Dhampur Sugar Mills Ltd

November 01, 2021

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	1,337.27 (Enhanced from 1,294.29)	CARE A+ (CWD) (Single A Plus) (Under Credit watch with Developing Implications)	Revised from CARE A (Single A); Continues to be on Credit watch with Developing Implications
Total Bank Facilities	**1,337.27 (Rs. One thousand three hundred thirty-seven crore and twenty-seven lakh only)**		
Fixed Deposit	35.00 (Enhanced from 30.00)	CARE A+ (FD) (CWD) [Single A Plus (Fixed Deposit)] (Under Credit watch with Developing Implications)	Revised from CARE A (FD) [Single A (Fixed Deposit)]; Continues to be on Credit watch with Developing Implications
Total Medium-term instruments	**35.00 (Rs. Thirty-five crore only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities and instruments of Dhampur Sugar Mills Limited (DSML) factors in the improvement in the financial risk profile of the company in FY21 (refers to period from April 01 to March 31) marked by improvement in its capital structure and debt coverage metrics and likelihood of the same remaining comfortable going forward. The rating revision, also factors in the further strengthening of the business risk profile with increased diversion of sugarcane towards ethanol production leading to improved revenue diversification and lower sugar inventory levels. As a result of the above, during FY21, working capital requirements decreased and operating cycle improved for the company, and the same is likely to continue going forward as well.

The rating assigned to DSML continue to remain under 'Credit watch with developing implications' on account of announcement of the Scheme of Arrangement for the demerger of the company between two promoter families. Under the Scheme of Arrangement, DSML will be demerged into two companies viz. DSML and Dhampur Bio Organics Ltd (DBOL). All the assets and liabilities of Asmoli, Mansurpur and Meerganj plants will be transferred to the resulting company viz. DBOL. DSML will retain its two plants situated at Dhampur and Rajpura. The scheme of arrangement is subject to the receipt of various regulatory approvals. As on date, the company has filed the Scheme with NCLT for approval in September 2021 & the final order is awaited. CARE will continue to monitor the developments in this regard and will resolve the credit watch once the Scheme of Arrangement for the demerger is implemented. Notwithstanding the demerger, the improvement in the operating performance and debt protection metrics witnessed during FY21 is expected to continue in the demerged DSML as well.

The rating assigned to DSML continues to derive strength from the well-established and long track record of the company in the sugar industry, forward integrated nature of operations with distillery and cogeneration power divisions mitigating the industry cyclicality to an extent and healthy operating performance. However, these rating strengths are partially offset by susceptibility of the revenues and
profitability to the demand-supply dynamics, susceptibility to agro-climatic conditions, cyclical and highly regulated nature of the industry. However, going forward, with the expected higher diversion of B-heavy molasses/sugarcane juice towards ethanol production the sugar inventory levels are expected to decline in the country resulting in lower volatility in the prices. Furthermore, continuation of government's policy in the form of fixing minimum support price (MSP) for sugar and remunerative ethanol prices, would continue to lend support to the industry. DSML being an integrated player, remains well-placed to benefit from these developments.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Sustained increase in the scale of operations along with improved revenue and geographic diversification in operations.
- Improvement in capital structure on a sustained basis with overall gearing below 0.5x and Total Debt/PBILDT below 1.5x.

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Increase in overall gearing above 1.0x on a sustained basis along with Total Debt/PBILDT above 3x.
- Decline in profitability margins as marked by PBILDT margin below 10% on a sustained basis.
- Adverse changes in government policies affecting the operations and cash flow of the entity.

Detailed description of the key rating drivers

Key Rating Strengths

Integrated business model and diversified revenue stream
The company is forward integrated into cogeneration and distillery operations that de-risk the core sugar business of the company to some extent. DSML operates 45,500 tonne crushed per day (TCD) of sugar capacities in Uttar Pradesh (UP), which are forward integrated into power and alcohol business with cogeneration capacity of 220.5 megawatt (MW) and distillery capacity of 400 kilo litre per day (KLPD) as on March 31, 2021. During FY21, the distillery and power division together contributed around 25% (PY: 26%) of the gross revenue from operations and balance 75% (PY: 74%) was from the sugar division. DSML produces ethanol using B-heavy molasses and during FY21 it supplied about 11.04 crore litres of ethanol of which 9.07 crore litres was produced through B-heavy molasses and the rest from C-Heavy molasses. The higher contribution from the non-sugar segments' augurs well for DSML's overall profitability as their EBIT margins are relatively more stable than that of the sugar segment.

