

India Ratings Places Shree Renuka Sugars on RWN

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India Ratings and Research (Ind-Ra) has placed Shree Renuka Sugars Limited's (SRSL) Long-Term Issuer Rating of 'IND BBB+' on Rating Watch Negative (RWN). The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating/Rating Watch	Rating Action
Non-convertible debentures (NCDs)#				INR2,500	IND BBB+/RWN	Placed on RWN
NCDs#				INR5,521	IND BBB+/RWN	Assigned; placed on RWN
Term loan			31 March 2029	INR11,835	IND BBB+/RWN	Assigned; placed on RWN
Proposed term loan	-	-	-	INR3,000	Provisional IND BBB+/RWN	Assigned; placed on RWN
Fund based limit	-	-	-	INR1,810	IND BBB+/RWN	Assigned; placed on RWN
Short-term loan	-	-	-	INR4,000	IND A2+/RWN	Assigned; placed on RWN
Non-fund-based limit	-	-	-	INR11,242	IND A2+/RWN	Assigned; placed on RWN

#Details are given in annexure

The RWN reflects the persisting uncertainty over the timeframe of resolution of the issue of reclassification of SRSL's account as a non-performing asset (NPA) by its lenders; although this has not had an immediate impact on the company, it could potentially affect SRSL's financial flexibility if unresolved for a longer period.

The re-classification by some of the banks in March 2019 has not impacted the company's liquidity so far, as it continues to receive support from its parent Wilmar Group (Wilmar), (ultimate holding company: Wilmar International Limited) (FY19: INR9.9 billion), in line with Ind-Ra's expectations. However, if the issue is not resolved, Ind-Ra believes it could eventually impact SRSL's financial flexibility due to the company's impaired ability to tie-up additional external funding, as most of its existing lenders have classified the account as NPA in the past five months. SRSL has been servicing all its debt obligations on due dates since the restructuring was implemented on 31 March 2018 and Ind-Ra derives comfort from the assurance given by Wilmar's management's that SRSL remains a strategically important entity for them, and that they would continue to offer financial and operational support to the company in the future.

According to SRSL's lenders a communication was received from the Reserve Bank of India (RBI) with regard to a change in ownership as considered in the resolution plan, suggesting that the former should give consequential effect of the disqualification of the acquirer, as Wilmar was technically a co-promoter prior to the restructuring.

As per the prudential framework for the resolution of stressed assets released by the RBI in June 2019, a restructured account can be upgraded to standard only after at least 10% of the outstanding principal debt as per the resolution plan has been paid and one year has passed from the commencement of the first payment of interest or principal (whichever is later) on the credit facility with the longest period of moratorium. While discussions are on to resolve the asset classification issue, clarity on the outcome is awaited and remains a key monitorable.

Analytical Approach: Ind-Ra continues to apply the top-down approach according to its Parent Subsidiary Linkage Criteria to arrive at the ratings, given the strong legal, operational and strategic linkages between SRSL and Wilmar.

KEY RATING DRIVERS

Continued Demonstration of Support from Strong Parent: Wilmar continued to provide tangible support to SRSL in the form of trade advances, extended credit periods for raw sugar purchase (total outstanding dues at 1QEFY20: INR22.5 billion; FYE19: INR15.6 billion; FYE18: INR5.7 billion) and a corporate guarantee for additional funding of INR4 billion availed by SRSL (in addition to the limits of INR27.1 billion guaranteed as part of the restructuring agreement). Wilmar had been a strategic investor in the company till 2017, with 27.24% shareholding. In FY18, Wilmar infused around INR14 billion in SRSL to increase its stake to 58.34%.

Wilmar is the largest branded consumer pack oils, specialty fats and oleochemicals producer and edible oils refiner in the world. It is also the largest producer of consumer pack edible oils and a leading sugar miller and refiner in India. It has over 500 manufacturing plants and an extensive distribution network covering over 50 countries. Wilmar reported a consolidated revenue of USD44.5 billion in 2018 (2017: USD43.8 billion), with operating margins of 6.6% (2017: 6%). Wilmar's net debt remained high at USD13.5 billion in 2018 (2017: USD12.6 billion), but majority of it was contributed by working capital borrowings. Its pro forma net leverage stood at 4.6x in 2018 (2017: 4.8x), while the EBITDA net interest coverage was 11.6x (14.5x).

