RATING REPORT

RYK Mills Limited

REPORT DATE:
January 21, 2020

RATING ANALYSTS:
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RATING DETAILS

	Initial Rating	
Rating Category	**Long-term**	**Short-term**
Entity	A	A-2
Rating Action	Initial	
Rating Outlook	Stable	
Rating Date	January 17, '20	

COMPANY INFORMATION

Incorporated in 2007	**External auditors:** Riaz Ahmad & Company Chartered Accountants
Public Limited (Unlisted) Company	**Chairman/CEO:** Makhdum Omer Shehryar

Key Shareholders (with stake 5% or more):

- Makhdum Omer Shehryar – 20.0%
- Cascade Tek (Private) Limited – 18.6%
- Axe Capital Limited – 16.2%
- Mr. Tarik Jawaid – 10.6%
- Mr. Wajid Ahmad Khan Bhatti – 9.6%
- Ms. Mahrukh Jahangir – 9.4%
- Ms. Iram Amin – 5.0%

APPLICABLE METHODOLOGY(IES)

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

RYK Mills Limited

OVERVIEW OF THE INSTITUTION

RYK Mills Limited (RYK) was incorporated in June 2007 under the repealed Companies Ordinance, 1984 (now Companies Act, 2017) and commenced commercial production in 2008. The head office of the company is located at 3-B Nisar Road, Nisar Colony, Cantt Lahore.

Profile of Chairman/CEO

Makhdum Omer Shehryar is a graduate from NYU Stern School of Business (USA). Mr. Shehryar is one of the founders and major shareholders of RYK Group. He has more than 20 years of experience in banking, industrial and power sectors.

Financial Snapshot

Tier-1 Equity: end-FY19: Rs. 5.6b; end-FY18: Rs. 4.8b; end-FY17: Rs. 4.5b.

Assets: end-FY19: Rs. 17.7b; end-FY18: Rs. 20b; end-FY17: Rs 17.5b.

Profit After Tax: FY19: Rs. 758m; FY18: Rs. 1b; FY17: Rs. 1.1b.

RATING RATIONALE

RYK is a part of RYK Group that was established in 2007. RYK has two wholly owned subsidiaries namely Alliance Sugar Mills (Private) Limited (ASML) and SW Sugar Mills Limited (SWS). The cumulative sugarcane crushing capacity of the group stands at over 38,000 tons per day (tpd) along with 30 MW of bagasse-based independent power generation unit (IPP). The assigned ratings take into account sponsors led experienced management, scalable sugarcane crushing operations and diversification into power generation business which provides some cushion against the cyclicality of sugar sector. The ratings also incorporate established relations with the suppliers where the company provides support to farmers in the form of better quality seeds and fertilizers that has helped in improving sucrose recovery on a timeline basis. The ratings draw comfort from notable growth in revenue during the past two years on account of higher volumetric sales and higher recovery rate. Sugar revenue model of the company encompasses open market and institutional sales and exports. Institutional sales more than doubled during FY19 as the company employed head of corporate marketing and sales to grow institutional clientele. Going forward, proportion of institutional sales is projected to increase further.

The ratings also take into account capital expenditure in process efficiencies, energy conservation and quality improvement, which has helped the company to more than double its institutional segment sales during FY19. While the commodity risk is embedded in sugar business, the recent increase in domestic sugar prices will bode well for the company, though increase in sugarcane support price may partially dilute the positive impact. However, the ratings also factor in fluctuation in margins and decline in cash flows generation owing to sizeable increase in finance cost. While there is room for improvement in the liquidity position, the company's capacity to meet its financial obligations is considered adequate despite some pressure on debt service coverage. The ratings positively factor in decrease in leverage indicators on account of enhanced equity and moderation of debt levels by end-FY19.

Key Rating Drivers

Corporate Profile

RYK is engaged in production and sale of white refined crystalline sugar and by-products as well as power generation business. The company commenced commercial production in December 2008. Over the years, the company has gradually enhanced its crushing capacity. The sugar mill is strategically located in Rukanpura, Tehsil Liaqatpur of district Rahim Yar Khan since the area has sugarcane crop friendly environment, with suitable soil chemistry, higher fertility and accessible water irrigation system. RYK diversified its business in 2015 by establishing 30 MW of bagasse-based power co-generation power plant, within the premises of its sugar mill.

Over the years, the company has conducted several Balancing, Modernization and Replacement (BMR) activities to enhance the production capacity and cost efficiencies. In line with the industry trends, quantum of sugarcane crushed has decreased over the past three years, however, sucrose recovery has improved. The improvement in sucrose recovery on a timeline basis is a function of the company's effort to secure better quality seed every season and continued farmer support in the form of seed and fertilizer as well as trainings about plant protection, better crop health and modern agricultural techniques to enhance output per acreage. Crushing season 2019-20 is currently in progress and the mill is expected to remain operational for over 100 days. Moreover, the government of Punjab has raised the sugarcane support price to Rs. 190 per 40 kilograms for the crushing season 2019-20 (2018-19: Rs. 180 per 40 kilograms).

