RATING REPORT

JDW Sugar Mills Limited (JDWS)

REPORT DATE:
February 07, 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	*17th May'23*		*15th April'22*	

SUKUK RATING DETAILS	
Rating Category	**Preliminary**
	Short-term
Sukuk-2	A-1
Rating Action	Preliminary
Rating Date	*07th February 2024*

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
https://docs.vis.com.pk/docs/CorporateMethodology.pdf

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JDWS was incorporated as a private limited company in May, 1990 under the Companies Ordinance, 1984 (Repealed with enactment of the Companies Act 2017) and was subsequently converted into a public limited company in August, 1991.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

The Board of the Company has recently resolved to set up an Ethanol/ Distillery Project having per day production capacity of 230,000 liters. This Ethanol/ Distillery Project will produce export quality Ethanol from the in-house available sugar molasses of the Company. The Ethanol Project is expected to achieve COD by January 2025, subject to fulfilment of all corporate and regulatory requirements.

Proposed Short-Term Sukuk-2 ('STS-2'):

- JDWS plans to raise a rated, unsecured, privately placed STS-2, 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 finance working capital requirements; whereas 75% of the total proceeds will be utilized for sugarcane procurement and the remainder 25% for general working capital expense.
- 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 and JDWS may repay the entire outstanding facility amount or part thereof through Company's internal cashflows with fifteen (15) days prior written notice.
- Profit rate on the instrument would be 6M KIBOR + 75-80 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 MY23 stood at 215,751 tonnes fetching USD 104 million against nil exports in MY22.

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

During 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 1QMY24, the Company recorded an 85.1% increase in net turnover, rising from Rs. 14.7b 1QMY23 to Rs. 27.2b. The gross profit ratio exhibited a significant improvement, rising from 11.3% to 35.0%, attributed to the sale of carry-over sugar stocks at favorable prices. Other income also saw a substantial increase, escalating from Rs. 88.0m to Rs. 759.8m, primarily due to a net fair value gain on sugarcane crop at the point of harvest, driven by a significant increase in yield per acre and higher sugarcane support prices. Financial charges experienced a reduction of Rs. 72.9m compared to the corresponding period last year. This decline can be attributed to the early repayment of entire long-term loans in Oct'23, originally scheduled for repayment over a period of 3½ years. Despite significant tax provisions and an increase in WPPF & WWF, the Company achieved a net profit after tax of Rs. 5.0b, compared to Rs. 455.8m in the same period last year. In MY24, management projects a YoY growth of ~67% in topline primarily backed by higher volumetric sales and favorable prices of sugar. This is expected to result in a significant enhancement of both gross and net profitability.

Backed by higher profitability, coverage metrics have rebounded to healthy levels while recovery in liquidity supported by significant cash build up.

After reporting deterioration in MY23 the Company's coverage metrics have recovered to healthy levels as a result of enhanced profitability in 1QMY24. During the first quarter Funds from Operations (FFO) increased significantly to Rs. 7.9b (MY23: Rs. 3.5b; MY22: Rs. 6.7b). Resultantly, on an annualized basis, FFO to total debt have increased to 1.47x (Sept'23: 0.21x; Sept'22: 0.29x) despite substantial increase in short-term seasonal borrowings. FFO to long term debt was sizable at 8.35x (Sept'23: 0.38x; Sept'22: 0.57x). Additionally, Debt Service Coverage Ratio (DSCR) has strengthened to 2.99x (Sept'23: 0.97x; Sept'22: 1.26x) in 1Q'MY24.

Meanwhile the liquidity profile also recovered to adequate levels during the quarter under review. Current ratio is close to one at 0.98x as of Dec'23. The constraint on current ratio is on account of sizable advances from customers and short-term borrowing. However, as of Dec'23 much of the Company's liquidity was reported in the form of cash amounting Rs. 11.4b providing comfort to assigned ratings. The quick ratio improved to 0.34x in 1Q'MY24 from 0.17x in MY23 (MY22: 0.28x). Moreover, short-term borrowing coverage has remained comfortable on a timeline basis. The Company maintains accessible short-term borrowing facilities amounting to Rs. 43b, with approximately 70% of this amount remaining unutilized as of Dec'23. This provides an additional buffer to the Company's ability to meet its upcoming financial commitments.

While capitalization metrics remain elevated, management expects improvement going forward.

