

Earnings Update

DBS Cholamandalam Securities Ltd

24 July, 2009

Shree Renuka Sugars Ltd.

Market Performer

CMP **Rs. 149**Sensex: **15,231**Price target: **Rs 171**

ANALYST

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Background: SRSL is the fifth largest sugar manufacturer with a capacity of 40,000tcd and the largest refiner with a capacity of 4000tpd in India. SRSL accounts for 20% of India's sugar exports and is the leader in fuel ethanol with a 20% market share. Company's current power and ethanol production capacity of 143MW and 930KLPD respectively is spread across various locations in Karnataka, Maharashtra and West Bengal. SRSL is an active corporate member on NCDEX dealing in sugar commodities to trade in spot market and in futures.

AT A GLANCE

Issued Equity Capital (Mn. shrs)	316.9
Mkt. Cap (Rs.in Mn/US\$m)	47,218/944
Major Shareholders	
Promoters (%)	39.1%
Free Float (%)	60.9%
Avg. Daily Vol.('000)	1,443
Sector:	Sugar
Bloomberg/Reuters Code:	SHRS IN/SRES.BO

FORECASTS AND VALUATION (Standalone)

YE Sept (Rs Mn)	2008	2009E	2010E
Turnover	18,242	25,460	40,491
EBITDA	2,183	4,320	6,265
Pre-tax Profit	1,137	2,734	4,822
Net Profit	928	1,793	3,163
Net Pft (Pre Ex.)	746	1,793	3,163
EPS (Rs)	2.8	5.7	9.4
DPS (Rs)	0.2	0.5	0.8
BV Per Share (Rs)	24.9	43.5	55.3
PE (X)	39.6	14.5	12.2
EV/EBITDA	23.0	12.3	9.1
P/BV (X)	4.4	2.5	2.0
ROE (%)	14.3%	17.4%	19.6%
P/S	5.2	2.7	2.1

Q3 FY09 performance review

For Q3FY09, Shree renuka sugars reported a YoY revenue growth of 19.3% and 118.9% on sequential basis. EBITDA registered a growth of 72.2% YoY while EBITDA margins increased by 544bps to 17.1% during the quarter. Net profit increased by whopping 165.7% YoY.

Key Highlights:

Revenue is in line with our expectations

Net sales increased mainly due to 177.4% YoY increase in the segment sales of sugar, 47.1% YoY growth in segment sales of ethanol and 28.8% increase in segment sales of power. However, trading sales decreased by 80.6% YoY to Rs671 million. Segment sales of sugar rose on the back of increase in average net realization by 73% YoY from Rs. 12,340 to Rs. 21,366 per MT and up from Rs18,873 per MT in Q1FY09. The average realisation for the quarter has declined by 7% YoY to Rs6.2 per unit for export of power and increased by 15% to Rs24,479 on selling per KL of ethanol on YoY basis.

EBITDA margins improved by 544 bps

On the back of higher sugar sales volume (up 63% YoY), and lower other expenditure, EBITDA for Q3FY09 up by 72.2% YoY. PBIT margins for sugar increased by 10.04 percentage points YoY on account of higher sugar realisations. The PBIT margins of cogen was at 25.3% down on YoY and sequential basis, mainly due to use of coal in co-generation due to unavailability of bagasse during the quarter. On account of higher proportion of ethanol (almost 40%) in total sales of distillery, PBIT margins for segment sales of ethanol dipped 23.8% on YoY and sequential basis.

NPM rose by 477bps

Despite of higher depreciation (up 65.7% YoY) and interest costs (up 7.1% YoY, down 5.8% QoQ) net profit was up by 20.7% YoY.

Segmental Sales

- ❖ Segmental sales of manufactured sugar rose 63% YoY and 117% on QoQ basis. With the commissioning of Haldia refinery unit SRSL produced about 826,452 MT of sugar during first nine months of FY09 out of which cane sugar was 375,835 MT and refined sugar was 450,617 MT. The company has sold about 517,214 MT of sugar during 9MFY09.
- ❖ Sales of ethanol up by 28.4% on YoY basis from 12,033 KL during Q2FY08 to 15,453KL during Q3FY09.
- ❖ Company exported 68 mnKwh in Q3FY09 as compare to 58 million in Q3FY09.

Exhibit 1

	Q3FY09	Q3FY08	YoY (%)	Q2FY09	QoQ (%)
Manufacturing (Qty)					
Sugar (MT)	263,518	161,661	63.0%	121,459	117.0%
Ethanol (KL)	15,453	12,033	28.4%	15,777	-2.1%
Power (mnKwh)	68	58	17.2%	59	15.3%

Source: Company, DCSEC Research

No funding issue for expansion plans...

