



The Pakistan Credit Rating Agency Limited

Rating Report

Mehran Sugar Mills Limited

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Rating History					
Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
05-Apr-2024	A-	A2	Stable	Maintain	-
06-Apr-2023	A-	A2	Stable	Maintain	-
06-Apr-2022	A-	A2	Stable	Maintain	-
30-Sep-2021	A-	A2	Stable	Maintain	-
30-Sep-2020	A-	A2	Stable	Maintain	-
22-Oct-2019	A-	A2	Stable	Maintain	-
03-May-2019	A-	A2	Stable	Maintain	-
03-Dec-2018	A-	A2	Stable	Initial	-

Rating Rationale and Key Rating Drivers

The Pakistani sugar sector, recognized as the second most substantial agro-based industry within the nation, encompasses 91 mills with a collective processing capacity of roughly 80–90 million metric tons. The season ended with a sugar output of ~6.6 million tons, a ~16% decrease from the previous year’s ~7.9 million tons due to severe floods that damaged the crop and shortened the harvesting period. Despite the lower crop, the country had sufficient sugar stocks to meet the annual demand, owing to the large carryover from the previous year. Anticipated water scarcity is projected to precipitate a significant ~13.7% contraction in the forthcoming sugarcane supply for MY24, ascribed to a decrement in cultivated area and yield.

Mehran Sugar Mills Limited has upheld its credit rating through a strong financial performance, marked by a 58% revenue increase to PKR ~10.9 bln in MY23 (MY22: PKR 6.9 bln), aligned with industry’s upward trajectory. The escalation in cane costs has catalyzed a concomitant rise in sugar prices within the domestic sphere during MY23, thereby engendering significant profitability for the Company. The gross profit stood at PKR ~2.34 bln, indicating a ~21.5% gross margin (MY22: ~11.7%), while the net income rose to PKR ~1.443 bln (MY22: PKR 289 mln), reflecting a ~13.1% net margin (MY22: 4.2%). The looming challenges posed by elevated policy rates and the pervasive inflationary milieu, which are projected to exert a marginal impact on profit margins in MY24. However, Mehran Sugar Mills Limited’s financial resilience is evident in its reduced net working capital days to 38 days in MY23 (MY22: 53 days) and a leverage ratio of ~47.3% (MY22: ~45.9%), with a focus on maintaining stable margins and financial discipline amidst market fluctuations. Looking ahead, the management harbors an optimistic outlook regarding the Company’s fiscal trajectory, bolstered by a consistent share of profits emanating from Unicol Limited and the anticipated capital gains/dividend income derived from its short-term trading portfolio. The Company’s financial risk profile is characterized by a moderately leveraged capital structure, adequate coverage ratios, and proficient working capital management, all of which underscore its financial acumen and strategic prudence.

The company’s credit ratings are predicated on its ability to fortify business margins, sustain robust cash flows, and uphold financial coverages through unwavering financial discipline. An intensified commitment to the meticulous management of working capital is paramount. Any substantive erosion in margins and/or financial coverages would precipitate an adverse recalibration of the company’s credit ratings

Disclosure

Name of Rated Entity	Mehran Sugar Mills Limited
Type of Relationship	Solicited
Purpose of the Rating	Entity Rating
Applicable Criteria	Methodology Corporate Rating(Jul-23),Methodology Correlation Between Long-term & Short-term Rating Scales(Jul-23),Methodology Rating Modifiers(Apr-23)
Related Research	Sector Study Sugar(Aug-23)
Rating Analysts	Usama Ali usama.ali@pacra.com +92-42-35869504

Profile

Legal Structure Mehran Sugar Mills Limited ('Mehran Sugar' or 'the Company') is a public limited company incorporated in December, 1965. The Company is listed on Pakistan Stock Exchange.

Background The company started its operations in 1968 with a cane crushing capacity of 1,500 TCD. Over the years, the company has increased its capacity to 12,500 TCD through BMR projects. The company also has a joint venture ethanol plant with United Ethanol Industries, which produces food and industrial grade ethanol. The company has also invested in a joint venture power plant with Mehran Energy, which generates electricity from bagasse. The company has also diversified into the FMCG and energy sectors through its joint ventures UniFoods Industries and Mehran Energy respectively.

Operations The Company is a leading producer of sugar and its by-products. The mill is situated in District Tando Allahyar, with a total capacity of 12,500 TCD. In MY23, the Company processed 804,872MT of sugarcane to produce 85,796MT (MY22: 95,642 MT) of sugar with a sucrose recovery rate of 10.66% (MY22: 11.16%).

Ownership

Ownership Structure The company has a concentrated ownership structure, with the Hasham family holding 75.6% of the total shares as of December 2023. The Hasham family has a long association with the sugar industry and a strong financial profile. The family also has interests in other sectors, such as textile, cement, and power. The remaining 24.4% of the shares are held by the general public, financial institutions, and other corporate entities.

Stability Company's controlling interests vests with one group and each family within the group holds a defined share. The ownership of the Company is seen as stable.

