RATING REPORT

Fatima Sugar Mills Limited (FSML)

REPORT DATE:
March 04, 2020

RATING ANALYSTS:

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RATING DETAILS		
	Initial Rating	
Rating Category	Long-term	Short-term
Entity	A-	A-2
Rating Outlook	*Stable*	
Rating Action	Initial	
Rating Date	February 12, 2020	

COMPANY INFORMATION	
Incorporated in 1988	**External auditors:** EY Ford Rhodes. Chartered Accountants
Public Limited Company (Unquoted)	**Chairman of the Board:** Mr. Fawad Ahmed Mukhtar **Chief Executive Officer:** Mr. Faisal Ahmed Mukhtar
Key Shareholders (with stake 5% or more):	
Fatima Holding Limited – 100%	

APPLICABLE METHODOLOGY

VIS Entity Rating Criteria: Corporates (May 2019)

https://www.vis.com.pk/kc-meth.aspx

Fatima Sugar Mills Limited

OVERVIEW OF THE INSTITUTION

Fatima Sugar Mills Limited was incorporated as a public limited company in 1988 under the Companies Ordinance 1984 (now Companies Act, 2017). The company is primarily engaged in the manufacturing & sales of refined sugar.

Profile of the Chairman & Chief Executive Officer

Mr. Fawad Ahmed Mukhtar is the chairman of the company. He has extensive experience in manufacturing & industrial management. He is also the chairman of five other group companies & CEO of four group companies.

Mr. Faisal Ahmed Mukhtar is the CEO of the company. He is also CEO of Fatima Holding Limited and director at eleven other group companies. He has also served as Mayor and District Nazim of Multan.

Financial Snapshot

Total Equity: end-FY19: Rs. 3.60b; end-FY18: Rs. 3.22b; end-FY17: Rs. 3.17b

Assets: end-FY19: Rs 8.29b; end-FY18: Rs. 8.73b; end-FY17: Rs 7.95b

Profit After Tax: FY19: Rs. 370m; FY18: Rs. 54m; FY17: Rs. 154m

RATING RATIONALE

Fatima Sugar Mills Limited (FSML) is part of an industrial conglomerate, 'Fatima Group' engaged in the manufacturing and production of fertilizer, textile, energy, sugar & trading of commodities. The group companies include Pakarab Fertilizer Limited, Fatima Fertilizer Company Limited, Fatimafert Limited, Reliance Weaving Mills Limited, Reliance Commodities (Pvt.) Limited, Fatima Sugar Mills Limited, Fatima Energy Limited, Fatima Packaging Limited, Fatima Holding Limited, etc. FSML utilizes sugarcane as a raw material for the production of refined sugar. FSML has overall crushing capacity of 11,500 tons per day while the plant normally operates from November to April for sugar production. The company has total electricity requirement of 14.5 MW which is produced in-house through bagasse based power unit. While short-term outlook of sugar sector looks favorable, the ratings are constrained by inherent cyclicality & price vulnerability in sector dynamics.

Shareholding mainly vested with sponsoring family with adequate experience in sugar & other manufacturing sectors

FSML is wholly owned by Fatima Holding Limited (FHL), which acts as the holding company of the group. The shareholding of FHL is owned by sponsoring family with three brothers and their families each having one third shareholding in the company. Board of Directors of FSML comprises seven members, with four executive directors, all being representatives of the sponsoring family.

Sales decline on account of lower sugar production while profit improved on account of better margins and higher recovery rate

The net sales of FSML decreased to Rs. 6.76b (FY18: Rs. 8.55b, FY17: 7.04b) during FY19 with revenues from sugar representing 87% (FY18: 95%) of total sales followed by molasses with 9% (FY18: 3.5%) & bagasse with 4% (FY18: 1.5%). The sugarcane crushing declined to 997,082 M.tons (FY18: 1,460,568 M.tons) during FY19. As a result, the total sugar produced by the company decreased to 107,116 M.Tons (FY18: 146,798 M.Tons) while the company was able to sell 105,105 M.Ton (FY18: 172,439 M.Tons) of sugar. Sucrose recovery rate stood higher at 10.74% (FY18: 10.05%) during the year. As per financials, the average price of local sugar increased to Rs. 54.8/Kg (FY18: Rs. 46.8/Kg) during FY19 while the average price of exported sugar increased to Rs. 57.0 /Kg (FY18: Rs. 47.5 /Kg). The procurement price of sugarcane stood at Rs. 188.9/40Kg (FY18: Rs. 170/ 40Kg) during FY19.

