers. During the last 3-year period (MY20-22), MSP has increased notably to encourage farmers for sugar production, as they were

moving towards alternate crop cultivation given lower profitability in sugarcane. Therefore, with increase in MSP, retail price has also escalated.

- Punjab and KPK sugarcane indicative price is Rs. 225/40kg, which is 12.5% higher than preceding year, while pricing in Sindh posted a YoY increase of 23.8%, to Rs. 250/40kg bag.

Table 3: Sugarcane Indicative Price and Retail Average Price

Year	Sugar Price (Rs.)			Season Avg. Retail/KG (Rs.)
	Punjab	Sindh	KPK	
2016-17	180	182	180	64.94
2017-18	180	182	180	53.7
2018-19	180	182	180	59.84
2019-20	190	192	190	76.6
2020-21	200	202	200	93.5
2021-22	225	250	225	-

Source - PSMA

- The recent flood has manifested devastating effects on the agricultural output including sugarcane. Sindh, which accounts for 31% of national aggregate sugarcane production, was the most affected area in terms of agricultural damage.
- Sugarcane is mainly grown in northeast region of Pakistan, where impact of flood was minimal. However, sugarcane area in Sindh has been affected, where loss is estimated at ~10.5m MTs i.e. 61% of the projected sugarcane production valued at USD 273m. The sugarcane losses in Punjab region are still under scrutiny, as officials are still estimating the numbers.
- Sugar consumption, which follows the population growth trajectory, is projected to increase by 5% in MY23 to 6.2m MTs.
- Given the higher carry-over stocks, there are ongoing discussions between the Sugar Advisory Board (SAB) and Pakistan Sugar Mills Association (PSMA) to allow export of sugar. In case the same materialized, it would have a positive impact of the profitability of sugar companies.

Business Update – FSML

Table 4: Installed Capacity and Production

Particulars	MY20	MY21	9M'MY21	9M'MY22
Installed Capacity				
Installed Crushing Capacity	1,620,000	1,620,000	1,620,000	1,620,000
Sugar Production Capacity	176,580	176,580	176,580	176,580
Total Production Days	180	180	180	180
Actual Production				
Cane Crushed	601,936	601,717	601,717	845,437
Days Worked	105	98	98	129
Actual Recovery Percentage	10.92%	10.58%	10.58%	10.98%
Actual Production (from sugar cane only)	65,739	63,691	63,691	92,862
Capacity Utilized (based on sugarcane crushing)	37.23%	36.07%	36.07%	52.59%

- Given the increase in sugarcane production across the country, the mill crushed 845,437 MTs during 9M'MY22 (9M'MY21: 601,717), up 41% vis-à-vis SPLY. The higher crushing quantum and improved recovery ratio allowed the Company to increase production quantum by 46% during 9M'MY22 vis-à-vis SPLY.
- Going forward, the Company's ability to secure adequate sugarcane for operations in MY23 is dependent on circumstances, such as progress in flood water drainage and availability of fields in time, which is likely to be challenging particularly in Southern Sindh, where FSML is situated. The management is confident of sugarcane availability. However, VIS views this as a concern, and will continue to monitor the same on an ongoing basis.

Sales & Operations

Table 5: P&L Extract

(In Rs. Millions)	MY19	MY20	MY21	9M'MY21	9M'MY22
Sales	4,619	5,751	4,860	3,526	4,956
GP Margin	6.1%	4.7%	0.8%	0.9%	11.4%
EBIT	604	108	(150)	(130)	429
Net Margin	8.2%	-3.0%	-7.6%	-8.1%	5.0%

- Net Sales of the Company was reported at Rs. 4,956m (9M'MY21: Rs. 3,526m) during 9M'MY22, up 41% from SPLY. The uptick in topline was mainly contributed by higher pricing.
- Gross margin has depicted volatility over the years, and net margin has remained negative over the past couple of years. As per management, the margins in the past 2 years were impacted by advance sales agreements and volatility in pricing, wherein FSML's pre-existing pricing was on the lower side. During 9M'MY22, given high quantity of carry over stock and rising trend in pricing, the profitability margin has depicted notable improvement is likely. The management is confident of posting a positive net margin for MY22.

Cash Flow Coverages

Table 6: Cash Flows Coverages

(In Million Rs.)	MY19	MY20	MY21	9M'MY22
FFO	541	14	(252)	375
FFO/Total Debt	30.7%	0.9%	-7.7%	9.1%*
FFO/Long Term Debt	222.8%	5.7%	-26.7%	40.9%*
DSCR (x)	2.20	0.83	(0.05)	1.98*
Current ratio (x)	0.93	0.80	0.87	0.88
(Stock in trade + debt)/STD	0.79	0.41	0.51	0.87

Annualized*

- Funds from Operations (FFO) escalated amidst 9M'MY22, given the improvement in profitability margins. Accordingly, DSCR rose to 1.98x 9M'MY22, notably improving from MY21. As DSCR in preceding year was negative, the debt repayment was done on the back of additional short-term borrowing.
- Going forward, the Company's cash flow coverage indicators are expected to improve, given higher profitability outlook, expectation of increased profitability from Subsidiary i.e. Unicol limited, which is an Ethanol exporter and a downstream company of FSML. Furthermore, historically, the Company's profitability was consistently being depressed on account of losses on Unifoods, which was sold during 9M'MY22 for Rs. 205m to Sunridge Foods (Pvt) Limited.

