Sharekhan by BNP PARIBAS

Powered by the Sharekhan 3R Research Philosophy

Stock Idea

Re-initiating coverage

Dhampur Sugar Mills Ltd

Fuelling a sweet growth story

Miscellaneous	Sharekhan code: DHAMPURSUG	
Reco/View: Buy	CMP: Rs. 532	Price Target: Rs. 692

↑ Upgrade ↔ Maintain ↓ Downgrade

3R MATRIX	+	=	-
Right Sector (RS)	✓		
Right Quality (RQ)	✓		
Right Valuation (RV)	✓		

\+ Positive = Neutral – Negative

Summary

- We re-initiate coverage on Dhampur Sugar Mills Limited (DSML) with a Buy recommendation, assigning a price target of Rs. 692. Discounted valuations at 10.5x/8.4x its FY2023E/FY2024E EPS and strong growth prospects (focusing on Ethanolisation) make it another strong play in the sugar sector.
- Increased distillery capacity to 650 KLPD will lead to a 29% CAGR in ethanol sales to Rs. 1,245.2 crore by FY2024; ethanol's contribution to total revenue will increase to 27% in FY2024 from 14% in FY2021.
- Better revenue mix and driving efficiencies focusing on Total Productive Maintenance (TPM) would help EBITDA margin to improve to ~15% in FY2024 from 11% in FY2021 and will consistently improve in the years ahead.
- Strong profitability and better working capital management would lead to cumulative free cash flow of ~Rs. 450 crore over FY2022-FY2024; Return profile would improve with RoE/RoCE standing at 18.6%/19.8% in FY2024.

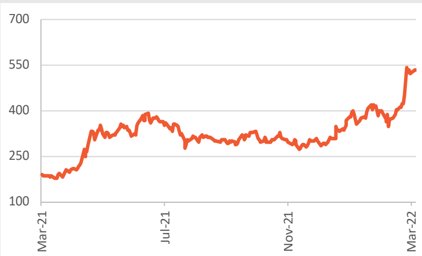
Company details

Market cap:	Rs. 3,534 cr
52-week high/low:	Rs. 567 / 174
NSE volume: (No of shares)	9.1 lakh
BSE code:	500119
NSE code:	DHAMPURSUG
Free float: (No of shares)	3.4 cr

Shareholding (%)

Promoters	49.1
FII	6.6
DII	0.6
Others	43.7

Price chart



Price performance

(%)	1m	3m	6m	12m
Absolute	43.2	81.6	77.4	184.6
Relative to Sensex	43.2	81.0	79.5	169.3

Sharekhan Research, Bloomberg

Dhampur Sugar Mills Limited (DSML) is one of the largest sugar companies in India with integrated facilities of 45,500 tonne per day (cane crushing capacity), distillery capacity of 500 kilo litres per day (KLPD), and co-generation capacity of 216.5 megawatts (MW). The company is focusing on achieving consistent earnings growth and enhancing shareholders' value by focusing on key initiatives such as 1) generating more cane from its command areas, 2) driving operating efficiencies through TPM strategy, 3) investing judiciously in scaling up the ethanol business, and 4) strengthening balance sheet with stable working capital and improved cash flows. Consistent improvement in profitability and reduction in debt will help DSML's earnings to post a CAGR of 22% over FY2021-FY2024. Further, the government's support for increasing ethanol blending to 20% by SS2025 provides further scope to improve growth prospects in the medium to long run. The company strengthened its balance sheet by reducing debt by Rs. 830 crore in the past two years because of improved cash flows (likely to further reduce debt by Rs. 320 crore by FY2024).

