February 24, 2022

Dalmia Bharat Sugar and Industries Limited: Change in limits and Ratings Reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loan	245.00	373.33	[ICRA]AA(Stable); reaffirmed
Fund Based – Working Capital Facilities	797.50	727.50	[ICRA]AA(Stable); reaffirmed
Non-fund Based – Working Capital Facilities	127.50	152.50	[ICRA]A1+; reaffirmed
Unallocated bank limits	89.63	6.30	[ICRA]AA(Stable)/[ICRA]A1+; reaffirmed
Total	**1,259.63**	**1,259.63**	
Commercial Paper	500.00	500.00	[ICRA]A1+; reaffirmed

**Instrument details are provided in Annexure-1*

Rationale

The rating action for the debt programmes of Dalmia Bharat Sugar and Industries Limited (DBSIL) factors in the expectation of a healthy growth in revenues and operating profits as well as the strengthening of debt protection metrics in FY2022. The company's revenue growth would be driven by healthy sugar exports under maximum admissible export quota (MAEQ) of SY2021 and open general licence (OGL) on the back of firmed up global sugar prices, higher distillery volumes and improved domestic sugar realisations. Further, higher sucrose diversion towards B-heavy molasses/juice-based ethanol is expected to result in improved blended distillery realisations, coupled with lower sugar inventory and in turn, lower working capital debt levels. Moreover, DBSIL has recently expanded its crushing and juice/molasses-based distillery capacities, which would strengthen its operational profile and improve revenue diversification. Additionally, DBSIL's board has approved the setting up of two grain-based distilleries, which are likely to become operational in FY2023-FY2024, providing a boost to revenues, profits and cash accruals over the medium term.

The ratings continue to factor in DBSIL's geographically diversified operations with a crushing capacity of 38,250 tonnes of cane per day (TCD) across UP and Maharashtra, providing buffer against any agro-climatic fluctuations in any one of the states. Further, its forward integration into distillery and cogeneration provides alternative revenue streams and acts as a cushion against the cyclicality of the sugar business to some extent.

The ratings also take into account its healthy gross recovery rate at 12.57% in FY2021 (12.38% in FY2020), aided by increased proportion of high-yielding cane in the varietal mix and the cane developmental activities taken by the company. ICRA notes that the introduction of the minimum support price (MSP) for sugar in FY2019 gives some protection against any downside in the operating profits in the sugar surplus years compared to the past. Over the medium term, DBSIL's operating profits are likely to remain less volatile than the historical levels, supported by the expected continuation of MSP and the industry's focus on diverting excess cane towards ethanol production.

Moreover, DBSIL enjoys strong financial flexibility emanating from its strong parentage as it is a part of the Dalmia Bharat Limited (DBL) Group and the market value of its investments in the latter. Further, the Group's access to low-cost funds at a short notice provides comfort.

The ratings, however, remain constrained by the vulnerability of DBSIL's profitability to the cyclical nature of the sugar industry (though the sharp fall in sugar prices is curtailed after the introduction of MSP) and the agro-climatic risks related to cane production. Further, the profitability of sugar mills, including DBSIL, are exposed to the policies of the Government of UP (GoUP) and the Central Government on cane prices, sugar international trade, sugar domestic quota, sugar and ethanol pricing and interest subvention loan for distillery capacity expansion.

The Stable outlook on the rating reflects ICRA's opinion that DBSIL will continue to benefit from its healthy operational profile. Further, ICRA does not expect the debt levels to increase materially despite the planned capex, keeping the debt coverage indicators at healthy levels.

Key rating drivers and their description

Credit strengths

One of the top sugar mills in India; geographically diversified operations – DBSIL has a sugar capacity of 38,250 TCD and continues to be one of the top sugar manufacturers in the country. Further, the company's geographically diversified operations (UP with 25,750 TCD and Maharashtra with 12,500 TCD capacity) are expected to cushion its profits against the fluctuation in operational performance in any of these regions. Additionally, both the states have advantages in sugar recoveries and pricing dynamics, with Maharashtra enjoying location-specific advantage for sugar exports.

