

Indushankar Chini Udhyog Limited: Ratings reaffirmed

December 18, 2023

Summary of rating action

Instrument* (Amount in NPR million)	Previous Rated Amount	Current Rated Amount	Rating Action
Long-term; Fund-based Limits	410.00	401.18	[ICRANP] LBB-; reaffirmed
Short-term; Fund-based Limits	1,337.50	1,480.00	[ICRANP] A4; reaffirmed
Short-term; Non-fund Based Limits	10.00	60.00	[ICRANP] A4; reaffirmed
Total	1,757.50	1,941.18	

* Instrument details are provided in [Annexure-1](#).

Rating action

ICRA Nepal has reaffirmed the long-term rating of [ICRANP] LBB- (pronounced ICRA NP L double B minus) assigned to the long-term limits of Indushankar Chini Udhyog Limited (ICUL or the company). ICRA Nepal has also reaffirmed the short-term rating of [ICRANP] A4 (pronounced ICRA NP A four) assigned to the company's short-term loan limits.

Rationale

The rating reaffirmation takes comfort from the company's improving revenue profile supported by better sugar production coupled with hardening of sugar prices. Improved cane availability amid steady recovery rate has helped in better sugar production in recent years. The growing domestic sugar consumption, inadequate production in Nepal and high duty protection accorded to the domestic sugar mills (through 30% import duty) remains a positive for incremental sugar realization. The ratings also derive comfort from the revenue diversification achieved through operation of distillery unit (contributing ~13% of total revenue in FY2023) supporting the operational profitability. Moreover, the rating continues to derive comfort from ICUL's long track record (operating since 1984), its strong promoter group and established sales channel.

However, the ratings continue to remain constrained by the company's high gearing and resulting moderation in coverage indicators amid the rise in borrowing cost in FY2023. The company has reported an increase in working capital intensity which has been financed by working capital loans resulting in elevated gearing levels. The rating also takes note of the increasing minimum support price (MSP) of cane which could have an impact on the margins, especially during the period of weak sugar prices. The rise in MSP from NPR 520 per quintal in crushing year 2021 (FY2022) to NPR 540 in crushing year 2022 (FY2023) (both prices excluding NPR 70 per quintal of government subsidy to farmers); can also be partly attributed to ICUL's operating margin in FY2023, as the selling price of sugar didn't rise commensurate with the rising MSP. The company also remains vulnerable to volatility in global sugar prices and/or reduction in duty protection from the GoN, as it could affect the sales realization and profit margins for the company. The ratings also remain constrained by ICUL's dependence on milling operations for a major chunk of revenue, although some diversification is offered post the operation of the distillery and co-gen.

Key rating drivers

Credit strengths

Long track record and experienced promoters– Incorporated in 1984, ICUL is among the established players in the domestic sugar industry. The company is involved in the production of white plantation sugar. The promoter's experience in agro-based businesses, and adequate financial strength also remains a comfort for the assigned rating.

Revenue diversification offered by distillery unit – The company's revenue profile achieved diversification following the commencement of distillery and cogeneration unit from FY2021 and FY2022 respectively. The distillery operation contributed ~13% of total revenue in FY2023 (~12% in FY2022), while the contribution from Cogen unit remains relatively nominal. The revenue diversification also remains a positive for the stability of the operating profit margins.

Duty protection comforts demand outlook – The GoN increased the duty tariff on imported sugar significantly from the FY2018 level, following the import-led crisis that affected the domestic sugar mills. Additionally, the GoN also introduced temporary quantitative restriction on sugar imports in FY2019, which reaffirms the Government’s stance of consistent policy intervention in favour of the industry. At present, the import of sugar is subjected to ~30% custom duty. Since domestic sugar production trails behind the demand, higher duty protection remains a positive for the offtake of the domestic production.

Credit challenges

High gearing and moderate financial profile– ICUL’s financial profile continues to remain moderate because of high gearing, because of increased working capital loan to finance rising working capital cycle in last two years. Amid high interest rate, this has led to suppressed debt coverage indicators. The gearing has increased to 4.5 times as of mid-July 2023 (including promoter loans) while the increased interest expenses has stretched the interest coverage to 1.9 times and DSCR to 1.5 times for FY2023 (2.6 times and 1.8 times respectively for FY2022). Further, the liquidity position of the company also remains stretched with limited head room in drawing power on the working capital loans.

Raw material availability and price volatility – ICUL entirely depends upon the sugarcane cultivated by the local farmers for its raw materials requirement. The availability of the raw materials during the crushing season is paramount for the company’s operation and survival. The decline in cane availability till FY2021 resulted in the shortening of the crushing period with lower capacity utilization, translating into the lower revenues for the sugar millers of the region. Although cane availability has improved in FY2022 and FY2023, its long-term sustainability will remain a key monitorable. Moreover, the MSP of cane fixed by the GoN, will also remain monitorable, given its direct impact on the profitability of the company.

Competition from imports and concentrated revenue profile – The sales price of sugar by the domestic millers are broadly guided by the landed cost of imported sugar. The large-scale advantage available with big players in the exporting nations (mainly India) and the consequent low cost of production partly offset the high customs duty in importing nations like Nepal. Therefore, over the near term, import will remain a major threat for domestic sugar producers. The continuation of a high import tariff and/or other import barriers will remain a key rating sensitivity.

