Dhampur Sugar Mills Limited

July 22, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	1,031.53 (Reduced from 1,337.27)	CARE A+; Stable (Single A Plus; Outlook: Stable)	Reaffirmed and removed from 'Credit Watch with Developing Implications'; Stable outlook assigned
Total bank facilities	**1,031.53 (₹ One thousand thirty-one crore and fifty-three lakh only)**		
Fixed deposit	35.00	CARE A+; Stable (Single A Plus; Outlook: Stable)	Reaffirmed and removed from 'Credit Watch with Developing Implications'; Stable outlook assigned
Total medium-term instruments	**35.00 (₹ Thirty-five crore only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The ratings assigned to the bank facilities and instruments of Dhampur Sugar Mills Limited (DSML) have been reaffirmed and the ratings are removed from 'Credit Watch with Developing Implications' following the completion of the demerger of DSML (demerged company) and Dhampur Bio Organics Limited (DBOL; resultant company) and CARE Ratings Limited's (CARE Ratings') assessment of the demerged credit profile of DSML. This scheme of arrangement was approved by the National Company Law Tribunal (NCLT) vide its order dated April 27, 2022. The said order became effective from May 03, 2022. The business of DSML (pre-demerger) has been almost equally split between DSML and DBOL to enable succession planning. The shareholders have been given one share of DBOL for every share held in DSML and no cash consideration was involved in the said deal. The business risk profile of DSML remains strong, despite the resultant decrease in its scale of operations following the demerger.

The ratings for the bank facilities and instruments of DSML continue to derive strength from the well-established and long track record of the company in the sugar industry, the forward-integrated nature of operations with the distillery and cogeneration power divisions mitigating the industry cyclicality to an extent, and the healthy operating and financial performance.

However, these rating strengths are partially offset by the susceptibility of the revenues and profitability to the demand-supply dynamics, the susceptibility to agro-climatic conditions, and the cyclical and highly regulated nature of the industry. That said, going forward, with the expected higher diversion of B-heavy molasses and sugarcane juice towards ethanol production, the sugar inventory levels are expected to decline in the country, resulting in lower volatility in the prices. Furthermore, the continuation of the government's policy in the form of fixing minimum support price (MSP) for sugar and remunerative ethanol prices, will 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 the capital structure on a sustained basis, with overall gearing below 0.5x and total debt (TD)/, profit before interest, lease rentals, depreciation and taxation (PBILDT) below 2x.
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Negative factors – Factors that could lead to negative rating action/downgrade:

- Any significant debt-funded capex or decline in profitability, leading to total debt/PBILDT above 3.5x on a sustained basis.
- Decline in profitability margins, as marked by PBILDT margin below 10%, leading to a moderation in the interest coverage indicators on a sustained basis.
- Adverse changes in government policies affecting the operations and cash flow of the entity.

Key rating drivers

Key rating strengths

Experienced promoters and long track record of operations: Post demerger, DSML is headed by AK Goel and Gaurav Goel. The company has been operating in the sugar industry for over nine decades. Gaurav Goel has been affiliated with DSML and has served on its board since 1994. He is a business management graduate from the American College of London, UK, and an alumnus of the Harvard Business School. He has over 27 years of experience in the sugar industry and has been the President of the Indian Sugar Mills Association (ISMA) and Chairman of the Indian Sugar Exim Corporation Limited during 2017-18. During 2006-

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

2007, he was President of the Entrepreneurs' Organisation (EO), Delhi; Chair of the Young Presidents' Organisation (YPO), Delhi, 2012-13and the YPO Greater India Chapter in 2015-16.

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, post the demerger, operates the Dhampur and Rajpura units with 23,500 tonne crushed per day (TCD) of sugar capacities in Uttar Pradesh, which are forward-integrated into the power and alcohol business with a cogeneration capacity of 121 megawatt (MW) and distillery capacity of 250 kilolitre per day (KLPD) as on March 31, 2022. During FY22 (refers to the period from April 01 to March 31), the distillery and power division together contributed around 46% of the gross revenue from operations and the balance was from the sugar division. However, the distillery segment accounted for 45% of earnings before interest and tax (EBIT) in FY22, and sugar and power respectively accounted for 20% and 28%, respectively. DSML produces ethanol using B-heavy molasses, and during FY22, it supplied about 660.52 lakh BL (Bulk Litres) under B-heavy and 61.35 lakh BL under syrup, as compared to 606.44 lakh BL and nil, respectively, in FY21. The higher contribution from the non-sugar segments augurs well for DSML's overall profitability, as its EBIT margins are relatively more stable than that of the sugar segment.