Forward-integrated operations supported by government policies to provide cushion against cyclicality in sugar business – DBSIL's operations are forward integrated with a co-generation capacity of 119 mega watt (MW) and a distillery capacity of 600 kilo litres per day (KLPD), which provide alternative revenue streams and act as a cushion against the cyclicality in the sugar business. These two segments accounted for ~24% and ~66% of the revenues and profit before interest and tax, respectively, in FY2021. The contribution from them is expected to increase going forward with the recent and ongoing capacity expansion. The company has recently enhanced its distillery capacity to 600 KLPD from 305 KLPD, further scaling up the operations and strengthening the operating profile. Additionally, DBSIL's board has approved the setting up of two grain-based distilleries, which are likely to become operational in FY2023-FY2024. These expansion plans will reduce the seasonality, to an extent, with the larger distilleries remaining operational throughout the year.

Operationally efficient sugar mills with healthy sugar recovery rates – The gross recovery rate (not factoring in the diversion of B-heavy for ethanol production) remains healthy at 12.57% in FY2021, an increase from 12.38% in FY2020. This is supported by the increased proportion of high-yielding cane in the varietal mix and the cane developmental activities taken by the company, supporting the cost of production. Going forward, over the medium term, though the proportion of high-yielding canes will remain elevated, higher production of ethanol from B-heavy molasses/juice to avoid sugar glut is likely to moderate the sugar net recovery rates to an extent. The net sugar recovery rate after the diversion for ethanol production declined to 9.5% in 3M SY2022 (PY: 10.0%). However, the same is compensated through higher ethanol production in the distillery segment.

Profitability likely to improve due to steady sugar realisations and higher volumes from distillery segment – DBSIL's overall operating profitability and cash accruals are expected to benefit from firm sugar realisations both internationally and domestically, along with better distillery performance in FY2022. Going forward, the company is anticipated to divert a higher proportion of cane to produce ethanol through B-heavy molasses and/or sugarcane juice, after the expanded capacity becomes operational. DBSIL's operating margins will be supported by the likely continuation of MSP, remunerative prices of ethanol and the industry's focus on diverting excess cane towards ethanol production, resulting in improved domestic demand-supply balance. Further, with the increase in sugar sacrifice towards ethanol, the working capital debt and hence the total debt levels are expected to reduce in FY2023-FY2024.

Strong capital structure and healthy coverage metrics – The company's capital structure is conservative with net debt to equity of 0.4 times as on March 31, 2021 (PY: 0.7 times). Improved capital structure and profitability resulted in better coverage indicators in FY2021 with interest cover of 8.1 times (PY: 4.3 times), net debt to OPBIDTA at 1.6 times (PY: 2.7 times) and DSCR of 2.9 times (PY: 2.3 times). Further, in 9M FY2022, its interest cover improved to 12.1 times (PY: 6.7times). Going forward, the debt metrics are expected to remain healthy over the medium term, with favourable operating margins, along with a reduction in the debt levels.

Credit challenges

Profitability vulnerable to policy interventions by the Government – DBSIL's profitability, along with other sugar mills, continues to be vulnerable to the GoUP and the Central Government's policy on cane prices. Thus, the company's performance can be adversely impacted by a disproportionate increase in cane price in any particular year. Further, the profitability remains vulnerable to the Government's policies on sugar international trade, domestic quota, sugar MSP, remunerative ethanol prices and interest subvention loan for distillery capacity expansion. However, the recent measures taken by the Central Government and the GoUP supported sugar prices and the liquidity of sugar mills. The continuation of Government support in the form of remunerative ethanol prices and interest subvention for the debt-funded distillery capex is likely to prevent the piling up of cane arrears. However, the UP state-advised price (UP-SAP) has recently been revised upwards by Rs. 25/quintal and the fair remunerative prices (FRP) by Rs. 5/quintal for SY2022, which could limit profitability. Nevertheless, firmed up domestic prices and increased contribution from ethanol supplies are likely to offset this risk to some extent for integrated sugar mills.

Sugar mills remain vulnerable to industry cyclicality and agro-climatic risks – Being an agri-commodity, the sugarcane crop is dependent on climatic conditions and is vulnerable to pests and diseases that may not only impact the yield per hectare but also the recovery rate. These factors can have a significant impact on the company's profitability. Further, high dependence on a single crop variety may affect the yields and recovery rate. However, DBSIL has been exploring other varieties to mitigate this risk to a certain extent. In addition, the cyclicality in sugar production results in a volatility in sugar prices. However, the sharp downfall in sugar prices has been curtailed after the introduction of MSP by the Central Government in June 2018. Over the long term, higher ethanol production with increased diversion towards B-heavy molasses and direct sugar juice-based ethanol will help to curtail the excess supply of sugar, resulting in lower volatility in sugar prices and hence, cash flows from the sugar business.