During FY21, total operating income of the company increased by 22% y-o-y to Rs.4,163 crore (PY: Rs.3,404 crore). The increase in total operating income was primarily due to increased sales in the distillery and sugar segment during the year. PBILDT margin decreased marginally to 11.68% (PY: 12.13%) due to decrease in sugar realization and higher selling expenses and repairs & maintenance expenses during the year. The average cane cost per MT during FY21 increased by 0.8% y-o-y, while average free sugar realization dipped marginally by 0.1% y-o-y.

During FY21, the company crushed 80.01 lakh tonnes of cane compared to 69.16 lakh tonnes in FY20, witnessing an increase of 16% y-o-y. The increase in crushing volumes was on account of increased crushing days during Q1FY21. Correspondingly, the company's sugar production and sales volumes increased y-o-y during FY21. The company's sugar sales increased 20% y-o-y to 9.83 lakh tonnes during FY21. However, the average free sugar realization decreased marginally to Rs.32.61 per kg compared with Rs.32.66 per kg in FY20. Out of total sales, the company exported 1.97 lakh tonnes of raw sugar (17% y-o-y increase) during FY21.

During Q1FY22, total operating income decreased 24% y-o-y to Rs.814 crore (PY: 1,071 crore) due to higher base of cane crushing volumes during Q1FY21. PBILDT margin improved to 13.22% (PY: 11.03%) driven by improved sugar and ethanol realizations during the period. During Q1FY22, the company has crushed 14.49 lakh tonnes of sugarcane and net sugar sales volume stood at 1.7 lakh tonnes. The average free sugar realization improved y-o-y to Rs.33.20 per Kg during the quarter as against Rs.32.18 per Kg during Q1FY21.

Improved financial risk profile
As on March 31, 2021, the overall gearing improved to 0.74x as against 1.28x as on March 31, 2020 and 1.47x as on March 31, 2019, on account of significant decrease in the working capital borrowings as on March 31, 2021. The Total debt/PBILDT improved from 3.58x as on March 31, 2019 to 2.38x as on March 31, 2021, while interest coverage improved from 4.91 times in FY19 to 5.54 times in FY21.
The reduction in the overall debt was primarily on account of working capital borrowings getting reduced which had decreased to Rs.711 crore as on March 31, 2021 from Rs.1,201 crore as on March 31, 2020, due to higher diversion of sugarcane towards ethanol. With continuous push towards ethanol production from the government, the integrated sugar mills have enjoyed benefits in terms of structural shift happening with decrease in inventory levels of sugar leading to lower working capital borrowings for the companies. Furthermore, the government has increased the sales quota under release mechanism for the mills with exports and ethanol production. The same has aided DSML is reducing its sugar inventory levels through higher sales during FY21. Further, sales of ethanol is realized within 21-30 days unlike the sugar and power segment, which also aided in improving the working capital of the company during FY21.

Ethanol demand and realizations have been improving over the past couple of years due to the government's focus on the ethanol blending programme and its effort to control sugar production by incentivizing ethanol which leads to overall inventory management and lower working capital requirements. Further with no major capex (apart from distillery capex as planned) and other regular maintenance capex, the overall gearing is expected to further reduce over the projected years with improvement in the net worth base by accretion of profits.

Update on the demerger
The Board of Directors of the company in its meeting on June 07, 2021, approved a Scheme of Arrangement for demerger of the business units of some plants of DSML (demerged company) into Dhampur Bio Organics Limited (resulting company). DSML currently has plants at 5 locations viz. Dhampur, Asmoli, Mansurpur, Rajpura and Meerganj. Now, with the Scheme of Arrangement for demerger, DSML will have Dhampur and Rajpura plants, aggregating sugarcane crushing capacity of 23,500 TCD, 121 MW of Cogen power and 250 KLPD of distillery capacity, while Dhampur Bio Organics Ltd will have Asmoli, Mansurpur and Meerganj plants, aggregating 25,000 TCD of crushing capacity (including recently commissioned capacity of 3,000 TCD), 99.5 MW of Cogen power, 250 KLPD of distillery capacity (including upcoming capacity of 100 KLPD) and 1,700 TPD of sugar refinery. The rationale for the demerger is to create opportunities for growth and expansion at demerged entities, enabling succession planning and long-term leadership for the entities.

