

## Press Release

L H Sugar Factories Limited

August 24, 2021

Rating Assigned



<b>Total Bank Facilities Rated*</b>	Rs. 582.00 Cr.
<b>Long Term Rating</b>	ACUITE A-/Positive (Assigned)
<b>Short Term Rating</b>	ACUITE A1 (Assigned)

\* Refer Annexure for details

### Rating Rationale

Acuite has assigned the long term rating of '**ACUITE A-**' (read as **ACUITE A minus**) and short term rating of '**ACUITE A1**' (read as **ACUITE A one**) on the Rs. 582.00 cr. bank facilities of LH Sugar Factories Limited (LHSF). The outlook is '**Positive**'.

### Rationale for rating assigned

The ratings assigned derive comfort from extensive experience of promoters in the sugar industry, long track record of operations, good relation with sugarcane farmers and reputed as well as diversified customer base across various industries. The company has sugar mill with capacity of 12,500 TCD and forward integrated business with bagasse based co-generation of 44.25 MW and distillery of 160 KLPD. The rating assigned also factors in moderate financial risk profile of the company marked by gearing of 1.42 times as on 31<sup>st</sup> March 2021, moderate debt-coverage indicators as evident from the interest coverage ratio of 5.22 times in FY2021 (Prov.) and debt service coverage ratio 1.65 times in FY2021 (Prov.). The company has net worth of Rs. 274.62 crore as on 31<sup>st</sup> March 2021 as a result of moderate profitability and healthy ploughing back of profits. On the contrary, ratings are constrained on account of working capital intensive nature of industry, industry cyclicality, agro-climatic risks and intense competition in the industry. Going forward, the ability of the company to further sustain its scale of operations along with the effective management of its working capital cycle and financial risk profile would be the key rating sensitivities.

Acuite believes the company is set to benefit from the increased capacity of distillery and the recent measures taken by government for ethanol blending.

### About the company

LH Sugar Factories Limited, was incorporated in 1933 by two brothers – Raja Lalta(L) and Sahu Hari(H). Company at present the company is being managed by the descendants of the two family. The company is engaged in manufacturing of sugar and its by-products such as molasses used for ethanol generation and bagasse used for power generation. LH Sugar Factories has 12,500 TCD sugar mill at Pilibhit in north-western UP. The sugar mill is forward integrated with co-generation of 44.25 MW and a distillery of 160 KLPD which was previously 60KLPD.

### Analytical Approach

For arriving at the rating, Acuite has taken the standalone view on the business and financial risk profile of LH Sugar Factories Limited.

### Key Rating Drivers

#### Strengths

- Experienced management and Forward integrated business model with sugar by-products**

LH Sugar Factories commenced its operations in 1910 by two brothers, Mr. Raja Lalta and Mr. Sahu Hari and later in 1933, it was converted into limited company. At present the company is being managed by the descendants of the two family. The company has broad outlook with the company's day to day operations are managed by qualified professionals which is ably supported by well experienced technical team. The company has developed healthy relations with sugarcane farmers as the company has low cane arrears as compared to other sugar mills in the locality. Acuite believes that the company will be benefitted over the medium term on the back of established presence in the sugar industry for more than ten decades.

The company has sugar mill with a capacity of 12,500 tonne crushed per day (TCD), the sugar mill is forward integrated with bagasse based co-generation of 44.25 MW. During the year FY2021, the company produced 16.85 Cr (KWh) of electric power out of which 7.79 Cr (KWh) was for captive consumption and 9.06 Cr (KWh) was sold to Uttar Pradesh Power Corporation Limited (UPPCL). There is also a distillery with capacity of 160 kilo liter per day (KLPD) which was previously 60 (KLPD). The additional capacity of 100 KLPD came into operation from January 2021 and the total cost of the project was Rs. 85.00 Cr which was financed from Rs. 25.00 crore of internal accruals and term loan of Rs.60.00 Cr. The company has tenders with oil marketing companies to supply ethanol.

- **Improvement in operating performance**

The company reported operating income of Rs. 1069.22 Cr in FY2021 (Prov.) as against Rs. 775.26 Cr in FY2020 and Rs.709.71 Cr in FY2019. This is majorly due to increased income in sugar as well as distillery segment over the years. The operating margins have grown significantly from 5.82 per cent in FY2019 to 13.06 per cent in FY2021 (Prov.) due to the diversion of sugarcane to distillery segment which has higher margins. The improvement in margins is expected to be sustained over the medium term due to increase in production capacity of distillery division from 60 KLPD to 160 KLPD. The operations for additional capacity commenced in January, 2021. This will further increase the revenues of the company over the medium term.

- **Moderate Financial Risk Profile**

The financial risk profile of the company is moderate marked by moderate net worth, moderate gearing levels and debt protection metrics and coverage indicators. The net worth of the company is moderate at Rs. 274.62 crore as on March 31, 2021 (Prov.). The net worth levels have seen improvement from FY2020 to FY2021 on account of higher ploughing back of profits in form of retained earnings.

The company has followed a moderately aggressive financial policy in the past and is continuing with the same policy as reflected through its gearing of 1.42 times as on 31<sup>st</sup> March 2021 (Prov.) as against 1.70 as on 31<sup>st</sup> March 2020 and total outside liabilities to tangible net worth (TOL/TNW) levels of 2.15 times as on March 31, 2021 (Prov.). Also, Debt-EBITDA improved from 3.45 times in FY2020 to 2.77 times in FY2021 (Prov.). The company's debt coverage indicators have deteriorated as evident by fall in debt-service-coverage-ratio of 1.65 times as on 31<sup>st</sup> March, 2021 (Prov.) as against 2.28 times as on 31<sup>st</sup> March, 2020 and interest coverage ratio of 5.22 times as on 31<sup>st</sup> March, 2021 (Prov.) as against 5.33 times as on 31<sup>st</sup> March, 2020.

