The Pakistan Credit Rating Agency Limited

Rating Report

Al-Abbas Sugar Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
09-May-2018	A	A1	Stable	Maintain	-
30-Sep-2017	A	A1	Stable	Maintain	-
30-Mar-2017	A	A1	Stable	Maintain	-
31-Mar-2016	A	A1	Stable	Maintain	-
10-Jun-2015	A	A1	Stable	Maintain	-

Rating Rationale and Key Rating Drivers

The ratings of Al-Abbas Sugar Mills Ltd (Al-Abbas) emanates from fortified position in its respective lines of business. The company drives its strength from diversified revenue streams – sugar, ethanol and storage terminals – enabling it to cope up with the sugar price volatility. While sugar is characterized by stable demand supported by fundamentals, ethanol takes benefit of the value addition that it signifies as a product. Sugar prices have remained depressed for an extended period of time on account of surplus availability of the commodity in the country. This has depressed relevant margins. Meanwhile, volumetric increase in ethanol division and stable income from storage terminals supports bottom-line. The de-leveraged balance sheet (from long term loans perspective) has kept the financial profile strong; hence, benefiting the ratings. Extended working capital requirements keep short-term borrowings somewhat high. Sufficient cash flows stabilizes coverages. Going forward, the management would continue to exploit better margins from distillery operations, while sugar segment profitability is mainly dependent on the government support to ease domestic stocks and pick-up in international prices.

The ratings are dependent on the sustained business volumes and margins of sugar, ethanol and terminal division. Strategic plan regarding asset build up (expansion and/or diversification) and related leveraging plan needs to be drawn. Resolution of shareholders' dispute, though lately it has diluted significantly, remains integral to the growth of the company. The company has build equities investment portfolio. although this brings potential of dividends and capital gains, respective market risk has to be attended diligently.

Disclosure

Name of Rated Entity	Al-Abbas Sugar Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating Methodology(Jul-17),Methodology | Correlation between long-term and short-term rating scale(Jun-17),Methodology | Criteria Modifiers(Jun-17)
Related Research	Sector Study | Sugar(Mar-18)
Rating Analysts	Muhammad Shahzad Saleem | shahzad@pacra.com | +92-42-35869504

PROFILE:	AL-ABBAS SUGAR MILLS LIMITED
Incorporated	1991
Major Business Lines	Production and Sale of refined sugar and ethanol
Legal Status	Listed Company
Mill Location:	Mirpurkhas and Dhabeji, Sindh
Crushing Capacity:	▪ Sugar crushing capacity: 7.5kT/day ▪ Ethanol Production capacity 172.5k Liters

INDUSTRY SNAPSHOT

- Pakistan experienced a bumper crop situation in 2016-2017 with a record production of 7.1MlnT of sugar
- Farmers have shifted their focus to sugarcane production as Government fixed minimum price for Sugarcane guaranteeing a better return to farmers.
- Sugarcane price in domestic market stayed flat while lower international prices without Government support make exports an unfavorable avenue for offloading excess stock.
- Export quota of 2 mln tons with a subsidy of PKR 10.7/Kg was announced to help ease the glut situation.
- However, with another year of bumper crop expected, industry dynamics would remain dependent in Government support.

OWNERSHIP

- **Ownership Structure:** Haji Ghani Group through family and associates own majority shareholding (58%) in Al- Abbas Sugar and exercise management control. Jahangir Siddiqui (JS) group (27%) is the other major shareholder; there are certain lawsuits between the two groups that are pending adjudication. The remaining shareholding (15%) is held financial institutions, mutual funds and general public.

GOVERNANCE

- **BoD Structure:** BoD, including the CEO, comprises nine members. Six members represent Haji Ghani group and associates, two members represent JS group and one is an independent director.
- **Members Profile:** The chairman of the board, Mr. Iqbal Usman, is a Chartered Accountant by profession and has 40 year's diversified experience in industrial, financial, construction, real estate and textile sector. The profile of all board is good comprising professionals whose experience diversifies from sugar to financial services. Mr. Zakria Usman joined the BoD as independent director in place of Mr. Sayyed Rafay Akbar Rashdi during FY17. Mr Zakria has over 40 years of experience primarily in the manufacturing industry. He has served on the board of various public and private sector organizations and is member of various associations.
- **Effectiveness:** The BoD met 6 times through FY17. Meetings were held in majority presence. BoD has constituted four committees. The audit committee met 4 times, Human resource committee met 2 times, Investment committee met 4 times whereas, Board evaluation committee met twice during FY17.
- **Transparency:** The Company has appointed Reanda Haroon Zakaria & Company, Chartered Accountants as external auditors. They have expressed unqualified opinion on financial statements for FY17 with an emphasis of matter paragraph drawing attention to the on-going litigation between the company and JS Group.

