

RATING REPORT

JDW Sugar Mills Limited (JDWS)

REPORT DATE:

January 25, 2024

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	17 th May'23		15 th April'22	

SUKUK RATING DETAILS

Rating Category	Final	Preliminary
	Short-term	Short-term
Entity	A-1	A-1
Rating Action	Final	Preliminary
Rating Date	25 th January 2024	07 th 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JDWS was incorporated as a private limited company in May, 1990 under the Companies Ordinance, 1984 (Repealed with enactment of the Companies Act 2017) and was subsequently converted into a public limited company in August, 1991.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.

Short-term Sukuk ('ST Sukuk'):

- JDWS has issued a rated, unsecured, privately placed Short-Term Sukuk (STS) on December 18, 2023, based on Musharakah (Shikat ul Aqd) framework. This issuance, structured as a redeemable capital under Section 66 of the Companies Act 2017, amounts to Rs. 8b (inclusive of a Green Shoe Option of Rs. 3b) 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.
- Maturity Date is falling on June 14, 2024.
- 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 cyclicity 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 MY23, net sales amounted at Rs. 72.3b (MY22: Rs 58.9b), recording a 22.8% increase over same period last year. This was driven by volumetric growth and increase in net average selling price. However, gross margins were slightly lower at 14.3% compared to last year 15.5% as a result of overall increase in cost of production due to inflationary impact. 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 mainly on account of fair value loss against agriculture produce. Finance costs saw a significant increase, reaching Rs. 5.4b in MY23, resulting in a lower profit after taxation of Rs. 2.2b (MY22: Rs 4.0b) and a net profit margin of 3.0% (MY22: 6.7%). In MY24, management expects an uptick in profitability, stemming from the increase in average selling price of sugar, high sucrose recovery rate and gains from carry forward inventory.

Sound cash coverage cash flow

In MY23, Funds from Operations (FFO) declined to Rs. 3.5b (FY22: Rs. 6.7b) primarily due to lower profitability. Moreover, even though there was reduction in overall debt at the year end, FFO to total debt and long-term debt have decreased to 0.21x (Sept'22: 0.29x) and 0.38x (Sept'22: 0.57x), respectively. Additionally, Debt Service Coverage Ratio (DSCR) has weakened to 0.93x (FY22: 1.21x) due to reduced FFO and increased long-term repayments as part of the debt re-profiling strategy. However, ratings draw comfort from liquidity cushion arising from sizeable unsold stock anticipated to be sold at higher prices. Short-term borrowing coverage has remained comfortable on a timeline basis.

Capitalization metrics to improve

Despite profits, the equity base of the Company decreased to Rs. 16.0b (Sept'22: Rs 16.9b) as a result of higher dividend payout and own shares purchased and cancelled during MY23. The overall debt profile has also reduced as of Sept'23 primarily due to high influx of advances received from customer which was utilized for working capital requirement. Resulting in an improvement in gearing to 1.03x (Sept'22: 1.36x), however leverage indicator has increased to 2.25x (Sept'22: 1.75x) as of Sept'23.

Going forward, the Company plans to secure additional long term borrowing for capital expenditure (CAPEX) aimed at establishing an Ethanol/ Distillery having per day production capacity of 200k-230k liters. The expected Commercial Operation Date (COD) by January 2025. Hence, capitalization

metrics in the medium term may increase due to additional capex borrowing, maintenance of capitalization profile in line with 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 eight members including Chairman and CEO. There are two independent members on the Board and a female representation. During MY23, twelve 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, Risk Management Committee and Corporate Social Responsibility Committee in line with Code of Corporate Governance for adequate Board oversight.

JDW Sugar Mills Limited
Annexure I

FINANCIAL SUMMARY (amounts in PKR millions)				
<u>BALANCE SHEET</u>	MY20	MY21	MY22	MY23
Property Plant and Equipment	20,772	19,671	19,335	19,513
Right-of-Use Assets	1,176	1,880	1,599	2,540
Investment Property	186	186	186	318
Long-term Investment	1,083	1,084	1,084	1,050
Intangibles	615	613	611	609
Stores, Spares, and Loose Tools	1,541	1,382	1,916	2,428
Stock-in-Trade	3,985	1,880	12,146	15,823
Trade Debts	8,452	4,196	3,552	3,178
Biological Assets	1,820	2,335	2,855	3,606
Short-term Investment	570	652	652	1,068
Cash & Bank Balances	129	247	290	159
Other Assets	764	1,420	2,270	1,609
Total Assets	41,093	35,546	46,496	51,901
Trade and Other Payables	2,252	2,200	3,028	3,024
Advances from Customers	2,678	1,064	2,518	15,336
Long-Term Debt (including current maturity)	15,809	14,477	11,887	9,310
Short-Term Debt	9,308	3,015	11,034	7,193
Total Debt	25,117	17,492	22,921	16,503
Other Liabilities	1,473	342	1,123	1,046
Total Liabilities	31,520	21,098	29,590	35,909
Tier-I/Total Equity	9,573	14,448	16,905	15,991
Paid Up-Capital	598	598	598	578
<u>INCOME STATEMENT</u>	MY20	MY21	MY22	MY23
Net Sales	52,270	56,800	58,888	72,343
Gross Profit	7,402	10,136	9,150	10,311
Other Expense	584	3,693*	393	219.0
Other Income	860	2,211	1,968	1,033
Finance Cost	3,550	2,252	3,404	5,453
Profit Before Tax	2,421	4,447	5,113	3,065
Profit After Tax	1,399	4,878	3,951	2,166
FFO	3,404	8,024	6,742	3,523
<u>RATIO ANALYSIS</u>	MY20	MY21	MY22	MY23
Gross Margin (%)	14.5	17.8	15.5	14.3
Net Profit Margin (%)	2.7	8.6	6.7	3.0
Net Working Capital	(932)	961	2,350	(5,941)
Current Ratio (x)	0.95	1.09	1.11	0.82
Cash Conversion Cycle (days)	96	46	56	81
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	0.21
Debt Servicing Coverage Ratio (x)	0.60	1.70	1.21	0.93
Gearing (x)	2.62	1.21	1.36	1.03
Leverage (x)	3.29	1.46	1.75	2.25
Inventory plus Receivables/Short-term Borrowings (x)	1.34	2.02	1.42	2.64

* 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	
	<u>RATING TYPE: ENTITY</u>					
	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	
	<u>RATING TYPE: SUKUK</u>					
	01/25/2024		A-1		Final	
	12/07/2023		A-1		Preliminary	
Instrument Structure	<p>JDW Sugar Mills Limited (“JDWS” or the “Company”) issued a Rated, Unsecured and Privately Placed Sukuk, structured on the basis of Musharakah (Shirkat-ul-Aqd) (“Musharaka Structure”) as a redeemable capital (under Section 66 of the Companies Act 2017) of up to PKR 8b (inclusive of a Green Shoe Option of PKR 3b) on December 18, 2023. 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 and maturing on June 14, 2024. 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.</p>					
Statement by the Rating Team	<p>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.</p>					
Probability of Default	<p>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.</p>					
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