

Muted sugar prices drag profit; ethanol story intact...

About the stock: Dwarikesh Sugar (DSL) is a UP based sugar company with sugar crushing capacity of 21500 TCD, distillery capacity of 337.5 KLD & co-generation capacity of 91 MW. It has commissioned a new distillery at its Dwarikesh Dham unit in June-2022 with capacity of 175 KLD and investment of ₹ 230 crore.

- The company would be able to increase distillery volumes to 11 crore litre in FY24 from 5.6 crore litre in FY22

Q2FY23 Results: DSL witnessed dismal results with a sharp decline in profits

- Sales were up 6.8% YoY, driven by 40.8% growth in distillery sales
- EBITDA was at ₹ 28.3 crore, down 62.1% YoY, with margins at 5.2%
- Consequent PAT was at ₹ 7.8 crore (down 80.2% YoY)

What should investors do? DSL's share price has gone up 23% in the last five years (from ₹ 72 in October 2017 to ₹ 89 in October 2022).

- We expect 44.6% CAGR in distillery sales, which would drive earnings growth with CAGR of 27.7% during FY22-24E for the company
- We maintain our **BUY** rating on the stock

Target Price and Valuation: We value the stock at ₹ 135, valuing the business at 10x FY24 PE.

Key triggers for future price performance:

- Distillery revenue to grow at 44.6% CAGR in FY22-24E with 2x increase in ethanol volumes and 6% increase in distillery realisation led by higher proportion of B-heavy & sugarcane juice ethanol
- With increasing profitability & reduction in sugar inventory, the company would be able to generate cumulative ₹ 373 crore free cash flows in the next two years. It would completely de-leverage the balance sheet
- With the continuous increase in sugar production, the ethanol blending programme can be extended beyond 20% blending with the introduction of flex fuel vehicles. This would result in sustainable growth in ethanol volumes beyond 2025-26

Alternate Stock Idea: We like Dalmia Bharat Sugar in our sugar coverage.

- It is fastest in utilising B-heavy & sugarcane juice to produce ethanol. Distillery volumes to grow 1.8x to 22 crore litre by FY24. The company is aggressively exporting sugar & utilising higher global white sugar prices
- We value the stock at ₹ 490/share with a BUY recommendation



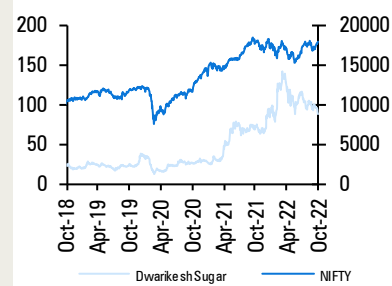
Particulars

Particulars (₹ crore)	Amount
Market Capitalization	1,672.1
Total Debt (FY22)	520.7
Cash and Investments (FY22)	38.6
EV	2,154.2
52 week H/L (₹)	148 / 63
Equity capital	18.8
Face value (₹)	1.0

Shareholding pattern

(in %)	Dec-21	Mar-22	Jun-22	Sep-22
Promoter	42.1	42.1	42.1	42.1
FII	4.1	7.7	7.2	7.0
DII	4.0	3.3	3.3	3.3
Others	49.8	47.0	47.5	47.7

Price Chart



Recent event & key risks

- Revision of wages with retrospective effect led to one-time payment of ₹ 9 crore in Q2
- Key Risk:** (i) Fall in global sugar prices may impact sugar exports (ii) Any dip in recovery rate due to weather disruptions

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Key Financial Summary

Key Financials	FY20	FY21	FY22	5 Year CAGR (FY17-22)	FY23E	FY24E	CAGR (FY22-24E)
Total Operating Income	1336.2	1838.9	1974.1	10.6%	2170.6	2330.1	8.6%
EBITDA	136.1	201.3	290.8	1.2%	285.1	410.9	18.9%
EBITDA Margin %	10.2	10.9	14.7		13.1	17.6	
Net Profit	73.5	91.5	155.2	-0.1%	162.0	253.0	27.7%
EPS (₹)	3.9	4.9	8.2		8.6	13.4	27.7%
P/E	22.7	18.3	10.8		10.3	6.6	
RoNW %	15.2	15.8	23.1		19.4	24.7	
RoCE (%)	9.0	14.4	20.6		18.5	28.5	

