Davangere Sugar Company Limited

July 02, 2020

Ratings

Facilities/Instruments	Amount (Rs. crore)	Rating[1]	Rating Action
Long term bank facilities – Term Loan	7.70 (12.23)	**CARE B; Stable (Single B; Outlook: Stable)**	**Revised from CARE D; ISSUER NOT COOPERATING (Single D; ISSUER NOT COOPERATING)**
Long Term Bank Facilities (Fund Based)	99.00	**CARE B; Stable (Single B; Outlook: Stable)**	**Revised from CARE C; Stable ISSUER NOT COOPERATING (Single C; ISSUER NOT COOPERATING*)**
Short Term Bank Facilities (Non Fund Based)	13.22	**CARE A4 (A Four)**	**Revised from CARE A4; ISSUER NOT COOPERATING (A Four; ISSUER NOT COOPERATING)**
Total	**119.92 (Rupees One hundred nineteen crore and ninety two lakhs only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE had earlier placed the ratings of Davangere Sugar Company Limited (DSCL) in issuer not cooperating category as it had not paid the surveillance fees for the rating exercise as agreed to in its Rating Agreement. Company has now paid the requisite fees and rating is therefore removed from Issuer Not Cooperating.

The revision in the rating of Davangere Sugar Company Limited (DSCL) is on account of the delay free track record in term loan repayments for more than 3 months, though there are ocassional overdrawals in the working capital limits. As per term loan statement submitted by the bank, there are no delays in debt servicing for 3 consecutive months. CARE takes into account the long track record and experience of the promoters, sales growth in FY20, improved capital structure and significant fall in inventory levels leading to improved working capital cycle. These strengths are however partially offset by the lower profitability margins in FY20, the inherent cyclical and regulated nature of the industry.

Rating Sensitivities

Positive Factors – Factors that could lead to positive rating action/upgrade

- Improvement in profitability and reduction in TDGCA on sustained basis.
- Improvement in liquidity position.

Negative Factors– Factors that could lead to negative rating action/downgrade

- Further stretching of WC cycle impacting liquidity
- Any large debt funded capex

Detailed description of the key rating drivers

Key Rating Weaknesses

Profitability margins affected by lower crushing days due to delay in start of SS19-20

During SS19-20, the heavy rainfall in Karnataka during the months of September and October 2019 had led to delay in the start of crushing season and as a result, the crushing days reduced to 117 days (SS18-19: 146 days). The recovery rate fell to 9% from the previous season's 9.5%. During FY20, despite lower sugar production, the company sold 47,542 MT of sugar (FY19: 28,760) offloading considerable amount of inventory. As on March 31, 2020 the company's finished goods inventory of sugar was worth Rs. 36.08 Cr against Rs. 91.16 Cr as on March 31, 2019. As on March 31, 2020, the company had cleared all the cane arrears. The PBILDT margin fell from 27.65% to 14.71% and PAT margin from 2.83% to 0.52% due to lower crushing days. The lower crushing days in SS19-20 had affected the power production of the co-gen plant due to reduced supply of the raw material, bagasse. The production almost halved in FY20 vis-à-vis FY19.

Cyclical and regulated nature of the industry

Cyclical nature of the sugar industry significantly impacts the operating performance and cash flow generation of the sugar companies. The raw material prices are regulated by the government. In addition to this, sale and distribution of

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

**Issuer did not cooperate; Based on best available information* by-products (molasses and power) are also regulated at different levels in different States. Integrated players are in a better position to counter cyclicality of the sugar business.

Significant inventory levels maintained by the company in past though reduced during FY20

The sugar industry is characterized by high levels of inventory holding (due to seasonality associated with sugarcane), coupled with low credit on sugarcane purchase, makes the operations of the company working capital intensive. During FY18 & 19, operating cycle of the company stood high at 404 days and 403 days respectively on account of holding inventory in expectation to realize at higher prices and high short term advances given for farmers and harvesting gangs. During Fy20, the company offloaded a huge amount of finished inventory at higher realization compared to FY19. The inventory days fell from 370 days in FY19 to 155 days in FY20. In addition to this, as on March 31, 2020 the company has cleared all the cane arrears with the farmers and thus creditor period fell by 11 days from 19 days to 8 days. All this led to a contraction of working capital cycle from 403 days to 200 days.

