RATING REPORT

Shahmurad Sugar Mills Limited

REPORT DATE:
June 30, 2021

RATING ANALYSTS:
Syed Fahim Haider Shah
fahim.haider@vis.com.pk

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	*Stable*		*Stable*	
Rating Action	Reaffirmed		Reaffirmed	
Rating Date	*30th June'21*		*2nd April'20*	

COMPANY INFORMATION	
Incorporated in 1979	External auditors: Kreston Hyder Bhimji & Co. Chartered Accountants.
Public Limited Company	Chairman of the Board: Mr. Noor Mohammad Zakaria Chief Executive Officer: Mr. Zia Zakaria
Key Shareholders (with stake 5% or more):	
Al-Noor Sugar Mills Limited – 15.62% CDC-Trustee National Investment Trust Fund – 6.50%	

APPLICABLE METHODOLOGY(IES)
VIS Entity Rating Criteria: Corporates (May 2019) ***https://www.vis.com.pk/kc-meth.aspx***

Shahmurad Sugar Mills Limited

OVERVIEW OF THE INSTITUTION

Incorporated in 1979, Shahmurad Sugar Mills Limited (SSML) is a public limited company and is listed on Pakistan Stock Exchange. The company is involved in production of sugar and ethanol and is a part of Al-Noor Group.

Financial Snapshot

Tier-1 Equity: end-HY21: Rs. 3.4b; end-MY20: Rs. 3.4b; end-MY19: Rs. Rs. 3.0b.

Assets: end-HY21: Rs. 15.5b; end-MY20: Rs. 11.3b; end-MY19: Rs 10.4.

Net Profit: HY21: Rs. 131m; MY20: Rs. 760m; MY19: Rs. 1.2b.

RATING RATIONALE

Shahmurad Sugar Mills Limited (SSML) is part of Al-Noor Group (ANG). The group has presence in sugar, ethanol, medium density fiber, rice, modaraba and insurance business. SSML is principally engaged in manufacturing of sugar and ethanol located at Jhok, District Sajawal in the province of Sindh.

Operating Performance

Sugar

The company has an installed sugarcane crushing capacity of 11,000 MT per day (MY20: 11,000 MT per day). During the crushing season MY21, the mill operated for 90 days (MY20: 96 days) due to lower sugarcane availability in the adjoining area of the mill. The mill crushed 441,293 MT (MY20: 444,430 MT) of sugarcane during the season while operating at a capacity utilization of 44.6% (MY20: 42.1%). In line with slightly lower sucrose recovery rate of 10.7% (MY20: 11.0%) mainly owing to early start of crushing seasonand insufficient water availability for crop, overall sugar produced decreased slightly to 47,220 MT (MY20: 48,786) during MY21.

	MY20	MY21
Installed Crushing Capacity (MTPD)	11,000	11,000
No. of days Mill Operated	96	90
Capacity based on Operating Days (MT)	1,056,000	990,000
Actual Crushing (MT)	444,430	441,293
Capacity Utilization	42.09%	44.58%
Sugar Produced (MT)	48,786	47,220
Recovery Rate	11.00%	10.70%

Ethanol

The company has two ethanol production units, each having production capacity of 100 MT per day. Ethanol plant II is a relatively new unit which became operational in MY18. Both ethanol units were operational for slightly lesser days vis-à-vis corresponding period of last year. Plant I produced 8,520 MT (MY20: 10,381 MT) while plant II produced 10,598 MT (MY20: 13,849 MT) of ethanol. The decreasein ethanol production was due to lower quantities of molasses purchased from the outside despite largely stable in-house production of 19,740 MT (MY20: 19,715 MT) which meets only 10% of overall requirement.

	MY20	MY21
PLANT – I		
Days in Operation	114	105
Capacity per day (MT)	100	100
Total Capacity	11,400	10,500
Actual Production	10,381	8,520
Capacity Utilization	91.1%	81.1%
PLANT – II		
Days in Operation	147	127
Capacity per day (MT)	100	100
Total Capacity	14,700	12,700
Actual Production	13,849	10,598
Capacity Utilization	94.2%	83.4%
Total		
Capacity	26,100	23,200
Production	24,230	19,118
Utilization	92.8%	82.4%

Business Risk

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-to-5 year cycle, driven largely by government support for farmers and crop yield. Sugarcane production has increased by 22% to 81m 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 of sugar in MY21. Meanwhile, sugar demand is projected at 5.9m MT for the period. While narrow demand and supply dynamics may lead to high sugar prices, government may intervene by importing sugar in order to control prices. Meanwhile, margins may also be curtailed by increasing trend in sugarcane prices. During MY21, sugarcane procurement prices have been recorded as higher against the minimum support price of Rs. 202 per mound in Sindh. However, sector's risk profile draws support from diversification into distillery, power and steel segments.

