December 29, 2021

Dwarikesh Sugar Industries Limited: Ratings reaffirmed; outlook revised to Positive from Stable and rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based - Term Loans	230.65	354.43	[ICRA]A+ (Positive); Reaffirmed and outlook revised to Positive from Stable
Long-term Fund-based-Working Capital Facilities	770.00	735.00	[ICRA]A+ (Positive); Reaffirmed and outlook revised to Positive from Stable
Long-term Non-fund based-Working Capital Facilities	25.00	10.00	[ICRA]A+ (Positive); Reaffirmed and outlook revised to Positive from Stable
Long-term Unallocated Limits	4.34	0.56	[ICRA]A+ (Positive); Reaffirmed and outlook revised to Positive from Stable
Total	**1,029.99**	**1,099.99**	
Commercial Paper^	**300.00**	**300.00**	[ICRA]A1+; Reaffirmed

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

Rationale

The rating outlook revision to positive for the debt programmes of Dwarikesh Sugar and Industries Limited (DSIL) reflects the likely healthy growth in its revenues and profits in FY2022, while maintaining a comfortable credit profile. ICRA notes that the expansion in revenues as well as profits in FY2022 would be driven by firmed-up domestic and international sugar prices, supported by increased ethanol volumes and improved blended distillery realisations with favourable change in feedstock mix for ethanol production. ICRA expects the company's revenues in FY2022 to grow by 7-12% over the previous year, with higher revenues from the distillery division, led by enhanced capacities and improved realisations, despite some moderation due to the likely reduction in sugar volumes. Further, higher sucrose diversion towards B-heavy molasses/juice-based ethanol would moderate the inventory levels and lower its working capital borrowing levels going forward, which would allow its coverage metrics to emerge stronger. Additionally, DSIL is in the process of setting up a new distillery of 175-KLPD capacity at an investment of around Rs. 232 crore (~80% debt funded). The commercialisation of this new distillery would strengthen its operational profile and improve revenue diversification.

The ratings continue to factor in DSIL's efficient operations with one of 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, which acts as a cushion against the cyclicality of sugar business. 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, DSIL'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 remain constrained, however, 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 UP (GoUP), sugar international trade, sugar domestic quota, sugar and ethanol pricing and interest subvention loan for distillery capacity expansion.

Key rating drivers and their description

Credit strengths

Forward-integrated operations – DSIL operates 21,500-tonnes crushed per day (TCD) of sugar capacities in UP at three sugar mills. The plant's operations are forward integrated into power and alcohol business—co-generation capacity of 91 mega-watt (MW) (surplus – 56 MW) and distillery capacity of 162.5 kilo litre per day (KLPD) as on September 30, 2021. DSIL is planning to increase its distillery capacity by 175 KLPD, by June-July 2022, to strengthen its operational profile. The integrated operation provides alternate revenues and cushions its profitability against the cyclicality in sugar business. The sugar business accounted around 80% of the company's revenue, followed by distillery contributing ~7% (increased from 2-3% over the previous years) and the balance being derived from the co-generation business in FY2021. Increased revenues from the expanded distillery capacity would moderate the seasonality associated with sugar business, as the distillery operates for around 325 days in the year.

Operationally efficient sugar mills with healthy recovery rates – Notwithstanding the moderation in gross recovery rate for sugar season to 12.3% in SY2021 from 12.4% in SY2020 owing to agro-climatic conditions, the same remains healthy. However, the net recovery rates moderated to 11.36% in SY2021 (P.Y.: 12.26%) owing to higher diversion of cane towards B-heavy molasses-based ethanol. 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 continue to remain elevated, the higher production of ethanol from B-heavy molasses and sugarcane juice is likely to moderate the recovery rates to some extent. However, the same is anticipated to be compensated by higher production in the distillery segment.

Profitability likely to improve owing to steady sugar realisations and higher volumes from distillery segment – DSIL's overall operating profitability and cash accruals are expected to benefit from firm sugar realisations both internationally and domestically, along with better distillery performance. From FY2023 onwards, the company plans to divert higher cane towards production of ethanol through B-heavy molasses and/or sugarcane juice with the expanded capacity becoming operational. DSIL's operating margins will be supported by the likely continuation of MSP, remunerative prices of ethanol and the industry's focus on diverting of excess cane towards ethanol production, resulting in improved domestic demand-supply balance. Further, with increase in sugar sacrifice towards ethanol, the working capital debt and hence the total debt levels (despite increase in debt for distillery capex) are anticipated to reduce in going forward.

Strong capital structure and healthy debt coverage metrics – The company has a comfortable capital structure with a gearing of 1.1 times as on March 31, 2021 (P.Y.: 1.7 times). Reduced borrowings and higher profits resulted in better coverage indicators in FY2021 with total debt/ OPBIDTA of 3.0 times (P.Y.: 6.2 times) and NCA/total debt of 22.9% (P.Y.: 6.0%), though the interest cover remained flat at 4.2 times (P.Y.: 4.1 times). Going forward, the debt metrics are expected to remain healthy over the medium term, driven by lower total debt levels (despite higher term debt for distillery capex which is under interest subvention), expanded operating profits and healthy cash accruals.

