RATING REPORT

JDW Sugar Mills Limited (JDWS)

REPORT DATE:
December 07, 2023

RATING ANALYST:

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RATING DETAILS				
Rating Category	**Latest Rating**		**Previous Rating**	
	Long-term	**Short-term**	**Long-term**	**Short-term**
Entity	A+	A-1	A+	A-1
Rating Outlook	*Stable*		*Stable*	
Rating Action	Reaffirmed		Upgrade	
Rating Date	*17th May'23*		*15th April'22*	

SUKUK RATING DETAILS	
Rating Category	**Preliminary**
	Short-term
Entity	A-1
Rating Action	Preliminary
Rating Date	*07th December 2023*

COMPANY INFORMATION	
Incorporated in 1990	**External auditors:** Riaz Ahmad, Saqib, Gohar & Co. Chartered Accountants.
Public Limited Company	**Chairman of the Board:** Mukhdoom Syed Ahmed Mahmud
Key Shareholders (with stake 5% or more):	**Chief Executive Officer:** Mr. Raheal Masud
Directors, CEO, and their spouse and minor children – 47.8%	
General Public – 44.4%	

APPLICABLE METHODOLOGY

VIS Entity Rating Criteria: Corporates (May 2023)
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

Rating The Issue (August 2023)
https://docs.vis.com.pk/docs/Rating-the-Issue-Aug-2023.pdf

VIS Rating Scale
https://docs.vis.com.pk/docs/VISRatingScales.pdf

JDW Sugar Mills Limited (JDWS)

OVERVIEW OF THE INSTITUTION

JDWS was incorporated as a private limited company in May, 1990 under the Companies Ordinance, 1984 (Repealed with enactment of the Companies Act 2017) and was subsequently converted into a public limited company in August, 1991.

Profile of Chairman

Mr. Mukhdoom Syed Ahmed Mahmud is a renowned political figure. He served as Governor of Punjab during 2012-2013.

RATING RATIONALE

JDW Sugar Mills Limited ('JDWS' or the 'Company') is a part of JDW Group. The group has a presence in sugar, corporate farming and power generation. JDWS is principally engaged in manufacturing of sugar, production of electricity and managing corporate farms.

Proposed Short-term Sukuk ('ST Sukuk'):

- JDWS plans to raise a rated, unsecured, privately placed ST Sukuk, structured on the basis of Musharakah (Shirkat-ul-Aqd) ("Musharaka Structure") to be issued as a redeemable capital (under Section 66 of the Companies Act 2017), amounting up to Rs. 5b to Rs. 8b (inclusive of a Green Shoe Option of up to Rs. 3b – Rs. 4b) to finance working capital requirements of the Company related to sugar production and sales.
- Tenor of the instrument is up to six (06) months from the date of disbursement of Issue (Issue Date).
- Principal will be redeemed in bullet payment six (06) months after the Issue Date.
- Profit rate on the instrument would be 6M KIBOR + 90 bps per annum.
- Profit will be payable at the time of redemption of ST Sukuk on the outstanding principal amount.
- The structure of ST Sukuk was developed under the advisory of Al- Hilal Shariah Advisors.

Sector Update

Pakistan is the seventh-largest producer and the fifth-largest consumer of sugar. According to the Economic Survey of Pakistan, sugar industry is the country's second-largest agro-based business after the textile industry. In terms of sugarcane production, Punjab produces 67% of the sugarcane, followed by Sindh (25%), Khyber Pakhtunkhwa (KPK) (8%), and Baluchistan (less than 1%). Its production contributes 0.8% to GDP and 3.7% to agriculture's value addition.

According to a report released by the US Department of Agriculture (USDA) on April 12, 2023, it anticipates that sugar production in Pakistan for the 2023/24 period will reach 7.05 million tonnes, marking a 3% increase compared to the estimated production in 2022/23. This modest upswing is attributed to the expected recovery in the harvested cane area, particularly in contrast to the flood-impacted crop of 2022/23.

Sugar consumption in 2023/24 is projected to stand at 6.3 million tonnes, reflecting a 3% uptick from the previous year (2022/23). This increase is primarily attributed to population growth. However, sugar exports in the 2023/24 period are expected to be lower than 2022/23 (projected at 800,000 tonnes), mainly due to Governments concern over potential domestic shortages and resultant price surge. Pakistan's sugar export during FY23 stood at 215,751 tonnes fetching USD 104 million against nil exports in FY22.

Price escalation in the domestic market has been impacted by substantial cross-border outflows due to import price differential, with international sugar prices fluctuating up to Rs 250/kg. Other factors contributing to the price hike has been the unpredictability of the high dollar exchange rate, along with increases in prices for petroleum and oil products (POL), exceptionally high bank interest rates, rising wage levels, the constant upward trajectory of prices for various other commodities, and the soaring costs of electricity. For the upcoming season, prices are expected to remain elevated with support price for sugarcane crop set at Rs. 400/maund for Punjab and Rs. 425/ maund for Sindh which is much higher than last year's rate. Government policy with respect to price control will remain critical.