As on date, the company has filed the Scheme with NCLT for approval in September 2021 post the receipt of in-principle approvals from the stock exchanges, CCI and majority of lenders. The approval is expected to be received in next few months.

For FY21, the gross income of demerged DSML stood at Rs.2,195 crore, which around 52% of DSML's (pre-scheme) income, while PAT stood at Rs.131 crore. Similarly, the gross income of demerged DBOL stood at Rs.2,038 crore and PAT stood at 87 crore for FY21. As on March 31, 2021, total debt of demerged DSML stood at Rs.755 crore and of demerged DBOL stood at Rs.403 crore. Going forward, CARE Ratings expects the credit profile of demerged DSML to remain comfortable post the demerger at the back of a healthy capital structure and comfortable business risk profile aided by conducive industry prospects.

Experienced promoters and long track record of operations
Mr Vijay Kumar Goel, the Chairman of the company, has served as a promoter director since 1960. The company has been operating in the sugar industry for over nine decades. The Managing Directors of the company, Mr Gautam Goel and Mr Gaurav Goel, are the sons of the promoters Mr VK Goel and Mr AK Goel respectively. Post demerger of the company, DSML is expected to be headed by Mr Gaurav Goel and DBOL to be headed by Mr Gautam Goel.

Industry Outlook
For SS2020-21, India's sugar output is estimated to have increased by 13% y-o-y to 30.9 million tonnes as per the estimates released by ISMA. The consumption is expected to be around 26 million tonnes and exports of about 6.8 million tonnes, leading to surplus of 8.7 million tonnes by end of season which is however lower from the earlier inventory levels which stood at 10.6 million tonnes. The export of sugar in the current SS is supported by the surge in global prices following which the Government reduced the export subsidy from Rs.6/kg to Rs 4/kg on any sugar contracted for export on or after May 20, 2021 and so far for the sugar season 2021-22 government has not declared any export subsidy owing to surge in the international prices. Currently it is expected India will end up exporting close to 6.8 or 7MT owing to recent surge in international prices. For next season SS21-22, sugar production is expected to remain stable y-o-y at 31 million tonnes and export sentiments also look strong in the wake of tight global supply scenario on the back of lower production from Brazil owing to drought. Further, with government's push toward boosting ethanol capacities, diversion of sugarcane / sugar juice towards the same has been reducing sugar output and thus rationalizing the sugar inventories in the country. The government has advanced 20% ethanol blending target from 2030 to 2025. Further, the government has announced remunerative ethanol pricing and incentive schemes (such as interest subvention) to build up capacities to achieve the same. It is believed that the with sugar inventories getting rationalised, demand-supply balance levelling out and considerable increase in ethanol sales, the cash flows of integrated sugar mills is going to enhance.

Key Rating Weaknesses

Working capital intensive operations
Sugar industry being seasonal in nature has high working capital requirements during the peak season which is from November to April. The companies have high working capital requirements during the peak season to procure their primary raw material, i.e., sugarcane and manufacture sugar during this period. DSML's focus on diverting more sugar to ethanol will be positive for the company as the manufacturing of ethanol (B-Heavy route) leads to quicker receivables compared with a gradual liquidation of the large sugar inventory spreading across 12-15 months.

The company's operating cycle has improved to 118 days in FY21 as compared with 170 days in FY20 primarily due to decrease in average inventory days from 203 days in FY20 to 147 days in FY21. The decrease in the inventory levels is primarily on account of diversion of sugar towards ethanol production. And the same has led to decrease in working capital borrowings for the company as well. The average working capital utilization for the twelve months period ended July 2021 stood at approximately ~46%.

Cyclical & Regulated nature of sugar business
The industry is cyclical by nature and is vulnerable to the government policies for various reasons like its importance in the Wholesale Price Index (WPI) as it classifies as an essential commodity. The government on its part resorts to various regulations like fixing the raw material prices in the form of State Advised Prices (SAP) and Fair & Remunerative Prices (FRP). All these factors impact the cultivation patterns of sugarcane in the country and thus affect the profitability of the sugar companies.