Asset base comprises current assets; no major capex plan underway

The accumulation of asset base to Rs. 15.5b (MY20: Rs. 11.3b) by end-HY21 was mainly manifested in higher inventory levels due to seasonality effect. Non-current assets, representing around one-third of overall asset mix, amounted to Rs. 5.3b (MY20: Rs. 5.4b) with depreciation expense exceeding capex of Rs. 40m (MY20: Rs. 247m) which mainly pertained to replacement of some key machinery components before the commencement of crushing season. Going forward, the capex plan is projected to remain in the range of Rs. 250m to Rs. 300m per annum over the rating horizon.

Stock in trade stood higher at Rs. 8.4b (MY20: Rs. 1.6b) which mainly pertained to sugar and ethanol finished inventory at end-HY21. Trade receivables increased, though remained on the lower side amounting Rs. 435m (MY20: Rs. 207m) as the company makes sugar sales on cash basis and ethanol is exported on LC. Loans and advances declined to Rs. 358m (MY20: Rs. 1.5b) primarily due to reduction in advances against purchase of molasses. The company normally makes advance payments during the 4th quarter of every year to secure the supply of molasses. Other receivables remained stagnant at Rs. 177m (MY20: 177m) with export subsidy receivables being the major component (99%) at end-HY21. Short-term investment amounted to Rs. 2m (MY20: Rs. 2.1b) as funds were utilized in working capital requirements. Cash and bank balance amounted to Rs. 497m (MY20: Rs. 36m) at end-HY21.

Profitability under pressure due to higher raw material prices

Net revenue of the company increased to Rs. 11.1b (MY19: Rs. 9.5b) driven by growth in sales of both sugar amounting Rs. 4.1b (MY19: Rs. 3.0b) and ethanol amounting Rs. 7.1b (MY19: Rs. 6.5b) during MY20. Contribution of sugar in overall revenue mix increased to 36% (MY19: 32%) on account of improved volumetric sales of 63,438 MT (MY19: 59,091 MT) at an average selling price of Rs. 63.9/kg (MY19: Rs. 51.3/kg).Despite lower volumetric exports of 45,808 MT (MY19: 60,645 MT), Ethanol sales increased due to higher average selling price of Rs. 154,787/MT (MY19: Rs. 106,633/MT) during MY20.

Cost of sales increased at a higher pace in relation to the top-line, amounting to Rs. 9.6b (MY19: Rs. 7.5b) during MY20.Increase was mainly led by higher average sugarcane price of Rs. 287 per mound vis-à-vis the minimum support price of Rs. 192 per mound and higher molasses price in view of increased demand.Resultantly, gross profit decreased to Rs. 1.6b (MY19: Rs. 2.0b) due to contraction of gross margin of ethanol division to 18.5% (MY19: 28.1%) despite marginal increase in sugar division margin of 7.0% (MY19: 6.4%). Operating expenses stood lower at Rs. 391m (MY19: Rs. 440m) due to lower export volumes, partially offset by increase in other expense owing to provision charge for export subsidy amounting to Rs. 59m (MY19: nil). Other income was also recorded lower at Rs. 75m (MY19: Rs. 134m) as the impact of higher income of bank deposits was more than offset by decrease in foreign exchange gain. Finance cost was Rs. 344m (MY19: Rs. 350m). Accounting for taxation, the company reported net income of Rs. 760m (MY19: Rs. 1.2b) as net margin declined to 6.8% (MY19: 12.7%) during MY20.

During HY21, net revenue was recorded lower at Rs. 3.6b (HY20: Rs. 5.1b) due to lower volumetric sales of both sugar and ethanol, partially offset by favorable prices. Gross profit also declined to 292m

(MY20: Rs. 560m) with the contraction of gross margin to 8.2% as the company couldn't pass on the impact of higher sugarcane and molasses prices. However, the company is expecting margins to improve in the second half of MY21 mainly due to increase in sugar price and export of high-margin ethanol that is currently in the stock. Operating cost amounted to Rs. 180m (HY20: Rs. 171m) while other income increased to Rs. 217m (HY20: Rs. 106m) mainly due to higher income on bank deposits. With short-term borrowings utilization at peak levels towards the end of crushing season and lower average interest rates, finance cost amounted to Rs. 154m (HY20: Rs. 190m). Accounting for the taxation, the company reported net profit of Rs. 131m (HY20: Rs. 249m) with lower net margin of 3.7% (HY20: 4.9%) during HY21.

