July 24, 2023

Saraswati Sugar Mills Limited: Long-term rating upgraded to [ICRA]A (Stable) and short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based – Working capital facilities	436.65	436.65	[ICRA]A (Stable); rating upgraded from [ICRA]A- (stable)
Long-term fund-based – Term loan	114.00	83.00	[ICRA]A (Stable); rating upgraded from [ICRA]A- (stable)
Short-term non-fund based – Working capital facilities	5.00	5.00	[ICRA]A1; rating reaffirmed
Long-term – Unallocated limits	0.30	31.30	[ICRA]A (Stable); rating upgraded from [ICRA]A- (stable)
Total	**555.95**	**555.95**	

**Instrument details are provided in Annexure-I*

Rationale

The upgrade in the long-term rating of the debt programmes of Saraswati Sugar Mills Limited (SSML) factors in the improved business profile following the operationalisation of the expanded 160-KLPD distillery in June 2023 (enhanced from 100 KLPD) that would aid revenue diversification, improve the working capital intensity and strengthen the coverage indicators in the medium term.

SSML's revenues grew by 49% in FY2023, with distillery sales increasing four times to Rs. 207 crore (Rs. 52 crore in FY2022) and sugar revenues rising by 30%. The increase in sugar revenues to Rs. 735 crore in FY2023 was driven by improvement in the total sugar volumes (by ~30% YoY) and to some extent the realisations (~2.2% YoY), while the distillery performance benefitted from the unit being operational for the whole year (operated for 359 days in FY2023 vs only 99 days in FY2022). Sale of by-products like molasses, bagasse, etc. stood at Rs 32 crores in FY2023. In FY2023, the distillery division contributed ~21% to the total net revenues, compared to ~8% in FY2022 (nil till FY2021). Going forward as well, the ethanol division's contribution is expected to increase to ~30-35%, partly due to higher distillery volumes following the capacity ramp-up and more operational days, but largely due to expectations of lower sugar sales volumes. Running the distillery at higher capacity for lower number of days is expected to result in savings in input costs, which should aid profitability.

Higher diversion of sugar towards ethanol and higher domestic and export sugar sales has enabled SSML to reduce its sugar inventory levels (sugar closing stock of 0.82 lakh MT as on March 31, 2023 vs 1.28 lakh MT as on March 31, 2022). SSML has been manufacturing the entire ethanol from B-heavy molasses. The diversion and the increased export volumes led to a significant improvement in the working capital intensity (NWC/OI at 25% in FY2023 against 52% in FY2022). This in turn reduced the working capital borrowings (Rs. 105 crore as on March 31, 2023 vs Rs. 232 crore as on March 31, 2022), providing better stability in operating profits and improving the liquidity. Moreover, the volatility in cash flows would be lower, going forward as well, as the distillery will be operational for ~300 days, with ethanol having a payment cycle of 2-3 weeks from OMCs.

The coverage indicators improved in FY2023 on the back of higher operating profits and lower debt. SSML's total debt declined to Rs. 193.4 crore as on March 31, 2023 from Rs. 345.3 crore as on March 31, 2022. This is majorly due to a decline in the short-term borrowings owing to lower working capital requirements as well as payment of scheduled term debt repayments Rs 25.4 crore for the term loan availed by the company for distillery capex. The lower debt levels improved the debt metrices in FY2023 with gearing of 0.5 times (PY: 1.1 times), total debt/OPBIDTA at 1.6 times (PY: 4.4 times), interest cover at 8.2 times

(PY: 5.8 times). However, the DSCR moderated to 2.6 times in FY2023 (PY: 3.3 times) due to term debt scheduled repayments, but remains comfortable.

However, with lower sugar closing stock as on March 31, 2023 and expectation of lower sugar sales quota allocation for FY2024, the revenues are expected to moderate by ~15% in FY2024, even as ethanol sales volumes are expected to increase by ~8-10%. The revenue growth FY2025-FY2026 onwards would depend on the allocation of domestic and export sugar sales quotas. Further, with expectation of lower OI in FY2024 and higher sugar closing stock as on March 31, 2024, the NWC/OI is also expected to moderate to ~30-35% during FY2024-FY2026, which is still a significant improvement over the average NWC/OI of 46% for the four years over FY2018-FY2022.

