August 13, 2019

Harinagar Sugar Mills Limited: Ratings downgraded; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Term Loan	93.77	151.52	[ICRA]A- (Stable); Downgraded from [ICRA]A (Stable)
Fund-based Limits	310.00	310.00	[ICRA]A- (Stable); Downgraded from [ICRA]A (Stable)
Non-fund Based Limits	15.00	15.00	[ICRA]A2+; Downgraded from [ICRA] A1
Total	**418.77**	**476.52**	

*Instrument details are provided in Annexure - 1

Rationale:

The ratings revision takes in to account the increased leveraging level with higher working capital requirements which in turn is expected to result into moderation of the debt coverage metrics of Harinagar Sugar Mills Limited (HSML). The company has availed fresh term loans (in May 2019) under the Central Govt "scheme for extending soft loan to sugar mills to facilitate payment of cane dues to farmers for SY2019. The company's working capital intensity has increased due to higher sugar inventory as on March 31, 2019 as compared to previous year & the same is reflected in NWC/OI of 55% in FY2019 as against 49% in FY2018.

The ratings, however, continue to factor in the support measures taken by the Government of India (GoI) for the sugar industry such as fixing the minimum sugar price (MSP) at Rs. 31,000/MT as well as creating four million metric tonnes (MT) of buffer stock, which has in turn helped in recovery of sugar price for the company. The company's operations are further expected to benefit from an increasing mix of high-yield variety of sugarcane going forward, as reflected by the improvement in the recovery rate in SY2018 and 9M-SY2019. The ratings continue to derive comfort from the existing forward integration of the company's sugar plant into distillery and cogeneration operations, wherein the realisation levels remain remunerative. The ratings also favourably factor in the expansion of distillery unit to 120 Kilolitres per day (KLPD) capacity (from 50 KLPD) in FY2019, which will support the revenues and the profitability metrics of the company. Moreover, the ratings factor in the large sized crushing capacity of the company and the benefits of being located in eastern India, which is a sugar-deficit zone. The cane pricing followed in Bihar is decided by sugar companies in consultation with the state government, resulting in the cane prices to fall below the state advised price (SAP) in Uttar Pradesh. Further, subsidy supports from Central Government (production subsidy of Rs. 21.37 crore and transport subsidy of Rs. 5.67 crore) and State Government of Bihar (subsidy of Rs. 12.55 crore) will support liquidity position of the company going forward and timely receipt of the same remains a key monitorable.

The ratings, however, remain constrained by the inherent cyclicality and agro-climatic risks in sugar operations and vulnerability to Government regulations. The ratings also factor in the geographical-concentration risks associated with the single-mill operations of the company in Bihar and Government policies on import and export of sugar. The operations of the company's cogeneration unit remain exposed to counterparty credit risks pertaining to the sale of electricity to Bihar State Electricity Board, though the payments have been timely so far.

Outlook: Stable

The stable outlook reflects ICRA's expectation that sugar prices will remain stable in the near term supported by the recent government initiatives. The outlook may be revised to Positive in case of significant improvement in sugar prices along with material reduction in debt levels lead to improvement in debt coverage metrics of the company. The outlook may be revised to Negative in case any significant increase in the cane procurement cost impacts the sugar contribution margins or there is any further increase in leveraging level of the company.

Key rating drivers

Credit strengths

Large-sized sugar manufacturer with benefits of location in sugar-deficit eastern India - The company has set up its 11,500-tonne crushed per day (TCD) capacity sugar manufacturing facility in Bihar and enjoys high bargaining power due to its presence in a sugar-deficit zone and limited competition from nearby sugar factories.

Forward integration negates sugar cyclicality to some extent - The company has also set up cogeneration and distillery facilities of capacities 14.5 MW and 120 KLPD (increased from 50 KLPD in FY2019) respectively, which counter the sugar cyclicality to quite an extent. Also, remunerative realisation levels from these facilities support overall profitability levels.

Healthy sugarcane crushing volumes and improvement in recovery rate in FY2019 - The crushing volume was healthy at 17.5 lakh MT in 9M-SY2019. In addition, the recovery rate was higher at 10.71% in 9M-SY2019 compared with 10.04% in SY2018. The improvement in recovery rate is supported by increasing mix of high-yield variety of sugarcane.

Cane pricing decided by sugar companies in consultation with state government - In Bihar, the sugar factories (in consultation with the state government) fix the cane pricing for the sugar season. The cane pricing is applicable for all sugar factories in the state. This pricing mechanism provides relief to sugar companies as opposed to the SAP mechanism followed in Uttar Pradesh, wherein only the state government decides the cane pricing, which is generally higher than the company's cane costs.

Government's measure to support sugar prices and sugar mills' liquidity – The Cabinet Committee on Economic Affairs (CCEA) has approved creation of 4 million MT of sugar buffer stock for one year. The estimated maximum expenditure for the creation of buffer stock is around Rs. 1674 crore. The reimbursement under the scheme would be met on quarterly basis to sugar mills which would be directly credited into farmers' account on behalf of mills against cane price dues and subsequent balance, if any, would be credited to the mill's account. The 4 million MT of buffer stock creation would improve the demand-supply situation in the domestic market and result in an increase in the sugar prices.