Source: Company, ICICI Direct Research

Key takeaways of recent quarter

Q2FY23 Results: Subdued sugar prices & one-offs adversely impact profitability

- DSL saw revenue growth of 6.8% to ₹ 540.1 crore led by 40.8% jump in distillery sales. Ethanol volumes grew 33.5% to 2.2 crore litre with 2.6% jump in average distillery realisation to ₹ 59.1/litre. The company has commissioned new 175 KLD distillery in June 2022, which has taken its annual distillery capacity to 337.5 KLPD (11 crore litre per annum)
- Sugar sales dipped 1.2% to ₹ 403.4 crore on the back of 4.8% decline in sugar volumes and mere 3.5% uptick in sugar realisation. The company sold 1.14 lakh tonnes of sugar with average realisation at ₹ 34.9/kg
- Power volumes declined 14.9% to 2.8 crore units with average tariff moved up from ₹ 3.2/unit to ₹ 3.3/unit
- The company witnessed a sharp decline in gross margin mainly on account of increase in sugarcane prices and lower recovery rate in 2021-22 sugar season. We estimate ₹ 3/kg increase in cost of production (₹ 2/kg due to sugarcane price increase & ₹ 1/kg due to lower recovery rate)
- Employee spends increased 65% to ₹ 33.5 crore, which includes one-time deferred wage payment of ₹ 8.9 crore. The higher cost of production & increase in employee spends led to 62.1% de-growth in operating profit during the quarter
- The company was holding 18,000 tonnes of sugar as on September 2022 valued at ₹ 34.9/kg. DSL started crushing operations in two of its plant on October 28, 2022 and will start crushing in the third plant from November 8, 2022 onwards
- Interest cost declined 28% to ₹ 6.2 crore with the reduction in debt. Net profit de-grew 80.2% to ₹ 7.8 crore. Total debt for the company declined from ₹ 520.7 crore to ₹ 306.9 crore. Cash flow from operations in H1FY23 was ₹ 694.3 crore
- The levy molasses quota increased from 18% to 20% in 2021-22 in Uttar Pradesh (UP), which resulted in additional supply of 3400 tonnes of molasses to the liquor companies. The company lost ₹ 6 crore of sales due to the change in levy molasses
- In the newly commissioned distillery at Dwarikesh Dham, the company experienced lower ethanol output due to some teething issues. This resulted in opportunity loss of ₹ 5-6 crore
- The company has contracted for 50,000 tonnes of raw sugar exports at the ex-factory price of ₹ 34/kg. This would be exported during Q3FY23
- DSL is expected to crush 2-3% higher sugarcane during 2022-23 season, which would be close to 39 lakh tonnes. Moreover, gross sugar recovery is expected to improve compared to last year (low recovery in 2021-22 due to unseasonal rains)
- With the commissioning of the new distillery, the company would be able to sacrifice 30% sugar in 2022-23 season. Sugar production is expected to be 3.0-3.5 lakh tonnes considering 2-3% increase sugarcane crushing & expected improvement in sugar recovery
- The company is expected to produce 11 crore litre of ethanol in 2022-23 season. Out of this, 6 crore would be produced from sugarcane juice and 5 crore would be produced from B-heavy molasses
- The company is considering capex ranging from ₹ 100-150 crore for adding sugarcane crushing, ethanol & sugar refining capacity. However, final decision of capex would be made by January 2023

- Gross sugar production in the country is expected to be close to 41 million tonnes. Out of this, 4.5 million tonnes of equivalent sugar would be diverted towards ethanol. The industry is required to export close to 8-9 million tonnes of sugar during 2022-23 season
- With the restriction on sugar exports under OGL, quota based exports would be allowed during the sugar season. The industry expects 6 million tonnes of initial export quotas to be announced in November followed by 2-3 million tonnes in January-February 2023