Business Acumen The company has a high business acumen, as the Hasham family has demonstrated its ability to identify and capitalize on the opportunities and challenges in the sugar industry and other sectors. The family has invested in BMR projects to enhance the production capacity and quality of the company, and has diversified its business portfolio to reduce its reliance on the sugar industry. The family has also established long-term relationships with its customers, suppliers, and financiers, and has maintained a good reputation and brand recognition in the market.

Financial Strength As at MY23, the Company had a consolidated asset base of PKR 6.5bln and consolidated equity base of PKR 3.9bln.

Governance

Board Structure The Board of Directors comprises of seven individuals, which include two executive directors, three non-executive directors, and two independent Directors. The board has a balanced mix of skills, experience, and diversity, and oversees the strategic direction and performance of the company.

Members' Profile Sponsoring family has a strong presence on the Board. However, members have significant experience in the sugar industry which is balanced by an adequate mix of business, finance, and legal experts. The board is chaired by Mr. Muhammad Kasim Hasham and has over 35 years of experience in the sugar industry.

Board Effectiveness In order to maintain effective oversight, the Board of Directors have formed two committees, namely, the Audit Committee and the Human Resource and Remuneration Committee. During MY23, four meetings of the Audit Committee and two meetings of the Human Resources and Remuneration Committee were conducted. Board election was also held during the aforementioned year.

Financial Transparency The external auditors of the Company, M/s Grant Thornton Anjum Rehman is a QCR rated firm and in SBP's panel of auditors with "A" category. Unqualified opinion was issued on Sep 23 financial statements.

Management

Organizational Structure The Company is headed by the Chief Executive Officer. The Company's Chief Financial Officer, Resident Director, and Director Cane report directly to the CEO. Internal Audit, HR & IT are headed by separate managers and they report functionally to CEO and CFO. However, the head of Internal Audit and HR functionally reports to the Board Audit Committee and Board HR & Remuneration Committee and the Company Secretary functionally reports to the Board's Chairman.

Management Team Management has long association with Mehran Sugar adding the required experience in sugar industry and their respective fields. Mr. Ahmed Ebrahim Hasham acts as the CEO of the Company and has 20+ years of practical experience in various sectors and is also chairman of Sindh for Pakistan Sugar Mill Association.

Effectiveness The Company has instituted an Executive Committee comprising all heads of departments. The Committee is headed by the CEO and meets on a monthly basis to review performance and enable short-term decision making.

MIS Mehran Sugar has deployed an in-house system which has a sugar cane management module, store management module and human resources module. These are all integrated with the accounting system which is also developed in-house.

Control Environment The Company has outsourced the internal audit function to BPO resources at work.

Business Risk

Industry Dynamics Pakistan's sugar industry, the 2nd largest in the country, has 91 mills and can crush ~80-90mln MT annually. It faces constraint from government-set sugarcane price. Floods in MY23 damaged crops and lowered yields. Sugar production fell by ~16% to ~6.6 million tons, below the expected ~8.0 million tons. Exports were not feasible and a big foreign exchange opportunity was lost. Export quota disputes and high finance costs also hurt the industry. Sugar prices dropped with the new season and large carryover. Water shortage may reduce sugarcane supply by ~13.7% in MY24.

Relative Position The Company contributed approximately ~1.5% to the total sugar production in the country.

Revenues Refined sugar (~89%) is the main revenue source, followed by molasses (~9%) and bagasse (~2%). Topline surged by ~59% to PKR 10.9bln in MY23 (MY22: PKR 6.9bln) due to higher prices and carryover stocks. Revenues are projected to decline marginally in MY24 as crop yield will drop by ~3.8% from inadequate rainfall. Local demand will absorb expected production, leaving little room for export.

Margins Gross margin improved to ~21.5% in MY23 (MY22: ~11.7%) from higher prices of lower-cost stocks. Operating margin was ~17.9% (MY22: 7.0%). Net profit soared to PKR 1.443bln (MY22: PKR 289mln), with net margin at 13.1% (MY22: 4.2%). Margins will dip slightly in MY24 due to higher policy rate and inflationary costs.

Sustainability The company operates in a volatile sugar industry with multiple external risks and uncertainties. The company achieved remarkable growth in MY23, leveraging its competitive position and favourable market conditions. The company faces potential challenges in MY24, requiring proactive risk management and strategic adaptation.

Financial Risk

Working Capital Net working capital days reduced significantly to 38 days in MY23 (MY22: 53 days) from lower inventory days (36 days in MY23 vs 56 days in MY22). Receivable days increased slightly to 6 days (MY22: 5 days), while payable days decreased to 4 days (MY22: 7 days). Short-term trade leverage turned positive and reached ~47.3% in MY23.

Coverages Free cash flows increased by ~212.2% to ~PKR 1.95bln in MY23 (MY22: ~PKR 625mln) from higher profitability. Finance cost increased by ~20.71% to PKR 635mln in MY23 (MY22: PKR 526mln) from interest rate hike. Interest coverage rose to ~3.1x (MY22: 1.2x) from higher EBITDA. Debt payback period decreased to 0.4x in MY23 (MY22: 10.2x) from debt reduction.