Liquidity impacted by lower profits

The company's cash flows has depicted a declining trend over the review period. In line with lower profitability, funds from operations (FFO) decreased to Rs. 1.3b (MY19: Rs. 1.6b) in MY20 and further to Rs. 207m in HY21. While the company's debt repayment capacity remains adequate, lower cash flows has led to decrease in debt service coverage ratio to 1.42x (MY20: 2.71x) in HY21. The annualized FFO-to-total debt ratio also weakened to 0.04x (MY20: 0.25x) as the impact of decline in long-term debt was more than offset by lower cash flows and higher short-term borrowings for elevated working capital requirements at end-HY21. Current ratio was recorded at 1.1x (MY20: 1.1x) at end-HY21.

Elevated capitalization indicators due to seasonality factor

Equity base of the company (excluding revaluation) remained largely stable at 3.4b (MY20: Rs. 3.4b) at end-HY21. Revaluation surplus amounted to Rs. 1.3b (MY20: Rs. 1.4b). Total liabilities, however, stood higher at Rs. 10.8b (MY20: Rs. 6.5b) mainly on account of increased short-term borrowings of Rs. 8.5b (MY20: Rs. 3.6b) to meet higher working capital requirements. Long-term debt decreased to Rs. 1.4b (MY20: Rs. 1.5b) by end-HY21. With stable equity base and higher short-term borrowings, gearing and debt leverage was recorded higher at 2.95x (MY20: 1.48x) and 3.23x (MY20: 1.89x) at end-HY21. With scheduled repayments of long-term debt and lower short-term borrowings, gearing levels are projected to decline by end-FY21.

Shahmurad Sugar Mills Limited — Annexure I

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**MY19**	**MY20**	**HY21**
Property, Plant & Equipment	5,499	5,387	5,250
Stock-in-Trade	1,968	1,603	8,413
Trade Debts	460	207	435
Loans and Advances	1,586	1,468	358
Short-term Investment	201	2,104	2
Cash & Bank Balances	62	36	497
Other Assets	615	506	583
Total Assets	**10,391**	**11,312**	**15,538**
Trade and Other Payables	1,107	1,329	840
Short-Term Borrowings	3,113	3,641	8,543
Long-Term Borrowings *(Inc. current matur)*	1,699	1,456	1,355
Other Liabilities	46	59	96
Total Liabilities	5,965	6,484	10,834
Tier-1 Equity	**2,950**	**3,438**	**3,355**
Total Equity	4,426	4,827	4,705
Paid up Capital	211	211	211
INCOME STATEMENT	**MY19**	**MY20**	**HY21**
Net Sales	9,498	11,144	3,559
Gross Profit	2,010	1,592	292
Operating Profit	1,705	1,276	329
Profit Before Tax	1,355	932	175
Profit After Tax	1,206	760	131
FFO	1,612	1,263	207
RATIO ANALYSIS	**MY19**	**MY20**	**HY21**
Gross Margin (%)	21.2	14.3	8.2
Net Margin (%)	12.7	6.8	3.7
Current Ratio	1.05	1.12	1.05
Net Working Capital	236	616	483
FFO to Long-Term Debt	0.95	0.87	0.31*
FFO to Total Debt	0.34	0.25	0.04*
Debt Servicing Coverage Ratio (x)	3.30	2.71	1.42
Gearing (x)	1.63	1.48	2.95
Debt Leverage (x)	2.02	1.89	3.23
Inventory + Receivable/Short-term Borrowings (x)	0.78	0.50	1.04

**Annualized*

ISSUE/ISSUER RATING SCALE & DEFINITIONS Annexure 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					Annexure III
Name of Rated Entity	Shahmurad Sugar Mills Limited				
Sector	Sugar				
Type of Relationship	Solicited				
Purpose of Rating	Entity Ratings				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	06/30/2021	A-	A-2	Stable	Reaffirmed
	04/02/2020	A-	A-2	Stable	Reaffirmed
	02/27/2019	A-	A-2	Stable	Reaffirmed
	11/30/2017	A-	A-2	Stable	Reaffirmed
	04/28/2016	A-	A-2	Stable	Reaffirmed
	2/11/2015	A-	A-2	Stable	Upgrade
	11/25/2013	BBB+	A-2	Stable	Reaffirmed
	08-30-2012	BBB+	A-2	Stable	Reaffirmed
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. Mumtaz Hussain	CFO	May 06, 2021		