Acuite believes that the financial risk profile of the company will continue to remain moderate on account of moderate net worth and debt protection metrics.

## **Weaknesses**

- **Profitability of sugar mills remains vulnerable to industry cyclicality and agro-climatic risks**

Being an agro-commodity, the sugar cane crop is dependent on climatic conditions and is vulnerable to pests and diseases that may not only impact the yield per hectare but also the recovery rate. These factors can have a significant impact on the company's profitability. In addition, the cyclicality in sugar production results in volatility in sugar prices. However, the sharp contraction in the sugar prices is curtailed after the introduction of MSP by the Central Government in June 2018. Over the long term, higher ethanol production with increased diversion towards B-heavy molasses and direct sugar juice is expected to help curtail the excess supply of sugar, resulting in lower volatility in sugar prices and in turn, cash flows from the sugar business. Further, the sugar industry is highly competitive and fragmented marked by presence of many organised and unorganised players in this industry, thus putting pressure on the profitability margins of the company.

- **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. However, the company is focusing on diverting more sugarcane to ethanol which will help the company to off-load the inventory quickly as compare to earlier. Though the company has de-risked their model by forward integration to some extent, the sugar segment may affect the overall profitability and fund requirement. However, the average working capital utilization for the 12 months period ended May 2021 stood at approximately ~31%.

### Rating Sensitivity

- Operating profitability margin dropping by more than 250 basis points, leading to lower-than-expected cash accrual
- Substantial deterioration in working capital operations leading to stretched liquidity

### Material Covenants

None

### Liquidity position: Healthy

The company has healthy liquidity marked by healthy net cash accruals to its maturing debt obligations. The company generated cash accruals of Rs. 101.68 crore for FY2021(Prov.) as against Rs. 52.25 crore of repayment obligations for the same period. The company has unencumbered cash and bank balances of only Rs. 5.97 crore as on 31st March 2021 (Prov.). The current ratio of the company stood at 1.78 times as on 31<sup>st</sup> March 2021 (Prov.). Further, the fund-based working capital limits are utilized at an average of 30.97 per cent in the last twelve months. Therefore, there are enough net cash accruals & limits available to utilize more funds if required to support incremental requirements.

### Outlook: Positive

Acuite believes that LHS will maintain a positive outlook over the medium term as the company is set to benefit from the recent measures taken by government for ethanol blending and the increased capacity of distillery from 60 KLPD to 160KLPD which will in turn improve the margins and scale of operations. The rating may be upgraded if the company registers higher-than-expected growth in revenues and profitability through the distillery segment while maintaining the working capital cycle. Conversely, the outlook may be revised to 'Stable' in case the company registers lower-than-expected growth in revenues and profitability or in case of deterioration in the company's financial risk profile or significant elongation in working capital cycle.

### About the Rated Entity - Key Financials

	Unit	FY21 (Prov.)	FY20 (Actual)
Operating Income	Rs. Cr.	1069.22	775.26
PAT	Rs. Cr.	53.68	32.50
PAT Margin	(%)	5.02	4.19
Total Debt/Tangible Net Worth	Times	1.42	1.70
PBDIT/Interest	Times	5.22	5.33

### Status of non-cooperation with previous CRA (if applicable)

None

### Any other information

None

### Applicable Criteria

- Default Recognition - <https://www.acuite.in/view-rating-criteria-52.htm>
- Manufacturing Entities - <https://www.acuite.in/view-rating-criteria-59.htm>
- Financial Ratios And Adjustments - <https://www.acuite.in/view-rating-criteria-53.htm>

### Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

### Rating History (Upto last three years)

Not Applicable

**\*Annexure – Details of instruments rated**

Lender's Name	Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Crore)	Ratings/Outlook
State Bank of India	Cash Credit	Not Applicable	Not Applicable	Not Applicable	145.00	ACUITE A-/Positive (Assigned)
State Bank of India	Cash Credit	Not Applicable	Not Applicable	Not Applicable	160.00	ACUITE A-/Positive (Assigned)
State Bank of India	Working Capital Term Loan - GECL	Not Available	7.95%	Not Available	82.97	ACUITE A-/Positive (Assigned)
State Bank of India	Term Loan - I	Not Available	3.40%	Not Available	12.53	ACUITE A-/Positive (Assigned)
State Bank of India	Term Loan –II	Not Available	8.40%	Not Available	21.15	ACUITE A-/Positive (Assigned)
State Bank of India	Term Loan –III	Not Available	8.55%	Not Available	59.08	ACUITE A-/Positive (Assigned)
State Bank of India	Term Loan –IV	Not Available	7.95%	Not Available	51.21	ACUITE A-/Positive (Assigned)
State Bank of India	Term Loan – V	Not Available	5.00%	Not Available	38.45	ACUITE A-/Positive (Assigned)
Not Applicable	Proposed Long Term Loan	Not Applicable	Not Applicable	Not Applicable	2.61	ACUITE A-/Positive (Assigned)
State Bank of India	Bank Guarantee	Not Applicable	Not Applicable	Not Applicable	9.00	ACUITE A1 (Assigned)

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**About Acuité Ratings & Research:**

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