The company sells its refined sugar both in the local and international markets with major portion of sugar sales derived from export sales. The local sales constituted around 48% (FY18: 30%) of total sugar sales during FY19. The revenue from local sugar sales increased to Rs. 3.02b (FY18: Rs. 2.52b) during FY19 as company was able to sell 48,371 M.Tons (FY18: 48,026 M.Tons) of sugar in the local market. However, major difference was witnessed in export sales where quantity sold declined to 56,734 M.tons (FY18: 124,413 M.tons) during FY19. The company generated export sales of Rs. 3.23b (FY18: Rs. 5.90b) which also includes subsidy on sugar export amounting to Rs. 248m (FY18: Rs. 1.25b) with major sales to Afghanistan amounting Rs. 1.58b (FY18: Rs. 3.72b) during FY19. As a result of that, total sugar sales declined to Rs. 6.25b (FY18: Rs. 8.43b) during FY19. The sales of molasses generated revenue of Rs. 617m (FY18: Rs. 308m) whereas quantity sold also increased to 60,438 M.tons (FY18: 47,000 M.tons). The average export selling price of molasses increased to Rs. 12,550 per ton (FY18: Rs. 9,450 per ton) during FY19 while local average selling price of molasses increased to Rs. 8,514 per ton (FY18: Rs. 4,000 per ton). The company was also able to generate sales of bagasse amounting to Rs. 340m (FY18: Rs. 103m) during FY19 while company was able to sell 111,834 M.tons (FY18: 79,332 M.Tons) of bagasse during FY19. The average selling price of bagasse increased to Rs. 2,593/M.Tons (FY18: Rs. 1,109/M.Tons) during FY19. Concentration among top 10 local customers remained high representing 95% (FY18: 96%) of the total local sales whereas concentration among top 10 international customers also remained high and stood around 84% (FY18: 82%) during FY19.

Although sugar remained the major revenue driver, the upward trend in sugar, molasses & bagasse prices along with increase in sucrose recovery rate positively impacted gross profit margins. The company generated gross profit of Rs. 1.2b (FY18: Rs. 745m) during FY19 while gross profit margin improved to 18.7% (FY18: 8.7%). Despite lower distribution cost, the operating expenses increased slightly to Rs. 393m (FY18: Rs. 389m) mainly due to higher other expenses related to workers' profit participation fund. Other income increased to Rs. 184m (FY18: Rs. 55m) mainly on account of higher mark-up on loan from associates amounting Rs. 91m (FY18: Rs. 37m) and net exchange gain of Rs. 63.9m (FY18: Nil) during FY19. The financial expenses increased to Rs. 649m (FY18: Rs. 317m) due to increase in average interest rates during the year. After accounting for taxation of Rs. 38m (FY18: Rs. 40m), the company posted net profit of Rs. 370m (FY18: Rs. 54m).

Total asset base decreased mainly on account of lower receivables while fixed assets increased

Total asset base of the company decreased to Rs. 8.29b (FY18: Rs. 8.73b; FY17: Rs. 7.95b) by end-FY19. The net fixed assets increased to Rs. 3.82b (FY18: Rs. 3.34b) by end-FY19. The company carried out BMR of Rs. 586m (FY18: Rs. 158m) during FY19 in order to improve efficiencies in the processes, replace old machineries & spare parts. There was slight decrease in inventory which decreased to Rs. 2.04b (FY18: Rs. 2.14b) during FY19 which consisted mainly of sugar inventory. The sugar inventory increased to Rs. 2.69b as of December 31, 2019 after production of new sugar inventory. The trade debts of the company decreased to Rs. 367m (FY18: Rs. 724m) while receivables days reduced to 20 days (FY18: 31 days). Local sales and export sales to Afghanistan are made against advance payment barring few premium clients while export sales to other countries are made against LC.

The receivables of Rs. 58m (FY18: Rs. 143m) during FY19 is 365 days overdue against bagasse sales to associate company 'Fatima Energy Limited'. Loans & advances decreased to Rs. 1.17b (FY18: Rs. 1.33b) which consisted of due from associated companies amounting to Rs. 891m (FY18: Rs. 1.04b) and Rs. 125.8m (FY18: Rs. 125.8m) from parent company "Fatima Holding Limited". The company has given interest bearing loans of Rs. 891m (FY18: Rs. 1.04b) to associated companies Fatima Energy Limited & Reliance Commodities (Pvt) Limited which carries markup at the rate of 3M-KIBOR + 3% per annum. Advance to growers & suppliers stood at Rs. 155m (FY18: Rs. 153m). Other receivables of the company stood at Rs. 150m (FY18: Rs. 570m) which mainly consisted of sugar export subsidy receivables of Rs. 116m (FY18: Rs. 536m) from GOP. The taxes refundable from government stood at Rs. 260m (FY18: Rs. 242m) was mainly an outcome of income tax deducted at source. However, cash & bank balances increased to Rs. 77m (FY18: Rs. 7m). Trade & other payables increased to Rs. 443m (FY18: Rs. 284m) was mainly due higher sales tax & federal excise duty payable of Rs. 120m (FY18: Rs. 4m) at end-FY19. Other liabilities stood at Rs. 275m (FY18: Rs. 300m) which mainly consisted of deferred taxation of Rs. 178m (FY18: Rs. 222m) and provision of taxation of Rs. 81m (FY18: Rs. 67m).

