



The Pakistan Credit Rating Agency Limited

Rating Report

Hunza Sugar Mills (Pvt.) Limited

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Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
08-Mar-2019	BBB	A2	Stable	Maintain	-
06-Sep-2018	BBB	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The ratings reflect the Company's diverse revenue streams (Sugar, Ethanol, Bagasse) and sponsors strong acumen in the sector. The Company remains exposed to volatility in Sugar sector. Low recovery rate and depressed sugar prices resulted in subpar performance in the sugar segment in FY18, having a significant impact on the Company's bottomline. However, sugar prices have recovered to an extent in the local market lately. Financial risk is high owing to highly leveraged capital structure. The Company utilizes short-term borrowings to finance its inventory and has also undertaken significant BMR activities during the year. This, coupled with high finance cost, has put the Company's coverages under distress. Meanwhile, Sponsors commitment to provide financial support in a timely manner cushions the risk profile of the Company.

The ratings are dependent upon the Company's ability to strengthen its margins, improve profitability and debt service coverages. Any further deterioration in margins and/or cash flows will impact the ratings. Improvement in governance framework and internal controls will be favorable for the ratings.

Disclosure

Name of Rated Entity	Hunza Sugar Mills (Pvt.) Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Ratings(Jun-18),Methodology Correlation Between Long-Term And Short-Term Rating Scale(Jun-18)
Related Research	Sector Study Sugar(Mar-18)
Rating Analysts	Adnan Dilawar adnan@pacra.com +92-42-35869504

Profile

Legal Structure Private Limited Company

Background Hunza Sugar Mills Limited ('Hunza Sugar') was incorporated in 2002. Hunza Sugar installed a distillery adjacent to its Sugar unit-1 that commenced commercial production in FY '14 and has CO2 processing plant that increased its capacity of 200MT during FY18

Operations The Company operates two sugar units in District Jhang and District Faisalabad. The sugar units have a combined crushing capacity of 16,000 MT per day. Distillery adjacent to its Sugar unit-1 has a production capacity of 125,000 Liters/day and is engaged in processing of food grade ethanol. Additionally, the company has CO2 plants with a processing capacity of 200MT

Ownership

Ownership Structure Hunza Sugar is a Family owned entity. Three brothers along with their members hold entire shareholding of the company. Mr. Idrees Chaudhry's family has 31% shareholding, Mr. Saeed Chaudhry's family has 32% and Mr. Waheed Chaudhry's family 37% shareholding.

Stability There is clear distinction as the shareholding is divided in three families.

Business Acumen Entities owned by the family are collectively called 'Hunza Group'. The groups flagship company is Hunza Ghee Industries (Pvt.) Limited in the Edile Oil sector which dates back to 1988. The company produces vegetable ghee and cooking oil that sells under the brand 'Swera Ghee' and 'Swera Cooking Oil'. It is involved in the import and sale of Edible Oil through its company Swera Traders (Pvt.) Limited. The Group diversified its operations and entered the sugar industry in 2002. Hunza Sugar expanded through forward integration by entering a distillery business in FY14. The group is in the process of setting up a bagasse based power plant under its' new group company 'Hunza Power'.

Financial Strength Hunza Group as a whole (Hunza Ghee, Hunza Sugar, Swera Traders & Power) have an asset base of PKR 13.8bln of which PKR 3.6bln are represented by equity in FY 18. Long-term debt exposure of the Group from banks is PKR 2.3 bln. The Group had a turnover PKR 18bln and a profit after tax of PKR 38mln.

Governance

Board Structure The Company has a three member board. All three are family members and shareholders of the company. There are no independent members on the Board.

Members' Profile The BoD is chaired by Mr. Idrees Chaudhry, the eldest brother, serves as Chairman of the board of all group companies (except Swera (Pvt) Ltd.). He serves as an advisor to the management. The directors have around fifteen years of experience in the Sugar Industry and over thirty years of experience in the Edile Oil Sector. Mr. Waheed looks after external relations of the company and represents the company at different forums i.e LCCI.

Board Effectiveness The BoD meets four times during FY18 to approve the financial statement. However, minutes of the meetings are restricted to formal approvals required for regulatory purposes.

