RATING REPORT

Madina Sugar Mills Limited (MSML)

REPORT DATE:
July 5, 2018

RATING ANALYSTS:

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RATING DETAILS

	Latest Rating		Previous Rating	
Rating Category	**Long-term**	**Short-term**	**Long-term**	**Short-term**
Entity	A-	A-2		
Rating Outlook	*Stable*		*NA*	
Rating Action	Initial			
Rating Date	*June 29th, '18*			

COMPANY INFORMATION

Incorporated in 2007	External auditors: Kreston Hyder Bhimji & Co. Chartered Accountants
Public Limited Company – Unquoted	Chairman of the Board/CEO: Mian Muhammad Hanif
Key Shareholders (with stake 5% or more):	
Mian Muhammad Usman Saleem – 36.47%	
Faisalabad Oil Refinery (Pvt.) Ltd. – 31.23%	

APPLICABLE METHODOLOGY(IES)

JCR-VIS Entity Rating Criteria: Industrial Corporates (May 2016)
http://jcrvis.com.pk/docs/Corporate-Methodology-201605.pdf

Madina Sugar Mills Limited

OVERVIEW OF THE INSTITUTION

Madina Sugar Mills Limited (MSML) was incorporated in 2007. The principle activity is production and sale of white crystalline sugar and ethanol.

Profile of the Chairman/CEO

Mr. Mian Muhammad Hanif has more than 25 years of experience in Sugar, Edible Oils, Textile, Steel, and Education sectors. He is also the chairman of Pakistan Edible Oils Refiners Association.

Financial Snapshot

Total Equity: end-FY17: Rs. 4.33b; end-FY16: Rs. 3.96b; end-FY15: Rs. 3.31b

Assets: end-FY17: Rs. 9.70b; end-FY16: Rs. 8.51b; end-FY15: Rs. 7.26b

Profit After Tax: end-FY17: Rs. 371.07m; end-FY16: Rs. 221.61m; end-FY15: Rs. 146.86m

RATING RATIONALE

MSML is a sugar and ethanol manufacturing unit and is one of the cornerstones of Madinah Group. Shareholding of the company is mainly vested with the sponsoring family which is actively involved in the day to day affairs of the company. The assigned ratings take into account the sizeable scale of operations and vertical integration. The enhanced diversification in ethanol business provides an adequate cushion against cyclicality in the sugar business. The operational performance of the company is supported by well-established relationships with the farmers and continuous improvement in both sucrose and molasses recovery rates. The ratings also reflect company's minimal reliance on long-term debt, improved cash flows generation and adequate debt service coverage. However, ratings remained constrained on account of stringent government policies on sugarcane procurement prices, depressed sugar prices, and declining profit margins.

Key Rating Drivers:

Seeking enhanced cushion against cyclicality in the sugar business
White crystalline sugar is the biggest revenue drivers of the company, accounting for 80% of total sales. However, the company is diversifying its revenue stream by increasing production capacity of ethanol business. Its second distillery unit commenced commercial production in October 2017. The third distillery unit is under construction and will become operational by the end of 2018. Consequently, the cumulative production capacity of ethanol business will increase to 375,000 liters per day.

Depressed profit margins despite sizeable revenue growth
MSML showcased a sizeable growth in revenue on account of a significant increase in sugar dispatches in the local market. Volumetric sugar sales augmented to 133,857 MT (FY16: 56,156 MT; FY15: 40,394 MT) primarily due to accelerated sugarcane crushing activity during FY17. Overall sales momentum was restrained by continued weakness in sugar prices in the open market and reduced ethanol deliveries to international buyers. Overall profitability remained under pressure as gross margin further declined to 10.2% during FY17 (FY16: 15.1%; FY15: 17.7%) owing to higher cost of production. The ongoing weakness in sugar prices due to oversupply remains a major risk, but growing contribution of ethanol business may positively impact the overall profitability as it fetches better profit margins.

Fairly stable cash flows position and adequate debt service coverage
Despite a considerable increase in profits, the Funds from Operations (FFO) marginally decreased to Rs. 446.4m during FY17 (FY16: Rs. 498.9m; FY15: Rs. 270.1m) on account of notable increase in finance cost and taxes paid. FFO to total debt ratio slightly weakened to 0.11x at end-FY17 (FY16: 0.14x; FY15: 0.10x owing to an uptick in short-term borrowings. The debt service coverage ratio stood at a comfortable level of 1.32x at end-FY17 as compared to 1.54x in FY16. Going forward, the cash flows position is expected to improve owing to increase in revenue from ethanol business.