Comfortable financial risk profile despite scale reduction post-de-merger: Notwithstanding the reduction in scale, post the demerger, DSML remains one of the leading sugar manufacturers in India with a healthy and integrated business profile and a long track record of operations.
The total operating income (TOI) in FY22 remained stable, at ₹2,208.71 crore, as against ₹2,245.03 crore in FY21. DSML crushed cane of 35.83 lakh tonne in FY22 vis-à-vis 38.47 lakh tonne in FY21, while the company sold 3.21 lakh tonne of sugar in FY22 (PY: 4.50 lakh tonne). The profitability margin improved due to the higher realisation of the sugar segment at ₹34.23 per kg in FY22, as against ₹32.01 per kg in FY21, and also the higher diversion towards B-heavy ethanol and the increased realisation in that segment year-on-year. The realisation from the power segment stood at ₹3.46 per unit in FY21 from ₹3.38 per unit in FY21. The company commenced ethanol production from cane juice as well during Q4FY22. The company is likely to increase the production through cane juice, going forward, which will aid DSML in optimising its working capital position and profitability.
As on March 31, 2022, the overall gearing stood at 1.00x. The balance sheet ratios are moderated due to a reduction in the net worth arising from the demerger. However, the TD in absolute terms is also reduced as on March 31, 2022, to ₹885.57 crore (of which ₹601.24 crore is working capital borrowing while the rest is term loan and lease liability).
Furthermore, CARE Ratings also notes that DSML is undergoing a capex of 130 KLPD of the distillery (of which 100 KLPD will be dual-feed based). The dual feed provides DSML with the flexibility to operate based on the prevalent parity prices and feedstock availability. The cost of the project is ₹160 crore, which is to be funded by term loans of ₹120 crore and the balance of ₹40 crore through internal accruals. The debt is tied-up and the project is likely to get completed in SS2023.

Supportive government policies: Starting 2018-19, the Government of India (GoI) has implemented a slew of measures and supportive mechanisms, providing much-needed support to the industry, which had been witnessing mounting cane arrears and high debt burden. With SS19 beginning with record inventory levels and production continuing to be high in SS19, the GoI continued to exert control on the volume of sugar sold (through the release order mechanism) and also pricing (through the enforcement of MSP). The other support offered by the government includes soft loans to clear cane arrears, cane subsidies, transportation subsidies for sugar exports, interest subvention on buffer stocks, and interest subvention schemes for setting up of ethanol capacity.

Industry outlook

On June 5, 2021, the government advanced the ethanol blending target of 20% in petrol by five years, from 2030 to 2025, to reduce pollution and India's dependence on expensive crude oil imports. This move is expected to provide a boost to the sugar industry by encouraging more diversion of sugarcane and sugar towards ethanol, thereby reducing the sugar glut in India. The EBP (Ethanol Blending Programme) aims to increase the ethanol blend level with petrol to 20% by 2025 (advanced from 2030). The blending percentage of 7.6% has been achieved in the current SS on average, with some states like Uttar Pradesh, Maharashtra, Karnataka, Uttarakhand, Bihar, etc, having even achieved higher blending percentage of up to around 10%. With the surplus sugar situation auguring well for the ethanol industry and with the support the government has shown in the recent past in the form of interest subventions for distillery capacity expansion, an aggressive capex is underway already, as around 1,000 crore litres of ethanol is required to achieve the target of 20% blending.
As per the ISMA, 3.4 million tonne of sugar equivalent is estimated to be deviated towards ethanol production using the diversion of sugarcane juice, sugar and sugar syrup, B-heavy molasses and C-heavy molasses. Excluding this sugar diversion towards ethanol, India is estimated to produce 35 million tonne of sugar during SS2021-22 (y-o-y growth of 12.2%). In addition to this, India has an opening stock of 8.2 million tonne of sugar, which is expected to increase the sugar availability to 41.5 million tonne during the year to meet the domestic requirements and also sugar exports from India.
An increase in crude oil prices due to the Russia-Ukraine crisis is aiding an uptick in ethanol prices. This may influence the diversion of sugarcane towards ethanol and, in turn, global sugar production. However, if India offloads 9 million tonne of sugar, the country will be left with around 7 million tonne of closing stock for the current SS2021-22, which will be sufficient to meet the normative requirements of India for the next sugar season.
Notably, this closing stock will be at a five-year low and much less than the level of closing stock seen in the past three sugar seasons 2017-18 to 2019-20, where the closing stock ranged between 10-15 million tonnes. The closing stock for SS2020-21, however, was lower, at 8.2 million tonne. Thus, if India ends SS2021-22 with a reduced closing stock of around 7 million tonne, backed by high sugar exports, the domestic sugar prices are likely to get support and remain firm amid the expected record-high production of 35 million tonne of sugar during the year.

Key rating weaknesses

Working capital-intensive operations: The 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, ie, 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 operating cycle increased in FY22 to 209 days on account of the high inventory, which increased to 324 days from 241 days in FY21. However, the same has reduced significantly in Q1FY23.

