The Pakistan Credit Rating Agency Limited

Rating Report

SGM Sugar Mills Limited

Report Contents

Rating History

Dissemination Date	Long Term Rating	Short Term Rating	Outlook	Action	Rating Watch
05-Apr-2024	BBB	A2	Stable	Maintain	-
06-Apr-2023	BBB	A2	Stable	Maintain	-
08-Apr-2022	BBB	A2	Stable	Maintain	-
27-Sep-2021	BBB	A2	Stable	Upgrade	-
02-Oct-2020	BBB-	A3	Positive	Maintain	-
06-Nov-2019	BBB-	A3	Stable	Maintain	-
07-May-2019	BBB-	A3	Stable	Maintain	-
31-Dec-2018	BBB-	A3	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.
SGM Sugar Limited's credit rating remains steadfast with a stable outlook, a reflection of the company's strategic acumen and financial fortitude. In MY23, the company's revenue surged to PKR 9,185 mln, (MY22: PKR 5,119 mln), a testament to its ability to capitalize on favorable market trends and a significant recovery rate of approximately ~10%. The gross profit margin climbed to a significant 18.3% (MY22: 14.6%), while the net income rebounded to PKR 324 mln, marking a turnaround from the previous year's loss of PKR 102 mln. This financial upswing is supported by a shrewd management of inventory and a buoyant sugar price. Despite these positive developments, the rationale for maintaining the existing rating is anchored in a prudent approach to financial management. The company’s trade leverage has stretched further. SGM Sugar Limited’s financial resilience is apparent in its improved working capital cycle, with inventory days reduced to 90 (MY22: 141 days) and net working capital days at 85 (MY22: 116 days). With a leverage ratio carefully managed at ~60%, SGM Sugar Limited is well-positioned to navigate the anticipated headwinds of MY24, including a modest dip in crop yield and escalating production costs. The decision to uphold the rating encapsulates the company's robust financial risk profile is marked by a moderately leveraged capital structure, adequate coverage ratios, and effective working capital management, highlighting its fiscal savvy and strategic foresight.

The Company's credit standings are contingent upon its capacity to enhance profit margins, sustain strong cash flow, and maintain financial safeguards through unwavering financial discipline. An escalated focus on the rigorous administration of working capital is crucial. Any substantial deterioration in margins and/or financial safeguards would be considered a credit negative event.

Disclosure	
Name of Rated Entity	SGM 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 SGM Sugar Mills Limited ("SGM" or "the Company") is a public unlisted company.

Background The Company was incorporated in Sep-07 and was formerly owned jointly by Dhabi Group (44%), Etihad Group (22%) and Mehar Family (34%). During May-18, United Group, represented by the Essarani Family, acquired shareholding of the Company. The Mehar Family still retains their shareholding in the Company.

Operations The primary business of the Company involves the sale and manufacturing of crystalline sugar along with ensuing by-products (Molasses and Bagasse). The Company has a crushing capacity of 12,000 TCD with its mill located in Ghotki, Sindh, whereas the head office is located in Karachi. During marketing year (MY) 23, the Company produced a total of 84,685 MT of sugar, crushing857,693 MT of sugarcane while achieving a recovery rate of 10%.

Ownership

Ownership Structure Major shareholding of the Company rests with Essarani Family (77%), through Mr. Deoo Mal Essarani (16%) and his three sons – Mr.Asha Ram (29%), Mr. Mahesh Kumar (13%) and Dr. Tara Chand (20%). Remaining shareholding resides with Mehar Family, through Mr. Sardar Muhammad Baksh Khan Mehar (10%) and Mr. Sardar Ali Gohar Khan Mehar (13%)

Stability Ownership is stable as the Company's controlling interest now vests with one family. Each individual in the family holds a defined share in the Company.

Business Acumen Essarani family has been involved in agriculture sector for a significant period of time and owns entities collectively represented under 'United Group'. The Group's entities include Sindh Abadgar's Sugar Mills Limited, United Ethanol Industries Limited, Agro Trade Private Limited, and United Agro Chemicals

Financial Strength The Company has adequate financial strength derived from its Group and support of sponsors. The company had total assets worth PKR 8.8bln, supported by an equity base of PKR 2.6bln as at MY23. The Company posted a net profit worth PKR 324mln during MY23.

Governance

Board Structure Board of Directors comprises four members including the Chairman, Chief Executive Officer and two Non-Executive Director. All four members belong to Essarani Family, with no representation of Mehar Family

Members' Profile Mr. Deo Mal Essarani acts as the Chairman of the Board. He has over 46 years of diversified experience and also acts as the Chairman for two other group companies - Sindh Abadgar's Sugar Mills and United Ethanol Industries Limited. Dr, Tara Chand acts as a Non-Executive Director. Mr. Chand has more than 15 years of experience in the sugar industry.

