Magadh Sugar & Energy Limited (Revised)

January 2, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	494.56 (reduced from 505.50)	**CARE BBB+; Positive (Triple B Plus; Outlook: Positive)**	**Reaffirmed with outlook revised from Stable**
Short-term Bank Facilities	39.55	**CARE A2 (A Two)**	**Reaffirmed**
Total Bank Facilities	**534.11 (Rupees Five Hundred and thirty four crore and eleven lakh Only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Magadh Sugar & Energy Limited (MSEL) continues to derive strength from experienced promoters with long track record of operations, integrated business model resulting in diversified revenue streams and improvement in financial performance in FY19 (refers to the period April 1 to March 31) and H1FY20 supported by forward integrated units of ethanol and co-generation and various measures announced by the government supporting the sugar industry.

The ratings also factor in the working capital intensive nature of business, vulnerability of operations to agro climatic conditions, cyclical, seasonal and regulated nature of the industry.

Going forward demand supply dynamics and price movements of sugar and sugarcane in domestic and international markets, government regulations pertaining to the sugar industry and ability of the company to manage its working capital are the key rating sensitivities.

Outlook: Positive

The outlook has been revised to 'Positive' in view of expected improvement in performance and capital structure going forward in light of improved industry and regulatory environment.

The outlook may be revised to 'stable' if the company is unable to sustain the profit margins and/or there is deterioration in its capital structure and/or debt protection metrics.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters and long track record of operations

MSEL belongs to Mrs. Nandini Nopany and Mr C.S. Nopany faction of the erstwhile KK Birla group of companies. The group is an established business house having interest in sugar, textiles and fertilizers. Sutlej Textiles and Industries Limited (rated CARE A+; Stable/CARE A1+) belonging to the promoters is among India's leading producers of dyed spun yarn and value added/speciality yarn. Chambal Fertilizers and Chemicals Limited, where the Nandini Nopany faction is one of the three promoter groups, is engaged in the manufacture of urea and trading of complex fertilizers and pesticides. The sugar units of MSEL have an operational track record of over eight decades which were earlier operating under Upper Ganges Sugar & Industries Limited (UGSIL) and Oudh Sugar Mills Limited (OSML). The combined sugar capacity of the group, (49,200 TCD) is one of the largest in the Indian sugar industry.

Integrated business model resulting in diversified revenue streams

All of MSEL's sugar manufacturing units located in Bihar are integrated with co-generation power plant. Further, of the above units, the sugar unit located in Narkatiaganj is forward integrated with a distillery unit. Integrated business model provides alternate revenue streams and cushion against cyclicality of the sugar business, to some extent. During FY19, the distillery and the cogeneration segment, collectively contributed to 16.57% of the gross revenue (as against 11.21% in FY18) and 83.85% of the PBIT (as against 82.50% in FY18).

Improvement in performance in FY19 and H1FY20 supported by forward integrated units of ethanol and co-generation and various measures announced by the government to support the sugar industry

The total operating income of the company remained stable in FY19, despite increase in production and sales in the sugar segment due to sharp decline in sugar prices (ASP of Rs.30.90/kg in FY19 as against Rs.36.40/kg in FY18), as a result of over-supply pursuant to record production in SS18 and SS19. The company, however, was able to post improved

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

profitability (PBILDT margin up from 8.88% in FY18 to 14.28% in FY19) led by improved performance of the cogeneration and the distillery segments (as a result of higher production of molasses and bagasse upon 22% higher quantum of sugar cane crushed in SS19), inventory gains and support in the form of various government incentives.

In H1FY20, although the y-o-y total operating income decreased pursuant to government imposed restriction on sugar sold, MSEL's PBILDT level increased from 8 crore in H1FY19 to Rs.45 crore in H1FY20 due to increase in sales realizations from Rs.30.13/kg in H1FY19 to Rs.33.55/kg in H1FY20.

Various government initiatives like introduction of minimum support price of sugar at Rs.29/kg in June 2018 and its increase to Rs.31/kg in February 2019, resulting in inventory gains, quota based supply controls minimising price impact, diversion of sugarcane for alternate usage by increasing ethanol blending standards and prices, increasing subsidised sugar exports (minimum export quantity increased from 2mn for SS18 to 5mn for SS19 and 6 mn for SS20) to reduce sugar supply, introduction buffer stock and increase of buffer stock from 3 mn tonnes from July 2018 to June 2019 and 4 mn from Aug 2019 to July 2020 valued at higher rates resulting in higher reimbursement of carrying cost along with state subsidies has had a positive impact on the company's financial health.

Segment wise performance analysis is hereunder:

Sugar Segment: 22% higher sugarcane crushing in FY19 coupled with higher recovery (10.88% vis-à-vis 10.14% in FY18) led to increased sugar production; however, realisations declined sharply to Rs.30.90/kg in FY19 from Rs.36.40/kg in FY18 owing to supply glut in the industry in spite of government measures for controlling supply and thereby, supporting prices. The segment PBIT increased from Rs.16.69 crore in FY19 vis-à-vis Rs.14.37 crore in FY18, mainly due to increase in sales volume of sugar.

