

## Himalaya Sugar Mills Limited

### Ratings

Facilities/Instrument	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	947.69	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	1,500.00	CARE-NP A4 [A Four]	Assigned
<b>Total Facilities</b>	<b>2,447.69</b> <b>(Two Thousand Four Hundred Forty- Seven Million and Six Hundred Ninety Thousand Only)</b>		

\* Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of Himalaya Sugar Mills Limited (HSML).

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of HSML are constrained by its leveraged capital structure with modest debt service coverage indicators amid declining financial performance of the company during FY23 (Unaudited; FY refers to the twelve-month period ending mid-July). The ratings also factor in concentrated customer profile though reputed and working capital intensive nature of business marked by high inventory holding period, susceptibility to raw materials availability. The ratings also factor in price fluctuation of seasonal agro products, competition from domestic as well as international market players and exposure to volatile interest rates.

The ratings, however, derive strengths from established track record with experienced and resourceful promoter group. The ratings also factor in locational advantage of the plant site for easy accessibility of raw materials, stable demand outlook of sugar industry over the medium term and government support for sugarcane production.

*Going forward, the ability of the company to manage growth in operations while maintaining the profit margins and rationalization of its debt through efficient working capital management would be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

##### Leveraged capital structure with modest debt service coverage indicators

The capital structure of the company stood leveraged with overall gearing of 3.08x at the end of FY23, deteriorated from 2.10x at the end of FY22 on account of decline in tangible net worth of the company amid accumulated losses coupled with increase in short term loans to fund working capital requirements. Debt service coverage indicators of HSML as indicated by interest coverage ratio stood weak at 0.52x in FY23, which declined from 2.68x in FY22 on account of decline in PBILDT coupled with increased interest expenses. Total debt/ GCA deteriorated to negative 16.73x during FY23 from 4.80x during FY22 owing to negative cash accruals incurred by the company during FY23. The prospects of an improved financial risk profile in FY24 will hinge on HSML's ability to achieve turnaround of its operations as envisaged, which will remain a key monitorable aspect.

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and in other CRNL publications.

**Declining financial performance in FY23, albeit substantial advance from the customers provide relief**

HSML generates its income majorly from sales of double refined (sulphur free) sugar. The company's total operating income (TOI) had been growing on y-o-y basis at CAGR of ~28% over the three-year period ended FY22 (FY20-FY22). However, during FY23 the company reported substantial decline in its TOI by ~67% to Rs. 399 Mn. This decline was majorly due to delays in offtake of a substantial order from a major customer during the year. The company also received the majority of the advances against the said order. Despite the decline in TOI, PBILDT margin remained steady at around ~21% during FY23. Furthermore, as majority of the payment from customers is as advance, which provides ample liquidity cover for the company. Order offtake pending from FY23 are expected to be completed in FY24, indicating a possible rebound in HSML's operations in FY24. However, with the challenge in raw material availability during crushing period, the company's ability to achieve operating income at envisaged levels will remain critical from credit perspective.

**Susceptibility to raw material availability and price fluctuation of seasonal agro products**

The major raw material for HSML is sugarcane which are procured from the local farmers. Prices are highly volatile in nature on account of direct dependency on the sugarcane crop and its yield. Sugar industry is susceptible to agro climatic risks including pest & diseases, more specifically, the monsoons, temperature and soil conditions, demand-supply dynamics, etc. that influence various operational parameters for a sugar entity, such as the crushing period and sugar recovery levels. Lower output of sugarcane will have an adverse impact on the revenue generation of the entities. Since, the company is only manufacturer in its region and raw materials availability will not be the challenge as long as adequate cultivation is made by the farmers. Furthermore, the price of sugarcane is determined by the government, which also includes Government subsidies for cane farmers, its ability to provide enough subsidies to farmers for supporting the industry will also remain key monitorable aspect.