Exhibit 1: Peer Comparison

Sector / Company	CMP		TP	Rating	M Cap (₹ Cr)	EPS growth (%)				EBITDA margins (%)				PE (x)				P/B (x)				RoCE (%)			
	(₹)	(₹)				FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E
Balrampur Chini (BALCHI)	317	515	Buy	6647	-3.2	-0.3	20.1	51.2	14.8	14.4	16.5	18.6	14.8	14.9	12.4	8.2	2.7	2.6	2.3	2.1	16.4	15.3	16.0	23.1	
Dalmia Bharat Sugar (DALSUG)	317	490	Buy	2567	39.9	10.0	15.8	16.5	17.6	14.8	18.0	19.0	10.2	9.2	8.0	6.8	1.3	1.2	1.2	1.0	13.3	12.3	15.5	17.7	
Triveni Engineering (TRIENG)	252	355	Buy	6103	-9.9	43.9	16.2	24.5	11.9	14.8	14.9	17.1	22.6	15.7	13.5	10.8	4.3	3.5	2.0	1.8	19.4	15.8	18.6	20.6	
Dwarikesh sugar (DWASUG)	89	135	Buy	1672	24.5	69.6	4.4	56.1	10.9	14.7	13.1	17.6	18.3	10.8	10.3	6.6	2.9	2.5	2.0	1.6	14.4	20.6	18.5	28.5	

Source: Company, ICICI Direct Research

Domestic sugar realisation has remained stable at ~₹ 35/kg in the last one year. However, cost of production has increased by ₹ 3/kg on the back of higher sugarcane costs & lower recovery rate in 2021-22 season. We believe domestic sugar prices would remain stable at ₹ 34-36/ kg given expected higher sugar production even in 2022-23 season. However, we believe cost of production will go down by ₹ 1/kg with the expectation of improvement in recovery rate in 2022-23 season. Moreover, expected increase in ethanol prices by ₹ 1-1.5/litre and higher ethanol volume would aid earnings growth in FY23 & FY24. We believe the Indian sugar industry needs to export 8-9 million tonnes of sugar in 2022-23 season to keep industry wide closing inventory at 6 million tonnes by September 2023. We also believe sugar mills exporting refined sugar would benefit from higher global white sugar prices. Though Dwarikesh may not benefit from higher global white sugar prices given limitation of refined sugar capacity but higher distillery volumes would boost profitability going forward. We maintain our **BUY** rating with a revised target price of ₹ 135/share (earlier ₹ 150).

Exhibit 2: Variance Analysis

	Q2FY23	Q2FY22	YoY (%)	Q1FY23	QoQ (%)	Comments
Total Operating Income	540.1	505.5	6.8	1,974.1	-72.6	Net sales witnessed growth of 6.8% led by 40.8% jump in distillery sales
Other Operating Income	0.0	0.0	N.A.	0.0	N.A.	
Raw Material Expenses	445.2	373.9	19.1	1,475.3	-69.8	Cost of production increased by ₹ 3/kg mainly on account of increase in sugarcane prices & lower recovery rate in 2021-22 season
Employee Expense	33.5	20.3	65.1	96.3	-65.2	Employee spends increased sharply by 65.1% due to arrears arising from revision of wages with retrospective effect from October 1, 2018
Other operating Expenses	33.1	36.6	-9.5	111.7	-70.4	
EBITDA	28.3	74.7	-62.1	290.8	-90.3	Operating profit declined 62.1% on account of dip in gross margins & one-off increase in employee spends
EBITDA Margin (%)	5.2	14.8	-954 bps	14.7	-949 bps	
Depreciation	13.3	10.6	25.3	43.6	-69.6	
Interest	6.2	8.6	-28.3	31.7	-80.5	Interest cost dipped by 28.3% with reduction in debt
Other Income	2.3	0.6	263.2	3.2	-27.0	
PBT	11.2	56.2	-80.1	218.7	-94.9	
Tax Outgo	3.4	16.6	-79.8	63.5	NC	
PAT	7.8	39.6	-80.2	155.2	-95.0	Net profit de-grew 80.2% to ₹ 7.8 crore due to a dip in operating profit
Key Metrics						
Sugar sales volume (in tonnes)	114,870	120,650	-4.8	152,920	-24.9	Sugar volumes declined 4.8% due to lower domestic sale quota during the quarter
Domestic Sugar realisation (₹ per kg)	34.9	33.8	3.5	34.6	1.0	Sugar realisation was up by merely 3.5%
Distillery volumes (in crore litre)	2.2	1.7	33.5	1.6	42.9	With the commissioning of new distillery, ethanol volume increased by 33.5% to 2.2 crore litre
Distillery realisation (₹ per litre)	59.1	57.6	2.6	59.1	0.0	Distillery realisation was up by 2.6% due to revision in prices last year