Going forward, the WC debt is also expected to increase in FY2024 to Rs. 180-200 crore, with the high capex of Rs ~70 crore for sugar refining capacity being funded by internal accruals and moderation in working capital intensity in FY2024, resulting in lower cash flow from operations (CFO) for FY2024. However, with expectations of moderate capex and improvement in CFO FY2025 onwards, the WC debt is also expected to gradually come down over the medium term. This should improve the debt coverage and capitalisation indicators as well.

The ratings continue to factor in SSML's long operational track record in the sugar industry and the financial support from its parent company, ISGEC Heavy Engineering Limited (IHEL; rated at [ICRA]AA (Stable)/[ICRA]A1+). ICRA notes that the parent company has supported SSML by providing relatively low-cost loans during the previous cyclical downturns.

Also, SSML's profitability remains vulnerable to the cyclical nature of the sugar industry and the agro-climatic risks related to cane production. Further, the profitability of sugar mills, including SSML, remains vulnerable to the policies of both the state and the Central Government, international sugar trade, 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 SSML will continue to benefit from its healthy operational profile, partially forward-integrated operations, the long track record and strong parentage.

Key rating drivers and their description

Credit strengths

Benefits of being a fully-owned subsidiary of IHEL – SSML benefits from being a wholly-owned subsidiary of IHEL, which has a strong financial risk profile, reflected in its rating of [ICRA]AA(Stable)/[ICRA]A1+. This has been demonstrated by the relatively low cost of the loans extended by the parent in times of cyclical downturns. Further, the company enjoys strong financial flexibility because of its strong parentage, as part of the ISGEC Group, and the access of the latter to low-cost funds at a short notice provides comfort.

Long track record, forward-integrated operations – SSML has a crushing capacity of 10,000 tonnes crushed per day (TCD) and a long track record of operations of over eight decades. Further, the company has forward integrated its operations with the commercialisation of a 100-KLPD distillery in December 2021 (enhanced to 160 KLPD in June 2023), thus strengthening its operational profile. The integrated operation provides alternative revenue sources and cushions its profitability against the cyclicality in the sugar business, lending stability to the operating profits.

Healthy operational performance continues in SY2023 – SSML crushed 16.62 lakh MT of cane in SY2023 (2.6% higher than SY2022 levels). The company's gross recovery rate for the sugar season slightly improved to 11.3% in SY2023 from 11.1% in SY2022 (11.5% in SY2021) and remained healthy. Similarly, the net recovery rates improved to 9.75% in SY2023 (PY: 9.51%) (entire cane was crushed through B-heavy route in SY2023 and SY2022 compared to the C-heavy route in SY2021). The net recovery might moderate if SSML decides to produce ethanol via the juice route in SY2024, however it will depend upon the price parity of sugar and molasses in relation to the price of Ethanol.

Profitability likely to remain healthy owing to steady sugar realisations and higher volumes from distillery segment – SSML'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 the near term. SSML'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, which will improve the domestic demand-supply balance. Further, with the increase in sugar sacrifice towards ethanol, the working capital debt and hence the total debt levels are anticipated to reduce.

Improved debt coverage metrics due to lower WC borrowings – SSML's total debt declined to Rs. 193.4 crore as on March 31, 2023 from Rs. 345.3 crore as on March 31, 2022. This is due to a decline in the short-term borrowings owing to lower working capital requirements as well as scheduled term debt repayments of Rs 25.4 crore for the term loan availed by the company for distillery capex. Lower debt levels improved the debt metrices in FY2023 with gearing of 0.5 times (PY: 1.1 times), total debt/OPBIDTA at 1.6 times (PY: 4.4 times) and interest cover at 8.2 times (PY: 5.8 times). However, the DSCR moderated to 2.6 times in FY2023 (PY: 3.3 times) due to term debt scheduled repayments but remains comfortable. The debt coverage metrices are expected to remain healthy, going forward as well, and might witness slight improvement in the medium term.

