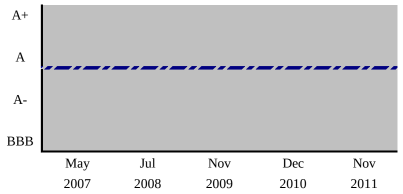
## AL-ABBAS SUGAR MILLS LIMITED (AASML)

### RATINGS (DECEMBER 2011)

| | NEW | PREVIOUS |
|---|---|---|
| **ENTITY** | | |
| Long Term | A | A |
| Short Term | A1 | A1 |
| **TFC** | | |
| Secured, privately placed (PKR 750mln) | A+ | A+ |

### HISTORY – LT ENTITY RATING




### FINANCIAL DATA

PKR (mln)

| | Jun-11* | Sep-10 | Sep-09 |
|---|---|---|---|
| Total Assets | 6,121 | 4,039 | 3,733 |
| Equity | 1,427 | 1,247 | 1,126 |
| Net Income | 270 | 205 | 282 |
| Gross Margins | 16.0 | 11.9 | 19.5 |
| ROA % | 1.8 | 1.2 | 1.9 |
| ROE % | 27.0 | 13.9 | 28.3 |
| Total Debt/Equity (%) | 70.8 | 58.1 | 58.1 |

** Based on unaudited accounts for 9 months ended June 30, 2011*

### ANALYSTS

Awais Z. Khan
+92 42 35869504
awais@pacra.com

Rana Muhammad Nadeem
+92 42 35869504
nadeem@pacra.com

### TFC Issue

The company issued a secured privately placed TFC of PKR 750mln in Nov07. The instrument has tenure of 6 years and carries profit at rate of 6-month KIBOR plus 175bps. The principal is being redeemed in 10 semi-annual equal installments (PKR 75mln each), commenced in May09. The issue is secured by first pari passu charge on the present and future fixed assets of AASML with 25% margin.

## RATING RATIONALE AND KEY DRIVERS

- The ratings reflect AASML's sound performance in its core business segments – sugar and ethanol – manifested from gradual increase in volumes and a rebound in gross margins, though largely led by appreciation in product prices. However, inflating operating and financial costs kept net margins under pressure. Meanwhile, the management's decision to dispose off loss making business units would yield benefits in future. The company's financial profile remained stretched, particularly during crushing season owing to higher working capital requirements. Nevertheless, adequate cashflows and largely stable coverages provide relief to it. The ratings continue to take support from the company's seasoned management team, having sound understanding of the industry dynamics. In order to further diversify its revenue stream, AASML is in the process of building a storage terminal at port; this is expected to add stable rental income.
- The ratings are dependent on the company's ability to maintain optimal capacity utilization while maintaining margins at adequate level. Meanwhile, any material deterioration in cashflows or accumulation of debts, in turn, compromising coverages, would have negative implications on the ratings.

## ASSESSMENT

- Sugarcane is one of the major crops in Pakistan with contribution of 4.5% in agriculture and ~1% in GDP. The demand of sugar in Pakistan is inelastic and is expected to increase in foreseeable future on the account of its strong correlation with population growth and lack of proper substitute. The country is expecting a bumper crop during the current season and the production of the sugar is projected to be higher as compared to last year. On international front, sugar prices have also observed a volatile pattern and are currently being traded at ~ $520 per ton. However, expected yield of sugarcane crop in major sugar producing countries (mainly Brazil) may help prices to achieve sustainability in near future.
- AASML's top-line witnessed a significant increase (53%) in FY10, mainly on account of high product prices and volumetric growth. However, gross margins declined due to sharp increase in input costs. Meanwhile, higher operating expenses and financial charges adversely impacted the bottom-line. Furthermore, significant increase in loss from discontinued operations, mainly representing impairment in value of assets, also dented the overall profitability. During 9MFY11, AASML, mainly benefiting from rising prices, posted a robust increase in its top-line. Gross margins also recovered as raw material prices remained largely stable. Despite registering lower other operating income and continuous losses from chemical and alloys divisions, AASML overall profitability benefiting from increased gross margins, improved as compared to same period last year.
- Going forward, the management intends to further consolidate its position in sugar and ethanol businesses. It would increase its ethanol sales by acquiring new clientele internationally. On sugar side, given expectation of bumper crop in the country, the domestic sugar prices may rationalize, which in turn, may affect AASML's margins. In order to further diversify its revenue stream, AASML is in the process of building a storage terminal at Karachi Port. Once on-line it is expected to provide a stable stream of PKR 40-50mln per annum. Meanwhile, demand for calcium carbide and ferro alloys products remain sluggish owing to cheap imports from China. Moreover, sale of electricity to Karachi Electric Supply Company (KESC) is terminated. Therefore, support from these operations to the bottom-line is not likely in FY12.
- At end-FY10, the company's working capital requirement increased owing to procurement of inventory. However, the company's cash cycle improved on the account of effective inventory management. During 9MFY11, AASML accumulated substantial short-term borrowings in line with high inventory buildups. However, it is expected to taper off, in line with gradual sales of finished goods before the start of crushing season. In 9MFY11, AASML's cash flows from operations remained stressed on account of significant increase in inventory levels. However, coverages slightly improved mainly benefiting from price led growth in profitability.
- AASML's leveraging remained dependent on the company's borrowings to finance its working capital needs. Moreover, AASML's leveraging reached 71% due to higher working capital requirements. However, the long-term debt of the company has decreased due to retirement of long-term obligations. Subsequent to end of crushing season, given gradual decline in inventories, leveraging is likely to ease out.

## PROFILE

- Al-Abbas Sugar Mills Limited (AASML), listed on the Karachi Stock Exchange (KSE), was incorporated in May 1991. Al-Abbas group owns majority shareholding (~48%) in AASML followed by Jahangir Siddiqui (JS) group with 24% holding.
- AASML's BoD, comprising seven members including the CEO, consists of key sponsoring individuals. The BoD, having diversified background and relative expertise, is a key source of guidance to the management. Mr. Shunaid Qureshi, the CEO, has been the driving force behind the company since its inception.
- The company has diversified businesses and operates in two different locations at Mirpurkhas and Dhabeji in Sindh. The businesses include a) Sugar (capacity of 7,500 M. tons per day), b) Ethanol (combined capacity of two units: 172,500 liters per day.) and c) Calcium carbide and Ferro Alloys (27,220 M. tons per annum). AASML meets its in-house power requirements through two captive power plants of 7.5MW and 15MW each.