MANAGEMENT & CONTROL ENVIRONMENT

- **Organizational Structure:** Al- Abbas Sugar has a well-defined organizational structure, whereby department heads have direct reporting lines to the CEO. The five departments comprise: a) Finance, b) Administration / Human resource, c) Procurement / Purchase, d) Audit, and e) Plant Operations.
- **Management Profile:** Mr Asim Ghani was appointed as CEO w.e.f December 5, 2017 in place of Mr Shunaid Qurieshi. Mr. Ghani previously overlooked the operational aspects of Al-Abbas Sugar as Executive Director. Mr Zuhair Abbas is the CFO of the Al-Abbas sugar is a qualified Chartered Accountant. He has been associated with the company since the past 10 years.
- **Control Environment:** Al-Abbas Sugar has an internal audit department that reports to the Audit Committee of the BoD on a monthly basis, in addition to quarterly reporting.

BUSINESS RISK

- **Performance:** Revenue increased by 8% over SPLY to PKR 1.9bln. Gross and net margins stabilized to 13% and 8% due to improved market dynamics in sugar and sugar exports. The ethanol division turnover close to doubled over SPLY closing in at PKR 730mln on the back of volumetric increase. The company was able to increase production because of bulk purchase of Molasses during crushing season. Further, the division's decision to change the sales mix by shifting its focus from bulk sales to ISO and drum sales yielded an increase in GP margin from 20% in FY16 to 23% in FY17 which continued in 1QFY18. The change in sales mix resulted in higher distribution costs dampening the operating profits. Finance cost continued to consume operating profits at PKR 17mln. Bottom-line closed in at PKR 123mln lower by 17% compared to SPLY.
- **Sustainability:** Going forward, the company performance in the sugar division would be largely dependent on the industry dynamics. Meanwhile, the company is expected to continue its stable performance in ethanol and storage terminal operations to maintain profitability.

FINANCIAL RISK

- **Capital Structure:** Total Leverage reduced to 30% at the end Dec '17 in comparison to 42% at Sept' 17. The company has no long-term borrowings, the entire debt constitutes of short-term borrowing to finance working capital requirements.
- **Working Capital:** The surged inventory levels of PKR 1.9bln at end Sept' 17 settled to PKR 1bln by the end Dec' 17 with sale of molasses and sugar. However, this the dilution in inventory had little impact on the net cash cycle days which stood at 53 days (Sept' 17: 55 days) due to the increase in receivable.
- **Coverages:** Significant improvement can be seen during 1QFY18 as the company managed to improve its FCFO resulting in coverage of 10x (FY17:3x). Owing to the companys' prudent management of its debt mix and stable income from the ethanol divison coverages Al-abbas sugar is expected to maintain healthy covreages.

PKR mln

Al-Abbas Sugar Mills Limited

BALANCE SHEET	30-Dec-17	30-Sep-17	30-Sep-16	30-Sep-15
	1QFY18	*FY*	*FY*	*FY*
Non Current Assets	**1,573**	**1,599**	**1,695**	**1,806**
Investments	**703**	**710**	**436**	**362**
Long term	0	0	201	134
Short Trem	703	710	236	228
Current Assets	**2,651**	**2,863**	**1,181**	**1,358**
Inventory	1,079	1,963	707	849
Trade Recieveables	437	28	41	189
Others	1,135	872	434	321
Total Assets	**4,927**	**5,171**	**3,312**	**3,526**
Debt	**1,145**	**1,789**	**16**	**457**
ShortTerm	1,145	1,789	16	457
LongTerm(Incl current maturity of long term)	-	-	-	-
Other Short term liabilities	1,053	771	887	773
Other Long term liabilities	104	103	74	69
Shahreholder's Equity	**2,624**	**2,508**	**2,335**	**2,228**
Total Liabilities & Equities	**4,927**	**5,171**	**3,312**	**3,526**
Income Statement				
Turnover	**1,932**	**5,327**	**5,794**	**5,867**
Gross Profit	243	511	764	825
Financial Charges	(17)	(112)	(85)	(125)
Net Inocme	**123**	**143**	**458**	**495**
Cashflow Statement				
Free cashflow from operations	181	342	693	733
Net cash changes in working capital	493	(1,817)	293	458
Net cash from operating activities	645	(1,566)	899	1,051
Net cash from investing activities	2	(87)	(0)	116
Net cash from financing activities	(643)	1,618	(883)	(1,143)
Net cash generated during period	4	(35)	17	24
Closing balance of Cash and Cash Equivalent	27	24	58	42
Ratio Analysis				
Profitability				
Turnover Growth	8%	-8%	-1%	6%
Gross Margin	13%	10%	13%	14%
Net Profit Margin	6%	3%	8%	8%
Return on Equity (ROE)	5%	7%	19%	20%
Coverages				
Debt Service Coverage-times (FCFO*/Gross	0.1	0.2	0.9	1.5
Interest Coverage-times (FCFO/Gross	10.4	3.0	8.1	5.9
Debt Payback (years) (Total Debt (excluding	-	-	-	-
Liquidity				
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	58	55	47	75
Capital Structure (Total debt/ total debt + total equity)	30%	42%	1%	17%

