The Pakistan Credit Rating Agency Limited

Rating Report

Mirpurkhas Sugar Mills Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
05-Apr-2022	A-	A2	Stable	Maintain	-
07-Apr-2021	A-	A2	Stable	Maintain	-
10-Apr-2020	A-	A2	Stable	Maintain	-
22-Oct-2019	A-	A2	Stable	Maintain	-
28-Jun-2019	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

Pakistan's sugar industry is the country's 2nd largest agro-based industry, comprising 90 mills with an annual crushing capacity estimated ~ 65–70mln MT. The industry has overcome the raw material supply challenges. However, support price of sugarcane, incurred by farmers, remains a constraint. The Government increased the support price of sugarcane from PKR 202 to 250 per maund for mills operating in Sindh in the current crushing season. Realized sugarcane prices at the mill gate were even higher. During MY21, the overall sugar production increased by 15%, YoY, to 5.7mln MT (MY20: 4.9mln MT) due to better crop availability and an increase in area under cultivation. Moreover, in FY21's budget, the Government levied 17% GST on price of PKR 72.22/kg instead of PKR 60/kg. Therefore an increase in sugar prices in the local market. To curb this, the Government planned to import 0.8mln MT of sugar. Out of this, 0.3mln MT was imported till Jun-21, whereas, 0.3mln MT till Nov-21. During the current crushing season (MY22), a further surge of 20% is expected in sugarcane production resulting in an increased total sugar production of ~7mln MT. Also, due to high production anticipated, sugar prices are already showing a downward trend and are expected to improve once the crushing season of MY22 ends.
The ratings demonstrate the Company's established position and its association with a leading group – Ghulam Faruque Group. The ratings incorporate diversified revenue stream of the Company emerging from sale of sugar, molasses & bagasse and strategic investments in Paper & Board project, a separate division being established under the Company. Investment in an associate; Unicol Limited, a leading ethanol producer, was also considered. This mitigates the impact of volatile nature of sugar industry and supplements the Company's profitability. High competition for sugarcane procurement amongst mills and increased support price of Sugarcane result in relatively higher input costs. Topline growth posted a declining trajectory, however, net profit margins remained stable due to profit share from associate. The Company's financial profile is characterized by moderately leveraged capital structure and adequate working capital management. Coverages remain stretched. Likely group support, in case need arises, remains one of the key ratings factor.

The ratings are dependent on the Company's ability to improve profitability while strengthening coverage ratios. Prudent management of debt structure and efficient working capital management to eliminate any mismatch, is critical. Continued negative trade, total leverage and deterioration in coverages would negatively impact ratings in future.

Disclosure

Name of Rated Entity	Mirpurkhas Sugar Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology | Corporate Rating(Jun-21),Criteria | Correlation Between Long-term & Short-term Rating Scales(Jun-21),Criteria | Rating Modifiers(Jun-21)
Related Research	Sector Study | Sugar(Dec-21)
Rating Analysts	Faiqa Qamar | faiqa.qamar@pacra.com | +92-42-35869504

Profile

Legal Structure Mirpurkhas Sugar Mills Limited (the Company) is a public limited company, listed on the Pakistan Stock Exchange.

Background The Company was incorporated in 1964 and started operations in 1966 with a crushing capacity of 1,500 TCD. Over the years, through frequent BMR and capacity enhancements, crushing capacity has been enhanced to 12,500 TCD. The Company's mill is located in Mirpurkhas, Sindh while the head office is in Karachi.

Operations Primary business activity of the Company involves manufacturing and sale of sugar. The Company's mill is located at Umerkot Road in Mirpurkhas, Sindh. Meanwhile the head office is based in Karachi. During MY21, the Company's mill operated for 98 days (MY20: 107days) crushing 488,464MT of sugarcane (MY20: 525,201MT) while producing 51,909MT of sugar (MY20: 57,286MT) at a recovery rate of 10.63% (MY20: 10.91%) due to lower availability of sugarcane in operational area.

Ownership

Ownership Structure Major shareholding of the Company lies with Faruque Family through associated companies (~51.9%) and individuals (~5.7%). General Public holds (~28.9%), NIT (~9%), Public Sector Companies & Corporations (~4%) and Banks & DFIs (~0.5%).

Stability The Group is being operated by the third generation of sponsors, with the fourth generation gradually being inducted in the business. The existence of a holding company structure with defined interests of each family and understanding among sponsoring family members reflects stability in ownership.