SRSL is likely to build a big refinery unit in Gujarat, whose capacity would be around 3000tpd. SRSL is also bolstering its existing refining capacity of 1,000tpd at its Athani unit to 2,000tpd and set up sugar refining capacity of 1,000tpd at its Havalga unit. The company expects, new capacities at Athani and Havalga would be operational by Dec-09 and the total refining capacity will increase to 6000tpd by the Dec-09 and 9000tpd by Dec-10. The estimated capex for the new refining unit at Gujarat and expansion plans at Athani and Havalgao will be Rs4800 mn (Rs 4000 mn for new unit in Gujarat and Rs800 mn for Athani and Havalga units). To meet the funding requirement for its expansion plans, SRSL has raised Rs5060.3 mn by way of QIP issue and part of the funds raised through QIP will be deployed for these expansion plans.

We expect SRSL will import 1.2 mn ton of raw sugar in FY10

The total refining output (including Haldia refinery) from raw sugar for the Q3FY09 was 251,446 MT. We expect for FY09, SRSL is likely to end with 750,000 MT of raw sugar imports, while for the next season management said that the company will process 1.2 mnt of raw sugar, which is 60% higher than our earlier estimates of 750,000 MT. We believe the company would immensely benefit from its large refining capacity during FY09 and FY10 on account of shortfall in domestic sugar production. We have assumed that company would make refining margin (EBITDA/ton) of Rs2.8 per kg during FY09 and Rs4.2 per kg during FY10.

SMP increase unlikely to impact raw material costs

The government has increased SMP for the next crushing season by over 32% to Rs107.7 per quintal. Farmers will get a premium of Rs1.13 for every 0.1 percentage additional recovery over 9.5%. The increase in SMP is unlikely to affect the margins of industry as a whole as almost every mills paid higher than SMP during current season. For SRSL, we have assumed cane cost of Rs1,800 per quintal for next crushing season, which is significantly higher than SMP fixed by the government.

Low coverage ratio but comfortable gearing ratio and cash flows

Though coverage ratio over the quarter improved from 2.6x to 4.7x during Q3FY09, but it is still 2.6x for the 9MFY09 period, which could be a concern for the company. However, on the back of comfortable gearing ratio 1.5x in FY08 and cash flows from operations at about Rs2,935 mn during FY09-10E, we do not envisage serious concern on the company ability to service its interest.

We expect sugar prices to remain buoyant

Indian Sugar Manufacturers Association (ISMA) has predicted domestic sugar production for FY09 to be around 14.7 mnt as against 26.3 mnt in FY08; a decline of almost 43% YoY. The production in the next season is expected to remain in the same line at about 18 mnt. This is primarily due to Northern India especially Uttar Pradesh had witnessed rain shortfall in the month of May and June, which would affect the yield level of cane crop, however due to late recovery of monsoon, Karnataka and Maharashtra had witnessed decent amount of rainfall in July. In addition to this, domestic consumption at 23 MT is expected to outpace the production during FY10. We expect with the reducing stock levels and expected lower cane production during FY10, sugar prices to remain firm and move northwards.

Investments Risks

- **Rising ocean freight costs and raw sugar price**

The prevailing price of raw sugar and ocean freight makes imports not viable until realisation on sugar is more than Rs 25,000 per ton. And given that SRSL is embarking on huge refinery capacity, inability to import raw sugar will negatively affect bottom line.

- **Sharp correction in sugar prices**

Company's earning is highly sensitive to fall in average sugar price - with 1% decrease in average sugar price company's overall EPS would drop by 8.8% during FY09 and 7.4% during FY10.

- **Depreciation of rupee against USD**

Depreciation of rupee by 1% against dollar would drop SRSL's overall EPS by 5.3% during FY09 and 3.2% during FY10.

Sensitivity Analysis - FY09E and FY10E Earnings

A. Sugar Price and Cane Cost

Exhibit 2

FY10E					
Cane cost (Rs/Quintal)	170	175	180	190	200
NSR (Rs/Kg)					
21.5	3.8	3.4	3	2.1	1.3
22.5	7	6.6	6.2	5.4	4.5
23.5	10.3	9.9	9.4	8.6	7.8
24.5	13.5	13.1	12.7	11.8	11
25.5	16.7	16.3	15.9	15.1	14.2

