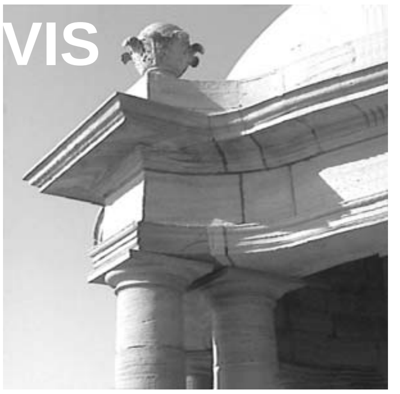
JCR-VIS



SUGAR INDUSTRY

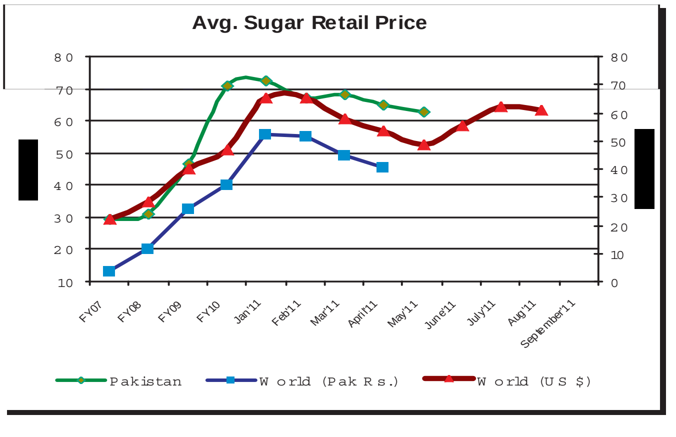
Sector Update - October 2011

Sugar industry, the second largest after textiles, currently has 86 factories in operation country-wide, with an installed capacity of 7.0 million tonnes of sugar annually. The industry, ranking 15th largest globally, produces one of the finest quality sugar of international standard and directly employs over 30,000 personnel.

Amidst the recession prevailing during the last two years, sugar was one of the main contributors to food inflation, reflecting the importance of the commodity in the country's economy. This was mainly on the back of a downward production cycle, thus causing the phenomenal rise in sugar cane prices during the last two seasons.

Sugar cane crushing in the country usually begins in October/November. Production for 2010/11 was about 4.1MMT, up from 3.1MMT during the previous season. The increase was largely attributable to increased cultivation area (approx. by 15%). Sugar cane support price of Rs 125 per 40 kg was set by the provincial government of Punjab & Khyber Pakhtunkhwa and Rs. 127 per 40 kg by Sindh. However, the average prices in the country have hovered around Rs. 200 per 40 kg level. On account of prevailing high sugar cane prices and low recovery rates vis-à-vis recovery rates in other countries, the domestic cost of production was considerably high.

The prices in international market have also reached an all time high during the outgoing year given lower world output for the second consecutive year. On the other hand, consumption has continued to grow, albeit at a lower rate (approx. 2.03%) relative to 10 year's average growth (approx. 2.59%) and global stocks have reduced considerably over the last two years.



The above chart presents the price behavior of sugar both locally and globally. Locally, this is influenced by various factors including policies affecting sugar cane pricing, the supply of sugar to markets and import possibilities to overcome demand – supply gap, if any. During the current financial year, demand – supply gap of sugar in the local market narrowed on account of somewhat reasonable carryover stocks and higher production vis-à-vis demand of sugar. This had exerted pressure on prices in local market, and sugar ex-mill prices which went over Rs. 75/kg in the previous year and 1QFY11, have declined gradually to below Rs. 60/kg during 2Q and 3Q of FY11. However, on account of usually high off-take before the month of Ramadan, which was in the last quarter of FY11, prices (ex-mill) of the commodity again recouped to around Rs. 75/kg. While the pressure was released subsequent to the month of Ramadan on account of lower demand as well as expected supply from the upcoming season, ability to sell sugar on a timely basis will continue to be key determinant of profitability and margins of industry players.

Presently, the sugar sector players have roughly disposed off 80% of their stocks. With still two months remaining in the crushing season, the supply though adequate, is not ample to exert any significant downward pressure on prices. Moreover, the prevailing uncertainty in the market amidst flood situation in some parts of the country will also play a key role in holding prices. In the upcoming crushing season, there will be ample availability of sugarcane due to increased acreage on the back of better support price. The current estimates are about 4.1 MMT but it is likely to cross 4.5 MMT, placing the country in a position of surplus as against the estimated annual consumption demand of below 4.4MMT. On the contrary, recent rains and flooding in some parts of the country has affected sugarcane crop. However, the resultant improvement in yield and sucrose recovery is likely to offset the impact of lost crop. In this scenario, companies may improve their profitability by enhancing capacity utilization while ensuring timely procurement of raw material.