Source: Company, ICICI Direct Research

Exhibit 3: Change in estimates

(₹ Crore)	FY23E			FY24E			Comments
	Old	New	% change	Old	New	% change	
Net sales	2,174.1	2,170.6	-0.2	2,279.8	2,330.1	2.2	Slight change in our revenue estimate with small change in our sugar volume, sugar realisation & ethanol realisation estimates
EBITDA	310.4	285.1	-8.1	430.0	410.9	-4.4	We factor in higher wage bill due to one-off arrear payments in Q2
EBITDA Margin (%)	14.3	13.1	-114 bps	18.9	17.6	-123 bps	
PAT	181.7	162.0	-10.8	270.3	253.0	-6.4	
EPS (₹)	9.6	8.6	-10.8	14.4	13.4	-6.4	

Source: ICICI Direct Research

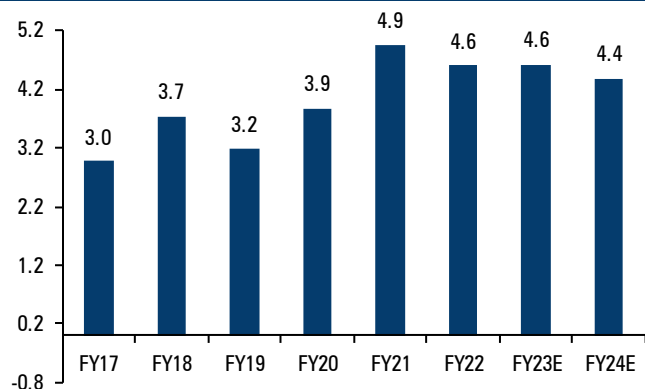
Exhibit 4: Assumptions

	Current				Earlier				Comments
	FY19	FY20	FY21	FY22	FY23E	FY24E	FY23E	FY24E	
Sugar Sold (in tonne)	3,17,700	3,87,848	4,94,890	4,59,850	4,62,149	4,39,042	4,50,653	4,28,120	We revise our sugar volume estimate according to domestic quota & export contracts
Sugar Price (₹ per tonne)	29,628	31,301	32,099	33,907	34,500	35,500	35,250	35,500	We revise sugar realisation estimate downwards for FY23 given dismal domestic sugar prices due to high sugar production
Distillery volume	9,017	11,600	31,700	55,700	80,133	1,09,725	80,133	1,09,725	
Distillery price (₹ per KL)	40,278	48,276	50,223	58,399	60,151	61,956	61,319	61,932	Slight change in distillery realisation estimate
Power Units sold	20.2	16.3	17.1	16.0	17.5	17.0	17.5	17.0	
Price per unit (₹ per units)	5.0	2.9	3.1	3.2	3.3	3.4	3.3	3.3	

Source: ICICI Direct Research

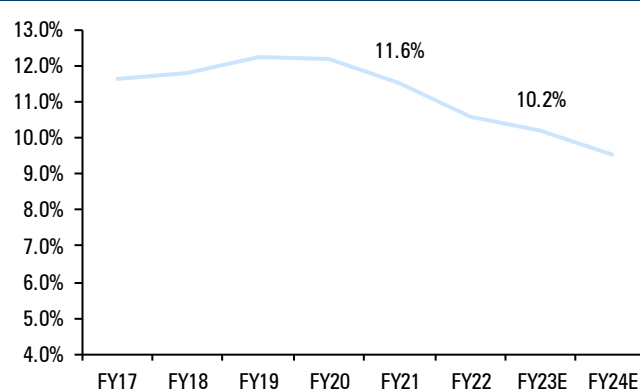
Key Metrics

Exhibit 5: Sugar sales volume (in lakh tonne)