Capitalization Debt coverage ratio dropped by ~72% to ~12.8% in MY23 (MY22: ~45.9%) from lower short-term borrowings (~PKR 14mln in MY23 vs ~PKR 1258mln in MY22). Total borrowings were ~PKR 570mln in MY23 (MY22: PKR 2,333mln). Coverages ratio will fluctuate as 1MFY24 shows gearing rising to almost 52%.



The Pakistan Credit Rating Agency Limited

Financial Summary

PKR mln

Mehran Sugar Mill Limited Sugar	Dec-23 3M	Sep-23 12M	Dec-22 3M	Sep-22 12M
A BALANCE SHEET				
1 Non-Current Assets	2,510	2,467	2,780	2,708
2 Investments	2,251	914	539	732
3 Related Party Exposure	1,814	1,804	1,517	1,167
4 Current Assets	5,664	1,419	3,082	1,989
<i>a Inventories</i>	4,837	593	2,414	1,553
<i>b Trade Receivables</i>	186	289	138	100
5 Total Assets	12,239	6,603	7,919	6,596
6 Current Liabilities	2,364	1,326	1,696	1,309
<i>a Trade Payables</i>	-	105	290	126
7 Borrowings	4,701	570	2,970	2,333
8 Related Party Exposure	-	-	-	-
9 Non-Current Liabilities	820	828	200	204
10 Net Assets	4,354	3,879	3,052	2,750
11 Shareholders' Equity	4,354	3,879	3,052	2,750
B INCOME STATEMENT				
1 Sales	1,705	10,984	2,039	6,898
<i>a Cost of Good Sold</i>	(1,411)	(8,620)	(1,937)	(6,091)
2 Gross Profit	294	2,364	102	807
<i>a Operating Expenses</i>	(100)	(396)	(71)	(328)
3 Operating Profit	194	1,968	31	479
<i>a Non Operating Income or (Expense)</i>	395	948	352	441
4 Profit or (Loss) before Interest and Tax	589	2,916	383	920
<i>a Total Finance Cost</i>	(84)	(635)	(66)	(526)
<i>b Taxation</i>	(32)	(838)	(28)	(104)
6 Net Income Or (Loss)	474	1,443	289	289
C CASH FLOW STATEMENT				
<i>a Free Cash Flows from Operations (FCFO)</i>	172	1,951	74	625
<i>b Net Cash from Operating Activities before Working Capital Changes</i>	142	1,275	(31)	173
<i>c Changes in Working Capital</i>	(3,338)	637	(605)	(483)
1 Net Cash provided by Operating Activities	(3,196)	1,912	(636)	(311)
2 Net Cash (Used in) or Available From Investing Activities	(1,030)	211	49	430
3 Net Cash (Used in) or Available From Financing Activities	(22)	(866)	628	(97)
4 Net Cash generated or (Used) during the period	(4,248)	1,257	41	22
D RATIO ANALYSIS				
1 Performance				
<i>a Sales Growth (for the period)</i>	-37.9%	59.2%	18.2%	13.8%
<i>b Gross Profit Margin</i>	17.2%	21.5%	5.0%	11.7%
<i>c Net Profit Margin</i>	27.8%	13.1%	14.2%	4.2%
<i>d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)</i>	-185.7%	23.6%	-26.1%	2.1%
<i>e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Sh</i>	46.1%	43.5%	39.9%	11.0%
2 Working Capital Management				
<i>a Gross Working Capital (Average Days)</i>	158	42	94	60
<i>b Net Working Capital (Average Days)</i>	152	38	85	53
<i>c Current Ratio (Current Assets / Current Liabilities)</i>	2.4	1.1	1.8	1.5
3 Coverages				
<i>a EBITDA / Finance Cost</i>	3.0	3.5	1.7	1.5
<i>b FCFO / Finance Cost+CMLTB+Excess STB</i>	2.1	2.6	0.5	0.7
<i>c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)</i>	1.2	0.4	29.7	10.2
4 Capital Structure				
<i>a Total Borrowings / (Total Borrowings+Shareholders' Equity)</i>	51.9%	12.8%	49.3%	45.9%
<i>b Interest or Markup Payable (Days)</i>	81.8	16.1	80.5	67.8
<i>c Entity Average Borrowing Rate</i>	8.9%	19.2%	6.4%	13.1%

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.

Scale	Long-term Rating Definition
AAA	Highest credit quality. Lowest expectation of credit risk. Indicate exceptionally strong capacity for timely payment of financial commitments
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.
AA-	
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.
A-	
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.
BBB	
BBB-	
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.
BB	
BB-	
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.
B-	
CCC	Very high credit risk. Substantial credit risk "CCC" Default is a real possibility.
CC	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.
C	
D	Obligations are currently in default.

Scale	Short-term Rating 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 conditions.
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 surveil 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):

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

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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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- (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)

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- (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 | Clause 11-(A)(p).
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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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- (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)
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- (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 | 17-(a)
- (19) PACRA reviews all the outstanding ratings periodically, on annual basis; Provided that public dissemination of annual review and, in an instance of change in rating will be made; | Chapter III | 17-(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 | 17-(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 | 17-(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 | 14-3(f)(vii)

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