- **'Ethanolisation' core of growth strategies:** DSML is focusing on increasing investment in ethanol capacity with strong support from the government's prudent blending policies, strengthening the non-sugar portfolio of the business, and enhancing overall profitability in the medium to long term. The company will be enhancing its distillery facility to 650 KLPD by FY2024 from 400 KLPD in FY2021 (enhanced to 500 KLPD in January 2022). Expansion in distillery capacity would help business revenue to post a 29% CAGR over FY2021-FY2024 to Rs. 1,245.2 crore. Contribution of the ethanol segment's revenue will go up to 27% by FY2024 from 14% in FY2021.
- **EBITDA margin to consistently improve:** DSML's EBITDA margin stood lower at 11% in FY2021 compared to peers at around 14-16%. Increased ethanol sales contribution to 25%+ in FY2024, driving efficiencies through TPM, and sweating of existing assets will help DSML's EBITDA margin to improve to 15% by FY2024. Further, the company is focusing on enhancing value of its existing produce by producing country liquor (in response to the government's mandate to supply 18% of the molasses produced by the company to liquor manufacturers), manufacturing high-margin specialty chemicals, and increasing the manufacturing of refined and packaged sugar. This will help EBITDA margin to consistently improve in the medium to long term.
- **Cumulative FCF to grow by ~Rs. 450 crore; Return profile to consistently improve:** Strong earnings growth and improved working capital would help cumulative FCF to grow by Rs. 450 crore over FY2022-FY2024 (despite ~Rs. 500-600 crore of capex for expansion of ethanol capacity). The company can utilise higher cash flows to reduce debt on books and reward shareholders with higher dividend payout in the coming years. Improved profitability and sustained reduction in debt on books would help the return profile (RoE/RoCE) to improve substantially to 18.6%/19.8% in FY2024 from 15.7%/14.0% in FY2021.

Our Call

View: Re-initiate coverage with Buy assigning a PT of Rs. 692: DSML is focusing on creating value for shareholders by strengthening the non-commodities business to achieve consistent earnings growth with higher EBITDA margins. The stock is currently trading at valuation of 10.5x/8.4x its FY2023E/FY2024E EPS, which is at a discount to some of its close peers. Strong earnings visibility, improving margin profile, and strengthening of the balance sheet would help the valuation gap with close peers to reduce in the coming years. Hence, we are re-initiating coverage on the stock with a Buy recommendation, assigning a price target (PT) of Rs. 692 (valuing the stock at 11x its FY2024E EPS, which is at 27% discount to the target multiple of Balrampur Chini Mills [BCML]).

Key Risks

Any change in the government's ethanol blending policy or decline in sugar supply due to weather vagaries or other supply constraints would act as a key risk to our earnings estimates.

Valuation (Consolidated)

Rs cr

Particulars	FY21	FY22E	FY23E	FY24E
Revenue	4,232	3,426	4,070	4,699
EBITDA margin (%)	10.8	14.3	14.4	14.7
Adjusted PAT	229	266	337	418
% YoY growth	*2.3*	*16.0*	*26.7*	*24.1*
Adjusted EPS (Rs.)	34.5	40.0	50.7	62.9
P/E (x)	15.4	13.3	10.5	8.4
P/B (x)	2.3	2.0	1.7	1.5
EV/EBITDA (x)	9.9	9.1	7.5	6.1
RoNW (%)	15.7	15.9	17.5	18.6
RoCE (%)	14.0	15.4	17.6	19.8

Source: Company; Sharekhan estimates

India is expected to continue to be one of the largest manufacturers and consumers of sugar. Demand for sugar will be driven by factors such as rising population, lower per capita beverage consumption, and preference for value addition among others. The Indian ethanol market is expected to grow to USD 7.38 billion by 2024, at a CAGR of 14.5% during 2019-2024. Growth of the ethanol sector will be driven by the government's target to achieve 20% ethanol blending by 2025.

Sugar Industry – Realisation to remain high due to expected global deficit

As per ISMA's latest estimates, total net sugar production for Sugar Season (SS) 2021-2022 is estimated at 31.45 million tonne after considering higher diversion of sugar of 3.40 million tonne towards ethanol production as against diversion of 2.07 million tonne in SS 2020-2021. The increase in production is largely due to higher production in Maharashtra and Karnataka, while production in Uttar Pradesh (UP) is expected to be lower this year. Estimated sugar production in Uttar Pradesh is ~10.18 million tonne in SS 2021-2022, as against 11.06 million tonne produced in SS 2020-2021 due to factors such as lower sugarcane yields and lower sugar recoveries in the state due to climatic factors, and much higher diversion of sugar for production of ethanol. Maharashtra is expected to produce ~11.68 million tonne in SS 2021-2022, as against 10.65 million tonne produced in SS 2020-2021 owing to increased sugarcane area by ~11% and better cane yields and sugar recovery as compared to the last season. Karnataka is expected to produce ~4.52 million tonne of sugar in SS 2021-2022, as against 4.47 million tonne produced in SS 2020-2021 due to increased sugarcane area and reportedly better cane yields and sugar recoveries. With no export assistance announced for SS 2021-2022, exports are estimated to be lower at ~5-6 million tonne as compared to 7.1 million tonne in SS 2020-2021, which were aided by export subsidy over and above favourable international prices. With an opening stock of 8.2 million tonne, consumption of 27 million tonne, exports of ~6 million tonne, and estimated production of 31.45 million tonne, the closing stock as on September 30, 2022, is estimated to be around 6.65 million tonne.