Credit challenges

Profitability reliant on Government policies – SSML's profitability, along with other Haryana-based sugar mills, continues to be vulnerable to the state government's policy on cane prices. Cane prices as well as the related subsidy is determined by the state government at the beginning of the crushing season. Thus, the company's performance can be impacted by a disproportionate increase in the net cane price. Further, its profitability remains vulnerable to the Central Government's policies on exports, minimum support price (MSP) and remunerative ethanol prices. However, the recent measures taken by the Central and state government have 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 are likely to prevent the piling up of cane arrears. Even as Haryana-SAP increased by Rs. 12/quintal for SY2022 and further by 10/quintal for SY2023, firm realisations, healthy sugar sales volumes and enhanced ethanol volumes support the profits.

Profitability of sugar mills vulnerable to industry cyclicality and agro-climatic risks – Being an agri-commodity, the sugarcane crop depends on climatic conditions and is vulnerable to pests and diseases, which may influence the yield per hectare and the recovery rate. These factors can have a significant impact on the company's profitability. Further, high dependence on a single crop may affect the yield and recovery rate. Nonetheless, SSML 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 contraction in sugar prices has been curtailed after the introduction of MSP by the Central Government. Over the long term, higher ethanol production with increased diversion towards B-heavy molasses and direct sugar juice is expected to help curtail the excess supply of sugar, resulting in lower volatility in sugar prices and in turn, cash flows from the sugar business.

Liquidity position: Adequate

SSML's liquidity position is adequate with likely healthy cash flow from operations and an average cushion of around Rs. ~50 crore in drawing power for the 12 months ended May 2023 in addition to ~Rs. 6.4 crore of free cash as on March 31, 2023. ICRA expects SSML to comfortably meet its debt repayment obligations of ~Rs. 25 crore during FY2024-FY2025. The company will be undertaking a capex of Rs ~68 crore in FY2024 towards sugar refining capacity, which shall be funded from internal accruals. Apart from the above, only routine capex is expected over the medium term, which is likely to be funded through internal accruals.

As on June 19, 2023, the working capital debt stood at Rs. 160 crore against a drawing power of Rs. 194 crore, implying a cushion of ~Rs. 34 crore. The borrowing levels for this year are at a peak and expected to come down, with nil cane dues. The company collects ~Rs. ~35-60 crore from sugar sales and ~Rs. 16-20 crore from ethanol sales per month.

Rating sensitivities

Positive factors – An upgrade will be backed by continued period of firm sugar prices, driven by favourable demand-supply dynamics, which will lower the volatility in cash flows from the sugar business and improve the operating profits and debt coverage metrics on a sustained basis.

Negative factors – Pressure on the ratings could arise if there is any sharp decline in sugar prices, cane crushing volumes and recovery rate, or if cane costs rise. Any significant decline in ethanol realisations, or any material change in Government policies moderating the profitability and debt coverage metrics on a sustained basis could also weigh on the ratings. The ratings will also be under pressure if the interest cover falls below 6 times on a sustained basis, or if the credit profile of the parent, i.e. IHEL, deteriorates, or if the linkage with the parent weakens.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Sugar Industry Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group support	Parent Company: ISGEC Heavy Engineering Limited (IHEL) ICRA expects SSML to benefit from the financial support extended by the parent company, if required
Consolidation/Standalone	Standalone

About the company

SSML was the earliest business of the Puri family and was established in 1933, translating to an operational track record of more than nine decades. SSML is a 100% subsidiary of Isgec heavy Engineering Limited, the flagship company of the ISGEC Group (established in 1946), engaged in the manufacturing of heavy engineering equipment and providing related engineering, procurement and construction (EPC)/turnkey services. SSML operates a 10,000-TCD sugar mill along with a 160-KLPD distillery at Yamuna Nagar, Haryana.