Credit challenges

Moderation of coverage metrics due to increase in leveraging level – HSML's leveraging level has increased, largely due to increased long-term borrowings (under the Central Govt "scheme for extending soft loan to sugar mills) to facilitate payment of cane dues to farmers for SY2019.This is expected to result into moderation in the projected debt coverage metrics of the company in the near term. Company's leveraging levels also remain high due to high reliance on working capital borrowings that are closer to the peak levels as on March owing to the seasonal nature of the business. Any significant increase in the working capital borrowings owing to higher-than-expected sugar inventory levels remains a key monitorable.

High working capital intensity characterised by high inventory holdings - As is inherent in the sugar business, the company's working capital intensity remains high because of high inventory holdings. The working capital intensity has gone up in FY2019 due to high sugar inventory as on March 31, 2019 and the same is reflected by the NWC/OI of 55% in FY2019 as against 49% in FY2018. The company sells sugar to agents that act as representatives of the wholesalers or purchase sugar from the company and then sell to wholesalers.

Exposure to agro-climatic risks and cyclical trends in sugar business; vulnerability to Government/regulatory policies - Profitability of sugar mills remain vulnerable to the cyclical nature of the sugar industry, agro-climatic risks related to cane production, geographical-concentration risks associated with single-mill operations of HSML and Government policies on import and export of sugar.

Exposure to counterparty credit risk of Bihar State Electricity Board (BSEB) - Cogeneration operations of the company are exposed to counterparty credit risks pertaining to the BSEB. BSEB, however, has been making the payments within one week of bill submission.

Liquidity position

The liquidity position of the company remains adequate with presence of undrawn line of credit of ~Rs. 33 crore as on Jun'19 end. Further, the company's drawing power stood at around Rs. 433.87 crore as on June 2019 end against which total utilisation was 64%. HSML's liquidity position will also be supported by various subsidy measures taken by Central Government (production subsidy of Rs. 21.37 crore and transport subsidy of Rs. 5.67 crore) and State Government of Bihar (subsidy of Rs. 12.55 crore), although timely receipt of the same remains a key monitorable. In addition, higher expected volumes from the distillery business augurs well for the overall liquidity position of the company.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation / Standalone	The ratings are based on the standalone financial profile of the company

About the company:

HSML, incorporated in 1933 by Late Mr. Narayanlal B. Pittie, is a closely-held company with majority of the shareholding remaining with the Pittie family. The manufacturing facility is located in the West Champaran region of Bihar. HSML started with an initial crushing capacity of 600 TCD and gradually increased its crushing capacity to 11,500 TCD. The company also operates a 120-KLPD (increased from 50 KLPD in December 2018) distillery unit commissioned in March 2008, and a 14.5-MW cogeneration unit commissioned in November 2011. HSML has a subsidiary – Shangrila Food Products Ltd. – which is involved in biscuit manufacturing (with capacity of 23,420 MT per annum) on jobwork basis on behalf of Britannia Industries Limited.

Key financial indicators (Audited)

	FY2018	FY2019
Operating Income (Rs. crore)	596.4	685.3
PAT (Rs. crore)	36.2	27.3
OPBDIT/OI (%)	12.2%	11.0%
RoCE (%)	9.6%	8.2%
Total Debt/TNW (times)	1.4	1.5
Total Debt/OPBDIT (times)	4.6	5.3
Interest Coverage (times)	3.9	3.4

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

		Current Rating (FY2020)				Chronology of Rating History for the past 3 years				
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating August 2019	Date & Rating in FY2019 February 2019	May 2018	Date & Rating in FY2018 December 2017	Date & Rating in FY2017 November 2016	July 2016
1	Fund-based Term Loan	Long Term	151.52	125.88	[ICRA]A- (Stable)	[ICRA]A (Stable)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Fund-based Limits	Long Term	310.00	310.00	[ICRA]A- (Stable)	[ICRA]A (Stable)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
3	Non-fund Based Limits	Short Term	15.00	15.00	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+

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 www.icra.in

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 Loans	FY2011	-	FY2019	0.11	[ICRA]A- (Stable)
NA	Term Loans	FY2015	-	FY2019	1.21	[ICRA]A- (Stable)
NA	Term Loans	FY2016	-	FY2023	25.07	[ICRA]A- (Stable)
NA	Term Loans	FY2016	-	FY2021	26.38	[ICRA]A- (Stable)
NA	Term Loans	FY2018	-	FY2024	30.00	[ICRA]A- (Stable)
NA	Term Loans	FY2015	-	FY2022	11.00	[ICRA]A- (Stable)
NA	Term Loans	FY2020	-	FY2025	57.75	[ICRA]A- (Stable)
NA	Fund-based Limits	-	-	-	310.00	[ICRA]A- (Stable)
NA	Non-fund Based Limits	-	-	-	15.00	[ICRA]A2+

Source: Harinagar Sugar Mills Limited

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About ICRA Limited:

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