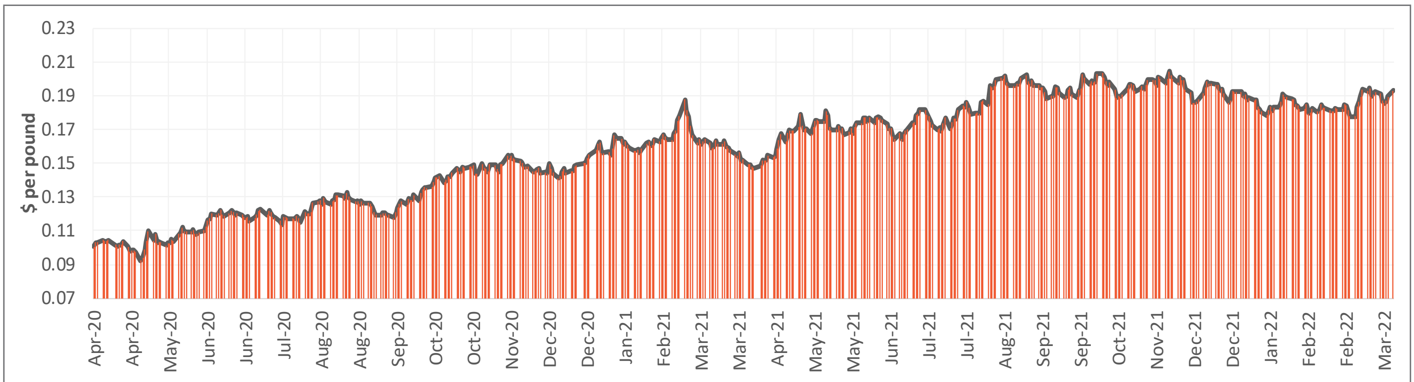
Sugar balance sheet — million tonne

Particulars	SS2017-18	SS2018-19	SS2019-20	SS2020-21	SS2021-22E
Opening balance (as on October 1)	**3.4**	**10.9**	**14.5**	**10.7**	**8.3**
Sugar Production	32.5	33.2	27.4	31.2	31.5
Imports	0.0	0.0	0.0	0.0	0.0
Sugar availability	**35.9**	**44.1**	**41.9**	**41.9**	**39.7**
Est. domestic consumption	24.5	26.1	25.5	26.6	27.0
Est. exports (MIEQ)	0.5	3.5	5.7	7.1	6.0
Closing balance (as on September 30)	**10.9**	**14.5**	**10.7**	**8.3**	**6.7**

Source: Company; Sharekhan Research

For the 2021-2022 sugar season, reports indicate a deficit of around 1.93 million tonne, higher than the 2020-2021 deficit of 1.4 million. Global sugar production is expected to be at 170.51 million tonne, with the consumption expected to be at 172.44 million tonne. In the current global turmoil, India has shown willingness to do excess supply into the world market.