Key Rating Drivers

Ratings incorporate business risk profile of the sugar sector

The inherent cyclicality in crop yields and raw material prices is believed to have a substantial impact on the business risk profile of the sugar sector. Furthermore, there is a noticeable difference in pricing mechanisms, with the price of the end product, granulated sugar, being set by market forces whereas sugarcane cost being regulated by the government. A typical sugarcane crop has a 3- to 5-year production cycle, with government assistance to farmers and crop productivity playing a major role.

Strong sponsor support

The assigned ratings incorporate JDWS market position as the leading player in the country's sugar industry, significant experience of sponsors in the sugar and agriculture sector and a professional management team. The Company has longstanding relationships with growers along with focus on research activities in sugarcane development. Business risk profile of the Company draws support from diversification of operations into power sector.

Profitability is expected to strengthen largely in tandem with rising trend in sugar prices and inventory gains

At the end of 9M'MY23, net sales amounted at Rs. 56.1b (9M'MY22: Rs 46.9b), recording a 19.6% increase over same period last year. The same is projected to increase to ~Rs 72b. This was driven by volumetric growth and nearly 12.95% increase in net average selling price. The average sugarcane procurement cost was also reported higher at Rs. 315 per maund, largely due to increase in support price in the outgoing season. However, while margins at the end of third quarter were lower at 13.0% compared to last year, the uptick in prices in the last quarter is expected to improve margins to ~15% (MY22: 15.5%). The distribution and administrative expenses were also rationalized with inflationary pressure. Other operating expenses reported a decline, primarily attributed to a substantial reduction in allowances for expected credit losses. Moreover, other income also registered a decline on account of fair value loss against agriculture produce. Finance costs saw a significant increase, reaching Rs. 4.2b in 9M'MY23, resulting in a lower profit after taxation of Rs. 1.5b (9M'MY22: Rs 3.7b) and a net profit margin of 2.6%.

In MY23 & MY24, management expects an uptick in profitability, stemming from the increase net average selling price of sugar, high sucrose recovery rate and gains from carry forward inventory. Increase in selling price is expected due to recent hike of the support price by the government on sugarcane. The increase in the bottom line is expected to be a consequence of a trickle-down effect, with the only caveat being the imposition of high income tax.

Sound cash coverage cash flow

As per 9M'MY23, Funds from Operations (FFO) were down to Rs. 3.0b primarily due to reduced profitability. However, management expects that with the reduction in overall debt at the year end, FFO to total debt and long-term debt is expected to improve to ~0.38x (Sept'22: 0.29x) and 0.65x (Sept'22: 0.57x), respectively. Additionally, Debt Service Coverage Ratio (DSCR) remains comfortable at 1.2x. Liquidity of the Company remains sound. Ratings draw comfort from liquidity cushion arising from sizeable unsold stock anticipated to be sold at higher prices. Short-term borrowing coverages also remain comfortable.

Capitalization metrics to improve

Despite profits, the equity base of the Company decreased to Rs. 16.2b (Sept'22: Rs 16.9b) as a result of higher dividend payout at the end of Q3'MY23. The overall debt profile was elevated as of Jun'23 primarily from borrowings against unsold inventory. As per management, a sizeable inventory has been sold in the last quarter, cash flows from which have been diverted to reduce debt levels, thereby improving debt profile substantially. Gearing and leverage indicators as of Jun'23 were recorded at 1.92x and 2.95x, respectively. The same are expected to reduce and range bound around 1.0x and 2.2x respectively at year-end. The Company has strong growth plans and while capitalization metrics in the medium term may increase due to additional capex borrowing, maintenance of capitalization profile in line with the benchmarks for the assigned ratings will remain important.

Regulatory matter update related to the imposed penalty

The ratings have incorporated the developments in relation to penalties imposed by Competition Commission of Pakistan (CCP) on selected sugar mills and the subsequent legal proceedings initiated by the subject Company. The impact of the imposed penalty amounting Rs. 8.2b on JDWS would be significant. However, the Company has filed an appeal before the Competition Appellate Tribunal against the order of CCP. 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. 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.

Corporate Governance

The Board comprises seven members including Chairman and CEO. There are two independent members on the Board and a female representation. During MY22, nine Board meetings were held. The minutes of the meetings were appropriately recorded and circulated while the attendance of Board members remained satisfactory. The Board has constituted Audit Committee, Human Resource & Remuneration Committee, Nomination Committee and Risk Management Committee in line with Code of Corporate Governance for adequate Board oversight.

