ICRA

August 05, 2020

Magadh Sugar and Energy Limited: [ICRA]A-(Stable)/A2+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loan	146.64	[ICRA]A-(Stable); Assigned
Fund Based – Working Capital	420.00	[ICRA]A-(Stable); Assigned
Non fund based	10.00	[ICRA]A2+; Assigned
Total	**576.64**	

**Instrument details are provided in Annexure-1*

Rationale

The rating assignment takes into consideration the long track record of Magadh Sugar & Energy Limited (MSEL or the company), experience of the promoters in the sugar industry and strong operational profile of the company with healthy sugar recovery rates along with forward integration into distillery and cogeneration facilities. The company's forward integration into cogeneration and distillery segments provides alternative revenue streams and cushion it from the cyclicality of the sugar business to a certain extent. Going forward, MSEL's cash flows are expected to be supported by firm sugar realisations and higher profits from the distillery division as the company is in the process of increasing its distillery capacity along with its policy to produce entire ethanol from B-heavy molasses only.

The long-term rating, however, continues to be constrained by the cyclical nature of the sugar industry, and the agro-climatic risks related to cane availability. The ratings also consider the regulatory risks associated with the sugar industry as it is susceptible to sudden changes in Government policies. However, ICRA notes that recent interventions by both the Central Government and the state government, which included revision in minimum support prices, interest subvention loans for setting up of ethanol manufacturing facilities, soft loans and export subsidy, have supported the sugar industry and benefited integrated sugar producers. The debt on the books of MSEL increased over the last two fiscals on account of an increase in the working capital debt, including interest-free debt to fund the buffer stock as well as soft loans availed at low interest rates under various Central/state Government schemes to fund the ongoing distillery capex as well as to make payment of cane arrears. Consequently, the gearing stood at ~1.2 times as on March 31, 2020 and debt coverage indicators were moderate with an interest cover of ~3.2 times and TD/OPBITDA of ~4.1 times in FY2020. However, the debt metrics are likely to improve going forward, with an improvement in profitability.

The Stable outlook on the rating reflects ICRA's opinion that MSEL will continue to benefit from its healthy operational profile. Besides, with its focus on increasing distillery capacity and ethanol production from B-heavy molasses are likely to keep its cash flows comfortable relative to its debt service obligations.

Key rating drivers and their description

Credit strengths

Experienced promoters and long track record of operations – MSEL is a part of the erstwhile KK Birla Group, currently managed by Mrs. Nandini Nopany and her son, Mr. C. S. Nopany. MSEL's sugar mills have a long operational track record of over 85 years, which were earlier operating under Upper Ganges Sugar & Industries Ltd. (UGSIL) and Oudh Sugar Mills Ltd. (OSML). Apart from MSEL, the promoters also have presence in the sugar industry in Uttar Pradesh with a capacity of ~31,200 TCD under Avadh Sugar & Energy Ltd.

Efficient operations with forward integration into co-gen and distillery – The volumes of cane crushed, and sugar recovery rates have been steadily increasing over the years due to cane developmental activities undertaken by the company, leading to a lower cost of production. The cane crushed increased to ~242 lakh quintal in FY2020 from ~165 lakh quintal in FY2017, while the sugar recovery rates have improved to ~11.1% in FY2020 from 9.6% in FY2017. Going forward, while the volumes of cane crushed are expected to increase marginally, the recovery rates will moderate as the company will be producing 100% ethanol via B Heavy molasses.

Additionally, MSEL has a co-generation capacity of 38 mega watt (MW) and a distillery capacity of 60 KLPD (kilo litres per day), which provide additional revenue streams and provide a buffer against cyclicality in the sugar industry. MSEL is in the process of enhancing its distillery capacity to 80 KLPD from SY2021 onwards. ICRA also takes note of MSEL's plan of setting up a new 75 KLPD distillery at one of its mills in the medium term, resulting in higher levels of forward integration, further strengthening the operating profile of the company. In the current year, 100% of ethanol is expected to be produced via B-heavy molasses, resulting in higher profitability from the distillery segment.

Cane pricing decided by sugar companies in consultation with state government - MSEL's sugar mills are located in Bihar, which is a sugar deficit state, and thus enjoy higher realisations and limited competition from nearby sugar factories. Moreover, in Bihar, the sugar factories (in consultation with the state government) fix the cane pricing for the sugar season, which is applicable for all sugar factories in the state. However, historically it has been noted that any change in Fair and Remunerative Price (FRP) or State Advised Price (SAP) in UP had led to a change in cane prices in Bihar.