International sugar prices saw a good run in the past two years



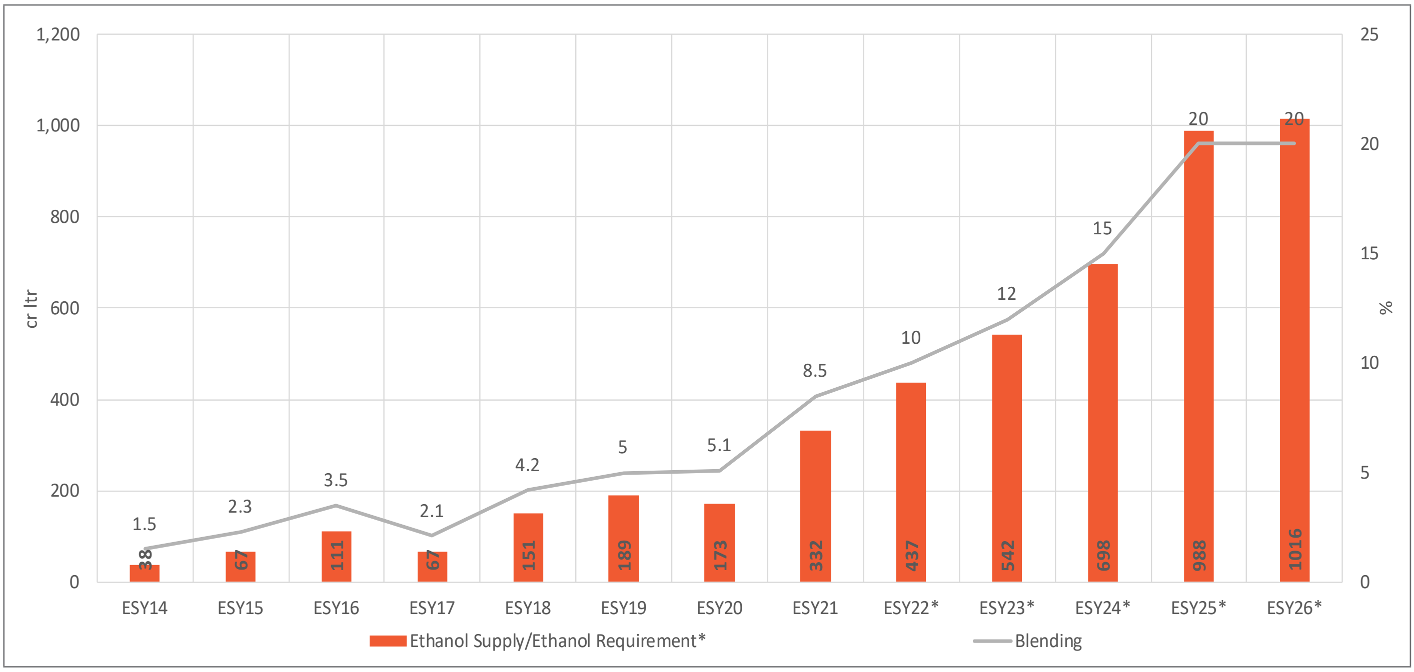
Source: Sharekhan Research; Industry reports

On the pricing side, even though sugar prices have come off their recent peaks both in domestic and global markets, they are higher than last year. International sugar prices are expected to remain high in the near term due to anticipated supply deficit and current disruption caused by the global turmoil. Thus, domestic prices will be well supported by higher international sugar prices. With spike in crude prices, ethanol blending is given higher preference in global markets (including Brazil and India), which will help prices to remain firm in the medium term.

Ethanol sector gaining momentum due to blending target of 20% by SS2025

To reduce export dependency for sugar and cut imports of fuels, besides cleaning up the environment, the government approved the National Policy on Biofuels in 2018 to achieve 20% blending of ethanol in petrol by 2030. In January 2021, the target of achieving 20% ethanol-blending was preponed to 2025. The blending of ethanol has increased to 9.45% in ongoing SS 2021-2022 from 8.5% blending achieved in SS2020-2021. Thus, blending has increased by over 11% in the current SS.

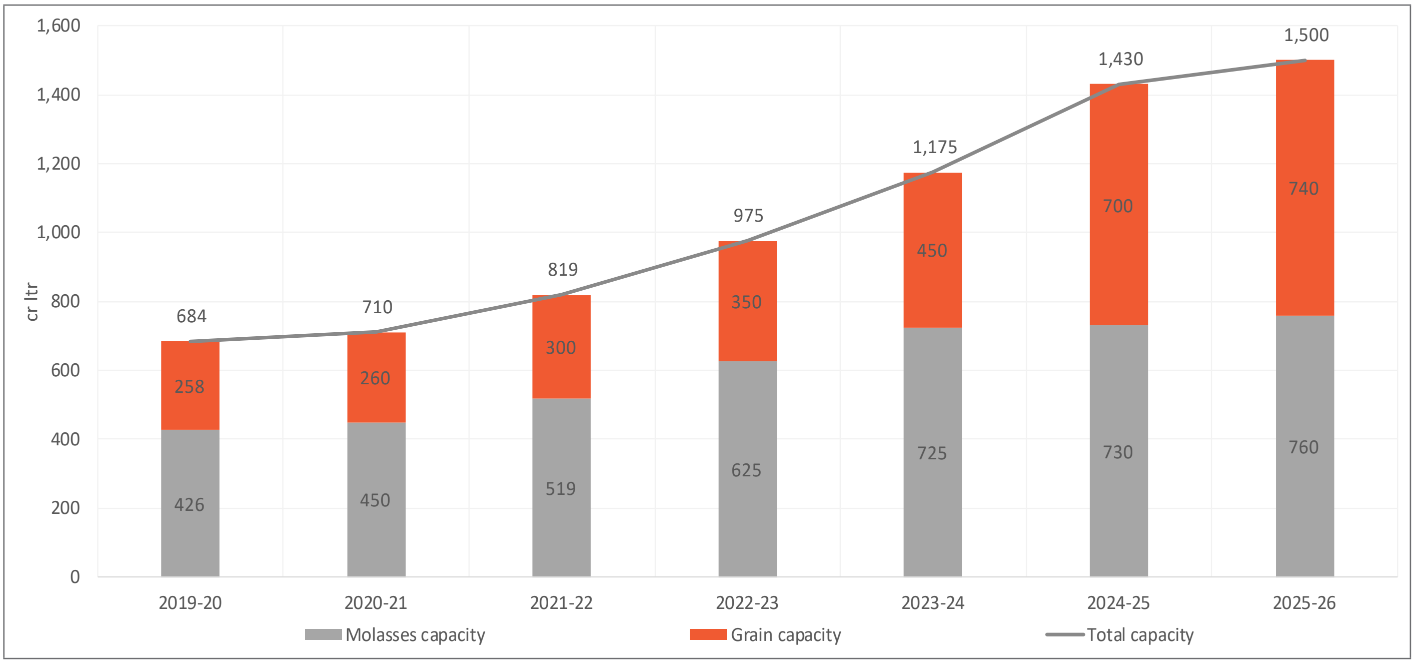
8.5% ethanol blending with petrol achieved in 2021, target to achieve 20% blending by 2025