Business Acumen The Company is a part of the Ghulam Faruque Group, which was incorporated in 1964. In addition to sugar, the Group has established a strong presence in the country's cement and packaging industry. Moreover, the Group is involved in air conditioning, industrial equipment trading, and software solutions.

Financial Strength The Company derives financial strength from its Group, which houses well-known entities, such as Cherat Cement Company Ltd and Cherat Packaging Ltd. The Group posted consolidated revenue of PKR ~40bln, with a Profit after tax of PKR ~4bln as at June-21. Total debt & equity stood at PKR ~31bln & PKR ~23bln respectively.

Governance

Board Structure The Company's Board of Directors comprises seven members, including the Chairman, two non-executive directors, two executive directors and two independent directors, one of whom is a representative of NIT.

Members' Profile Members have diversified backgrounds with noteworthy experience and specialization in sugar, cement, packaging and steel industries.

Board Effectiveness The Board maintains effective oversight through Board Audit Committee and HR & Remuneration Committee. High frequency of Board of Directors & Committees' meetings bodes well for the Company.

Financial Transparency Kreston Hyder Bhimji & Co. Chartered Accountants, has expressed an unqualified opinion on the financial reports for the Company for the year ending in Sept-21. The firm is classified under category 'A' by the SBP and possesses a satisfactory QCR rating.

Management

Organizational Structure The Company is operated through ten departments, including finance, sales, marketing, procurement and internal audit among others. All department heads report to COO, who holds position of CFO as well. However, heads of Internal Audit and HR reports administratively to the CEO and functionally to the Board Audit Committee and Board HR & Remuneration Committee, respectively.

Management Team Management comprises experienced individuals. The CEO, Mr. Aslam Faruque has experience of over 37 years. He also serves as the CEO of Unicol Limited, a joint venture distillery project of the Company. He is ably supported by COO & CFO - Mr. Wasif Khalid who has experience of over ~22 years. He has been associated with the Group for the past 18 years.

Effectiveness The Company monitors efficiency and effectiveness of management systems through two committees, namely, Technical Committee and IT Steering Committee. Meetings are conducted at regular intervals with high frequency during the crushing period.

MIS The Company implemented SAP in 2010. Production and sales reports are submitted to the senior management periodically.

Control Environment In order to ensure operational efficiency, the Company has setup an internal audit function. The department conducts regular reviews to monitor effectiveness of operations while identifying potential areas of improvement.

Business Risk

Industry Dynamics Pakistan's sugar industry is the country's 2nd largest agro-based industry, comprising 90 mills with an annual crushing capacity estimated ~ 65–70mln MT. The industry has overcome the raw material supply challenges. However, support price of sugarcane, set by considering the cost incurred by farmers, remains a constraint. The Government increased the support price of sugarcane to PKR 250 per maund for mills operating in Sindh in the current crushing season (previously, it was increased to PKR 202). Actual realized sugarcane prices at the mill gate were even higher. During MY21, the overall sugar production increased by 15%, YoY, to 5.7mln MT (MY20: 4.9mln MT) due to better crop availability and an increase in area under cultivation. Moreover, in FY21's budget, the Government levied 17% GST on price of PKR 72.22/kg instead of PKR 60/kg. This led to an increase in sugar prices in the local market. To curb this, the Government planned to import 0.8mln MT of sugar. Out of this, 0.3mln MT was imported till Jun-21, whereas, 0.3mln MT was imported till Nov-21. During the current crushing season (MY22), a further surge of 20% is expected in sugarcane production resulting in an increased total sugar production of ~7mln MT. Also, due to high production anticipated, sugar prices are already showing a downward trend and are expected to improve once the crushing season of MY22 ends.

Relative Position The Company held ~0.9% share in total sugar production of the country and holds a relatively low market share.

Revenues The Company generates revenues from sale of sugar (90%), molasses (9%), and bagasse (1%). During MY21, revenue stood at PKR 3,861mln (MY20: PKR4,637mln), posting a dip of 17% due to lower availability of cane at a higher avg. sugarcane cost. Despite better sugar prices, the Company was able to off-load relatively lesser stock in anticipation of improved sugar price. Going forward, comparatively high sugar prices and stable demand for molasses in the ethenol export market will bode well for the Company.

