April 07, 2021

Dwarikesh Sugar Industries Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	230.65	230.65	[ICRA]A+ (Stable); Reaffirmed
Cash Credit	770.00	770.00	[ICRA]A+ (Stable); Reaffirmed
Long-term -Non-Fund Based Limits	25.00	25.00	[ICRA]A+ (Stable); Reaffirmed
Long-term Unallocated Limits	4.34	4.34	[ICRA]A+ (Stable); Reaffirmed
Total	**1029.99**	**1029.99**	
Commercial Paper^	300.00	300.00	[ICRA]A1+; Reaffirmed

**Instrument details are provided in Annexure-1 ^carved out of working capital limits.*

Rationale

The reaffirmation of ratings for the debt programmes of Dwarikesh Sugar and Industries Limited (DSIL) factors in the healthy growth in its revenues and profits in FY2021 and maintenance of comfortable coverage indicators. The expansion in revenues as well as profits in FY2021, driven by higher domestic sugar sales volumes, increased sugar exports backed by export subsidy and rise in contribution of distillery operations following enhanced diversion of B-heavy molasses to ethanol that have remunerative realisations. While reaffirming the rating ICRA takes cognisance of the expected reduction in debt levels in the near term, driven by lower sugar inventories following increased sugar sales volumes (both domestic and exports) coupled with higher diversion of B-heavy molasses to ethanol. Notwithstanding the improved operating performance and coverage indicators in FY2021, DSIL's operating profits are expected to moderate in FY2022 on account of contraction in export subsidy (~Rs. 6.0/kg for SY2021 against Rs. 10.4/kg for SY2020). This coupled with its proposed debt-funded investment plans and resultant high debt levels would moderate the coverage indicators with total debt/OPBITDA of over 4 times. Despite the expected increase in indebtedness in FY2022, ICRA notes that DSIL continues to benefit from strong financial flexibility and significant cushion in the working capital limits.

The rating continues to factor in DSIL's efficient operations with the company being among units reporting the highest recovery rates in Uttar Pradesh (UP). Moreover, being forward integrated into co-generation and distillery operations, the company benefits from access to alternate revenue streams and cushion against cyclicality of sugar business. Although DSIL enhanced its distillery capacity to 130 KLPD in FY2020, the management is proposing further capacity addition for ethanol production from B- heavy and sugarcane juice that would further enhance the contribution of distillery operations. ICRA also notes that the sustained favourable Government policy framework, such as continuation of minimum support price (introduced from FY2019), export subsidy, soft loans and interest subvention loans for ethanol expansion as well as the recent advancement of enhanced ethanol-blending timelines would allow integrated players like DSIL to report lesser volatility in operating profits against historical levels.

However, the ratings remain constrained by the vulnerability of DSIL'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 agro-climatic risks related to cane production. Further, the profitability of sugar mills, including DSIL, remain vulnerable to the policies of the Government of Uttar Pradesh (GoUP) on cane prices, as well as the Central Government's policies on sugar trade, sugar and ethanol pricing.

The Stable outlook factors in the expectations of DSIL maintaining stable profitability and coverage metrics over the medium term (despite some moderation in the near term), driven by continued favourable Government support measures.

Key rating drivers and their description

Credit strengths

Forward-integrated operations – DSIL operates 21,500 tonne crushed per day (TCD) of sugar capacities in UP. The plant's operation is forward integrated into power and alcohol business—co-generation capacity of 91 mega-watt (MW) (surplus – 56 MW) and distillery capacity of 130 kilo litre per day (KLPD). DSIL is planning to increase its distillery capacity to further strengthen its operational profile. The integrated operation provides alternate revenues and cushions profitability against cyclicality in sugar business.

Operationally efficient sugar mills with healthy recovery rates – The company's recovery rate for sugar seasons stood at 11.9% in SY2018, 12.3% in SY2019 and 12.3% in SY2020. The recovery rate, however, is expected to moderate in SY2021 owing to a decline in gross recovery due to agro-climatic conditions in addition to diversion of cane towards production of B-heavy molasses. Healthy recovery rates aided in reducing the company's cost of production substantially. Going forward, over the medium term, though the proportion of high-yielding canes will remain elevated, the higher production of ethanol from B-heavy molasses is likely to moderate the recovery rates to some extent. However, the same is likely to be compensated by higher production in the distillery segment.

Healthy growth in operating profits in FY2021; downside in operating profits likely to be limited compared to historic levels during years of surplus sugar production – DSIL reported healthy growth in operating profits and cash accruals in FY2021 driven by higher sugar sales, export subsidies and improved distillery performance. With the introduction of the MSP in FY2019, the downside in the OPBIDTA has been curtailed compared to the previous surplus years of sugar production. Over the medium term, DSIL's OPBIDTA and debt metrics are expected to be less volatile than the historical levels, supported by the likely continuation of MSP and also the industry's focus on diverting of excess cane towards ethanol production.

Strong capital structure and healthy debt coverage metrics – DSIL's capital structure is estimated to have strengthened (gearing around 1.2–1.3 times as on March 31, 2021, lower than 1.7 times as on March 31, 2020). This was primarily on account of reduced long-term debt (long-term debt-to-equity estimated around 0.35–0.40 times as on March 31, 2021) with borrowings largely on account of working capital to support the higher sugar stocks. The interest coverage is healthy and is estimated at 3.5– 4.0 times for FY2021. Notwithstanding improved operating performance and coverage indicators in FY2021, DSIL's operating profits are expected to moderate in FY2022 on account of contraction in export subsidy. This coupled with its proposed debt-funded investment plans and resultant high debt levels would moderate the coverage indicators with total debt/OPBITDA around over 4 times in FY2022.