Wilmar's financial flexibility is strengthened by the presence of a large promoter - Kuok Group, a leading corporate group in Asia - and a strategic stakeholder Archer Daniels Midland (Fitch Ratings Ltd; Issuer Default Rating: 'A'/Stable), which is one of the largest agro commodity companies in the world and holds around 25% stake in Wilmar. Wilmar is listed on the Singapore stock exchange.

Strong Linkages between SRSL and Wilmar: The legal linkages between SRSL and Wilmar are underpinned by the corporate guarantee extended by Wilmar towards the majority (FYE19: around 73%) of SRSL's bank facilities. Additionally, the non-payment of any redemption instalment of NCDs issued to lenders as part of the restructuring exercise (around 6% of the total facilities at FYE19) would enable the lenders to invoke the corporate guarantee on the term loan and working capital facilities based on the cross default provision.

The guarantees are post-default in nature, with a cure period of 20 days allowed to SRSL before the guarantee can be invoked. However, based on its discussions with Wilmar's management, Ind-Ra believes that Wilmar would continue to provide any required support to SRSL for the timely servicing of debt obligations.

The operational ties between the entities are driven by the overlap in SRSL and Wilmar's businesses, as sugar is one of the three key business segments of Wilmar (tropical oils and grains being the other two), with a total sugar milling capacity of 27 million tonnes (mnt) and refining capacity of 3mnt, spread across India, Australia, Indonesia, Myanmar, New Zealand and Morocco. SRSL procures most of its raw sugar requirement for the refining business (which accounts for around 60-65% of its revenue) from Wilmar at competitive prices and credit terms. Wilmar has full management control of SRSL, with the latter's board including the group CFO of Wilmar and its group sugar head.

Strategic linkages emanate from the fact that Wilmar has been increasing its focus on sugar with a view to widen its consumer products portfolio and increase its wallet share in populated markets. The acquisition of stake in SRSL has given Wilmar a leading presence in India, which is the currently world's largest producer and consumer of sugar.

SRSL's Credit Profile Remains Stretched despite Improvement in FY19: SRSL's revenue declined by 27% yoy to INR42.8 billion in FY19 as a result of lower volumes and realisations in the sugar segment. The company's EBITDA turned positive at INR3.4 billion in FY19 (FY18: negative INR1 billion) as performance improved across all three segments- sugar, distillery and cogeneration- on the back of better operating efficiencies and measures taken by the government to support prices. The EBITDA margin improved to 8% in FY19 (FY18: EBITDA loss), and is likely to improve further in FY20, as sugar prices increased to INR33/kg in 1HFY20 from an average of INR30-31 per kg in FY19, and could rise further, albeit marginally, in 2HFY20. International prices could also witness some improvement in FY20, as the market is likely to swing to a marginal production deficit from a marginal surplus scenario.

In the distillery division, the realisations and profitability are likely to improve on account of a strong order book and increase in procurement prices of OMCs as the government has announced a 5% increase in the prices of ethanol made from C-molasses and an 11% increase in the prices of ethanol made from B-heavy molasses. Sugarcane costs are likely to remain flat, as the government has kept the fair and remunerative price unchanged for SS2019-20 and a likely surplus production will prevent cane prices from exceeding the FRP.

SRSL's EBITDA interest coverage (excluding non-cash interest expense) remained low at 0.8x in FY19, although though it improved as compared to the previous year due to the improvement in EBITDA. The coverage is likely to improve in FY20 on the back of higher EBITDA and lower interest expense. However, the company might continue to need support from Wilmar in the near term. The company's net adjusted leverage improved to 7.8x in FY19.