Revenue growth emanated from higher volumes and favorable pricing while bottom-line impacted by increased finance cost

Net revenue of the company increased by 17% to Rs. 12.6b during FY19 mainly on account of higher volumetric sales and favorable selling price of sugar. Sugar segment remained the leading revenue contributor and accounted for 87% of total sales mix. Sugar revenue model of the company encompasses open market and institutional sales and exports. Institutional sales more than doubled during FY19 as the employed head of corporate marketing and sales to grow institutional clientele. Going forward, the management plans to further increase the share of institutional sugar sales. Revenue from molasses segment was almost flat, as the impact of lower volumetric sales was offset by higher average selling price. Revenue from power segment declined on account of lower electricity deliveries, partially offset by higher average tariff rate.

Gross profit increased by 27% during FY19 on account of higher revenue and improved gross margin of 25.7% due to higher sucrose recovery and selling price of sugar. The increase in distribution cost was mainly a function of higher freight & handling charges. Administrative expenses also increased to during the year, mainly due to higher salaries, wages and benefits to staff against inflationary adjustment. Finance cost was recorded higher at Rs. 1.7b owing to increase in benchmark rate during FY19. Accounting for taxation, the company report net profit of Rs. 758m for FY19 mainly due to sizeable increase in finance cost.

Liquidity profile has room for improvement, though capacity to meet financial obligations is considered adequate

RYK generated Rs. 1.1b in funds from operations (FFO) during FY19 (FY18: Rs. 1.5b; FY17: Rs. 1.6b) owing to lower net income and sizeable increase in finance cost paid. Resultantly, FFO to long-term debt and FFO to total debt ratios were recorded marginally lower at 0.4x (FY18: 0.47x; FY17: 0.49x) and 0.13x (FY18: 0.14x; FY17: 0.15x) respectively, at end-FY19. The debt service coverage ratio (DSCR) also decreased to 1.1x (FY18: 1.65x; FY17: 1.91), though still remained slightly above the minimum benchmark. Current ratio was recorded lower at 0.64x at end-FY19 (FY18: 0.72; FY17: 0.73x) on account of reduction in stock-in-trade and other receivables. Inventory plus receivables to short-term borrowings ratio also stood lower at 0.83x (FY18: 0.9x; FY17: 0.8x). RYK's liquidity indicators have room for improvement.

Moderation of leverage indicators supported by augmentation of equity and reduction in borrowings

Equity base of the company augmented to Rs. 5.6b by end-FY19 on account of partial retention of profits and increase in share deposit money. Total liabilities decreased to Rs. 12.1b mainly on account of lower borrowings and trade and other payables, as a result of reduction in advances from sugar customers. The debt profile of the company comprises a mix of short-term and long-term borrowings. The outstanding balance of short-term borrowings decreased to Rs. 5.7b by end-FY19 with the decline in inventory levels due to higher volumetric sales during the period. Total long-term debt, inclusive of current maturity, also declined to Rs. 2.9b, as the impact of new long-term debt was more than offset by scheduled repayment during the year. Given growth in equity and reduction in total debt, gearing and debt leverage ratios of the company improved to 1.51x (FY18: 2.2x; FY17: 2.37x) and 2.15x (FY18: 3.17x; FY17: 2.87x) respectively by end-FY19. Considering reduction in the company's sugar stock and potentially stable crushing operations during 2019-20 season, no significant increase in leverage indicators from current levels is expected in FY20.

RYK Mills Limited **Annexure I**

FINANCIAL SUMMARY *(amounts in PKR millions)*			
BALANCE SHEET	**FY17**	**FY18**	**FY19***
Property, Plant & Equipment	7,032	7,364	7,751
Long-term Investment	3,239	3,739	3,739
Stock in Trade	5,355	4,814	3,187
Trade Debts	639	1,819	1,472
Cash & Bank Balance	122	186	117
Total Assets	**17,535**	**20,027**	**17,678**
Trade & Other Payables	1,421	3,493	2,321
Short-term Borrowings	7,494	7,369	5,633
Long-Term Borrowings *(Inc. current matur)*	3,251	3,185	2,856
Total Liabilities	**13,002**	**15,228**	**12,064**
Tier-1 & Total Equity	4,533	4,800	5,614
Paid-up Capital	**1,420**	**1,420**	**1,420**
INCOME STATEMENT	**FY17**	**FY18**	**FY19***
Net Sales	6,855	10,723	12,568
Gross Profit	2,296	2,540	3,225
Operating Profit	2,012	2,208	2,612
Profit Before Tax	1,199	1,142	910
Profit After Tax	1,100	1,002	758
FFO	1,593	1,511	1,142
RATIO ANALYSIS	**FY17**	**FY18**	**FY19***
Gross Margin (%)	33.5	23.7	25.7
Net Margin (%)	16.1	9.3	6.0
Net Working Capital	(2,636)	(3,530)	(3,482)
FFO to Long-Term Debt (x)	0.49	0.47	0.40
FFO to Total Debt (x)	0.15	0.14	0.13
Debt Servicing Coverage Ratio (x)	1.91	1.65	1.10
ROAA (%)	7.6	5.3	4.3
Gearing (x)	2.37	2.20	1.51
Debt Leverage (x)	2.87	3.17	2.15
Current Ratio (x)	0.73	0.72	0.64
Inventory + Receivables to Short-term Borrowings (x)	0.80	0.90	0.83

**Management Accounts*

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	RYK 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				
17-01-2020	A	A-2	Stable	Initial

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.
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Due Diligence Meetings Conducted

Name	Designation	Date
Mr. Irfan Qamar	Head Internal Audit	18-Nov-2019