Board Effectiveness Low frequency of Board meetings and lack of Board committees reflects a room for improvement on effectiveness of the Board.

Financial Transparency M/s Rahman Sarfaraz Rahim Iqbal Rafiq Chartered Accountants, classified in Category 'A' by the SBP with a satisfactory QCR rating by ICAP, have been appointed as the external auditors of the Company. They have expressed an unqualified opinion on the financial statements for the year Sep-23

Management

Organizational Structure Highest level of authority lies with the Chief Executive, who is supported by Resident Director Mills and Chief Financial Officer. The Company has established functions for cane procurement, production, mechanical etc at mill location that report to the Resident Director. All functions at head office pertaining report to CFO.

Management Team Mr. Asha Ram has been appointed as CEO. However, key responsibility for managerial oversight and decision making rests with Dr. Tara Chand Essarani. Dr. Tara Chand is a medical doctor by profession and a member of Pakistan Sugar Mills Association. He is also the CEO of Sindh Abadgar's Sugar Mills Limited and United Ethanol Industries Limited. He has over fifteen years of experience in the Sugar Industry.

Effectiveness The Company has no management committees in place. However, meetings are conducted fortnightly to discuss business performance and organizational structure changes. All HODs and CEO are present at the meetings. In addition, further meetings are called as required.

MIS The Company has deployed ERP software from Cosmosoft.

Control Environment Oversight and effective management is maintained through the internal audit department which is shared on a group level. The department is headed by Mr. Ali Raza Dosani, who acts as the Group Internal Auditor. The group has expanded the internal audit department by inducting more individuals recently.

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 Due to high number of players in industry, companies relatively have low market share. The Company had a market share of ~ 1.5% during MY23 in production terms .

Revenues During MY23, Company posted sales worth PKR 9185mln in comparison to PKR 5199mln in MY22 owing to higher volumetric sales supported by increased prices and regulated inventory movement after the crushing season. Going forward, during MY24, the Company's revenues are anticipated to decline marginally from the previous year as there will be an estimated drop in crop output by ~3.8% due to insufficient rainfall, resulting in lower yield. Expected production will meet domestic demand as population is also rising yearly, leaving less room for export.

Margins Gross margin increased to 18.3% in MY23 (MY22: 14.6%), as the Company benefited from higher sugar prices and export compared to the previous year. Likewise, operating margin rose to 16.6% (MY22: 12.0%) due to the positive impact from gross margin. At net level, the Company recorded net profit of PKR 324mln (MY22: Net Loss PKR 102mln). As a result, the Company's net margin improved to 3.5% (MY22: -2.0%). Looking ahead, during MY24, the Company's margins are expected to decline slightly because of the rise in the producion costs and high policy rates.

Sustainability Going forward, the management aims to improve business performance through efficient operations with no major expansion activity planned.

Financial Risk

Working Capital The Company witnessed improvement in working capital cycle during MY23. During the period, inventory days stood at 90 days as compared to 141 days as at MY22. This was the primary reason behind improvement in net working capital days of 85 days (MY22: 116 days). Borrowing cushion for additional short-term funds has remained negative for the Company. Short term trade leverage and short-term total leverage stood at -17% and -14%, respectively as at MY23.

Coverages The Company's Free Cash Flows from Operations stood at PKR 1,885 mln during MY23 (MY22: PKR 1,021mln. However, finance cost witnessed significant increase amidst interest rate hike during MY23 and stood at ~PKR 1041mln as compared to ~PKR 748mln during MY22. Subsequently, the Company's coverages slightly improved with interest coverage standing at 1.8x (MY22: 1.4x) and debt payback period standing at 3.5x (MY22: 12.3x).

Capitalization The Company has a moderately leveraged capital structure represented by a leveraging ratio of ~60% as at MY23. Total debt (MY23: PKR 3.2bln, MY22: PKR 4.9bln) is constituent of short-term borrowings (37% of total debt) (MY23: PKR 1,550mln, MY22: PKR 2,150mln) undertaken for working capital requirements, and long-term debt undertaken for BMR (MY22: PKR 1,307mln, MY22: 1,7266mln). Additionally, the Company's equity base stood at PKR 2.687bln as at MY23.