Source: Sharekhan Research; Industry reports

The country will require ~1,016 crore litre of ethanol for blending in petrol in 2025 to fulfil the target of 20% ethanol blending. The distillation capacity required to meet this target would be 1,500 crore litres, whereas in 2020, the existing capacity of ethanol was at 684 crore litre. This means that significant ethanol capacity addition will be required to meet the blending target. As per the report by the government on 'Roadmap for Ethanol Blending in India 2020-25', ~50% of ethanol requirement will come from the sugar industry and rest from grain and other sources.

Molasses/grain-based ethanol blending to be 50:50 by FY2025



Source: Sharekhan Research; Industry reports

In order to meet the additional ethanol requirement, major sugar companies in the country have undertaken capacity addition of their distilleries.

Distillery capacities of various sugar companies

Company	Distillery capacity (KLPD)	Capacity addition (KLPD)	Total enhanced capacity (KLPD)
Balrampur Chini Mills	560	490	1,050 (Q3FY2023)
Triveni Engineering	320	340	660 (Q1FY2023)
Dhampur Sugar Mills	500	150	650 (FY2024)
Dalmia Bharat Sugar	590	Recently expanded	590
DCM Sriram	350	120	470 (Q2FY2023)
EID Parry	327	120	447 (Q3FY2023)
Dwarikesh Sugar	162.5	175	337.5 (Q1FY2023)
Avadh Sugar	325	Recently expanded	325
Magadh Sugar	150	Recently expanded	150

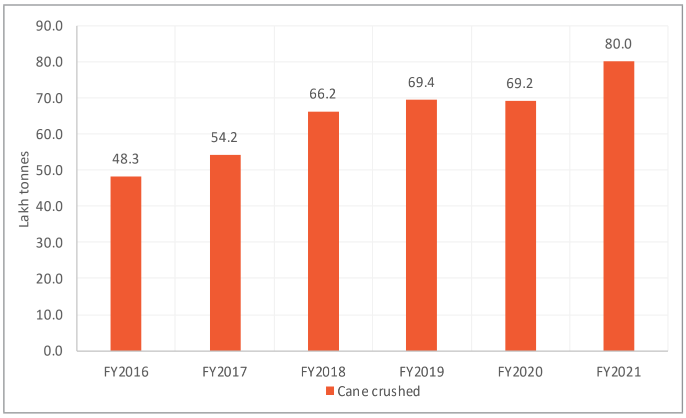
Source: Sharekhan Research

DSML is one of the largest sugar companies in India with integrated facilities of 45,500 tonne per day (cane crushing capacity), distillery capacity of 500 KLPD, and co-generation capacity of 216.5 MW. The company is focusing on achieving consistent earnings growth and enhancing shareholders' value by focusing on initiatives such as 1) generating more cane from its command areas, 2) driving operating efficiencies through TPM strategy, 3) investing judiciously in scaling up the ethanol business, and 4) deleveraging balance sheet with stable working capital and improved cash flows. Consistent improvement in profitability and reduction in debt will help DSML's earnings to post a CAGR of 22% over FY2021-FY2024.