Cyclical and regulated nature of sugar business: The industry is cyclical by nature and is vulnerable to government policies for various reasons, such as 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 and remunerative prices (FRP). All these factors impact the cultivation patterns of sugarcane in the country, and thus, affect the profitability of the sugar companies.

Profitability of Uttar Pradesh-based sugar mills continues to depend on the state government policy on cane prices: DSML's profitability, along with other Uttar Pradesh-based sugar mills, continues to be vulnerable to the Government of Uttar Pradesh's (GoUP's) policy on cane prices. Cane prices are 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 prices. Furthermore, 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 support 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 is likely to prevent the piling up of cane arrears. Even as Uttar Pradesh-SAP increased by ₹25 per quintal for the current season, firm realisations, as well as enhanced ethanol volumes, support profits.

Liquidity: Adequate

The liquidity is marked by healthy accruals against the repayment obligations of the company. For FY23, the scheduled repayment obligations are ₹46.53 crore and ₹138.67 crore for FY24, with average debt service indicators likely to remain above 1.5x over the medium term. The total cash and equivalents stood at ₹2.26 crore as on June 30, 2022. The cash flow from operations is likely to remain healthy in the medium term with robust profits and a reduction in inventory levels.
As on March 31, 2022, sugar inventory stood at ₹701 crore (2.05 lakh tonne valued at an average rate of ₹34.23 per kg) and cane arrears stood at ₹115.82 crore. Subsequently, cane arrears were nil as on June 30, 2022, and inventory stood at ₹426.73 crore (1.39 lakh tonne valued at an average rate of ₹30.77 per kg).
Also, notably, the inventory days remain relatively high in comparison to other industries, as manufacturing of sugar takes place from November to April, while sales take place uniformly during the complete year and also due to the imposition of the sales quota on sugar companies, which led to high inventory days. The average utilisation of the working capital facilities for the 12 months ended March 31, 2022, stood at around 30%. The current ratio stood at 1.12x as on March 31, 2022, as against 1.19x as on March 31, 2021.

Analytical approach: Standalone

Applicable criteria

Criteria on assigning 'outlook' and 'credit watch'
CARE Ratings' policy on Default Recognition
Rating methodology – Manufacturing companies
Rating methodology – Sugar sector
CARE Ratings' methodology for short-term instruments
Liquidity analysis of non-financial sector entities
CARE Ratings' methodology for financial ratios (non-financial sector)

About the company

DSML is promoted by the Goel family of Bareilly, Uttar Pradesh. In March 2021, the promoters of the company, Gaurav Goel and Gautam Goel, jointly decided to segregate the management and ownership of different manufacturing facilities and units, equally between the two promoter family groups. Consequently, the board of directors, in its meeting on June 07, 2021, approved a scheme of arrangement for the demerger of the business units of Asmoli, Mansurpur, and Meerganj into Dhampur Bio Organics Limited (resulting company), which will be listed on the stock exchanges, with a mirror shareholding. This scheme of arrangement was ratified by the NCLT vide its order dated April 27, 2022. The said order became effective from May 03, 2022. DSML, post the demerger, has a total sugar capacity of 23,500 TCD, 121 MW of power, and 250 KLPD of ethanol.

Brief Financials (₹ crore)	FY21 (A)*	FY22 (A)	Q1FY23 (UA)
TOI	2,245.03	2,208.71	NA
PBILDT	288.87	304.95	NA
PAT	143.44	146.95	NA
Overall gearing (times)	0.74	1.00	NA
Interest coverage (times)	7.40	6.08	NA

A: Audited, UA: Unaudited; NA: Not available.
*FY21 financials are restated.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years: Please refer Annexure-2

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

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

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Cash credit		-	-	-	810.00	CARE A+; Stable
Fund-based - LT-Term loan		-	-	September 2027	221.53	CARE A+; Stable
Fixed deposit		-	-	-	35.00	CARE A+; Stable

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1.	Fund-based - LT-Cash credit	LT	810.00	CARE A+; Stable	-	1)CARE A+ (CWD) (November 01, 2021) 2)CARE A (CWD) (June 16, 2021)	1)CARE A; Stable (October 06, 2020)	1)CARE A; Stable (October 09, 2019)
2.	Fund-based - LT-Term loan	LT	221.53	CARE A+; Stable	-	1)CARE A+ (CWD) (November 01, 2021) 2)CARE A (CWD) (June 16, 2021)	1)CARE A; Stable (October 06, 2020)	1)CARE A; Stable (October 09, 2019)
3.	Fixed deposit	LT	35.00	CARE A+; Stable	1)CARE A+ (CWD) (June 22, 2022)	1)CARE A+ (FD) (CWD) (November 01, 2021) 2)CARE A (FD) (CWD) (June 16, 2021)	1)CARE A (FD); Stable (October 06, 2020)	1)CARE A (FD); Stable (October 09, 2019)

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

Not applicable

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 the complexity levels of the rated instruments: 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@careedge.in for any clarifications.

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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