Cash flows improved on the back of profitability while coverages and liquidity ratios also showcased improvement

The liquidity profile of the company improved during FY19 mainly on account of higher profitability. Funds from Operations (FFO) improved to Rs. 374m (FY18: Rs. 80m). FFO to long-term debt improved to 38.6% (FY18: 23.3%) while FFO to total debt improved to 9.7% (FY18: 1.6%). The debt service coverage ratio also improved to 1.53x (FY18: 0.92x) and remained adequate. The current ratio increased to 1.18x (FY18: 1.06x) mainly on account of significant decrease in short term debt. Inventory plus inventory to short term borrowing ratio increased to 0.84x (FY18: 0.63x).

Improved leverage indicators with adequate equity base

Paid up capital remained unchanged at Rs. 2.1b. Total equity increased to Rs. 3.59b (FY18: Rs. 3.22b) on the back of profit retention. The debt matrix of the company is tilted towards short term debt comprising around 75% of total debt. Long term loan increased to Rs. 968m (FY18: Rs. 344m) by end-FY19 on account of new long term loan of Rs. 620m (FY18: Rs.137m) availed by the company for BMR. Short term loan decreased to Rs. 2.87b (FY18: Rs. 4.53b) in line with decline in working requirement. Given lower borrowings at end-FY19 in comparison to last year, debt leverage and gearing decreased to 1.31x (FY18: 1.71x) and 1.07x (FY18: 1.51x), respectively.

The company has proposed BMR of around Rs. 1b to be carried out in two phases during FY20 & FY21 which will be financed through long term loan of Rs. 500m & Rs. 375m, respectively while the rest will be funded through internal sources. The gearing of the company will not increase with these long term loan since company is also going to repay principal of around Rs. 500m each in next two years of its existing long term loans amid enhanced equity due to profit retention. The company has projected high gross margins during the next 3 years on the assumption of sustained high sugar prices.

Fatima Sugar Mills Limited – Financial Statements Appendix I

BALANCE SHEET *(amounts in PKR millions)*	Sep 30, 2017	Sep 30, 2018	Sep 30, 2019
Non-Current Assets	3,401	3,459	3,940
Stock-in-Trade	3,065	2,140	2,045
Stores, spares & loose tools	185	242	264
Trade Debts	187	724	367
Loans & Advances	722	1,334	1,177
Other receivables	151	570	150
Tax Receivables from Government	227	242	260
Other Assets	14	15	11
Cash & Bank Balances	5	7	77
Total Assets	7,957	8,733	8,291
Trade and Other Payables	346	284	443
Accrued Mark Up	47	49	135
Short Term Borrowings	3,845	4,531	2,876
Long-Term Borrowings *(Inc. current maturity)*	221	344	968
Total Bank Borrowing	4,066	4,875	3,844
Other Liabilities	328	300	275
Total Liabilities	4,787	5,508	4,697
Total Equity	3,170	3,225	3,594
Paid up Capital	2,102	2,102	2,102
INCOME STATEMENT	**Sep 30, 2017**	**Sep 30, 2018**	**Sep 30, 2019**
Net Sales	7,041	8,551	6,767
Gross Profit	828	745	1,266
Operating Profit	431	411	1,057
Profit Before Tax	220	94	408
Net Profit	154	54	370
FFO	256	80	374
RATIO ANALYSIS	**Sep 30, 2017**	**Sep 30, 2018**	**Sep 30, 2019**
Gross Margin (%)	11.8	8.7	18.7
Net Profit Margin (%)	2.2	0.6	5.5
Current Ratio	1.03	1.06	1.18
Net Working Capital	113	287	652
FFO to Total Debt (%)	6.3	1.6	9.7
FFO to Long Term Debt (%)	115.9	23.3	38.6
Debt Servicing Coverage Ratio (x)	1.24	0.92	1.53
(Inventory + Receivables) / Short Term Debt	0.85	0.63	0.84
ROAA (%)	1.9	0.6	4.5
ROAE (%)	4.8	1.7	10.3
Debt Leverage (x)	1.51	1.71	1.31
Gearing (x)	1.28	1.51	1.07

ISSUE/ISSUER RATING SCALE & DEFINITIONS 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	Fatima Sugar Mills Limited
Sector	Sugar
Type of Relationship	Initial
Purpose of Rating	Entity Ratings
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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Rating History

Rating Date	Medium to Long Term	Short Term	Rating Outlook	Rating Action
RATING TYPE: ENTITY				
12-02-2020	A-	A-2	Stable	Initial

Due Diligence Meetings Conducted

	Name	Designation	Date
1	Mr. Mukhtiar Ahmad Khan	CFO	14-Jan-2020
2	Mr. Jawad Ahmad	Manager Finance	14-Jan-2020