Distillery Segment: MSEL's distillery segment posted improvement in profitability (PBIT of Rs.37.28 crore in FY19, up from Rs.15.07 crore in FY18) as a result of increased production of ethanol (on the back of higher production of molasses) and also due to increase in realizations of ethanol.

Power Segment: Increased bagasse production as mentioned above had a corresponding effect on power division's performance (PBIT of Rs.37.25 crore in FY19 as against Rs.29.07 crore PBIT in FY18).

The overall gearing ratio of the company, remained comfortable at 1.18x as on March 31, 2019 (1.22x as on March 31, 2018). The borrowings were mainly taken for working capital financing in the form of long term loans and short term borrowings. In addition, around 15% of the total debt outstanding as on March 31, 2019 comprised soft loans under various financial assistance schemes of the government where interest rates ranged between 0%-4%.

Key Rating Weaknesses

Working capital intensive nature of operations

Since sugar is an agro-based commodity (with sugarcane crushed mainly during November to April), sugarcane has to be crushed within a day or two of its arrival in the mills. Hence, the sugar inventory is piled up during the crushing season and gradually released till the commencement of the next crushing season, resulting into high inventory carrying cost and requirement of high working capital. Gradually, the inventory declines and reaches a minimum by the end of September or October. In line with the level of inventory, the overall gearing of MSEL stood at 1.18x as in March 31, 2019 (as against 1.22x as on March 31, 2018) which was at relatively lower levels at 1.07x as on September 30, 2019 and at 0.84x as on September 30, 2018. Various government measures to control supply of sugar amidst record production such as maintenance and increase of buffer stock, monthly sales quota also resulted in increase in inventory period increased from 236 days in FY18 to 318 days in FY19 and 339 days in H1FY20. However, in case of increase in buffer stock inventory, support in the form increase carrying cost reimbursement is to benefit sugar companies including MSEL. MSEL's outstanding creditors which had increased from around Rs.170 crore as on March 31, 2018 to Rs.348 crore as on March 31, 2019 reduced to Rs.57 crore as on September 30, 2019 on the back of higher sugar realizations and government's support in the form of soft loan to clear cane dues. Further, the company has cleared its dues from SS19 cane purchases till date.

Vulnerability of operations to agro climatic conditions

Being an agro-based industry, performance of MSEL is dependent on the availability of sugarcane for crushing which may get adversely affected due to adverse weather conditions resulting into lower availability and diversion of cultivable lands to alternate crops.

Cyclical and seasonal nature of the industry

The production of sugarcane is on an uptrend for two years and then declines over the next two years, before trending up again. It is a typical cycle which is affected more by cane and sugar supply than by sugar demand. Further, depending on the variety of the cane, the sugar cane takes around 12-18 months to be harvested from the time it is sown. The crushing of cane typically begins from the month of November and goes up to April while sugar sales happen throughout the year.

Regulated nature of the industry

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), Minimum Sale Price of Sugar, mandatory ethanol blending etc. All these factors impact the cultivation patterns of sugarcane in the country and thus affect the profitability of the sugar companies. Further, the government has also announced various other incentives like export quotas and subsidies, financial assistance for carrying of buffer stock and in the form of soft loans to clear cane dues, introduction of monthly sales quota, etc. to support the industry.

Prospects

According to revised estimates released by the Indian Sugar Mills Association (ISMA), India's sugar output is estimated to decline by 19% y-o-y to 26.85 mn MT during the sugar season 2019-20. As on November 30, 2019, sugar production in India stood at 1.9 mn MT for the current sugar season, a y-o-y fall of 54%.

While production is expected to fall, the opening stock for the new season 2019-20 stands at an all-time high of about 14.6 mn MT. Considering production and opening stock, India will have an availability of 41.45 mn MT of sugar to fulfil the domestic and export requirements.

Domestic consumption can be expected to stand at 26.7 mn MT. In addition to this, the Government has announced subsidy of Rs.10.4/kg for export of 6 mn MT of sugar and allowed carry over export of 1.2 mn MT of SS 18-19. Government has also increased procurement prices for ethanol to divert sugarcane towards production of ethanol through B-heavy molasses, which will further lower sugar production. Considering sugarcane diversion for ethanol blending, domestic consumption and exports, sugar stock is expected to decline below the previous year's closing stock levels by the end of SS19-20; though it may continue to remain above the normative levels. Further with the announcement on increase in buffer stock, this quantity will be out of the system till July 2020.

Overall, the outlook is stable, supported by with slew of measures by the government including MSP for sugar, ethanol-blending and export incentive. However, linking of cane price to sugar price realization still remains far from being implemented. Overall, the stock situation which is prevalent in the industry at present is expected to diminish by the next year. Thus, the sugar prices are expected to remain range bound or increase moderately and average in the range of Rs.34-Rs.35 per kg in the coming months.