Improvement in sugar business through sustained cane development

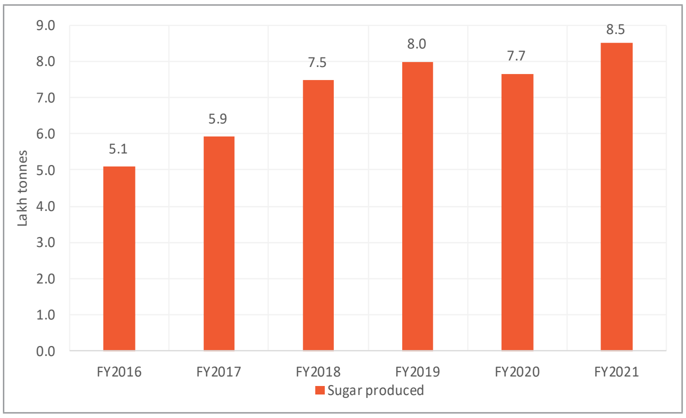
The company has placed higher emphasis on maximising cane output across command areas of Rajpura, Meerganj, and Asmoli. It has recognised that access to a growing volume of cane from within existing command areas and promoting the early maturing cane variety will aid in growth of the company. The key to a progressively larger cane access lies in patient engagement with farmers in convincing them to plant more cane, demonstrating the use of superior cane varieties (higher yield and, hence, higher income), timely growing support (provision of seeds, fertilisers, and crop protecting agents), and prompt payment. Over the years, the company has deepened the culture of cane growing by educating farmers and encouraging and incentivising cane planting. The company has almost doubled its cane crushing capacity from 48.31 lakh tonne in FY2015-FY2016 to 80.01 lakh tonne in FY2020-FY2021. Going ahead, DSML aims to explore the available headroom for incremental cane planting in three units of Meerganj, Asmoli, and Rajpura, which should increase capacity utilisation at those units and accelerate overall revenue growth.

Rising trend of cane crushed...



Source: Company, Sharekhan Research

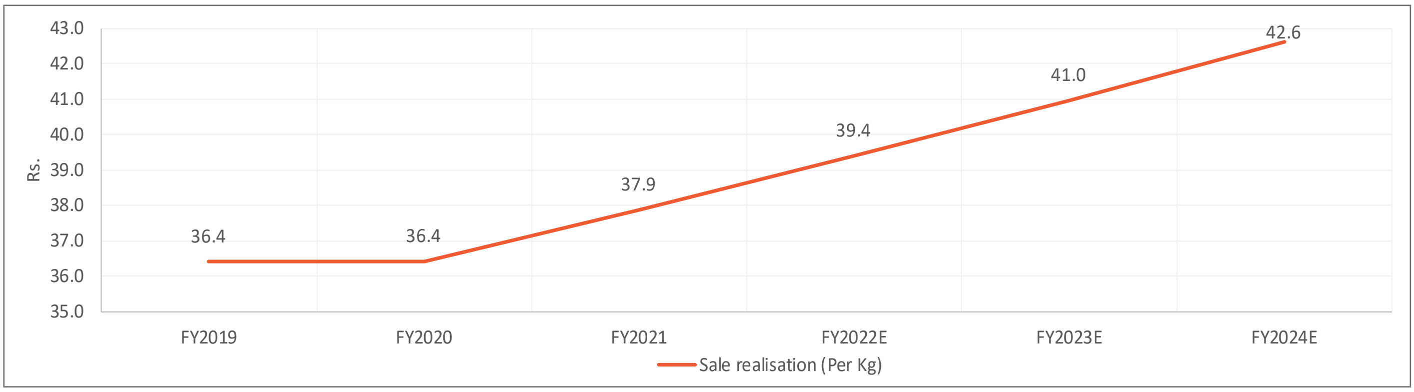
...leading to increased sugar production



Source: Company, Sharekhan Research

The company also undertook certain other initiatives such as providing subsidised fertilisers to farmers, focusing on nursery development to provide quality seeds to farmers, progressively replacing the CO 0238 sugarcane variety with CO 15023 variety, mitigating the impact of the red rot disease, and enhancing productivity (The CO 15023 variety is said to have a recovery rate of 14%, which is higher than all other varieties). These initiatives are likely to generate larger cane availability, broad-basing the company's production across the coming years and improve realisation rate.