**Working capital intensive nature of business marked by high inventory holding**

The operations of the company are working capital intensive in nature marked by high inventory holding period. HSML is required to keep adequate inventory for smooth operations and fund the debtors leading to reliance on bank borrowings to meet working capital requirements. Being seasonal agro product, the company generally keeps inventory for around six months. However, due to unexecuted order at the end of FY23, average inventory turnover was substantially high. Consequently, total average operating cycle of the company was high in FY23 which was 116 days during FY22. The overall working capital requirements are met through bank borrowings as well as advance received from the customers. The average utilization of fund-based working capital limits remains moderate at 60% against sanctioned limits.

**Exposure to volatile interest rate**

Sustained requirement for short-term working capital borrowings has led to relatively high interest outgo for HSML. The company's interest rates are based on a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. Higher interest rates than envisaged could result in squeezed margins of the company. Hence, funding taken by the company is exposed to volatile interest rate.

## Key Rating Strengths

### Established track record with experienced and resourceful promoter group

HSML is a joint venture of two groups of Nepal i.e. MS Group and SB Group with the strong presence in diversified fields. The company is managed under the overall guidance of the company's board of directors (BOD) who possess wide experience in different business sectors. The company has three directors in its board chaired by Mr. Sumit Kumar Agarwal who has more than three decades of cross-sector experience. He is also chairman in Bhagawati Steel Industries Private Limited [CARE-NP BBB- /A3], Everest Hospitality and Hotel Limited [CARE-NP BBB-/A3]. Mr. Kaushal Kishor Sarraff, Vice Chairman, has work experience over two decades in manufacturing and trading industries. Mr. Suresh Kumar Sarraff, executive directors, has work experience of 15 years in related field. He is also chairman of SB group. BODs are further supported by an experienced team across various functions/ departments.

### Locational advantage

The plant site is located at Siraha district, which is one of the sugarcane producing area in Nepal. The company derives comfort from its strategic location in terms of easy accessibility of raw materials owing to established suppliers' presence in the same location. It is also connected to potential market leading to less transportation cost. Furthermore, the region has moderate recovery rate on account of favourable climatic conditions for growing sugarcane. Sustained availability of sugarcane for crushing remains crucial for sugar production.

### Stable demand outlook of sugar industry over the medium term

Consumption of sugar has been growing over the years with its applicability for household consumption as well as for industrial purpose. Since, there are few players like HSML in Nepal producing sulphur free sugar, demand for the same remains on higher side for industrial consumption majorly in beverage industries. According to Agriculture Ministry, annual requirement for sugar stands at 260,000 tons based on consumption. The outlook for the sugar industry over the medium term remains stable because of key demand drivers leading to industrial growth and industrial outputs.

### Government support for sugarcane production

Sugar industry is one of the potential industries in Nepal as the major raw materials for sugar production are locally available. With favourable topography and climate, terai region of Nepal is suitable for sugarcane farming. Sugarcane is one of the cash crops of Nepal. Despite its potentiality, total local production is not sufficient to fulfill demand. Government has set higher import tariff on sugar import in order to support local producers. Government put import tariff on sugar and sugar confectionery at 30% from FY24. To support farmers, the government also provides a subsidy of Rs 70 per quintal of sugarcane. With the government prioritizing sugarcane farming and sugar production in the country, the prospect of this sector looks encouraging over the medium-term.

### About the Company

Himalaya Sugar Mills Limited (HSML) is a public limited company incorporated on August 17, 2010 for manufacturing of sugar having plant at Chandraayodhapur, Siraha, Nepal. The company has a total installed capacity of 2,500 Ton Crushing Per Day (TCD) for production of a doubled refined sugar (Sulphur Free). Besides sugar, the company also sells molasses and bagasse.

## Financial Performance

(Rs. Million)

Particulars	FY21 (A)	FY22 (A)	FY23 (UA)
Income from Operations	896	1,239	399
PBILDT Margin (%)	20.35	25.02	20.91
Overall Gearing (times)	3.34	2.10	3.08
Interest coverage (times)	1.55	2.68	0.52
Current Ratio (times)	0.78	1.41	0.95
Total Debt/Gross Cash Accruals (times)	19.28	4.80	Negative

A: Audited, UA: Unaudited

## Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	947.69	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limit	1,500.00	CARE-NP A4 [A Four]
<b>Total</b>		<b>2,447.69</b>	

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