Liquidity: Adequate
Liquidity is marked by healthy accruals against the repayment obligations of the company. For FY22, the scheduled repayment obligations of term debt of the company is Rs.111 crore and is Rs.71 crore for the proposed demerged entity of DSML. Total cash & equivalents stood at Rs.15.39 crore as on September 30, 2021. The average utilization of the working capital facilities for the twelve months ended July 2021 stood at ~46%.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch' to credit ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Liquidity Analysis of Non-Financial Sector Entities
Financial ratios - Non-Financial Sector
Rating Methodology - Manufacturing companies
Rating Methodology - Sugar sector

About the Company
As on March 31, 2021 DSML's sugarcane crushing capacity stood at 45,500 TCD, co-generated power capacity at 220.5 MW and ethanol production capacity per day at 400 KL. The company is having integrated operations comprising of sugar manufacturing, distillery operations and power generation across 5 plants in UP.
DSML has announced with its notification dated June 07, 2021, that the Board of directors of the Company have considered and approved Scheme of Arrangement between Dhampur Sugar Mills, Dhampur Bio Organics and their respective shareholders and creditors. Under the scheme, DSML will have Dhampur and Rajpura plants while Dhampur Bio Organics Ltd will have Asmoli, Mansurpur and Meerganj plants. Further, in consideration of the transfer of the Demerged Undertaking from the DSML to Dhampur Bio Organics, the DBOL shall issue 1 (one) fully paid up equity share of face value Rs.10 (Rupees Ten) each of the DBOL to the shareholders of the DSML for every 1 (one) fully paid up equity share of Rs.10 (Rupees Ten) each held in the DSML.

Brief Financials (Rs. crore)	FY20 (A)	FY21 (A)	Q1FY22 (U/A)
Total operating income	3,404	4,163	814
PBILDT	413	486	108
PAT	211	219	45
Overall gearing (times)	1.28	0.74	NA
Interest coverage (times)	3.45	5.54	4.14

A: Audited;

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Complexity level of various instruments rated for this company : Annexure 4

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	-	1100.00	CARE A+ (CWD)
Fund-based - LT-Term Loan	-	-	-	Sep 2027	237.27	CARE A+ (CWD)
Fixed Deposit	-	-	-	-	35.00	CARE A+ (FD) (CWD)

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Fund-based - LT-Cash Credit	LT	1100.00	CARE A+ (CWD)	1)CARE A (CWD) (16-Jun-21)	1)CARE A; Stable (06-Oct-20)	1)CARE A; Stable (09-Oct-19)	1)CARE A-; Stable (08-Mar-19)2)CARE A-; Negative (24-Sep-18)3)CARE A-; Negative (05-Jun-18)
2	Fund-based - LT-Term Loan	LT	237.27	CARE A+ (CWD)	1)CARE A (CWD) (16-Jun-21)	1)CARE A; Stable (06-Oct-20)	1)CARE A; Stable (09-Oct-19)	1)CARE A-; Stable (08-Mar-19)2)CARE A-; Negative (24-Sep-18)3)CARE A-; Negative (05-Jun-18)
3	Fixed Deposit	LT	35.00	CARE A+ (FD) (CWD)	1)CARE A (FD) (CWD) (16-Jun-21)	1)CARE A (FD); Stable (06-Oct-20)	1)CARE A (FD); Stable (09-Oct-19)	1)CARE A- (FD); Stable (08-Mar-19)2)CARE A- (FD); Negative (24-Sep-18)3)CARE A- (FD); Negative (05-Jun-18)
4	Commercial Paper	ST	-	-	-	-	-	1)Withdrawn (24-Sep-18)2)CARE A1 (05-Jun-18)

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities - NA

Annexure 4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Fixed Deposit	Simple
2	Fund-based - LT-Cash Credit	Simple
3	Fund-based - LT-Term Loan	Simple

Annexure-5: Bank Lender Details for this Company
To view the lender wise details of bank facilities please **click here**

Note on complexity levels of the rated instrument: *CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Contact us

Media Contact
Name: Mradul Mishra
Contact no.: +91-22-6837 4424
Email ID: mradul.mishra@careratings.com

Analyst Contact 1
Name: Ravleen Sethi
Contact no: +91-11-4533 3251
Email ID: ravleen.sethi@careratings.com

Analyst Contact 2
Name: Jasmeen Kaur
Contact no: +91-11-4533 3245
Email ID: jasmeen.kaur@careratings.com

Relationship Contact
Name: Swati Agrawal
Contact no: +91-44-4533 3200
Email ID: swati.agrawal@careratings.com

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