JDW Sugar Mills Limited — Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*				
BALANCE SHEET	**MY20**	**MY21**	**MY22**	**9M'MY23**
Property Plant and Equipment	20,772	19,671	19,335	20,220
Right-of-Use Assets	1,176	1,880	1,599	2,066
Investment Property	186	186	186	318
Long-term Investment	1,083	1,084	1,084	1,084
Intangibles	615	613	611	609
Stores, Spares, and Loose Tools	1,541	1,382	1,916	2,632
Stock-in-Trade	3,985	1,880	12,146	25,778
Trade Debts	8,452	4,196	3,552	4,493
Biological Assets	1,820	2,335	2,855	2,270
Short-term Investment	570	652	652	1,002
Cash & Bank Balances	129	247	290	1,010
Other Assets	764	1,420	2,270	2,397
Total Assets	**41,093**	**35,546**	**46,496**	**63,879**
Trade and Other Payables	2,252	2,200	3,028	3,298
Advances from Customers	2,678	1,064	2,518	11,857
Long-Term Debt *(including current maturity)*	15,809	14,477	11,887	10,635
Short-Term Debt	9,308	3,015	11,034	20,406
Total Debt	25,117	17,492	22,921	31,042
Other Liabilities	1,473	342	1,123	1,491
Total Liabilities	31,520	21,098	29,590	47,688
Tier-I/Total Equity	**9,573**	**14,448**	**16,905**	**16,191**
Paid Up-Capital	598	598	598	578
INCOME STATEMENT	**MY20**	**MY21**	**MY22**	**9M'MY23**
Net Sales	52,270	56,800	58,888	56,141
Gross Profit	7,402	10,136	9,150	7,273
Other Expense	584	3,693**	393	89
Other Income	860	2,211	1,968	580
Finance Cost	3,550	2,252	3,404	4,161
Profit Before Tax	2,421	4,447	5,113	1,686
Profit After Tax	1,399	4,878	3,951	1,478
FFO	3,404	8,024	6,742	3,044
RATIO ANALYSIS	**MY20**	**MY21**	**MY22**	**9M'MY23**
Gross Margin (%)	14.5	17.8	15.5	13.0
Net Profit Margin (%)	2.7	8.6	6.7	2.6
Net Working Capital	(932)	961	2,350	(2,002)
Current Ratio (x)	0.95	1.09	1.11	0.95
Cash Conversion Cycle (days)	96	46	56	108*
FFO to Long Term Debt (x)	0.22	0.55	0.57	0.38*
FFO to Total Debt (x)	0.14	0.46	0.29	0.13*
Debt Servicing Coverage Ratio (x)	0.60	1.70	1.21	1.13*
Gearing (x)	2.62	1.21	1.36	1.92
Leverage (x)	3.29	1.46	1.75	2.95
Inventory plus Receivables/Short-term Borrowings (x)	1.34	2.02	1.42	1.48

**Annualized*

*** includes write-off amounting Rs. 3.3b against receivable from CPPA-G*

REGULATORY DISCLOSURES — Annexure II

Name of Rated Entity	JDW Sugar Mills Limited (JDWS)
Sector	Sugar
Type of Relationship	Solicited
Purpose of Rating	Entity Ratings & Sukuk Rating

Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
05/17/2023	A+	A-1	Stable	Reaffirmed
04/15/2022	A+	A-1	Stable	Upgrade
07/27/2021	A	A-2	Stable	Reaffirmed
04/27/2020	A	A-2	Stable	Reaffirmed
03/13/2019	A	A-2	Stable	Downgrade
10/31/2017	A+	A-1	Stable	Reaffirmed
04/13/2017	A+	A-1	Stable	Upgrade
10/27/2015	A	A-1	Positive	Reaffirmed
02/17/2015	A	A-1	Positive	Maintained
10/7/2013	A	A-1	Stable	Reaffirmed
09/5/2012	A	A-1	Stable	Reaffirmed
08/16/2011	A	A-1	Stable	Upgrade
RATING TYPE: SUKUK				
12/07/2023		A-1		Preliminary

Instrument Structure	JDW Sugar Mills Limited ("JDWS" or the "Company") intends to issue a Rated, Unsecured and Privately Placed Sukuk, structured on the basis of Musharakah (Shirkat-ul-Aqd) ("Musharaka Structure") to be issued as a redeemable capital (under Section 66 of the Companies Act 2017) of up to PKR 5b-8b (inclusive of a Green Shoe Option of up to PKR 3b-4b). The funds will be will be utilized for fulfilling the working capital requirements of the Company related to sugar production and sales. The issue has a tenor of six (06) months from the Issue Date. The principal will be redeemed as bullet payment six (06) months after the Issue Date. Profit will be payable at the time of redemption of ST Sukuk on the outstanding principal amount with a base rate of 6-Month KIBOR plus a spread of 0.90% per annum. The ST Sukuk is Unsecured on best effort basis.
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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