Source: DCSEC Research

B. Sugar Price and Exchange rate

Exhibit 3

FY10E					
Exchange rate	49	50	51	52	53
NSR (Rs/Kg)					
21.5	3.8	3	2.2	1.4	0.6
22.5	7	6.2	5.4	4.7	3.9
23.5	10.2	9.4	8.7	7.9	7.1
24.5	13.5	12.7	11.9	11.1	10.4
25.5	16.7	15.9	15.1	14.4	13.6

Source: DCSEC Research

C. Refined Sugar Volume and EBITDA margins (USD/ton)

Exhibit 4

FY10E					
EBITDA Margin (USD/tonne)	64	74	84	94	104
Volume					
900000	6.3	7.2	8.1	8.9	9.8
1000000	6.6	7.5	8.5	9.5	10.5
1100000	6.8	7.9	9	10.1	11.1
1200000	7.1	8.3	9.4	10.6	11.8
1300000	7.4	8.6	9.9	11.2	12.4
1400000	7.6	9	10.4	11.7	13.1

Source: DCSEC Research

Scenario Analysis

Exhibit 5

FY10E			
	Worst Case	Base Case	Best Case
Cane Cost* *(Rs/ton)	1980	1800	1620
Landed Cost of raw sugar (USD/ton)	330	330	330
NSR (Rs/kg)	22.3	23.5	24.7
EBITDA (Mn)	3559	6265	8971
PAT (Mn)	2435	3163	5985
EPS (Rs)	4.1	9.4	14.7
Recommendation	Underperformer	Market Performer	Outperformer
Target Price (Rs)	84	171	258
CMP	149	149	149
Upside (%)	-43.6%	14.8%	73.2%

**Includes transportation charge, purchase tax and road cess

Source: DCSEC Research

Valuation

Up FY10 EPS estimates by ~80.8%; TP increased to Rs 171

We have tweaked our estimates to incorporate higher expectation on 1.2 million tonnes of raw sugar imports (up 60% YoY than our earlier expectations) during next season, which in couple with rising sugar price will bolster the earnings in FY10 and now expect SRSR to report earnings of Rs5.7 in FY09 and Rs9.4 in FY10. We have valued this stock on EV/EBITDA basis. At CMP of Rs 149, the stock is currently quoting at P/E of 14.5x and 12.2x its FY09 and FY10 earnings respectively and EV/EBITDA of 12.3x and 9.1x of its FY09 and FY10 estimates respectively. We reiterate our 'Market Performer' rating with a price target of Rs171, based on 10x 1year rolling forward EV/EBITDA.

Exhibit 6 : EV/EBITDA band: Shree Renuka Sugars



Source: DCSEC Research

Q3FY09 Result update

Exhibit 7

(Rs Million)	Q3FY09	Q3FY08	YoY%	Q2FY09	QoQ (%)
Gross Sales	7414	6215	19%	3387	119%
Less: Excise Duty	259	114	127%	146	77%
Net Sales	7155	6101	17%	3241	121%
Total Expenditure	5934	5392	10%	2453	142%
EBITDA	1221	709	72%	788	55%
Depreciation	164	99	66%	155	6%
EBIT	1057	610	73%	633	67%
Other Income	93	-35		24	
PBIT	1150	575	100%	657	75%
Interest	226	211	7%	292	-23%
PBT	924	364	154%	365	153%
Tax	313	134	134%	124	152%
Adjusted PAT	611	230	166%	241	154%
Paid up equity share capital (Mn)	280	270		280	
Basic and Diluted EPS (INR)	2.2	0.9		0.9	

Source: Company, DCSEC Research

Segmental Performance

Exhibit 8

(Rs Million)	Q3FY09	Q3FY08	YoY(%)	Q2FY09	QoQ (%)
Segment Revenue					
Sugar	5859	2112	177%	2939	99%
Trading	671	3451	(81)%	72	832%
Cogeneration	801	622	29%	869	(8)%
Ethanol	378	257	47%	379	0%
Others	10	11	(9)%	10	0%
Total	7719	6453	20%	4269	81%
Less: Intersegment revenue	564	352	60%	1028	(45)%
Net sales/Income from operations	7155	6101	17%	3241	121%
Profit before interest and tax	0	0	0%	0	0%
Sugar	863	99	772%	206	319%
Trading	7	95	(93)%	3	133%
Cogeneration	203	353	(42)%	380	(47)%
Ethanol	90	106	(15)%	129	(30)%
Others	5	5	0%	1	400%
PBIT	1168	658	78%	719	62%
Unallocated Corporate expenses	111	48	131%	86	29%
Operating profit	1057	610	73%	633	67%
Less: Interest	226	211	7%	292	(23)%
Other Income	93	-35		24	
PBT	924	364	154%	365	153%
PBIT Margins %					
Sugar	14.7%	4.7%		7.0%	
Trading	1.0%	2.8%		4.2%	
Cogeneration	25.3%	56.8%		43.7%	
Ethanol	23.8%	41.2%		34.0%	
Others	50.0%	45.5%		10.0%	