Trend in sales realization

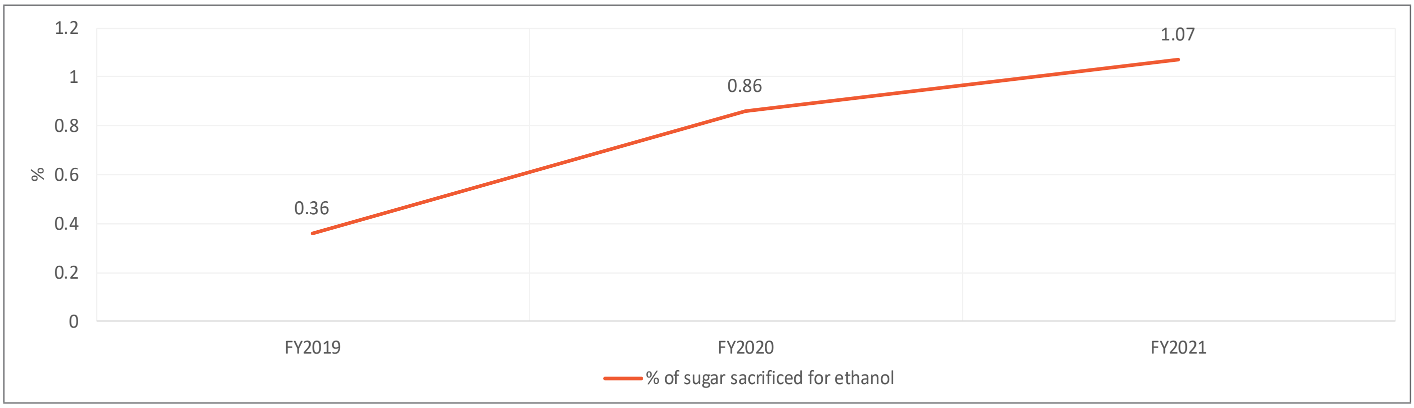


Source: Company; Sharekhan Research

Ethanol business revenue to post a 29% CAGR

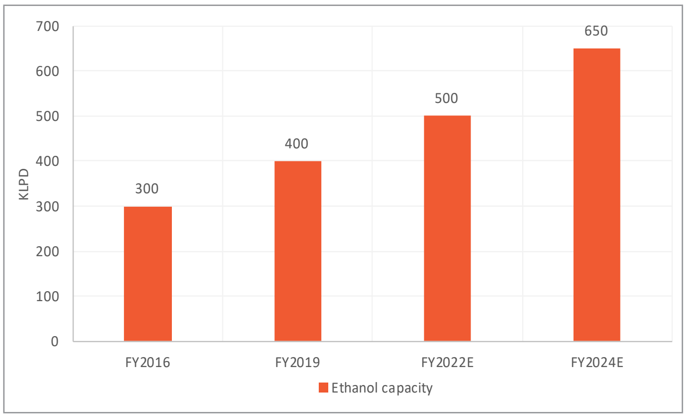
DSML intends to scale up its ethanol business with the objective to address a growing national priority, strengthen the non-sugar segment of its business, and enhance overall profitability. The company plans to enhance ethanol output through the B-Heavy route and cane juice route. DSML intends to invest judiciously in the ethanol business, either through a timely 'sacrifice' of sugar production when sugar realisations are low (and vice versa) as well through expansion of distillery capacity at Asmoli unit based in Uttar Pradesh from 150 KLPD to 250 KLPD, which was completed in January 2022. The company will be enhancing its distillery facility to 650 KLPD by FY2024 from 400 KLPD in FY2021 (enhanced to 500 KLPD in January 2022). Expansion in distillery capacity would help business revenue to post a 29% CAGR over FY2021-FY2024 to Rs. 1,245.2 crore. Contribution of the ethanol segment's revenue will go up to 27% by FY2024 from 14% in FY2021.

Increased sugar sacrifice over the years...