Capitalization

Table 7: Balance Sheet Extract

(In million Rs.)	Sep'19	Sep'20	Sep'21	Jun'22
Total Assets	5,637	4,563	5,699	8,665
Total Liabilities	3,317	2,439	3,944	6,661
Total Equity	2,320	2,124	1,755	2,003
Total Debt	1,765	1,642	3,274	5,477
- **Short Term Debt**	1,522	1,394	2,330	4,259
- **Long term Debt**	243	248	944	1,218
Gearing Ratio	0.76	0.77	1.86	2.73

- Given the stress on profitability, the Company's reliance on debt financing increased, which is reflected in terms of increase in gearing. During MY21, the Company obtained Rs. 500m worth of Diminishing Musharaka for procurement of Plant and Machinery. Additionally, the Company also raised further long-term debt of Rs. 600m under ITERF for 10 years at a markup rate of 2.75% of which Rs. 377.9m has been disbursed.
- Going forward, the management has envisaged the gearing to reduce, on the back of profit retention, to 1.5x during the course of the rating horizon. Given a stronger profitability outlook, maintaining gearing should not be a challenging task, albeit reducing gearing may be challenging given the likely higher running finance requirements. VIS views the elevated gearing as a risk, and would continue to monitor the financial risk profile of the Company on an ongoing basis.

Key Rating Drivers - FSML

Rating incorporate track record of sponsors
The assigned ratings take into account satisfactory operating track record, and extensive experience of sponsors in the sugar sector.

Rating take into account business risk profile of Sugar Sector

VIS classifies the business risk profile of Sugar sector as 'Medium', which incorporates high cyclicality medium competition, capital intensity and technology risk, low energy sensitivity and high regulatory risk. Business risk profile of FSML is diversified, given additional revenues from ethanol sales through Unicol Limited, which are sizable. Given the sale of Uni Food Industries recently, which was a loss making entity, business risk has improved.

Ratings incorporate elevated financial risk profile of the Company

Given the stress on profitability, the Company's reliance on debt financing increased, which is reflected in terms of increase in gearing. Going forward, the management has envisaged the gearing to reduce on the back of improved profitability outlook. The rating incorporates improvement in cash flow coverage indicators and envisaged improvement in gearing.

Faran Sugar Mills Limited Appendix I

FINANCIAL SUMMARY				*(amounts in PKR millions)*
BALANCE SHEET	**Sep'19**	**Sep'20**	**Sep'21**	**Jun'22**
Fixed Assets	1,875	1,885	2,184	2,674
Stock-in-Trade	1,070	385	1,046	3,567
Trade Debts	128	183	144	142
Cash & Bank Balances	396	160	139	97
Total Assets	5,637	4,563	5,699	8,665
Trade and Other Payables	966	360	249	596
Long Term Debt	243	248	944	1,218
Short Term Debt	1,522	1,394	2,330	4,259
Total Debt	1,765	1,642	3,274	5,477
Paid-up Capital	250	250	250	250
Total Equity	2,320	2,124	1,755	2,003

INCOME STATEMENT	**MY19**	**MY20**	**MY21**	**9M'MY21**	**9M'FY22**
Net Sales	4,619	5,751	4,860	3,526	4,956
Cost of sales	5,743	4,336	5,483	4,820	3,228
Gross Profit	283	269	40	32	563
Operating Profit	85	93	(174)	(140)	399
Finance Cost	310	301	260	176	307
Profit before Tax	521	(152)	(390)	(228)	415
Profit After Tax	380	(171)	(371)	(286)	250

RATIO ANALYSIS	**MY19**	**MY20**	**MY21**	**9M'MY21**	**9M'FY22**
Gross Margin (%)	6.1%	4.7%	0.8%	0.9%	11.4%
Net Margin (%)	8.2%	-3.0%	-7.6%	-8.1%	5.0%
Net Working Capital	(193)	(390)	(350)	(663)	(618)
FFO	541	14	(252)	(128)	(375)
FFO to Total Debt (%)	30.7%	0.9%	-7.7%	-4.5%*	9.1%*
FFO to Long Term Debt (%)	222.8%	5.7%	-26.7%	-50.1%*	40.9%*
Debt Servicing Coverage Ratio (x)	2.20	0.83	(0.05)	(0.04)*	1.98*
Current Ratio (x)	0.93	0.80	0.87	0.83	0.88
Leverage (x)	1.43	1.15	2.25	2.50	3.33
Gearing (x)	0.76	0.77	1.86	2.08	2.73
ROAA (%)	6.7%	-3.4%	-7.2%	-5.3%*	4.1%*
ROAE (%)	17.5%	-7.7%	-19.1%	-19.5%*	17.2%*
(Stock in trade + trade debts)/STD	0.79	0.41	0.51	0.64	0.87

**Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITION 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	Faran Sugar Mills Limited				
Sector	Sugar Industry				
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				
	31-10-2022	A-	A-2	Negative	Reaffirmed
	11-08-2021	A-	A-2	Negative	Maintained
	20-03-2020	A-	A-2	Stable	Reaffirmed
	20-02-2019	A-	A-2	Stable	Initial
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 Meeting Conducted	**Name**	**Designation**	**Date**		
	Mr. Muhammad Ayub	Chief Financial Officer & Company Secretary	**30-September-2022**		
	Mr. Atif Dhedhi	Manager Finance			