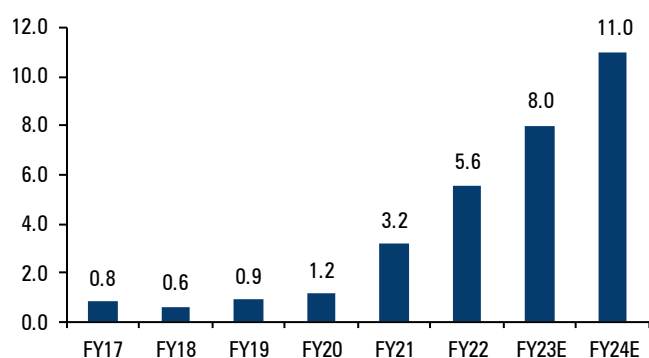
Source: ICICI Direct Research, Company

Exhibit 6: Sugar recovery rate (%)



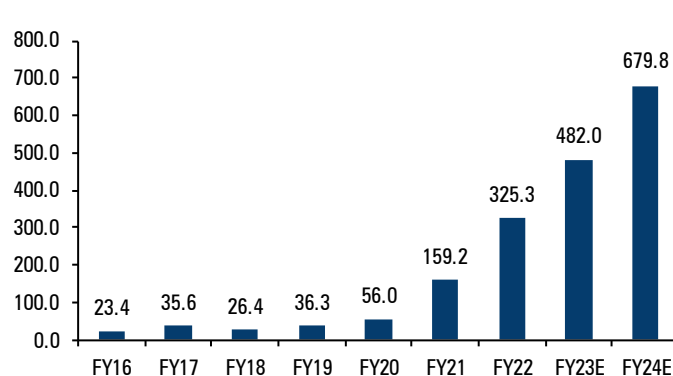
Source: ICICI Direct Research, Company

Exhibit 7: Ethanol volumes (in crore litre)



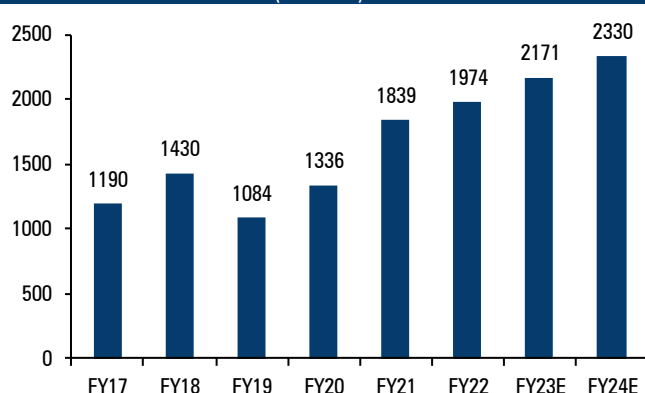
Source: Company, ICICI Direct Research

Exhibit 8: Ethanol sales (₹ crore)



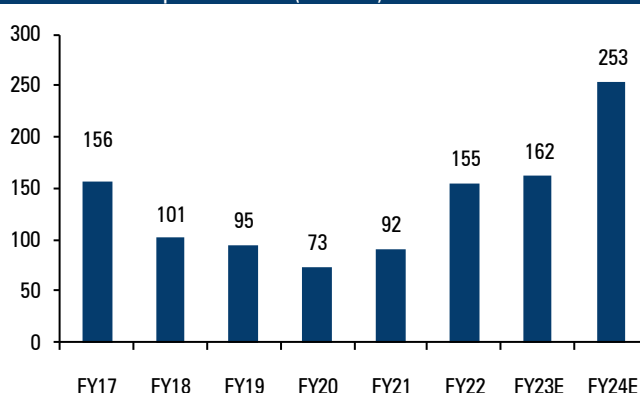
Source: Company, ICICI Direct Research

Exhibit 9: Revenue trend (₹ crore)



Source: Company, ICICI Direct Research

Exhibit 10: Net profit trend (₹ crore)