High prices have eaten into consumption all over the globe. Prices struck a 30-year peak in the month of January and February in 2011 on account of cyclone damage to crop in Australia and Brazil and considerable shortfall in Western & Eastern Europe due to unfavorable weather. However, since the peak in February 2011, the prices started experiencing considerable decline on account of more than forecasted supply from the world's largest producers and suppliers of sugar in the first quarter of current calendar year. The production estimates of sugar have been surprised by production tail in Thailand, Australia and Brazil where supply outstripped demand. Thailand, the world's second-largest exporter after Brazil, produced a record of about 9.0MMT in 2010/11 harvest, up by about 3.0MMT (30%) relative to the previous season preceding year. Sugar production in Brazil continued to rise and registering another record volume season, despite a drop in yields caused by dry weather in 2010/11. India, the world's largest consumer, has also allowed exports of 0.5 MMT of sugar following a bumper crop.

After two seasons of large deficits, the production estimates of outgoing season registered a significant surplus. Global sugar surplus estimate for 2010/11 stood at 10.6 MMT, after a deficit of 0.1 MMT a year ago. Global sugar output estimated at 176.4 MMT as against the forecasted consumption of 168.8 MMT for 2010/11. The 2011/12 season is expected to see the sugar balance in surplus: however, the size of surplus is in question. Considering the stock balances and projected increased production, the downward pressure on prices of sugar in international market is expected to remain during the ongoing financial year. Sugar prices are expected to remain volatile however these are likely to be contained within a downward trend, going forward. In domestic market the prices may not experience any significant move in either direction, and are expected to remain strong in short and medium term on account of prevailing uncertainty in the market amidst flood situation.

Sugar future also fell in view of revised production estimates. As of September 01, 2011, future contracts of London (white sugar) and New York (raw sugar) markets have dropped from US$ 770/MMT and US$ 654.33/MMT, respectively to US$ 735/MMT and US$ 633/MMT, respectively for December 2011. Sugar futures for the second quarter of Calendar Year 2012 (May 2010), fell to US$ 705/MMT and US$ 573/MMT in London and New York markets, respectively.

Production Statistics

KSML's main product is white sugar while molasses, bagasse and filter cake are the by-products. Sugar and molasses are sold on commercial basis while bagasse is largely used for internal electricity generation. Over the years, decline in recovery rate has exerted pressure on production of sugar. Recovery rate of sucrose is important in determining production levels, which primarily depends on soil fertility, availably of water, efficient machinery and manual expertise. The increase in production during FY11 was on account of a prolonged crushing season of 126 days as compared to 104 days in FY10. Nevertheless, plant efficiency remained compromised as manifested in capacity utilization below:

	Sugar			Molasses		
	FY11	**FY10**	**FY09**	**FY11**	**FY10**	**FY09**
Capacity (TCD)	16,000	14,000	14,000	-	-	-
Days of Crushing	126	104	104	-	-	-
Cane Crushed(MT)	887,484	773,266	975,579	-	-	-
Production	87,501	77,317	101,356	39,290	32,960	43,584
Utilization	50.3%	53.11%	67%	-	-	-
Recovery	9.67%	10%	10.39%	4.42%	4.26%	4.47%
Per Day Crushing	7,044	7,435	9,381	-	-	-

Production of molasses was largely in line with its recovery while the company also produced leftover products i.e. bagasse and filter cake.

Jahangir Kothari Parade (Lady LLoyd Pier)
Inspired by Her Excellency, The Honorable Lady Lloyd, this promenade pier and pavillion was constructed at a cost of 3 Lakhs and donated to the public of Karachi by Jahangir Kothari to whose genrosity and public spirit the gift is due. Foundation stone laid on January 5, 1920. Opened by Her Excellency, The Honorable Lady Lloyd on March 21, 1921.

Dome: A roof or vault, usually hemispherical in form. Until the 19th century, domes were constructed of masonry, of wood, or of combinations of the two, frequently reinforced with iron chains around the base to counteract the outward thrust of the structure.

Origins: The dome seems to have developed as roofing for circular mud-brick huts in ancient Mesopotamia about 6000 years ago. In the 14th century B.C. the Mycenaean Greeks built tombs roofed with steep corbeled domes in the shape of pointed beehives (tholos tombs). Otherwise, the dome was not important in ancient Greek architecture. The Romans developed the masonry dome in its purest form, culminating in a temple built by the emperor Hadrian. Set on a massive circular drum the coffered dome forms a perfect hemisphere on the interior, with a large oculus (eye) in its center to admit light.


Jahangir Kothari Parade

National Excellence, International Reach

JCR-VIS Credit Rating Company Limited is committed to the protection of investors and offers a blend of local expertise and international experience to serve the domestic financial markets. With its international reach, JCR-VIS is positioned to aim for an international mark. In this regard, the global experience of our principal, Japan Credit Rating Agency, Ltd. has been invaluable towards adding depth to our ongoing research endeavors, enriching us in ways, that enable us to deliver our responsibilities to the satisfaction of all investors.

The edifice of the Jahangir Kothari Parade has stood proudly through the years and is a symbol of our heritage. Its 'Dome' as the most stable of building structures, exemplifies architectural perfection. Committed to excellence, JCR-VIS continues its endeavor to remain an emblem of trust.

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