**FCFO: Free Cashflow from operations*

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ENTITY CREDIT RATING SCALE & DEFINITIONS

Credit rating reflects forward-looking opinion on credit worthiness of underlying entity; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long Term Ratings

AAA	**Highest credit quality.** Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments.
AA+ **AA** **AA-**	**Very high credit quality.** Very low expectation of credit risk. Indicate very strong capacity for timely payment of financial commitments. This capacity is not significantly vulnerable to foreseeable events.
A+ **A** **A-**	**High credit quality.** Low expectation of credit risk. The capacity for timely payment of financial commitments is considered strong. This capacity may, nevertheless, be vulnerable to changes in circumstances or in economic conditions.
BBB+ **BBB** **BBB-**	**Good credit quality.** Currently a low expectation of credit risk. The capacity for timely payment of financial commitments is considered adequate, but adverse changes in circumstances or economic conditions are more likely to impair this capacity.
BB+ **BB** **BB-**	**Moderate risk.** Possibility of credit risk developing. There is a possibility of credit risk developing, particularly as a result of adverse economic or business changes over time; however, business or financial alternatives may be available to allow financial commitments to be met.
B+ **B** **B-**	**High credit risk.** A limited margin of safety remains against credit risk. Financial commitments are currently being met; however, capacity for continued payment is contingent upon a sustained, favorable business, and economic environment.
CCC **CC** **C**	**Very high credit risk.** "CCC" Default is a real possibility. Capacity for meeting financial commitments is solely reliant upon sustained, favorable business or economic developments. "CC" Rating indicates that default of some kind appears probable. "C" Ratings signal imminent default.
D	Obligations are currently in default.

Short Term Ratings

A1+: The highest capacity for timely repayment.

A1:. A strong capacity for timely repayment.

A2: A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial conditions.

A3: An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.

B: The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.

C: An inadequate capacity to ensure timely repayment.

Rating Watch
Alerts to the possibility of a rating change subsequent to, or in anticipation of, a) some material identifiable event and/or b) deviation from expected trend. But it does not mean that a rating change is inevitable. Rating Watch may carry designation – Positive (rating may be raised, negative (lowered), or developing (direction is unclear). A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled.

Outlook (Stable, Positive, Negative, Developing)
Indicates the potential and direction of a rating over the intermediate term in response to trends in economic and/or fundamental business or financial conditions. It is not necessarily a precursor to a rating change. 'Stable' outlook means a rating is not likely to change. 'Positive' means it may be raised. 'Negative' means it may be lowered. Where the trends have conflicting elements, the outlook may be described as 'Developing'.

Suspension
It is not possible to update an opinion due to lack of requisite information. Opinion should be resumed in foreseeable future. However, if this does not happen within six (6) months, a suspended rating should be considered withdrawn.

Withdrawn
A rating is withdrawn on a) termination of rating mandate, b) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, or e) the entity/issuer defaults.