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Financial Summary
PKR mln

SGM Sugar Mills Limited	Sep-23	Jun-23	Sep-22	Sep-21
Sugar	12M	9M	12M	12M
A BALANCE SHEET				
1 Non-Current Assets	6,329	6,170	6,477	6,691
2 Investments	69	-	-	-
3 Related Party Exposure	-	-	-	-
4 Current Assets	2,390	5,292	3,278	1,562
a Inventories	*1,766*	*3,630*	*2,824*	*1,194*
b Trade Receivables	*8*	*833*	*0*	*21*
5 Total Assets	8,788	11,462	9,755	8,252
6 Current Liabilities	1,265	948	1,478	623
a Trade Payables	*247*	*199*	*91*	*88*
7 Borrowings	3,290	6,542	4,291	3,369
8 Related Party Exposure	860	860	860	-
9 Non-Current Liabilities	686	706	763	836
10 Net Assets	2,687	2,406	2,363	3,426
11 Shareholders' Equity	2,687	2,407	2,363	3,425
B INCOME STATEMENT				
1 Sales	9,185	6,347	5,202	4,705
a Cost of Good Sold	*(7,505)*	*(5,423)*	*(4,443)*	*(4,036)*
2 Gross Profit	1,680	924	759	670
a Operating Expenses	(151)	(110)	(135)	(116)
3 Operating Profit	1,529	815	624	554
a Non Operating Income or (Expense)	*(2)*	*22*	*22*	*(6)*
4 Profit or (Loss) before Interest and Tax	1,527	837	646	548
a Total Finance Cost	*(1,041)*	*(767)*	*(752)*	*(374)*
b Taxation	*(162)*	*(26)*	*4*	*(6)*
6 Net Income Or (Loss)	324	44	(102)	168
C CASH FLOW STATEMENT				
a Free Cash Flows from Operations (FCFO)	*1,885*	*1,070*	*1,021*	*805*
b Net Cash from Operating Activities before Working Capital Changes	*908*	*424*	*447*	*448*
c Changes in Working Capital	*425*	*(2,495)*	*(793)*	*(1,247)*
1 Net Cash provided by Operating Activities	1,333	(2,071)	(347)	(799)
2 Net Cash (Used in) or Available From Investing Activities	(263)	(51)	(426)	(134)
3 Net Cash (Used in) or Available From Financing Activities	(100)	1,963	1,022	778
4 Net Cash generated or (Used) during the period	970	(159)	250	(156)
D RATIO ANALYSIS				
1 Performance				
a Sales Growth (for the period)	76.6%	62.7%	10.5%	-13.9%
b Gross Profit Margin	18.3%	14.6%	14.6%	14.2%
c Net Profit Margin	3.5%	0.7%	-2.0%	3.6%
d Cash Conversion Efficiency (FCFO adjusted for Working Capital/Sales)	25.1%	-22.5%	4.4%	-9.4%
*e Return on Equity [Net Profit Margin * Asset Turnover * (Total Assets/Shareho*	12.8%	2.4%	-3.5%	5.8%
2 Working Capital Management				
a Gross Working Capital (Average Days)	91	157	142	62
b Net Working Capital (Average Days)	85	151	135	53
c Current Ratio (Current Assets / Current Liabilities)	1.9	5.6	2.2	2.5
3 Coverages				
a EBITDA / Finance Cost	1.9	1.5	1.5	2.5
b FCFO / Finance Cost+CMLTB+Excess STB	1.0	0.8	0.7	1.0
c Debt Payback (Total Borrowings+Excess STB) / (FCFO-Finance Cost)	3.5	7.5	12.3	5.7
4 Capital Structure				
a Total Borrowings / (Total Borrowings+Shareholders' Equity)	60.7%	75.5%	68.6%	49.6%
b Interest or Markup Payable (Days)	101.0	122.6	108.6	78.2
c Entity Average Borrowing Rate	19.9%	17.6%	15.4%	9.3%

Credit Rating

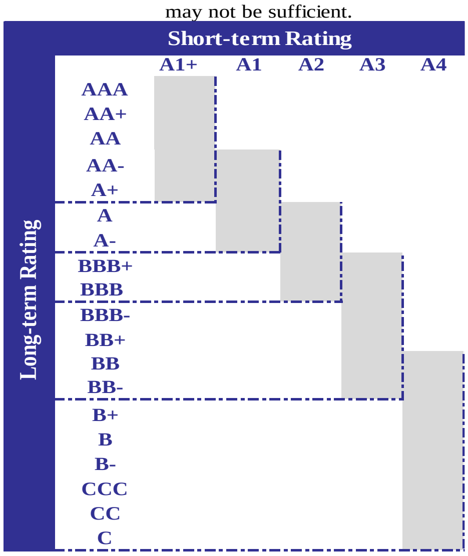
Credit rating reflects forward-looking opinion on credit worthiness of underlying entity or instrument; more specifically it covers relative ability to honor financial obligations. The primary factor being captured on the rating scale is relative likelihood of default.

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):

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

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 | Clause 11-(A)(p).
(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 | 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)
Proprietary Information