Credit challenges

Profitability of UP-based sugar mills reliant on GoUP's policy on cane prices – DSIL's profitability, along with other UP-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 company's performance can be impacted by a disproportionate increase in cane price. Further, its profitability remains vulnerable to the Government's policies on exports, MSP and remunerative ethanol prices. However, the recent measures taken by the Central Government and the GoUP 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 UP-SAP increased by Rs. 25/quintal for the current season, firm realisations as well as enhanced ethanol volumes support profits.

Profitability of sugar mills 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, 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 variety may affect the yields and recovery rate. Nonetheless, DSIL has been exploring other varieties to mitigate this risk to a certain extent. The process of shifting to other varieties could be slow. In addition, the cyclicality in sugar production results in volatility in sugar prices. However, the sharp contraction in sugar prices is 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 are expected to help in curtailing the excess supply of sugar, resulting in lower volatility in sugar prices and in turn, cash flows from the sugar business.

Liquidity position: Adequate

DSIL's liquidity position is adequate with likely healthy cash flow from operations and average cushion of around Rs. 260 crore in drawing power in the twelve-month period ending in October 2021. ICRA expects DSIL to comfortably meet its debt repayment obligations of Rs. 50-55 crore per annum over FY2022-FY2023. Moreover, the company is in process of expanding its molasses/juice distillery capacities at an investment of around Rs. 232 crore, planned to be operational by June-July 2022. With respect to the proposed capex, DSIL has a sanction of Rs. 185.6 crore (nil availed till November 30, 2021) having a moratorium of two years and a comfortable repayment tenure of five years.

Rating sensitivities

Positive factors – A sustained period of firm sugar prices, driven by favourable demand–supply dynamics and benefits derived from investments in forward integration, resulting in lower volatility of cash flows from the sugar business and improved operating profitability and debt coverage metrics, on a sustained basis, may trigger an upgrade. Specific metric that may drive a favourable rating action could be interest cover of 7 times on a sustained basis.

Negative factors – The outlook can be revised to stable 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

Promoted by Mr. Gautam R. Moraraka, DSIL 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. It has been raising the 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 co-generation 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 also has a distillery of 162.5 KLPD at its DN unit, which is capable of manufacturing industrial alcohol and ethanol. Further, DSIL has embarked upon a project to set up a

175-KLPD distillery in DD in July 2021, which is expected to be operational by June-July 2022. This would increase the total distillery capacity to 337.5 KLPD.

Key financial indicators

DSIL Standalone	Audited	Audited
	FY2020	FY2021
Operating Income (Rs. crore)	1336.1	1838.8
PAT (Rs. crore)	73.5	91.5
OPBDIT/OI (%)	10.2%	11.0%
PAT/OI (%)	5.5%	5.0%
RoCE (%)	8.7%	13.3%
Total Outside Liabilities/Tangible Net Worth (times)	2.2	1.4
Total Debt/OPBDIT (times)	6.2	3.0
Interest Coverage (times)	4.1	4.2
DSCR (times)	2.4	0.8

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; RoCE: PBIT/Avg. (Total Debt + Tangible Net Worth + Deferred Tax Liability – Capital Work in Progress); DSCR: (PBT + Mat Credit Entitlements – Fair Value Gain through P&L – Non-Cash Extraordinary Gain/Loss)/(Interest + Repayments made during the Year)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2022)			Current Rating		Chronology of Rating History				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Sep 2021) (Rs. crore)			FY2021	FY2020	FY2019		
					Dec 29, 2021	Apr 7, 2021	Apr 2, 2020	Apr 2, 2019	Oct 22, 2018	Jun 28, 2018	May 15, 2018
1	Term Loans	Long Term	354.43	173.31	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
2	Working Capital Facilities	Long Term	735.00	-	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
3	Non-fund based-Working Capital Facilities	Long term	10.00	-	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Negative)
4	Unallocated Limits	Long term	0.56	-	[ICRA]A+ (Positive)	[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+	[ICRA]A1+

Amount in Crores; Source: Company; ^ carved out of working capital limits

Complexity level of the rated instrument

Instrument	Complexity Indicator
Term Loans	Simple
Working Capital Facilities	Simple
Non-fund based-Working Capital Facilities	Very Simple
Unallocated Limits	NA
Commercial Paper	Very Simple

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: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Punjab National Bank	Term Loans	Nov 2018 – Aug 2021	5%-8%	Jun 2024 – Sep 2028	354.43	[ICRA]A+ (Positive)
Punjab National Bank	Working Capital Facilities	-	NA	-	735.00	[ICRA]A+ (Positive)
Punjab National Bank	Non-fund based-Working Capital Facilities	-	NA	-	10.00	[ICRA]A+ (Positive)
NA	Unallocated Limits	-	NA	-	0.56	[ICRA]A+ (Positive)
Not Placed as on Nov 30, 2021	Commercial Paper^	-	-	-	300.00	[ICRA]A1+

Source: *Company; ^ carved out of working capital limits*

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

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