Source: Company, ICICI Direct Research

Exhibit 11: Valuation

	Sales (₹ cr)	Growth (%)	EPS (₹)	Growth (%)	PE (x)	EV/EBITDA (x)	RoNW (%)	RoCE (%)
FY21	1838.9	37.6	4.9	24.5	18.3	11.1	15.8	14.4
FY22	1974.1	7.4	8.2	69.6	10.8	7.3	23.1	20.6
FY23E	2170.6	10.0	8.6	4.4	10.3	7.3	19.4	18.5
FY24E	2330.1	7.3	13.4	56.1	6.6	8.8	24.7	28.5

Source: Company, ICICI Direct Research

Financial Summary

Exhibit 12: Profit and loss statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Total Operating Income	1,838.9	1,974.1	2,170.6	2,330.1
Growth (%)	37.6	7.4	10.0	7.3
Raw Material Expenses	1,431.1	1,475.3	1,653.3	1,672.2
Employee Expenses	92.7	96.3	112.9	118.8
Administrative Expenses	0.0	0.0	0.0	0.0
Excise Duty	0.0	0.0	0.0	0.0
Other expenses	113.8	111.7	119.4	128.2
Total Operating Expenditure	1,637.6	1,683.3	1,885.5	1,919.2
EBITDA	201.3	290.8	285.1	410.9
Growth (%)	47.9	44.5	-2.0	44.1
Depreciation	40.9	43.6	50.7	60.4
Interest	47.7	31.7	21.5	16.1
Other Income	7.1	3.2	3.8	3.8
PBT	112.7	215.5	212.8	334.4
Exceptional items	0.0	0.0	0.0	0.0
Total Tax	28.3	63.5	54.6	85.2
PAT	91.5	155.2	162.0	253.0
Growth (%)	24.5	69.6	4.4	56.1
EPS (₹)	4.9	8.2	8.6	13.4

Source: Company, ICICI Direct Research

Exhibit 13: Cash flow statement				
	₹ crore			
(Year-end March)	FY21	FY22	FY23E	FY24E
Profit/Loss after Tax	119.8	218.7	162.0	253.0
Add: Depreciation	40.9	43.6	50.7	60.4
Add: Interest	47.7	31.7	0.0	0.0
(Inc)/dec in Current Assets	108.1	132.5	127.1	29.7
Inc/(dec) in Current Liabilities	-15.0	-34.6	-18.5	1.1
CF from operating activities	295.6	352.5	321.3	344.2
(Inc)/dec in Investments	0.0	0.0	0.0	0.0
(Inc)/dec in Fixed Assets	-19.5	-175.3	-255.0	-50.0
Others	1.9	0.7	38.3	0.0
CF from investing activities	-17.6	-174.7	-216.7	-50.0
Issue/(Buy back) of Equity	0.0	0.0	0.0	0.0
Inc/(dec) in loan funds	-236.1	-85.0	-90.0	-230.0
Dividend paid & dividend tax	0.0	-61.2	-37.7	-65.9
Inc/(dec) in Sec. premium	-0.3	-0.2	38.8	0.0
Others	-43.4	-31.3	0.0	0.0
CF from financing activities	-279.8	-177.7	-88.9	-295.9
Net Cash flow	-1.8	0.1	15.7	-1.7
Opening Cash	1.9	0.1	0.2	16.0
Cash with bank	1.0	38.3	0.0	0.0
Closing Cash	1.2	38.6	16.0	14.3

Source: Company, ICICI Direct Research

Exhibit 14: Balance Sheet				
	₹ crore			
	FY21	FY22	FY23E	FY24E
Liabilities				
Equity Capital	18.8	18.8	18.8	18.8
Reserve and Surplus	560.1	654.5	817.6	1,004.7
Total Shareholders funds	578.9	673.3	836.4	1,023.5
Total Debt	556.8	520.7	430.7	200.7
Long Term Provisions	21.8	22.3	20.3	18.3
Other Non-current Liabilities	2.2	1.4	1.4	1.4
Total Liabilities	1,159.7	1,217.7	1,288.8	1,243.9
Assets				
Gross Block	931.5	953.2	1,208.2	1,258.2
Less: Acc Depreciation	521.5	565.1	615.9	676.3
Net Block	409.9	388.1	592.4	582.0
Capital WIP	0.5	142.5	142.5	142.5
Intangible assets	0.0	0.0	0.0	0.0
Non Current Investments	0.1	0.3	0.3	0.3
Other non-current assets	53.2	41.7	41.7	41.7
Current Assets				
Inventory	855.3	757.7	572.8	517.8
Debtors	67.9	34.5	72.4	77.7
Cash	1.2	38.6	16.0	14.3
Loans & Advances	0.1	0.3	0.3	0.3
Other Current Assets	57.2	15.8	35.8	55.8
Current Liabilities				
Creditors	187.2	96.3	79.8	82.9
Provisions	3.8	4.4	4.4	4.4
Other CL	94.7	101.1	101.1	101.1
Net Current Assets	696.0	645.0	511.9	477.4
Total Assets	1,159.7	1,217.7	1,288.8	1,243.9