ICUL’s revenue profile remains concentrated as its revenue remains driven by sugar sales. Although revenue from distillery unit has offered some revenue diversification, sugar (86% of total sales in both FY2022 and FY2023) is likely to remain the major revenue driver for the company over the medium term.

Industry cyclicity - As sugarcane is an agro-commodity, it is exposed to industry cyclicity (for example- years of weak monsoon resulting in a sharp correction of production) and agro-climatic risks like damage from pests, untimely precipitation, weather conditions etc. which affect the cane recovery rate. This also remains a rating concern.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

Link to previous detailed rating rationale:

[Bank Loan Rating Surveillance – September 27, 2022](#)

About the company

Indushankar Chini Udhyog Limited (ICUL) was incorporated in 1984 as a public limited company. It operates one of the large domestic sugar mills with installed sugarcane crushing capacity of 4,500 TCD (tonne crushed per day). ICUL manufactures and sells the white plantation sugar under the brand name “RajHans”. The company’s distribution channel comprises wholesale dealers who then pass on the sugar to retail traders and finally to the consumers.

ICUL is a family-owned business wherein Mr. Rajesh Kumar Kedia and his family members hold the entire equity stake. The company’s sugar mill is located in the Hariwan city of Sarlahi District in South-Eastern Nepal. The sugarcane required for the manufacturing process is procured mostly from the local farmers of Sarlahi and adjoining districts of Southeastern

Nepal. ICUL also has an operational 30-KLPD¹ distillery unit (since FY2020) and 3-MW co-generation unit (since FY2021).

Key financial indicators

	FY2020	FY2021	FY2022	FY2023
	(Audited)	(Audited)	(Audited)	(Provisional)
Operating Income-OI (NPR million)	3,138	1,574	1,597	2,004
OPBDITA ² /OI (%)	10.1%	11.1%	13.8%	12.5%
Total Debt/Tangible Net Worth (TNW; times)	3.7	3.2	3.73	4.5
Total Outside Liabilities/TNW (times)	4.2	3.6	3.9	4.8
Total Debt/OPBDITA (times)	2.8	4.7	5.2	5.4
Interest Coverage (times)	3.0	2.8	2.6	1.9
DSCR ³ (times)	1.7	1.2	1.8	1.5
NWC ⁴ /OI (%)	12%	23%	48%	51%
Current Ratio (times)	0.97	1.04	1.08	1.17

Source: Company data

Annexure-1: Instrument Details

Instrument (Amount in NPR million)	Previous Rated Limit	Current Rated Limit	Rating Action
Long-term, fund based			
Term loan	410.00	401.18	[ICRANP] LBB-; reaffirmed
Total long term, fund based (A)	410.0	401.18	
Short-Term Loans			
Fund based (OD/TR/DL/STL)	1,337.5	1,480	[ICRANP] A4; reaffirmed
Non-fund based (LC)	(50.0)	(50.0)	[ICRANP] A4; reaffirmed
Non-fund based (BG/PB/APG)	(20.0)	(20.0)	[ICRANP] A4; reaffirmed
Non-fund based (BG)	10.0	60.0	[ICRANP] A4; reaffirmed
Total short term, fund/non-fund based (B)	1,347.5	1,540	
Grand total (A+B)	1,757.5	1,941.18	

Analyst Contacts:

Mr. Sailesh Subedi, (Tel No. +977-1-4519910/20)

sailesh@icranepal.com

Mr. Bipin Timilsina, (Tel No. +977-1-4519910/20)

bipin@icranepal.com

Relationship Contacts:

Ms. Barsha Shrestha, (Tel No. +977-1-4519910/20)

barsha@icranepal.com

¹ Kilo Litre per day

² Operating profit before depreciation, interest, tax and amortization

³ Debt service coverage ratio

⁴ Net working capital intensity

About ICRA Nepal Limited:

ICRA Nepal Limited, the first Credit Rating Agency of Nepal, is a subsidiary of ICRA Limited (ICRA) of India. It was licensed by the Securities Board of Nepal (SEBON) on October 3, 2012. ICRA Nepal is supported by ICRA Limited through a technical support services agreement, which envisages ICRA helping ICRA Nepal in areas such as rating process and methodologies, analytical software, research, training, technical and analytical skill augmentation.

Our parent company, ICRA Limited, was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency. Today, ICRA and its subsidiaries together form the ICRA Group of Companies.

For more information, visit www.icranepal.com

ICRA Nepal Limited,

Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu, Nepal.

Phone: +977 1 4519910/20

Email: info@icranepal.com

Web: www.icranepal.com

All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA Nepal.

ICRA Nepal ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. The ICRA Nepal ratings are subject to a process of surveillance which may lead to a revision in ratings. Please visit our website (www.icranepal.com) or contact ICRA Nepal office for the latest information on ICRA Nepal ratings outstanding. All information contained herein has been obtained by ICRA Nepal from sources believed by it to be accurate and reliable. Although reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA Nepal in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. All information contained herein must be construed solely as statements of opinion and ICRA Nepal shall not be liable for any losses incurred by users from any use of this publication or its contents