December 24, 2021

Uttam Sugar Mills Limited: Ratings reaffirmed and outlook revised to Positive from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term Loan	377.51	270.25	[ICRA]BB+(Positive); Reaffirmed and outlook revised to Positive from Stable
Long-term Fund-based – Cash Credit	521.50	670.00	[ICRA]BB+(Positive); Reaffirmed and outlook revised to Positive from Stable
Short-term Non-fund based Working Capital Facilities	35.00	35.00	[ICRA]A4+; Reaffirmed
Long-term Unallocated Limits	103.00	61.76	[ICRA]BB+(Positive); Reaffirmed and outlook revised to Positive from Stable
Total	**1037.01**	**1037.01**	

**Instrument details are provided in Annexure-1*

Rationale

The rating action for the debt programmes of Uttam Sugar Mills Limited (USML) factors in the expectation of healthy growth in operating revenues and profits, in addition to strengthening of debt protection metrics in FY2022. The ratings note the favourable impact of higher domestic and international sugar prices, along with increased distillery volumes from the expanded capacities in H1 FY2022 as well as improved ethanol realisations on its profitability and coverage metrics. ICRA expects USML's revenues to grow by 7-12% YoY in FY2022, driven by better distillery performance and improved realisations from sugar sales, despite stagnant growth in sugar volumes (both domestic and exports). The company has completed its distillery expansion recently and does not have any major medium-term capex plans. Additionally, with repayment of the scheduled term debt, likely reduced inventory levels leading to lower working capital debt and healthy operating profits, the debt metrics are expected to improve in FY2022 with gearing at 1.3-1.7 times, total debt /OPBIDTA at 2.4-2.8 times and interest cover of above 3 times. The debt metrics would strengthen further thereafter with steady operating profits, cash accruals and reduced borrowings with scheduled debt amortisation.

The ratings continue to factor in USML's established operational track record with a crushing capacity of 23,750 tonnes of cane per day (TCD) across UP and Uttarakhand, in addition to healthy crushing volumes and recovery rates. These operational metrics are expected to remain healthy in SY2022 as well. Further, its forward integration into distillery and co-generation provides alternate revenue streams and acts as a cushion against the prevalent cyclicality in the sugar business to some extent. Further, 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 sugar surplus years compared to the past. Over the medium term, USML's operating profits are likely to be less volatile than the historical levels, driven by the expected continuation of MSP and the industry's focus on diverting of excess cane towards ethanol production.

The ratings are, however, constrained by USML's moderate financial profile, as reflected by the leveraged capital structure, and moderate debt coverage metrics, notwithstanding the expected strengthening in FY2022. Further, USML has relatively high debt repayments in the range of Rs. 120-150 crore in FY2022-FY2023. Timely debt servicing would be dependent on adequate cane availability, healthy recovery rates, favourable sugar realisations, higher ethanol supplies and continued supportive Government policies.

USML's ratings remain constrained by risks associated with inherent cyclicality in the sugar business (though the sharp fall in sugar prices is curtailed after the introduction of MSP and ongoing structural changes in the sector with sucrose diversion towards ethanol) and the agro-climatic conditions related to cane production. Moreover, the Government policies on cane pricing, domestic sugar quota pertaining to the pricing and offtake of co-generation power and ethanol, along with the counterparty credit risk associated with the sale of power to the utilities in UP constrain the ratings. ICRA notes an outstanding amount of Rs. 10.81 crore from the Uttarakhand Government is overdue. As shared by the management, these loans remain outstanding basis an understanding of a waiver consideration by the state government. Further, the state government has not raised the demand and has given subsidies (higher than this amount) since then, not adjusting for this amount.

The Positive outlook on the rating reflects ICRA's opinion that USML will continue to benefit from its improved operational profile with expanded distillery capacities, lower volatility and expansion of operating profits.

Key rating drivers and their description

Credit strengths

Established track record of operations with efficient operations – USML has an established operational track record of over two decades with a crushing capacity of 23,750 TCD. While the cane crushing slightly moderated in SY2021 to 36.6 lakh MT (PY: 38.3 lakh MT), it remained healthy. Further, its gross recovery rates improved over the past few years due to varietal change of sugarcane with developmental activities being undertaken by the company, leading to lower cost of production. However, the recovery rate slightly moderated to 12.03% in SY2021 (PY: 12.18%) on account of unfavourable agro-climatic conditions. The net recovery rate moderated to 11.44% in SY2021 (PY: 11.75%) due to higher diversion towards B-heavy molasses. However, increased contribution from the distillery division with higher proportion of ethanol production from B-heavy molasses would offset the impact of the moderated recovery rate on USML's operating margin.