Key financial indicators (audited)

SSML Standalone	FY2022	FY2023
Operating income	661.7	984.5
PAT	40.5	66.8
OPBDIT/OI	11.8%	12.3%
PAT/OI	6.1%	6.8%
Total outside liabilities/Tangible net worth (times)	1.7	1.0
Total debt/OPBDIT (times)	4.4	1.6
Interest coverage (times)	5.8	8.2

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as of June 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	
					July 24, 2023	June 30, 2022	April 12, 2021	March 23, 2021	July 31, 2020
1	Fund-based – Working capital facilities	Long term	436.65	--	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
2	Fund-based – Term loan	Long term	83.00	~83.00	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
3	Non fund-based – Working capital facilities	Short-Term	5.00	--	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1
4	Unallocated limits	Long-Term	31.30	--	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-	[ICRA]A- (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Working capital facilities	Simple
Long-term fund-based – Term loan	Simple
Short-term non-fund-based – Working capital facilities	Very Simple
Long-term – Unallocated limits	NA

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 are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Long-term fund-based – Working capital facilities**	NA	5.00%-8.50%	NA	436.65	[ICRA]A (Stable)
NA	**Long-term fund-based – Term loan**	Aug-2020	8.20%*	FY2027	83.00	[ICRA]A (Stable)
NA	**Short-term non-fund based – Working capital facilities**	NA	NA	NA	5.00	[ICRA]A1
NA	**Long-term – Unallocated limits**	NA	NA	NA	31.30	[ICRA]A (Stable)

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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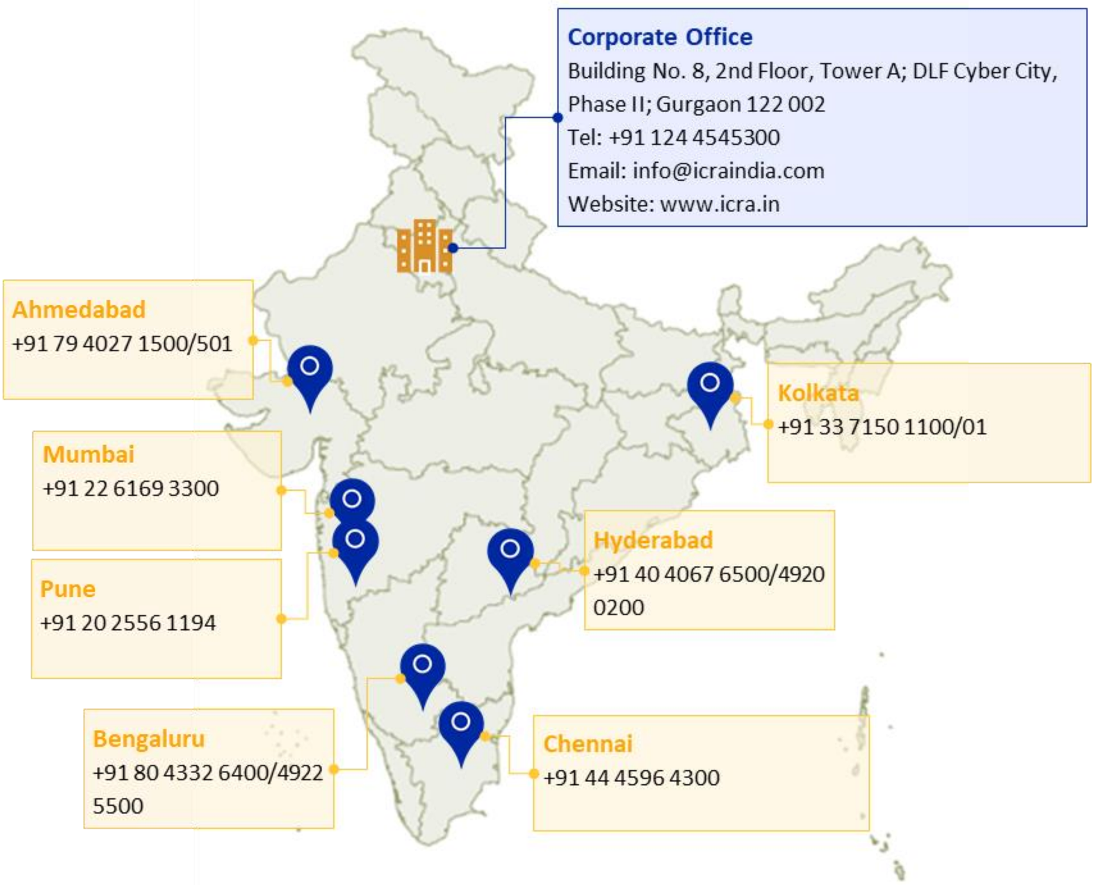

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