Liquidity position: Adequate

DBSIL's liquidity position is **adequate** with bank balance and current investments of around Rs. 190 crore as on December 31, 2021 in addition to a cushion of around Rs. 340 crore in drawing power. ICRA expects DBSIL to comfortably meet its debt repayment obligations in the medium term with healthy cash flows from operations. However, the company is in the process of setting up grain-based distilleries with a capex of Rs. 250-300 crore over the medium term, which is expected to be funded by a mix of debt and equity in the ratio of around 1:1.

Rating sensitivities

Positive factors – A sustained period of firm sugar prices, driven by favourable demand-supply dynamics, resulting in lower volatility of cash flows from the sugar business and sustained operating profitability and debt coverage metrics may trigger a rating upgrade.

Negative factors – The ratings can be downgraded if there is any sharp decline in sugar prices, cane crushing volumes, recovery rate or an increase in cane costs; or any significant decline in ethanol realisations or any material change in Government policies that may result in a moderation of profitability and debt coverage metrics on a sustained basis. Specific metrics that could lead to a downgrade include an interest cover below 10 times on sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Sugar Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	ICRA has considered the consolidated financial statements of DBSIL; List of entities consolidated are provided in Annexure 2

About the company

Dalmia Bharat Sugar and Industries Limited (erstwhile Dalmia Cement (Bharat) Limited) was established in 1939 at Dalmiapuram in Tamil Nadu. Post demerger, DBSIL operates as an integrated sugar player with a cane crushing capacity of 36,500 tonnes crushed per day (TCD), distillery capacity of 305 kilo litres per day (KLPD) and co-generation capacity of 119 mega watt (MW) (across UP and Maharashtra). The company has the benefit of having capacities in two major sugar producing states, i.e. U.P. and Maharashtra.

Key financial indicators (audited)

DBSIL (Consolidated)	FY2020	FY2021
Operating Income (Rs. crore)	2,155.7	2,713.0
PAT (Rs. crore)	193.2	270.3
OPBDIT/OI (%)	17.7%	18.4%
PAT/OI (%)	9.0%	10.0%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	0.7
Total Debt/OPBDIT (times)	3.3	1.9
Interest Coverage (times)	4.3	8.1

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation
Source: Company, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)					Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Dec 31, 2021 (Rs. crore)	Date & Rating in		FY2021	FY2020	FY2019
					Feb 24, 2022	Oct 01, 2021	Feb 02, 2021	Jan 06, 2020	Nov 30, 2018
1	Fund Based – Term Loan	Long Term	373.33	361.54	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
2	Fund Based – Working Capital Facilities	Long Term	727.50		[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
3	Non-fund Based – Working Capital Facilities	Short Term	152.50		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Unallocated bank limits	Long Term/ Short Term	6.30		[ICRA]AA (Stable) /[ICRA]A1+	[ICRA]AA (Stable) /[ICRA]A1+	-	-	-
5	Commercial Paper	Short Term	500.00		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund Based – Term Loan	Simple
Fund Based – Working Capital	Simple
Non fund based – Working Capital	Very Simple
Unallocated bank limits	Not Applicable
Commercial Paper	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No/Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
Yet to be placed	Commercial Paper	-	-	-	500.0	[ICRA]A1+
NA	Fund Based – Term Loan	FY2014-FY2019	3.60%-7.50%	FY2024-FY2032	373.33	[ICRA]AA (Stable)
NA	Fund Based – Working Capital Facilities	-	-	-	727.50	[ICRA]AA (Stable)
NA	Non-fund Based – Working Capital Facilities	-	-	-	152.5	[ICRA]A1+
NA	Unallocated bank limits	-	-	-	6.3	[ICRA]AA (Stable) /[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis:

Company Name	DBSIL Ownership	Consolidation Approach
Himshikhar Investment Limited	100.00%	Full Consolidation

Source: *DBSIL annual report;* ***Note:*** *ICRA has taken a consolidated view of the parent (DBSIL) and its subsidiaries while assigning the ratings.*

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