Source: Company, DCSEC Research

Detailed financial statements (Standalone)

Income Statement

Exhibit 9

(Rs Million)	FY06	FY07	FY08	FY09E	FY10E
Gross Sales	8347	7619	18718	26192	41716
Excise Duty	331	295	476	733	1225
Net Sales	8016	7324	18242	25460	40491
Var %	25%	(9)%	149%	40%	59%
Other Income	50	162	4	129	129
Total Income	8066	7486	18246	25589	40620
Expenditure					
Raw material cost	3964	3379	5361	18768	28125
Cost of traded goods	2161	1589	8049	848	900
(Increase)/Decrease in Inventory	(128)	115	24	(3642)	(1741)
Refining cost				1500	2400
Personnel expenses	122	238	341	476	757
Operating & Administrative expenses	926	735	1562	2180	2180
Selling & distributive expenses		221	723	1009	1604
Operating expenditure	7045	6277	16059	21139	34226
Var %	23.3%	(10.9)%	155.9%	31.6%	61.9%
EBITDA	971	1047	2183	4320	6265
% Margin	12.1%	14.3%	12.0%	17.0%	15.5%
Var %	42.6%	7.8%	108.4%	97.9%	45.0%
Depreciation & Amortization	88	249	365	638	702
EBIT	883	798	1818	3682	5563
PBIDT	1021	1209	2187	4449	6394
Depreciation & Amortization	88	249	365	638	702
PBIT	934	960	1822	3811	5692
Financial Expenses	188	180	685	1077	870
PBT	746	780	1137	2734	4822
Taxation	183	236	392	940	1659
Reported PAT before Prior period items	563	545	746	1793	3163
% Margin	7.0%	7.4%	4.1%	7.0%	7.8%
Add: Excess provision of depreciation written back			182.0		
Less: Prior period expense	7.0				
Adjusted PAT	556	545	746	1793	3163
Var%	66.1%	(2.0)%	36.9%	140.5%	76.4%
Number of equity shares	238	248	276	317	335
Basic EPS	2.4	2.2	2.7	5.7	9.4
Diluted EPS	2.4	2.2	2.7	5.7	9.4

Source: DCSEC Research

Balance Sheet

Exhibit 10

(Rs Million)	FY06	FY07	FY08	FY09E	FY10E
Shareholder's Fund					
Share Capital	238	311	507	523	335
Reserve and Surplus	1986	3047	5893	12791	17727
Networth	2224	3357	6399	13314	18062
Secured Loans	3544	6211	8276	7716	6144
Unsecured Loans	167	259	1598	2556	2556
Total Debt	3711	6470	9873	10273	8700
Deferred tax liability	57	202	461	461	461
Sources of Funds	5993	10029	16734	24047	27223
Application of Funds					
Fixed assets					
Gross Block	1630	6314	7789	14060	18274
Less: Depreciation	436	691	877	1517	2229
Net Block	1194	5623	6912	12545	16045
Capital WIP	3313	2077	5140	2000	3000
Investments	6	168	1506	1506	1506
Current assets, Loans and Advance					
Inventory	1122	1002	1869	4159	5900
Sundry debtors	539	387	486	699	791
Cash and Bank Balances	172	307	134	3263	315
Other current assets	33	323	853	775	878
Loans and Advances	775	1334	1994	1994	1994
Less: Current Liabilities and Provisions					
Current Liabilities	916	822	1644	2363	2675
Provisions	319	390	531	531	531
Net current assets	1405	2140	3161	7996	6673
Deferred revenue expenditure	76	21	16	0	0
Application of Funds	5993	10029	16734	24047	27223