Rating Team Statements
(1) Rating is just an opinion about the creditworthiness of the entity and does not constitute recommendation to buy, hold or sell any security of the entity rated or to buy, hold or sell the security rated, as the case may be | Chapter III; 14-3-(x)

2) **Conflict of Interest**
i. The Rating Team or any of their family members have no interest in this rating | Chapter III; 12-2-(j)
ii. PACRA, the analysts involved in the rating process and members of its rating committee, and their family members, do not have any conflict of interest relating to the rating done by them | Chapter III; 12-2-(e) & (k)
iii. The analyst is not a substantial shareholder of the customer being rated by PACRA [Annexure F; d-(ii)] Explanation: for the purpose of above clause, the term "family members" shall include only those family members who are dependent on the analyst and members of the rating committee

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(4) PACRA does not disclose or discuss with outside parties or make improper use of the non-public information which has come to its knowledge during business relationship with the customer | Chapter III; 10-7-(d)
(5) PACRA does not make proposals or recommendations regarding the activities of rated entities that could impact a credit rating of entity subject to rating | Chapter III; 10-7-(k)

Conduct of Business
(6) PACRA fulfills its obligations in a fair, efficient, transparent and ethical manner and renders high standards of services in performing its functions and obligations; | Chapter III; 11-A-(a)
(7) PACRA uses due care in preparation of this Rating Report. Our information has been obtained from sources we consider to be reliable but its accuracy or completeness is not guaranteed. PACRA does not, in every instance, independently verifies or validates information received in the rating process or in preparing this Rating Report.
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(9) PACRA ensures before commencement of the rating process that an analyst or employee has not had a recent employment or other significant business or personal relationship with the rated entity that may cause or may be perceived as causing a conflict of interest; | Chapter III; 11-A-(r)
(10) PACRA maintains principal of integrity in seeking rating business | Chapter III; 11-A-(u)
(11) PACRA promptly investigates, in the event of a misconduct or a breach of the policies, procedures and controls, and takes appropriate steps to rectify any weaknesses to prevent any recurrence along with suitable punitive action against the responsible employee(s) | Chapter III; 11-B-(m)

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(12) PACRA receives compensation from the entity being rated or any third party for the rating services it offers. The receipt of this compensation has no influence on PACRA´s opinions or other analytical processes. In all instances, PACRA is committed to preserving the objectivity, integrity and independence of its ratings. Our relationship is governed by two distinct mandates i) rating mandate - signed with the entity being rated or issuer of the debt instrument, and fee mandate - signed with the payer, which can be different from the entity
(13) PACRA does not provide consultancy/advisory services or other services to any of its customers or to any of its customers' associated companies and associated undertakings that is being rated or has been rated by it during the preceding three years unless it has adequate mechanism in place ensuring that provision of such services does not lead to a conflict of interest situation with its rating activities; | Chapter III; 12-2-(d)
(14) PACRA discloses that no shareholder directly or indirectly holding 10% or more of the share capital of PACRA also holds directly or indirectly 10% or more of the share capital of the entity which is subject to rating or the entity which issued the instrument subject to rating by PACRA; | Reference Chapter III; 12-2-(f)
(15) PACRA ensures that the rating assigned to an entity or instrument is not be affected by the existence of a business relationship between PACRA and the entity or any other party, or the non-existence of such a relationship | Chapter III; 12-2-(i)
(16) PACRA ensures that the analysts or any of their family members shall not buy or sell or engage in any transaction in any security which falls in the analyst's area of primary analytical responsibility. This clause shall, however, not be applicable on investment in securities through collective investment schemes. | Chapter III; 12-2-(l)
(17) PACRA has established policies and procedure governing investments and trading in securities by its employees and for monitoring the same to prevent insider trading, market manipulation or any other market abuse | Chapter III; 11-B-(g)

Monitoring and review
(18) PACRA monitors all the outstanding ratings continuously and any potential change therein due to any event associated with the issuer, the security arrangement, the industry etc., is disseminated to the market, immediately and in effective manner, after appropriate consultation with the entity/issuer; | Chapter III | 18-(a)
(19) PACRA reviews all the outstanding ratings on semi-annual basis or as and when required by any creditor or upon the occurrence of such an event which requires to do so; | Chapter III | 18-(b)
(20) PACRA initiates immediate review of the outstanding rating upon becoming aware of any information that may reasonably be expected to result in downgrading of the rating; | Chapter III | 18-(c)
(21) PACRA engages with the issuer and the debt securities trustee, to remain updated on all information pertaining to the rating of the entity/instrument; | Chapter III | 18-(d)
Probability of Default
(22) PACRA´s Rating Scale reflects the expectation of credit risk. The highest rating has the lowest relative likelihood of default (i.e, probability). PACRA´s transition studies capture the historical performance behavior of a specific rating notch. Transition behavior of the assigned rating can be obtained from PACRA´s Transition Study available at our website. (www.pacra.com). However, actual transition of rating may not follow the pattern observed in the past | Chapter III | 14-(f-VII)
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