Credit challenges

Profitability of UP-based sugar mills continues to depend on GoUP policy on cane prices – DSIL's profitability, along with other Uttar Pradesh-based sugar mills, continues to be vulnerable to the GoUP's policy on cane prices. The cane price is determined by the GoUP at the start of the crushing season. Thus, the performance of the company can be impacted by disproportionate increase in cane price. Further, the profitability remains vulnerable to government's policies on exports, export subsidy, MSP and remunerative ethanol prices. The recent measures taken by the Central Government and the GoUP have supported sugar prices and liquidity of sugar mills. The continuation of Government support in the form of remunerative ethanol prices and subsidies for exports are also likely to prevent the piling up of cane arrears.

Sugar mills remain vulnerable to industry cyclicality and agro-climatic risks – Being an agri-commodity, the sugar cane crop is dependent on weather conditions and is vulnerable to pests and diseases that may impact not only the yield per hectare but also the recovery rate. These factors can have a significant impact on the company's profitability. In addition, the cyclicality in sugar production results in significant volatility in sugar prices. However, the sharp downfall in the sugar prices is curtailed after the introduction of MSP by the Central Government in June 2018. Over the long term, it is expected that higher ethanol production with increased diversion towards B-heavy molasses and direct sugar juice would help curtail the excess supply of sugar, resulting in lower volatility in sugar prices and hence, cash flows from sugar business.

Liquidity position: Adequate

DSIL's liquidity position is adequate, with an average cushion of around Rs. 220 crore in the drawing power from February 2020 to January 2021. ICRA expects DSIL to comfortably meet its debt repayment obligations of around Rs. 50 crore per annum in FY2022–FY2023. However, the company has plans to set up a new distillery for capex of around Rs. 200 crore, of which ~80% is expected to be funded from debt with concessional interest rates.

Rating sensitivities

Positive factors – A sustained period of firm sugar prices driven by favourable demand–supply dynamics and increase in forward integration, the benefits of which would translate in reduced volatility of cash flows from the sugar business and reflect stability in operating profitability and debt coverage metrics on a sustained basis, may trigger an 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 result in moderation of profitability and debt coverage metrics 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 financial statements

About the company

Dwarikesh Sugar Industries Limited (DSIL), promoted by Mr. Gautam R. Moraraka, was incorporated in 1994 through the establishment of a 2,500 TCD sugar plant in the sugar-rich belt of UP at the Bundki village in the Bijnor district. DSIL has been raising its crushing capacity regularly and the capacity has since been increased to 21,500 TCD. It has three sugar plants, viz. Dwarikesh Nagar (DN), Dwarikesh Puram (DP) and Dwarikesh Dham (DD), at present. DN and DP are located in the Bijnor district and DD is located in the Bareilly district. Besides, DSIL has cogeneration facilities of 17 MW at DN, 33 MW at DP and 36 MW at DD unit. Of these, DSIL exports 8 MW from DN, 24 MW from DP and 24 MW from DD unit to the state grid. The company has a distillery of 130,000 litres per day at its DN unit, which is capable of manufacturing industrial alcohol and ethanol.

Key financial indicators (audited)

DSIL Standalone	FY2019	FY2020
Operating Income (Rs. crore)	1112.0	1336.1
PAT (Rs. crore)	95.1	73.5
OPBDIT/OI (%)	14.1%	10.2%
PAT/OI (%)	8.6%	5.5%
Total Outside Liabilities/Tangible Net Worth (times)	1.9	2.2
Total Debt/OPBDIT (times)	4.2	6.2
Interest Coverage (times)	7.4	4.1

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

Source: DSIL, 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* (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019		
					Apr 7, 2021	Apr 2, 2020	Apr 2, 2019	Oct 22, 2018	Jun 28, 2018	May 15, 2018
1	Term Loan	Long Term	230.65	211.02	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
2	Cash Credit	Long Term	770.00	--	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
3	Long term - Non-Fund Based Limits	Long Term	25.00	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
4	Long term - Unallocated Limits	Long Term	4.34	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
5	Commercial Paper^	Short Term	300.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

* as on December 31, 2020, ^carved out of working capital limits.

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 No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs Crore)	Current Rating and Outlook
NA	Term Loan 1	November 2018	5%	June 2024	116.55	[ICRA]A+ (Stable)
	Term Loan 2	January 2019	8.40%*	December 2025	114.10	[ICRA]A+ (Stable)
NA	Cash Credit	-	8.75%	-	770.00	[ICRA]A+ (Stable)
NA	Non-fund Based Limits	-	NA	-	25.00	[ICRA]A+ (Stable)
NA	Unallocated Limits	-	NA	-	4.34	[ICRA]A+ (Stable)
Not Placed	Commercial Paper^	-	-	-	300.00	[ICRA]A1+

** Subvention is available @ 4.20% (50% of the interest cost) on Rs. 72.98 crores for a period of 5 years on reducing balance.*

Source: *Company, ^ carved out of working capital limits.*

Annexure-2: List of entities considered for consolidated analysis: Not Applicable

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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.

For more information, visit www.icra.in

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