Source: DCSEC Research

Cash Flow Statement

Exhibit 11

(Rs Million)	FY06	FY07	FY08	FY09E	FY10E
Net Profit	563	545	746	1793	3163
Add:					
Depreciations	88	249	365	638	702
Increase in deferred tax liability	16	145	259	0	0
Profit before working capital changes	667	939	1370	2432	3865
Change in operating assets					
Inventory	2	120	(867)	(2290)	(1741)
Sundry debtors	(341)	152	(100)	(213)	(92)
Other receivables	(401)	(826)	(1041)	78	(102)
Trade and other payables	(709)	(94)	822	719	312
Increase/Decrease in working capital	(1448)	(647)	(1186)	(1706)	(1624)
Others	(75)	177	48	0	0
Cash flow from operations	(856)	469	233	726	2241
Cash flow from investing activities					
Purchase of fixed assets	(3463)	(3448)	(4537)	(3132)	(5214)
Loss on sale of investments	0	0	3	0	0
Purchase of quoted investments	0	0	(309)	0	0
Investment in subsidiary companies	0	(2)	(805)	0	0
Acquisition cost	0	(160)	(284)	0	0
Net cash from investing activities	(3463)	(3611)	(5933)	(3132)	(5214)
Cash flow from financing activities					
Increase in capital	38	73	196	16	(188)
Share Premium	1048	616	1988	5270	2041
Dividend Paid	(48)	(85)	(55)	(150)	(255)
Proceeds from borrowings	2826	2674	3399	399	(1573)
Net cash flow from financing activities	3864	3277	5527	5535	25
Increase/Decrease in Cash	(455)	135	(173)	3129	(2947)
Opening cash Balance	627	172	307	134	3263
Closing cash Balance	172	307	134	3263	315
Free cash flow	(4319)	(2980)	(4305)	(2406)	(2973)

Source: DCSEC Research

Ratio Analysis

Exhibit 12

	FY06	FY07	FY08	FY09E	FY10E
Margin Ratios (%)					
EBITDA Margin	12.1	14.3	12.0	17.0	15.5
EBIT Margin	11.0	10.9	10.0	14.5	13.7
PBT Margin	9.3	10.7	6.2	10.7	11.9
PAT Margin	7.0	7.4	4.1	7.0	7.8
Solvency Ratios (X)					
Debt/Equity	1.8	2.0	1.6	0.8	0.5
Net debt/Equity	1.7	1.9	1.5	0.5	0.5
EBITDA/Interest	5.2	5.8	3.2	4.0	7.2
EBIT/Interest	4.7	4.4	2.7	3.4	6.4
Debt/EBITDA	4.3	6.9	4.9	2.5	1.5
Valuation Ratio (X)					
P/E	4.6	5.2	39.6	14.5	12.2
P/BV	11.5	7.7	4.4	2.5	2.0
P/Sales	13.2	9.0	5.2	2.7	2.1
EV/EBITDA	40.6	41.8	23.0	12.3	9.1
Turnover Ratio					
Inventory Turnover (X)	5.3	4.8	9.4	5.8	5.9
Days of Inventory on Hand (Days)	68.3	76.2	39.0	63.0	61.8
Receivable Turnover (X)	21.7	15.8	41.8	43.0	54.3
Average Collection Period (Days)	16.8	23.1	8.7	8.5	6.7
Payable Turnover (X)	4.7	5.7	11.6	9.9	12.1
Number of days of payable (Days)	77.3	63.9	31.5	37.0	30.1
Operating Cycle	85.1	99.3	47.7	71.5	68.6
Cash Conversion Cycle	7.8	35.4	16.3	34.4	38.5
Asset turnover ratio (X)	2.0	0.9	1.3	1.2	1.5
Working Capital turnover (X)	8.9	4.1	6.9	4.6	5.5
Du- Pont Analysis					
Tax Burden (%)	75.5	69.8	65.6	65.6	65.6
Interest Burden (%)	84.4	97.7	62.6	74.2	86.7
EBIT Margin (%)	11.0	10.9	10.0	14.5	13.7
Asset turnover ratio (X)	2.0	0.9	1.3	1.2	1.5
Leverage ratio (X)	2.7	2.9	2.7	2.0	1.6
ROE (%)	38.0	18.6	14.3	17.4	19.6
ROCE (%)	12.6	6.3	9.4	12.7	15.2
Per share (Rs)					
Basic EPS	24.0	21.0	2.8	5.7	9.4
CEPS	2.7	3.2	4.0	7.7	11.5
Book Value	9.6	14.3	24.9	43.5	55.3
DPS	0.2	0.2	0.2	0.5	0.8

Source: DCSEC Research

Adjustments in Valuation

	Numerator	Denominator
DEBT/Equity	Debt = (Loans + Interest accrued + outstanding commitments)	Equity + Reserve & Surplus + Deferred tax liability)
Net Debt	Net debt - Cash	N/A
Free Cash flow	Cash flow from operations - capex	N/A
Return on Capital Employed	NOPAT = (NOPAT + Interest expense)*(1-tax rate)	Debt + Equity
Enterprise value/EBITDA	Current share price*Current shares + Minority interests+Debts -cash - Investments)	EBITDA
Forward P/E ratio (FY09 & FY10)	Current Market Price	EPS= (Average ROE for the most recent full cycle*Current book value per share)

Source: DCSEC Research

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