Key Rating Strengths

Delay free track record of 3 months

The company had earlier delayed the servicing of debt obligations pertaining to two term loans during the month of December 2019. However, the company started making advance payments of debt obligations pertaining to the term loans since Feb 2020. The company has also been regularly submitting No Default Statement. Bank has confirmed the servicing of interest and installment is regular. As far as working capital facilities are concerned, there are over drawals for not more than 30 days.

Long track record and experienced promoters

DSCL has more than four decades of track record in the present line of business. DSCL enjoys established relationship with farmers having operated in the same region over the decades. The day to day operations of the company are looked after by Mr S S Ganesh (MD), who is adequately supported by a group of professionals having rich business experience in the operative industry. The company is also supported by the CFO Mr. Onkarappa who has three decades of experience.

Growth in sales in FY20 and improvement in capital structure

During FY20, the company's sales improved on the back of higher realization and higher sales volume when compared to FY19. However, the margins were affected due to the late start of the season and lower recovery rate in FY20. The debt to equity ratio of the company improved from 0.4x as on march 31, 2019 to 0.34x as on March 31, 2020 as the term loans were repaid. The overall gearing of the company reduced from 2.43x the previous year to 2.14x as on Mar'20 due to term loan repayment and accruals in FY19 and FY20. The directors have brought unsecured loans to the extent of Rs.22 crores to meet the company's working capital operations. During FY21, the company is planning to replace around Rs. 40 Cr worth WC borrowing by Working Capital Term Loan, to be paid over a period of 7 years.

Liquidity : Stretched

The company's average fund utilisation for the 12 month period ended April '20 was 96%. As on March 31, 2020, the company had current ratio of 0.94x (PY: 0.92x) and cash and bank balance of Rs. 5.83 Cr.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology- Manufacturing Companies
Financial ratios - Non-Financial sector
Criteria for Short Term Instruments

About the Company

Davangere Sugar Company Limited was incorporated in 1970 as a joint sector undertaking between Karnataka Agro Industries Corporation (KIAC), Karnataka State Industrial Investment and Development Corporation (KSIIDC) and Farmers. DSCL commenced commercial operations in October 1974. However, owing to continuous losses from operation, it was declared a sick unit in FY87. Subsequently, with the debt restructuring and support from financial institutions, DSCL came out of Board of Industrial and Financial Reconstruction in 1996. The present promoters acquired the shares owned by KIAC and KSIIDC and took over the management of DSCL in 1995. Shri. S S Ganesh, MD, takes care of the day to day functioning of the company. As on March 31, 2019, the promoters hold 59.54% stake in DSCL. The company has an installed sugar crushing capacity of 4750 TCD and a multi fuel co-generation unit of 24.5MW.

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

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)	FY20(UA)
Total operating income	63.97	113.96	203.30
PBILDT	-2.07	31.51	29.90
PAT	-8.61	3.22	1.05
Overall gearing (times)	2.22	2.43	2.14
Interest coverage (times)	NM	1.76	1.53

A: Audited; UA: Unaudited; NM- Not Meaningful

Status of non-cooperation with previous CRA:
Not Applicable
Any other information:
Not Applicable
Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	99.00	CARE B; Stable
Non-fund-based - ST-Letter of credit	-	-	-	13.22	CARE A4
Term Loan-Long Term	-	-	July, 2023	7.70	CARE B; Stable

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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Cash Credit	LT	99.00	CARE B; Stable	1)CARE C; Stable; ISSUER NOT COOPERATING* (06-May-20)	1)CARE C; Stable (28-Jan-20)	1)CARE BB+; Stable (11-Jan-19)	1)CARE BB+; Stable (05-Jan-18) 2)CARE BBB-; Negative (05-Apr-17)
2.	Non-fund-based - ST-Letter of credit	ST	13.22	CARE A4	1)CARE A4; ISSUER NOT COOPERATING* (06-May-20)	1)CARE A4 (28-Jan-20)	1)CARE A4+ (11-Jan-19)	1)CARE A4+ (05-Jan-18) 2)CARE A3 (05-Apr-17)
3.	Term Loan-Long Term	LT	7.70	CARE B; Stable	1)CARE D; ISSUER NOT COOPERATING* (06-May-20)	1)CARE D (28-Jan-20)	1)CARE BB+; Stable (11-Jan-19)	1)CARE BB+; Stable (05-Jan-18) 2)CARE BBB-; Negative (05-Apr-17)

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

Name of the Instrument	Detailed explanation
A. Financial covenants	
I	
Ii	
Iii …and so on..	
B. Non financial covenants	
I	
Ii	
Iii …and so on..	

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

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