The average utilisation of fund-based working capital limits was around 60%-70% during the 12 months ended June 2019. The cash flow from operations turned positive at INR0.6 billion in FY19 due to the improvement in the EBITDA.

Divestment from Brazilian Operations: SRSL's subsidiary, Shree Renuka Global Ventures Limited (SRGVL, holding company of SRSL's Brazil operations), entered into a binding term sheet with an investor in August 2019 to divest its stake in Brazilian operations and reduce it to 19%.

Oversupply Scenario to Continue in Sugar Market: Sugar production is likely to hit a record level of 33mnt in SS2018-19, surpassing the previous record high of 32.3mnt in SS2017-18. The total exports in SS2018-19 are likely to around 3-3.5mnt against the MIEQ target of 5mnt, given the weak global sugar prices. While production could drop to 28-29mnt in SS2019-20, it is likely to exceed sugar demand (26.5mnt, 2-3% yoy growth). Besides, the opening stock is likely to be at a record high of 14-14.5mnt (2018-19: 10.7 million tonnes) versus the normative requirement of 4.5-5.0mnt. This would give rise to the need to export at least 6-7mnt of sugar in SS19-20 to restore balance in the market, which is unlikely in view of the global oversupply.

Continued Government Support Positive for Sector: The government continued to support the sector by increasing the MSP to INR31 per kg in February 2019 (from INR29/kg set in June 2018), increasing the buffer stock to 4mnt in July 2019 (from 3mnt), providing soft loans to the sector, and incentivising ethanol. The government also created a regulated monthly release mechanism in June 2018 to limit the quantity of sugar sold in the domestic market. However, while the reduction in sugar availability in the market has provided support to prices, it has also pushed up stocks with mills, impacting the liquidity position of companies. The government has also provided subsidy on the exports of sugar.

RATING SENSITIVITIES

The RWN indicates that the ratings may be affirmed or downgraded upon resolution. Ind-Ra expects to resolve the RWN in the next three months based on its assessment of the financial flexibility of SRSL.

COMPANY PROFILE

SRSL is one of the leading sugar manufacturers in India with a track record of over 25 years. Its operations are integrated, encompassing crushing of cane, refining of raw sugar, ethanol production and power generation.

FINANCIAL SUMMARY

Particulars	FY19	FY18
Net revenue (INR billion)	42.8	58.5
EBITDA margin (%)	8	-1.7
EBITDAR interest coverage (x)	0.8	-0.2
Net adjusted leverage (x)	7.8	-23.5

Source: SRSL, Ind-Ra

RATING HISTORY

Instrument Type	Current Rating/Rating Watch			Historical Rating/Outlook		
	Rating Type	Rated Limits (million)	Rating	24 September 2018	9 June 2017	1 April 2016
Issuer rating	Long-term	-	IND BBB+/RWN	IND BBB+/Stable	IND D	IND D
NCDs	Long-term	INR8,021	IND BBB+/RWN	IND BBB+/Stable	IND D	IND D
Term loan	Long-term	INR14,835	IND BBB+/RWN	-	-	-
Fund-based limit	Long-term	INR1,810	IND BBB+/RWN	-	-	-
Short-term loan	Short-term	INR4,000	IND A2+/RWN	-	-	-
Non-fund-based limit	Short-term	INR11,242	IND A2+/RWN	-	-	-

ANNEXURE

Instrument Type	ISIN	Date of Issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating/Rating Watch
NCDs	INE087H07060	3 April 2012	11.7	31 March 2024	INR1,500	IND BBB+/RWN
NCDs	INE087H07078	24 December 2012	11.3	31 March 2024	INR1,000	IND BBB+/RWN
NCDs	INE087H07086	9 March 2018	0.01	31 March 2027	INR5,521	IND BBB+/RWN
Total NCDs					INR8,021	

COMPLEXITY LEVEL OF INSTRUMENTS

For details on the complexity levels of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

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Applicable Criteria

[Corporate Rating Methodology](#)

[Parent and Subsidiary Rating Linkage](#)

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