The equity base of the Company augmented to Rs. 21.0b (Sept'23: Rs. 16.0b; Sept'22: Rs 16.9b) as a result of profit retention during the first quarter MY24. Meanwhile, core equity was reported lower as of Sep'23, as a result of higher dividend payout and own shares purchased and cancelled during MY23. The short-term borrowings have significantly increased from Rs. 7.2b as of Sept'23 to Rs. 17.9b as of Dec'23 primarily due to enhanced working capital requirements during crushing season. This also includes recently issued unsecured, privately placed short term sukuk (STS-1) amounting to Rs. 8.0b, to meet the sugarcane procurement requirement. There was a high influx of advances received from customers amounting to Rs. 19.9b (Sept'23: Rs. 15.3b; Sept'22: Rs. 2.5b) as of Dec'23, against molasses and sugar sales. The long-term debt inclusive of current portion also stood lower at Rs. 3.8b (Sept'23: Rs. 9.3b; Sept'22: Rs. 11.9b) in line with principal repayments. As a result gearing remained the same at 1.03x (Sept'23: 1.03x; Sept'22: 1.36x) while debt leverage has increased to 2.60x (Sept'23: 2.25x; Sept'22: 1.75x) as of Dec'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 ethanol plant is expected to become online in January 2025. However, the capitalization indicators are projected to remain manageable on the back of growth in equity base due to internal capital generation. 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)*				
BALANCE SHEET	**MY21**	**MY22**	**MY23**	**1QMY24**	**MY24(P)**
Property Plant and Equipment	19,671	19,335	19,513	19,929	24,493
Right-of-Use Assets	1,880	1,599	2,540	2,538	2,181
Investment Property	186	186	318	318	318
Long-term Investment	1,084	1,084	1,050	1,050	1,084
Intangibles	613	611	609	608	609
Stores, Spares, and Loose Tools	1,382	1,916	2,428	2,727	2,575
Stock-in-Trade	1,880	12,146	15,823	27,410	15,283
Trade Debts	4,196	3,552	3,178	4,080	5,729
Biological Assets	2,335	2,855	3,606	3,218	4,065
Short-term Investment	652	652	1,068	1,068	-
Cash & Bank Balances	247	290	159	11,452	185
Other Assets	1,420	2,270	1,609	1,196	1,415
Total Assets	**35,546**	**46,496**	**51,901**	75,594	57,937
Trade and Other Payables	2,200	3,028	3,024	9,846	9,340
Advances from Customers	1,064	2,518	15,336	19,932	-
Long-Term Debt *(including current maturity)*	14,477	11,887	9,310	3,803	11,296
Short-Term Debt	3,015	11,034	7,193	17,867	5,841
Total Debt	17,492	22,921	16,503	21,670	17,137
Other Liabilities	342	1,123	1,046	3,163	3,578
Total Liabilities	21,098	29,590	35,909	54,611	30,055
Tier-I/Total Equity	**14,448**	**16,905**	**15,991**	20,983	27,882
Paid Up-Capital	598	598	578	578	578
INCOME STATEMENT	**MY21**	**MY22**	**MY23**	**1QMY24**	**MY24(P)**
Net Sales	56,800	58,888	72,343	27,170	120,839
Gross Profit	10,136	9,150	10,311	9,495	27,157
Other Expense	3,693*	393	219.0	604	1,412
Other Income	2,211	1,968	1,033	760	1,715
Finance Cost	2,252	3,404	5,453	826	4,592
Profit Before Tax	4,447	5,113	3,065	8,122	20,085
Profit After Tax	4,878	3,951	2,166	4,992	13,595
FFO	8,024	6,742	3,523	7,941	18,808
RATIO ANALYSIS	**MY21**	**MY22**	**MY23**	**1QMY24**	**MY24(P)**
Gross Margin (%)	17.8	15.5	14.3	34.9	22.5
Net Profit Margin (%)	8.6	6.7	3.0	18.4	11.3
Net Working Capital	961	1,620	(5,941)	(934)	11,819
Current Ratio (x)	1.09	1.08	0.82	0.98	1.68
Cash Conversion Cycle (days)	46	56	81	118**	40
FFO to Long Term Debt (x)	0.55	0.57	0.38	8.35**	1.67
FFO to Total Debt (x)	0.46	0.29	0.21	1.47**	1.10
Debt Servicing Coverage Ratio (x)	1.76	1.26	0.97	2.99**	1.65
Gearing (x)	1.21	1.36	1.03	1.03	0.61
Leverage (x)	1.46	1.75	2.25	2.60	1.08
Inventory plus Receivables/Short-term Borrowings (x)	2.02	1.42	2.64	1.76	3.60

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

***Annualized*

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		
01/25/2024		A-1		Final
12/07/2023		A-1		Preliminary
		RATING TYPE: SUKUK 2		
02/07/2024		A-1		Preliminary

Instrument Structure	JDW Sugar Mills Limited ("JDWS" or the "Company") intends to issue a Rated, Unsecured and Privately Placed Sukuk (STS-2), 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. The funds will be will be utilized for fulfilling the working capital requirements of the Company; whereas 75% of the total proceeds will be utilized for sugarcane procurement and the remainder 25% for general working capital expense. 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 0.75-0.80% 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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