Gearing levels are expected to improve further
The equity base of the company augmented to Rs. 5.4b at end-FY17 (FY16: Rs. 4.7b; FY15: Rs. 4.0b) with the accumulation of internally generated capital. On the other hand, total debt rose to Rs. 4.0b at end-FY17 (FY16: Rs. 3.5b; FY15: 2.6b) primarily due to higher utilization of short-term borrowings for working capital. The outstanding balance of long-term debt stood higher at Rs. 845.0m at end-FY17 (FY16: Rs. 783.8m; FY15: Rs. 921.1m). Gearing was reported at 0.73x at end-FY17 (FY16: 0.74x; FY15: 0.66x) and is considered lower as compared to the peer group. The gearing indicators are expected to improve due to planned issuance of right shares and repayment of long-term debt.

Room for improvements in corporate governance framework
The Board of Directors of MSML comprises four members, all being the family members of

sponsoring family. The senior management team comprises well-experienced staff who plays an active role in establishing the future strategy. The corporate governance framework of the company has significant room for improvements.

Adequate IT infrastructure in place but internal control system requires more attention
The company uses ERP platform with integrated modules and other applications to manage its business processes. A group level internal audit team of eight employees overseas the audit-related matter of FORL. The external auditors review the effeteness of internal controls once a year. Mr. Haider Amin overseas the group level IT team of ten employees.

Madina Sugar Mills Limited — Appendix I

FINANCIAL SUMMARY *(amounts in PKR millions)*

BALANCE SHEET	**Sep 30, 2015**	**Sep 30, 2016**	**Sep 30, 2017**
Non-Current Assets	5,241.7	5,734.5	6,403.4
Stock-in-Trade	1,685.3	2,112.4	2,347.9
Trade Debts	-	201.9	268.9
Cash & Bank Balances	17.1	53.6	6.4
Total Assets	7,260.2	8,506.2	9,702.1
Trade and Other Payables	449.0	228.8	286.2
Short Term Borrowings	1,987.2	2,944.7	3,477.0
Long-Term Borrowings *(Inc. current matur)*	657.6	506.7	461.9
Tier-1 Equity	4,020.9	4,677.3	5,398.4
Total Equity	4,020.9	4,677.3	5,398.4
INCOME STATEMENT	**Sep 30, 2015**	**Sep 30, 2016**	**Sep 30, 2017**
Net Sales	2,086.2	4,558.5	7,163.4
Gross Profit	369.3	687.0	729.9
Operating Profit	289.5	482.3	560.9
Profit After Tax	146.9	221.6	370.1
FFO	270.1	498.9	446.4
RATIO ANALYSIS	**Sep 30, 2015**	**Sep 30, 2016**	**Sep 30, 2017**
Gross Margin (%)	17.7%	15.1%	10.2%
Net Working Capital	-524.9	-458.4	-507.5
FFO to Long-Term Debt	0.41	0.98	0.97
FFO to Total Debt (%)	0.1	0.14	0.11
Debt Servicing Coverage Ratio (x)	-	1.54	1.32
ROAA (%)	-	2.8%	4.1%
ROAE (%)	-	5.1%	7.3%
Gearing (x)	0.66	0.74	0.73
Debt Leverage (x)	0.81	0.82	0.80

ISSUE/ISSUER RATING SCALE & DEFINITIONS — Appendix II

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: JCR-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.jcrvis.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.jcrvis.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.

'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.jcrvis.com.pk/images/policy_ratings.pdf

'SD' Rating: An 'SD' rating is assigned when JCR-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 DISCLOSURESs	**Appendix III**				
Name of Rated Entity	Madina Sugar Mills Limited				
Sector	Consumer Goods				
Type of Relationship	Solicited				
Purpose of Rating	Entity Rating				
Rating History	**Rating Date**	**Medium to Long Term**	**Short Term**	**Rating Outlook**	**Rating Action**
	RATING TYPE: ENTITY				
	29/06/2018	A-	A-2	Stable	Initial
Instrument Structure	N/A				
Statement by the Rating Team	JCR-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.				
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