Financial Transparency The auditors of the company, Amin, Mudassar & Co, issued an unqualified opinion the financial statements for FY18. The firm has been auditors of the company since FY18. The firm has satisfactory QCR rating and listed on SBP panel in category 'B'. From FY09 - FY17, the Company was audited by Javed Chaudhry & Co. who were not on the panel maintained by State Bank of Pakistan and are not QCR rated by ICAP.

Management

Organizational Structure The Company is headed by the CEO who is supported by Senior General Manager and Manager Finance & Accounts at the Head office. On Site, the company has GM projects with a team of production and technical staff including a head responsible for cane purchase and accounts personnel dealing with operational matters. IT function is provided to entities at group level.

Management Team Mr. Saeed is the youngest brother and is CEO of all Group companies (except Swera (Pvt) Ltd.). He has fifteen years of experience in the Sugar Industry and over thirty years of experience in the Edile Oil Sector.

Effectiveness The CEO and directors monitor the company's performance on a monthly basis through review of management accounts, accounts receivable and payable balance.

MIS Hunza Sugar has developed an in house software for managing its financial accounting needs. It has an Inventory module (Purchases and Inventory Management stores), Sales module (Sales Management and Stock Management), Payroll management and Cane Procurement System. Currently, the company is negotiating installation/implementation of a new ERP system to meet the growing needs of Hunza Sugar.

Control Environment The Company relies on segregation of duties and established processes and procedures as a means of internal control. The company should lay emphasis on improving its' control environment.

Business Risk

Industry Dynamics Sugar industry is characterized as competitive with a large number of players having relatively small shares in the market. Sugar production decreased to 6.57 Mln Tons during FY18 in comparison to 7.01 Mln tons in FY17 on the back of limited sugarcane utilization by mills. With carryover stock inventory of 1.974 mln, there is excess sugar of almost 3.391 mln Tons in the market creating significant stocks piled up at the end of Sept '18.

Relative Position Hunza Sugar contributed approximately 2.2% making it one of the top 20 sugar producers in the country and a leading sugar mill in Punjab region.

Revenues Hunza Sugar has experienced an increasing trend line in its turnover with revenues increasing by 36% in FY18 on account of heightened exports of refined sugar. The sales mix is dominated by local and export sales of refined sugar comprising 70% of the sales mix, followed by ethanol exports at 28%. Remaining portion of sales comprise of CO2, molasses and bagasse.

Margins GP Margins have decreased from 12% in FY17 to 6% in FY18 owing to low recovery rates and depressed sugar prices.

Sustainability Going forward, Hunza Sugar is expected to increase its turnover due to scheduled BMR activities underway in unit-2 that will add another 4,000MT to the crushing capacity per day. Performance of the company would mostly depend on the ethanol division which is expected to remain stable however, performance in the sugar division would largely depend on industry dynamics.

Financial Risk

Working Capital The Company experienced a drop in its working capital days as they decreased from 107 days in FY17 to 93 days in FY18 owing to an increase in trade payable days, with the elevation in payables pertaining to Unit 2 BMR activities being carried out for Capacity enhancement.

Coverages The Company's interest coverage stood at 1.4x during FY18 deteriorating from 2.6x in FY17 owing to decrease in FCFO and a highly leveraged balance sheet. Total coverage stood at 0.4x in FY18 dropping from 1x in FY17.

Capitalization Total Debt: Debt plus equity ratio stood constant at 76% in FY18 as it was in FY17. This debt majorly comprises of short-term debt and approaching current maturity of long-term debt (75%). Further, borrowing for BMR activity that will enhance capacity in Unit-2 and addition of CO2 plant contributed to the increase in long-term loans. Total Borrowings stood at PKR 7,598 Mln in FY18 resulting in a highly leveraged ratio of 76%.