Credit challenges

High working capital intensity leads to moderate debt coverage indicators – The seasonality involved in sugarcane crushing results in high inventory of finished goods at the end of March. The working capital availed to fund such high inventory, including buffer stock, along with soft loans availed for making cane payments resulted in an increase in debt on the books of domestic sugar companies, including MSEL, over the last two fiscals. As of end FY2020, the total debt on the books of MSEL stood at ~ Rs. 641.2 crore. Notwithstanding the steady accretion to reserves, MSEL's gearing stood at ~1.2 times as on March 31,2020. The debt coverage indicators also remain moderate with an Interest cover of 3.2 times and Total Debt/OPBITDA of ~4.1 times in FY2020. Although the debt levels are high, it is primarily working capital, which limits debt repayment obligation. Moreover, the company has adequate headroom in terms of drawing power vis-a-vis the working capital debt outstanding. Going forward, the debt coverage indicators are expected to improve given the likelihood of higher profitability on account of firm sugar prices and higher volumes of B-heavy ethanol sales and repayment of debt.

Risks associated with operating in a regulated industry – MSEL's profitability, along with sugar mills, continues to remain vulnerable to the Government policies and schemes such as creation of buffer stock, export subsidies, mandatory blending of ethanol and its pricing, sugar pricing etc. Hence, discontinuation of any subsidies/schemes or any material decrease in sugar or ethanol pricing would have an impact on the company's financials. Nonetheless, recent measures taken by the Central and the state government have supported the financial performance and liquidity of sugar mills.

Sugar mills remain vulnerable to industry cyclicality and agro-climatic risks – Being an agricultural product, the sugarcane crop is dependent upon weather conditions and is vulnerable to pests and diseases that may impact the yield per hectare and the recovery rate. These factors can have a significant impact on the company's profitability. In SY2020, ICRA expects sugar consumption to be lower by ~4%. So, the closing stock will continue to remain high at ~11-11.5 million MT at the end of SY2020, however, the same would be lower compared to ~14.5 million MT in the previous year. In the next season, large players are expected to increase ethanol production from B-heavy molasses, so any significant increase in sugar production is expected to be checked. However, the trend in domestic demand and export policies would determine the supply-balance scenario in SY2021.

Liquidity position: Adequate

MSEL's liquidity is **adequate** with healthy cash flow from operations and moderate average working capital utilisation levels of ~60-65% (adjusted for buffer stock borrowing) of the total sanctioned limits over the last one year. Overall, ICRA expects MSEL to be able to meet its near-term commitments. Also, the expected equity infusion, partly to fund the project capex in FY2021/FY2022 is expected to support the overall liquidity position of the company.

Rating sensitivities

Positive triggers – The rating may be upgraded if the company is able to maintain an interest cover of ~4 times or higher on a sustained basis.

Negative trigger – The rating may be downgraded if the interest cover is less than 3 times and/or TD/OPBITDA (adjusted for buffer stock borrowing) is more than 3.5 times on a 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	Standalone financials have been considered

About the company

MSEL has three sugar mills namely New Swadeshi Sugar Mills, Narkatiaganj (West Chamaparan district, Bihar), Bharat Sugar Mills (Sidhwalia district, Bihar), and Hasanpur Sugar Mills, Hasanpur (Samastipur district, Bihar) with a combined crushing capacity of 17,500 TCD. It also has one distillery at Narkatiaganj with a total capacity of 60 KLPD and a cogen facility and produces 38 MW power.

In FY2020, the company reported a net profit of Rs. 83 crore on an operating income of Rs. 918.0 crore compared to a net profit of Rs. 34.2 crore on an operating income of Rs. 742.5 crore in the previous year.

Key financial indicators (audited)

	FY2019	FY2020
Operating Income (Rs. crore)	742.5	918.0
PAT (Rs. crore)	34.2	83.0
OPBDIT/OI (%)	14.1%	17.1%
PAT/OI (%)	4.6%	9.0%
Total Outside Liabilities/Tangible Net Worth (times)	2.0	1.9
Total Debt/OPBDIT (times)	5.1	4.1
Interest Coverage (times)	3.0	3.2

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
					5-Aug-2020			
1	Fund Based – Term Loan	Long term	146.64	146.64	[ICRA]A- (Stable)	-	-	-
2	Fund Based – Working Capital	Long term	420.00		[ICRA]A- (Stable)	-	-	-
3	Non fund based	Short term	10.00		[ICRA]A2+	-	-	-

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website click here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
	Fund based - Term Loan	FY2016	9.6%-11%	FY2026	146.64	[ICRA]A- (Stable)
	Fund Based – Working Capital				420.00	[ICRA]A- (Stable)
	Non fund based				10.00	[ICRA]A2+

Source: Magadh Sugar & Energy Limited

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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