Margins During MY21, gross margin improved to ~7.3% (MY20: ~6.6%) due to rise in sugar prices. Operating margins also surged minutely (MY21: 2.7%, MY20: 2.6%), from trickle down effect of gross margins. Finance cost (MY21: PKR 246mln, MY20: PKR 366mln) declined due to lower interest rates. Moreover, the Company received supplementary income from its strategic investment (Unicol Limited), standing at PKR 168mln in MY21 (MY20: PKR 175mln). Resultantly, net income improved to PKR 140mln (MY20: PKR -116mln), translating into a net margin of 4% (MY20: -2.5%). Going forward, margins are expected to improve on the basis of stable sugar price, lower sugarcane cost, and increased production.

Sustainability The Company is establishing paper and board division with a maximum production capacity of 84,000 MT per year which is expected to achieve COD by Oct 2022. Total investments is ~PKR3.2bln funded by 70:30 debit & equity mix.

Financial Risk

Working Capital In MY21, the Company's net working capital days increased to 77days (MY20: 64days) due to high inventory held days and receivable days. The Company faces inherent volatility owing to seasonality in crushing cycle. Inventory held days stood at 78 days (MY20: 66days) as the Company had higher unsold stock. Payable days posted stable trend (MY21: 8 days, MY20: 6 days) as the Company paid of farmers in a weeks time. The Company has an adequate borrowing cushion. Going forward, working capital management is expected to remain stable.

Coverages In MY21, interest coverage improved to 1.9x (MY20: 1.5x) due to reduced in finance cost (MY21: PKR 246mln, MY20: PKR 366mln). Core and total operating coverage reduced to (MY21: 0.4x, MY20: 0.7x) due to lower free cash flows. Going forward, coverages is expected to improve.

Capitalization The Company has a moderately leveraged capital structure with a debt-to-equity ratio of 52% in MY21 (MY20: 45%). This increase is mainly due to increased borrowings (MY21: PKR 3,444mln, MY20: PKR2,284mln). Tilt in total borrowings remain towards short term borrowings, which posted an increase (MY21: PKR 1,798mln, MY20: PKR 1,099mln) and are mainly used to fund the working capital requirement. Moreover, long term borrowings posted an increased (MY21: PKR 1,258mln, MY20: PKR 1,044mln) to finance the Paper & board division. Going forward, leverage ratio is expected to remain adequate.

The Pakistan Credit Rating Agency Limited

Financial Summary
PKR mln

Mirpurkhas Sugar Mills Limited	Dec-21	Sep-21	Sep-20	Sep-19
Sugar	3M	12M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	4,344	3,473	2,624	2,489
2 Investments	5	2	2	-
3 Related Party Exposure	2,283	1,992	2,211	1,484
4 Current Assets	3,401	2,277	1,543	1,827
a Inventories	*1,846*	*993*	*662*	*1,011*
b Trade Receivables	*57*	*61*	*91*	*28*
5 Total Assets	10,033	7,744	6,379	5,801
6 Current Liabilities	1,425	593	608	553
a Trade Payables	*276*	*112*	*61*	*99*
7 Borrowings	4,879	3,444	2,284	2,575
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	482	480	641	688
10 Net Assets	3,246	3,226	2,846	1,984
11 Shareholders' Equity	3,246	3,226	2,846	1,984
B INCOME STATEMENT				
1 Sales	1,268	3,861	4,637	3,729
a Cost of Good Sold	*(1,139)*	*(3,579)*	*(4,332)*	*(3,121)*
2 Gross Profit	129	283	305	608
a Operating Expenses	(58)	(177)	(185)	(184)
3 Operating Profit	71	105	120	424
a Non Operating Income or (Expense)	*75*	*356*	*199*	*398*
4 Profit or (Loss) before Interest and Tax	146	461	318	822
a Total Finance Cost	*(54)*	*(246)*	*(366)*	*(404)*
b Taxation	*(20)*	*(75)*	*(68)*	*(110)*
6 Net Income Or (Loss)	72	140	(116)	307
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*98*	*317*	*461*	*551*
b Net Cash from Operating Activities before Working Capital	*53*	*63*	*52*	*423*
c Changes in Working Capital	*(1,015)*	*(313)*	*440*	*331*
1 Net Cash provided by Operating Activities	(962)	(249)	491	754
2 Net Cash (Used in) or Available From Investing Activities	(1,224)	(883)	(186)	(155)
3 Net Cash (Used in) or Available From Financing Activities	1,435	1,156	(312)	(574)
4 Net Cash generated or (Used) during the period	(751)	24	(7)	24
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	31.4%	-16.7%	24.4%	-10.6%
b Gross Profit Margin	10.2%	7.3%	6.6%	16.3%
c Net Profit Margin	5.7%	3.6%	-2.5%	8.2%
d Cash Conversion Efficiency (FCFO adjusted for Working C	-72.3%	0.1%	19.4%	23.7%
*e Return on Equity [Net Profit Margin * Asset Turnover * (T*	9.0%	4.6%	-4.8%	14.5%
2 Working Capital Management				
a Gross Working Capital (Average Days)	106	85	71	107
b Net Working Capital (Average Days)	92	77	64	96
c Current Ratio (Current Assets / Current Liabilities)	2.4	3.8	2.5	3.3
3 Coverages				
a EBITDA / Finance Cost	2.1	1.9	1.5	1.3
b FCFO / Finance Cost+CMLTB+Excess STB	0.4	0.4	0.7	0.5
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Fi	16.3	23.6	13.6	8.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equit	60.0%	51.6%	44.5%	56.5%
b Interest or Markup Payable (Days)	91.7	47.9	36.9	63.9
c Entity Average Borrowing Rate	5.5%	7.2%	12.1%	12.0%

