

RATING REPORT

Deharki Sugar Mills (Pvt.) Limited (DSML)

REPORT DATE:

May 13, 2024

RATING ANALYSTS:

Muhammad Subhan
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RATING DETAILS				
Rating Category	Latest Rating		Previous Rating	
	Long-term	Short-term	Long-term	Short-term
Entity	A	A-2	A	A-2
Rating Date	13 th May, 2024		May 17, 2023	
Rating Outlook	Stable		Stable	
Rating Action	Reaffirmed		Reaffirmed	

COMPANY INFORMATION

Incorporated in 2010

External Auditors: M/s Riaz Ahmad, Saqib, Gohar & Co.
 Chartered Accountants

Private Limited Company

Chief Executive Officer: Mr. Raheel Masud

Key Shareholders (with stake 5% or more):

JDW Sugar Mills Limited – 100.00%

APPLICABLE RATING SCALE(S)

VIS Issue/Issuer Rating Scale:

<https://docs.vis.com.pk/docs/VISRatingScales.pdf>

APPLICABLE METHODOLOGY

VIS Entity Rating Criteria: Corporates

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

Deharki Sugar Mills (Pvt.) Limited

OVERVIEW OF THE INSTITUTION RATING RATIONALE

Deharki Sugar Mills (Pvt.) Limited (DSML) is a private limited company which was incorporated in Pakistan under the Companies Ordinance, 1984 (Repealed with the enactment of the Companies Act, 2017 on May 30, 2017). The principal activity of The Company is manufacturing and selling of crystalline sugar.

Corporate Profile

Deharki Sugar Mills (Pvt.) Limited (“DSML” or “The Company”), a wholly owned subsidiary of JDW Sugar Mills Limited, is a private limited company which was incorporated in Pakistan under the Companies Ordinance, 1984 (Repealed with the enactment of the Companies Act, 2017 on May 30, 2017). Located in district Ghotki, Sindh, the principal activity of The Company is manufacturing and selling of crystalline sugar.

Operational Performance:

<u>Sugar Segment</u>	<u>Units</u>	<u>MY24</u>	<u>MY23</u>	<u>MY22</u>
Crushing Period in days	Numbers	112	106	136
Cane Crushed	Tons	1,694,259	1,585,515	1,953,090
Sugar Production	Tons	177,720	165,410	195,560
Sucrose Recovery	% age	10.49%	10.43%	10.00%
Molasses Produced	Tons	72,589	72,025	96,603
Molasses Recovery	% age	4.28%	4.54%	4.94%

The mills has crushing capacity of 13,000 TCD. The Company in MY23, faced production challenges in terms of availability of sugarcane. The after effects of damages caused by devastating floods during MY23 disrupted the sugarcane production at extent. This led to shortened crushing season of 106 days against 136 days in MY22. Resultantly sugarcane crushed and sugar production declined in MY23.

In addition, improvement in the operational performance in MY24 is witnessed with crushing period increasing to 112 days (MY23: 106 days). In MY24, the cane crushed for the year is recorded at 1,694,259 tons (MY23: 1,585,515 tons) and sugar production increased to 177,720 tons (MY23: 165,410 tons). The sucrose recovery slightly improved to 10.49% (MY23: 10.43%) respectively.

Key Rating Drivers

Medium business risk profile characterized by high cyclicity and moderate capital and competitive intensity

VIS has assigned a medium business risk to the sugar industry given its moderate level of barriers of entry, technology risk, and capital-intensive nature. However, industry’s high cyclicity with the production of sugarcane possess a raw material availability risk.

The industry faces an inelastic demand linked with the growing population in the country coupled with government’s measure to allow exports further supporting its stable demand. However, unfavorable sugar prices due to surplus of carryover sugar stock expose the industry to lower revenue gains.

The future outlook of the sugar industry appears challenging due to prevailing economic conditions of the country, higher discount rate of SBP may cause drastic increase in finance cost of The Company, and increase in sugarcane support prices by the provinces which increases the production cost of sugar with no adequate corresponding increase in the sugar prices.

Profitability performance on a positive momentum on account of higher topline growth backed by volumetric and price increases

The Company generate revenue from five (5) different segments; sugar, molasses, bagasse, agriculture, and mud. DSML witnessed an 80.3% growth in its topline in MY23. This revenue growth is primarily attributed to both,

volumetric and price increases in the reporting year. Moreover, initiation of export sales in MY23 also supported the topline. This significant topline growth further translated into improvement in the gross and net margin, reporting at 15.6% (MY22: 14.7%) and 4.8% (MY22: 3.2%) in MY23, respectively. Almost full retirement of the long-term loan in MY23 helped the Company to contain the finance cost, which otherwise would have depressed the bottom-line.

Healthier coverage profile on the back of higher profitability and operational efficacy

In MY23, DSML's coverage profile strengthened on account of improvement in the debt service coverage ratio (DSCR) to 2.1x (FY22: 1.3x). This improvement in the DSCR came with increase in FFO by 300.6% to PKR1,254.1 mln (MY22: PKR 313.2mln) in MY23 due to operational efficiency and higher profitability in the year.

Capital structure improved due to company's continuous repayment of its debt

The Company's capitalization metrics depicted a significant improvement with its leverage and gearing ratio improving to 1.2x (MY22: 2.5x) and 0.1x (MY22: 1.9x) in MY23. This positive momentum in DSMPL's capital structure is due to company's strategy to reduce reliance on debt with the total loan reducing to PKR 253.3 mln in MY23 from PKR 5,827.4 mln. The Company is projected to become debt free from MY24 onwards.

Current ratio maintained while STD coverage witnessed a significant improvement

DSML in MY23 depicted no change in its current ratio, reporting at 1.2x (FY22: 1.2x). However, the short-term debt (STD) coverage increased to 12.7x (MY22: 1.7x) in MY23. This significant increase in the STD coverage is on account of DSMPL's continuous reduction in its short term borrowings.

Pending Litigations

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 is still pending. The impact of the imposed penalty amounting PKR 774.4 mln on DSML 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.

REGULATORY DISCLOSURES		Appendix I			
Name of Rated Entity	Deharki Sugar Mills (Pvt.) 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
	<u>RATING TYPE: ENTITY</u>				
	05/13/2024	A	A-2	Stable	Reaffirmed
	05/17/2023	A	A-2	Stable	Reaffirmed
	04/15/2022	A	A-2	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
	04/13/2017	A	A-2	Stable	Upgrade
	06/08/2016	A-	A-2	Stable	Initial
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 Meetings Conducted	Name	Designation	Date		
	Mr. Muhammad Jaffar	DGM - Accounts	March 25, 2024		