Forward-integrated operations and Government policies providing cushion against cyclicality in sugar business – USML's operations are forward integrated with a co-generation capacity of 103 mega-watt (MW) and a distillery capacity of 200 KLPD as on September 30, 2021, which provide alternate revenue streams and acts as a cushion against the cyclicality inherent in the sugar business. Together, these two segments accounted for ~14% of revenues and ~52% of the profit before interest and tax in FY2021. The company has recently concluded its distillery capacity expansion by 50 KLPD resulting in higher forward integration, thus strengthening the operating profile. This would also increase distillery's contribution to revenues going forward and offset the seasonality associated with sugar business with distillery operating for around 330 days in the year.

Expected improvement in revenues and operating profits in FY2022 – USML's overall operating profitability and cash accruals are likely to benefit from firm sugar realisations (both domestic and global), higher export volumes, along with better distillery performance in the current fiscal. Distillery revenues are likely to be supported by higher sucrose diversion towards ethanol and expanded capacities being operational from July 2021. Further, its operating margins are anticipated to be supported by the likely continuation of MSP while market prices firm up, remunerative prices of ethanol and the industry's focus on diverting of excess cane towards ethanol production, resulting in improved domestic demand-supply balance.

Credit Challenges

Financial profile characterised by leveraged capital structure and moderate debt coverage indicators – USML's total debt remained high at Rs. 870.9 crore as on March 31, 2021, comprising ~58% of working capital borrowings. While term debt continues to remain on the higher side due to debt-funded capex, it requires working capital debt to fund high inventory at March end owing to the seasonality involved in cane crushing. Notwithstanding the steady accretion to reserves, the high debt resulted in a leveraged capital structure with a gearing of 2.6 times as on March 31, 2021, despite some improvement over the previous year. Further, with healthy operating profits, the debt coverage metrics improved in FY2021 with interest coverage at 2.5 times (PY: 2.3 times), TD/OPBIDTA at 4.0 times (PY:4.8 times) and NCA/TD at 14% (PY: 11%). However, expectations of better cash accruals, along with scheduled repayments and moderation in working capital intensity with higher sucrose diversion and healthy exports in FY2022-FY2023 amid firmed up global sugar prices would allow a decline in borrowings and strengthening of debt metrics going forward.

High debt repayments – USML has relatively high debt repayments ranging within Rs. 120 – 150 crore in FY2022-FY2023. However, the company has prepaid a part of its scheduled repayments by November 2021. It has also paid majority of the cane dues by September 2021. Notwithstanding its large repayments, the healthy accruals, supported by sufficient cane availability, healthy recovery rates, favourable contribution aided by firm sugar prices, increased ethanol supplies and realisation, along with its comfortable liquidity profile would allow timely servicing.

Profitability of UP/Uttarakhand-based sugar mills continue to depend on Government's policy on cane prices – USML's profitability, along with other Uttar Pradesh / Uttarakhand-based sugar mills, continues to remain vulnerable to the state government's policy on cane prices. Thus, the company's performance can be impacted by disproportionate increase in cane price in any particular year. Further, the profitability remains vulnerable to the Government's policies on exports, MSP and remunerative ethanol prices. The continuation of Government support in the form of remunerative ethanol prices and interest subvention for debt-funded distillery capex are also likely to prevent the piling up of cane arrears and support the industry. While the recent upward revision in UP-SAP by Rs. 25/quintal could limit the profitability, firmed up domestic prices are likely to offset this risk to some extent.

Profitability of sugar mills remain vulnerable to industry cyclicality and agro-climatic risks – Being an agri-commodity, the sugar cane crop is dependent upon 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 impact the yields and recovery rate. Nonetheless, USML has been exploring other varieties to mitigate this risk to certain extent. In addition, the cyclicality in sugar production results in volatility in sugar prices. However, the sharp contraction in the sugar prices is curtailed after the introduction of MSP by the Central Government in June 2018. Further, healthy exports and higher diversion of sucrose towards ethanol in the recent years resulted in favourable demand-supply dynamics in the country, thus resulting in improved realisations currently. Over the long term, higher ethanol production with increased diversion towards B-heavy molasses and direct sugar juice by the industry is expected to help in curtailing the excess supply of sugar, resulting in lower volatility in sugar prices and cash flows from the sugar business.