Hunza Sugar Mills (Pvt). Limited
Private Limited

BALANCE SHEET	Sep-18 12M	Sep-17 12M	Sep-16 12M
a Non-Current Assets	5,198	4,634	4,129
b Investments (Incl. Associates)	201	122	113
Equity Instruments	-	-	-
Debt Instruments	201	122	113
c Current Assets	5,782	6,170	1,941
Inventory	2,524	4,270	867
Trade Receivables	247	251	-
Others	3,011	1,649	1,074
d Total Assets	11,181	10,927	6,182
e Debt/Borrowings	7,598	7,646	3,497
Short-Term	5,732	6,611	2,810
Long-Term (Incl. Current Maturity of Long-Term Debt)	1,866	1,035	687
Other Short-Term Liabilities	1,140	802	505
Other Long-Term Liabilities	-	-	-
f Shareholder's Equity	2,443	2,478	2,180
g Total Liabilities & Equity	11,181	10,927	6,182
INCOME STATEMENT			
a Turnover	12,041	8,866	8,751
b Gross Profit	717	1,047	603
c Net Other Income	409	89	536
d Financial Charges	(481)	(378)	(366)
e Net Income	(35)	299	473
CASH FLOW STATEMENT			
a Free Cash Flow from Operations (FCFO)	661	979	1,087
b Total Cashflows (TCF)	661	979	1,087
c Net Cash changes in Working Capital	847	(3,978)	51
d Net Cash from Operating Activities	1,024	(3,263)	831
e Net Cash from Investing Activities	(950)	(905)	(360)
f Net Cash from Financing Activities	(53)	4,149	(450)
g Net Cash generated during the period	21	(19)	21
RATIO ANALYSIS			
a Performance			
Turnover Growth	36%	1%	38%
Gross Margin	6%	12%	7%
Net Margin	0%	3%	5%
ROE	-1%	13%	25%
b Coverages			
Debt Service Coverage (X) (FCFO/Gross Interest+CMLTD+Uncovered STB)	0.4	1.0	1.2
Interest Coverage (X) (FCFO/Gross Interest)	1.4	2.6	3.0
Debt Payback (Years) (Total Debt (excluding Covered Short Term Borrowings) / FCFO)	16.1	3.8	2.8
c Capital Structure (Total Debt/Total Debt+Equity)			
Net Cash Cycle (Inventory Days + Receivable Days - Payable Days)	93	107	61
d Capital Structure (Total Debt/Total Debt+Equity)	76%	76%	62%

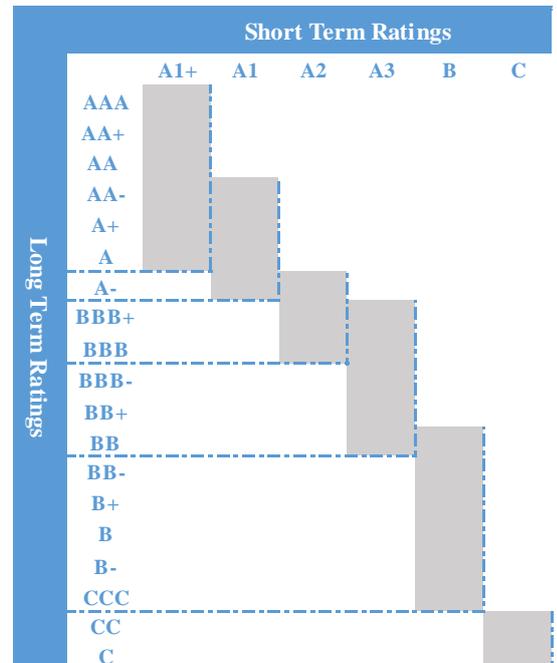
Hunza Sugar Mills (Pvt). Limited

Mar-19

Credit Rating Scale & Definitions

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 Ratings		Short Term Ratings	
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments	A1+	The highest capacity for timely repayment.
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.	A1	A strong capacity for timely repayment.
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.	A2	A satisfactory capacity for timely repayment. This may be susceptible to adverse changes in business, economic, or financial 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.	A3	An adequate capacity for timely repayment. Such capacity is susceptible to adverse changes in business, economic, or financial conditions.
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	The capacity for timely repayment is more susceptible to adverse changes in business, economic, or financial conditions.
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.	C	An inadequate capacity to ensure timely repayment.
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.		



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, a) some material identifiable event and/or b) deviation from expected trend. 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 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) cessation of underlying entity, c) the debt instrument is redeemed, d) the rating remains suspended for six months, e) the entity/issuer defaults, or/and f) PACRA finds it impractical to surveil the opinion due to lack of requisite information.

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

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(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)
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- (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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