Source: Company, ICICI Direct Research

Exhibit 15: Key ratios				
	FY21	FY22	FY23E	FY24E
Per share data (₹)				
EPS	4.9	8.2	8.6	13.4
Cash EPS	7.0	10.6	11.3	16.6
BV	30.7	35.8	44.4	54.4
DPS	0.0	1.3	2.0	3.5
Cash Per Share	27.7	30.0	32.7	35.9
Operating Ratios (%)				
EBITDA Margin	10.9	14.7	13.1	17.6
PBT / Net Sales	6.5	11.1	10.0	14.5
PAT Margin	5.0	7.9	7.5	10.9
Inventory days	169.8	140.1	96.3	81.1
Debtor days	13.5	6.4	12.2	12.2
Creditor days	37.2	17.8	13.4	13.0
Return Ratios (%)				
RoE	15.8	23.1	19.4	24.7
RoCE	14.4	20.6	18.5	28.5
Valuation Ratios (x)				
P/E	18.3	10.8	10.3	6.6
EV / EBITDA	11.1	7.3	7.3	4.5
EV / Net Sales	1.2	1.1	1.0	0.8
Market Cap / Sales	0.9	0.8	0.8	0.7
Price to Book Value	2.9	2.5	2.0	1.6
Solvency Ratios				
Debt/EBITDA	2.8	1.8	1.5	0.5
Debt / Equity	1.0	0.8	0.5	0.2
Current Ratio	4.9	7.2	7.1	6.6
Quick Ratio	0.6	0.5	1.1	1.4

Source: Company, ICICI Direct Research

Exhibit 16: ICICI Direct coverage universe (Sugar)

Sector / Company	CMP	TP	M Cap	EPS (₹)				P/E (x)				EV/EBITDA (x)				P/B				RoCE (%)				
	(₹)	(₹)		Rating	(₹ Cr)	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E	FY24E	FY21	FY22E	FY23E
Balrampur Chini (BALCHI)	317	515	Buy	6,647	22.8	22.8	27.4	41.3	13.9	13.9	11.6	7.7	11.5	11.7	10.1	7.0	2.7	2.6	2.3	2.1	16.4	15.3	16.0	23.1
Dalmia Bharat Sugar (DALSUG)	317	490	Buy	2,567	33.4	36.7	42.5	49.6	9.5	8.6	7.5	6.4	7.5	7.7	5.8	4.6	1.3	1.2	1.2	1.0	13.3	12.3	15.5	17.7
Triveni Engineering (TRIENG)	252	350	Buy	6,103	12.2	17.5	20.5	25.0	20.7	14.4	12.3	10.1	11.2	10.9	8.8	7.1	3.5	2.8	2.4	2.0	19.4	15.8	18.3	20.5
Dwarikesh sugar (DवासUG)	89	135	Buy	1,672	4.9	8.2	8.6	13.4	18.3	10.8	10.3	6.6	11.1	7.3	7.3	4.5	2.9	2.5	2.0	1.6	14.4	20.6	18.5	28.5
Avadh Sugar (AVASUG)	477	790	Buy	954	38.8	62.2	90.3	104.8	12.3	7.7	5.3	4.6	8.6	7.3	5.3	4.2	1.5	1.3	1.1	0.9	11.5	12.5	16.0	18.6

Source: Bloomberg, ICICI Direct Research

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Buy: >15%

Hold: -5% to 15%;

Reduce: -15% to -5%;

Sell: <-15%



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