Liquidity position: Adequate

USML's liquidity is adequate with sufficient cushion in the drawing power of around Rs. 160 crore during October 2020 – October 2021. Further, ICRA expects its cash flow from operations to increase in FY2022, driven by higher operating profits and lower working capital intensity due to the expected decline in the sugar inventory. This along with the cushion in the working capital limits would allow the company to comfortably meet its the debt repayment obligation of around Rs. 150 crore in FY2022. Moreover, currently USML has no major medium-term capex plans.

Rating sensitivities

Positive factors – Higher-than-anticipated sugar sales volume, along with a sustained period of firm sugar prices, driven by favourable demand-supply dynamics and the consequent improvement in profitability as well as debt coverage metrics may trigger a rating upgrade.

Negative factors – The outlook can be revised to Stable if higher-than-anticipated decline in sugar prices, recovery rate or increased cane costs or longer-than-expected timeline to scale up distillery operations weakens the profitability and debt coverage metrics on a sustained basis. Further, any large debt-funded capex or any material change in Government policies that may result in deterioration of credit profile, or interest cover below 2.5 times on a sustained basis, could also trigger an outlook revision.

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	Standalone

About the company

The company was incorporated as Associated Sugar Mills Limited in October, 1993, by Mr. M.K Swarup, along with his family members. In 1998, the Adlakha family, along with their associates, acquired 100% shareholding from the erstwhile promoters. Subsequently, the name was changed to Uttam Sugar Mills Limited w.e.f. November, 1998. Now, Uttam Sugar Mills Limited (USML), a part of the Uttam Group, is one of the leading integrated sugarcane processing companies. It has a corporate office at Noida.

The company manufactures sugar and forward integrated products—power and ethanol. It has an aggregate cane crushing capacity of 23,750 TCD, co-generation capacity of 103 MW and ethanol production capacity of 200 KLPD. USML has four sugar plants, out of which one is in Uttarakhand and other three in Uttar Pradesh.

Key financial indicators (audited)

USML	FY2020	FY2021
Operating Income (Rs. crore)	1644.8	1818.6
PAT (Rs. crore)	51.6	59.8
OPBDIT/OI (%)	11.1%	12.0%
PAT/OI (%)	3.1%	3.3%
Total Outside Liabilities/Tangible Net Worth (times)	5.1	4.3
Total Debt/OPBDIT (times)	4.8	4.0
Interest Coverage (times)	2.3	2.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

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 of Nov 30, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Dec 24, 2021	Oct 30, 2020	Apr 05, 2019	-
1	Long term - Fund based - Term loans	Long Term	270.25	256.19	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	
2	Long term - Fund based - Cash Credit	Long Term	670.00	-	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	
3	Short term - Non-fund based-Working Capital Facilities	Short Term	35.00	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	
4	Long term – Unallocated Limits	Long Term	61.76	-	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based - Term Loans	Simple
Long-term – Fund-based - Cash Credit	Simple
Short-term - Non-fund based-Working Capital Facilities	Very Simple
Long-term – Unallocated Limits	Not Applicable

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: Click Here

Annexure-1: Instrument details

ISIN No/ Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term – Fund-based - Term loans	FY2016-FY2022	5.0%-12.0%	FY2022-FY2025	270.25	[ICRA]BB+(Positive)
NA	Long-term – Fund-based - Cash Credit	NA	NA	FY2024	670.00	[ICRA]BB+(Positive)
NA	Short-term - Non-fund based-Working Capital Facilities	NA	NA	FY2026	35.00	[ICRA]A4+
NA	Long-term – Unallocated Limits	NA	NA	FY2025	61.76	[ICRA]BB+(Positive)

Source: *Company*

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

ANALYST CONTACTS

Sabyasachi Majumdar
+91-124-4545304
sabyasachi@icraindia.com

Girishkumar Kadam
+91 22 6114 3441
girishkumar@icraindia.com

Anupama Arora
+91-124-4545303
anupama@icraindia.com

Suksham Arora
+91-124-4545300
suksham.arora@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches

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