Credit Rating

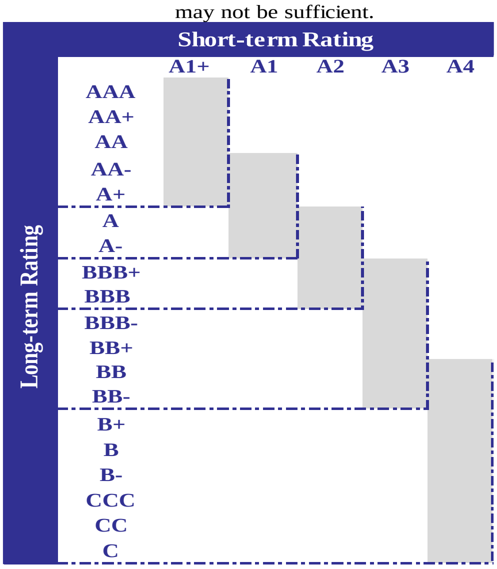
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

Long-term Rating

Scale	Definition
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 and in 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.** Substantial 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 Rating

Scale	Definition
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
A4	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions. Liquidity may not be sufficient.



**The correlation shown is indicative and, in certain cases, may not hold.*

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/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'.

Rating Watch Alerts to the possibility of a rating change subsequent to, or, in anticipation of some material identifiable event with indeterminable rating implications. But it does not mean that a rating change is inevitable. A watch should be resolved within foreseeable future, but may continue if underlying circumstances are not settled. Rating watch may accompany rating outlook of the respective opinion.

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, the rating should be considered withdrawn.

Withdrawn A rating is withdrawn on a) termination of rating mandate, b) the debt instrument is redeemed, c) the rating remains suspended for six months, d) the entity/issuer defaults., or/and e) PACRA finds it impractical to surveill the opinion due to lack of requisite information.

Harmonization A change in rating due to revision in applicable methodology or underlying scale.

Surveillance. Surveillance on a publicly disseminated rating opinion is carried out on an ongoing basis till it is formally suspended or withdrawn. A comprehensive surveillance of rating opinion is carried out at least once every six months. However, a rating opinion may be reviewed in the intervening period if it is necessitated by any material happening.

Note. This scale is applicable to the following methodology(s):

Entities
a) Broker Entity Rating
b) Corporate Rating
c) Financial Institution Rating
d) Holding Company Rating
e) Independent Power Producer Rating
f) Microfinance Institution Rating
g) Non-Banking Finance Companies (NBFCs) Rating

Instruments
a) Basel III Compliant Debt Instrument Rating
b) Debt Instrument Rating
c) Sukuk Rating

Regulatory and Supplementary Disclosure

(Credit Rating Companies Regulations,2016)

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

Restrictions

(3) No director, officer or employee of PACRA communicates the information, acquired by him for use for rating purposes, to any other person except where required under law to do so. | Chapter III; 10-(5)

(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.

(8) PACRA prohibits its employees and analysts from soliciting money, gifts or favors from anyone with whom PACRA conducts business | Chapter III; 11-A-(q)

(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)

Independence & Conflict of interest

(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)

Proprietary Information