Adequate Liquidity:

The company earned GCA of Rs.60.43 crore in FY19 against a term debt repayment obligation of Rs.56.09 crore in the year. In FY20, MSEL has a term debt obligation of Rs.41 crore, of which it has repaid Rs.36 crore till Sep 30, 2019. In sugar industry, H2 is generally better in which crushing and the other integrated activities take place. Accordingly, the cash accruals of MSEL in H2FY20, is expected to be higher and sufficient to meet the balance debt repayment obligations.

For sugar companies, the utilization of bank limit (& drawing power) follows a certain cycle. It peaks at the end of sugar crushing season due to build-up of inventory and gradually becomes low before start of the next sugar season. The liquidity is also supported by subsidy receivable of Rs.22 crore and by average fund based working capital utilisation of the company which remained moderate at around 69% and 54% (excluding buffer stock) during the last 12 months ending Oct 2019, the peak utilization stood at 89% and 75% (excluding buffer stock) in April/May 2019.

Analytical approach*:* Standalone Approach.

Applicable Criteria

Criteria on assigning Outlook and Credit Watch to Credit Ratings
Criteria for Short Term Instruments
CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
Rating Methodology- Sugar Sector

About the Company

MSEL was incorporated on March 19, 2015 as a subsidiary of Upper Ganges Sugar & Industries Limited (UGSIL). UGSIL and Oudh Sugar Mills Limited (OSML) were incorporated in 1932 by the erstwhile KK Birla group. Ms Nandini Nopany and Mr Chandra Shekhar Nopany, eldest daughter and grandson of the late Mr. K. K. Birla, inherited UGSIL and OSML after the demise of Mr. K. K. Birla on August 30, 2008. Through a Composite Scheme of Arrangement, the business undertakings located at Sidhwalia and Hasanpur, Bihar of UGSIL have been demerged to MSEL at book value from appointed date i.e. April 1, 2015. Also, the business undertaking located at Narkatiaganj, Bihar of OSML has been first transferred to Vaishali Sugar and Energy Limited (VSEL) via slump sale and is subsequently merged with MSEL from the appointed date i.e. April 1, 2015. MSEL is primarily engaged in manufacture and sale of Sugar and its By-products (molasses and bagasse), Spirits including Ethanol and co-generated power in the state of Bihar.

MSEL is operating sugar mills of capacity 17,500 TCD, TCD, co-generation power plants of 35 MW and distillery units of 50 KLPD.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	744.09	744.13
PBILDT	66.07	106.23
PAT	24.91	34.22
Overall gearing (times)	1.22	1.18
Interest coverage (times)	1.54	3.04

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

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	-	-	-	375.00	CARE BBB+; Positive
Fund-based - LT-Term Loan	-	-	June 2025	119.56	CARE BBB+; Positive
Non-fund-based - ST-Bank Guarantees	-	-	-	19.55	CARE A2
Fund-based - ST-Working Capital Demand loan	-	-	-	20.00	CARE A2

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Cash Credit	LT	375.00	CARE BBB+; Positive	1)CARE BBB+; Stable (05-Jul-19)	1)CARE BBB+; Stable (31-Mar-19) 2)CARE A-; Negative (25-Jul-18) 3)CARE A-; Negative (06-Apr-18)	1)CARE A-; Stable (03-Aug-17)	-
2.	Fund-based - LT-Term Loan	LT	119.56	CARE BBB+; Positive	1)CARE BBB+; Stable (05-Jul-19)	1)CARE BBB+; Stable (31-Mar-19) 2)CARE A-; Negative (25-Jul-18) 3)CARE A-; Negative (06-Apr-18)	1)CARE A-; Stable (03-Aug-17)	-
3.	Non-fund-based - ST-Bank Guarantees	ST	19.55	CARE A2	1)CARE A2 (05-Jul-19)	1)CARE A2 (31-Mar-19) 2)CARE A2+ (25-Jul-18) 3)CARE A2+ (06-Apr-18)	1)CARE A2+ (03-Aug-17)	-
4.	Non-fund-based - ST-Letter of credit	ST	-	-	-	1)Withdrawn (31-Mar-19) 2)CARE A2+	1)CARE A2+ (03-Aug-17)	-

						(25-Jul-18) 3)CARE A2+ (06-Apr-18)		
5.	Fund-based - ST-Working Capital Demand loan	ST	20.00	CARE A2	1)CARE A2 (05-Jul-19)	1)CARE A2 (31-Mar-19) 2)CARE A2+ (25-Jul-18) 3)CARE A2+ (06-Apr-18)	-	-

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.*

Media Contact

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

Analyst Contact

Name: Mr Anil More
Tel: 033-4018 1623
Cell: +91 8444 867144
Email: anil.more@careratings.com

Business Development Contact

Name: Mr Lalit Sikaria
Tel: 033-4018 1607
Cell: +91 98303 86869
Email ID : lalit.sikaria@careratings.com

About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

****For detailed Rationale Report and subscription information, please contact us at www.careratings.com**