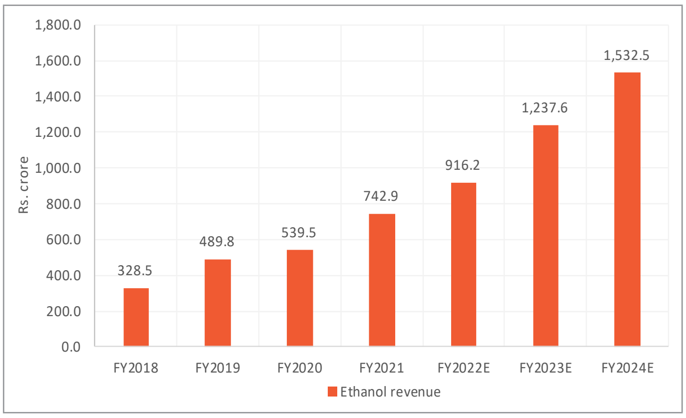
Source: Company; Sharekhan Research

...coupled with capacity expansion...



Source: Company, Sharekhan Research

...leading to higher ethanol revenue

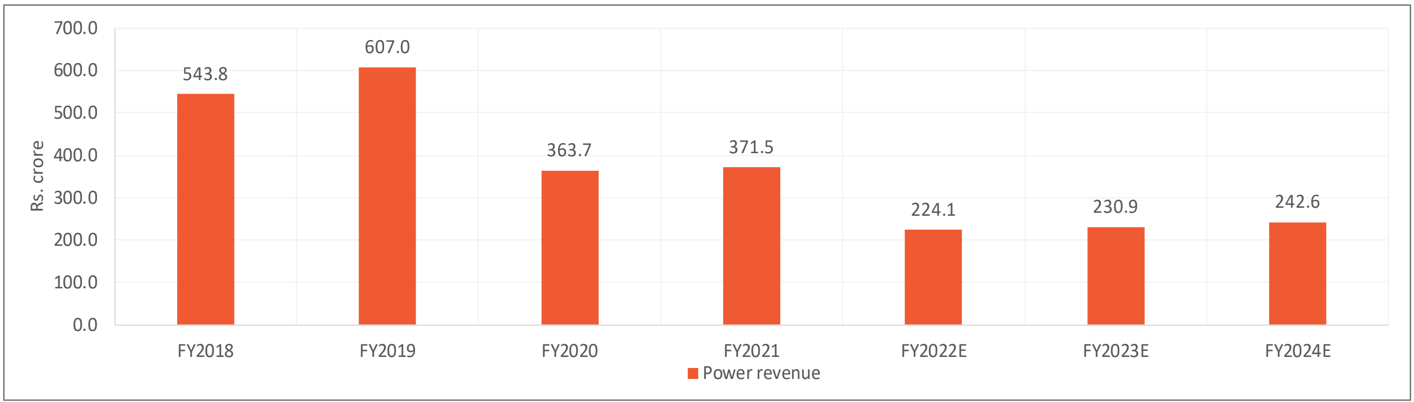


Source: Company, Sharekhan Research

Sustainable revenue from the co-generation business

The company's co-generation business generates sustainable and predictable revenue every year without being affected by market realities or factors. Over the years, the company enhanced its co-generation capacity to 216.5 MW in tranches, one of the largest in India. The company's power generation capacity accounted for 52% of its captive consumption, while the rest was channelised for merchant sale to the State Electricity Grid. DSML's cogenerated sales have been contracted for sales to the Uttar Pradesh State Electricity Board for 20 years against a pre-contracted tariff, providing long-term revenue visibility. The business provides an attractive hedge in a year marked by low sugar realisations.

Revenue generated from the power business



Source: Company; Sharekhan Research

Maximising business excellence through TPM leading to enhanced efficiencies and margins

In the past, 10-15% of mechanical circulations and 15-17% production machines reported repeated downtime, pulling down the organisational average. The company, in collaboration with TQMI International, introduced Total Productive Maintenance (TPM) in FY2018-FY2019, a comprehensive tool for enhancing efficiencies encompassing every business aspect (raw material, equipment, employees, safety, and quality). TPM was implemented across all the company's manufacturing facilities to replace legacy practices with modern equivalents. Equipment analysis was conducted; equipment 'personalities' were mapped; corresponding maintenance initiatives were identified; robotics (introduced earlier) was strengthened; new equipment investments were made; and training was intensified.

TPM implemented across key businesses

Sugar business:	Power business:
Despite having one of the shortest off-seasons (crushing went on till mid-June), the company placed emphasis on process strenghtening initiatives throughout the course of the year. Crush rate increased across all Dhampur units, sugar quality improved, heat and steam balance strengthened and overtime hours declined.	The company conducted a study on the slow boiler project. Because of the increased people engagement, a fresh perspective was perceived and modifications were made to ensure the reduction of bagasse consumption and overhead costs, a significant step towards sustainability.

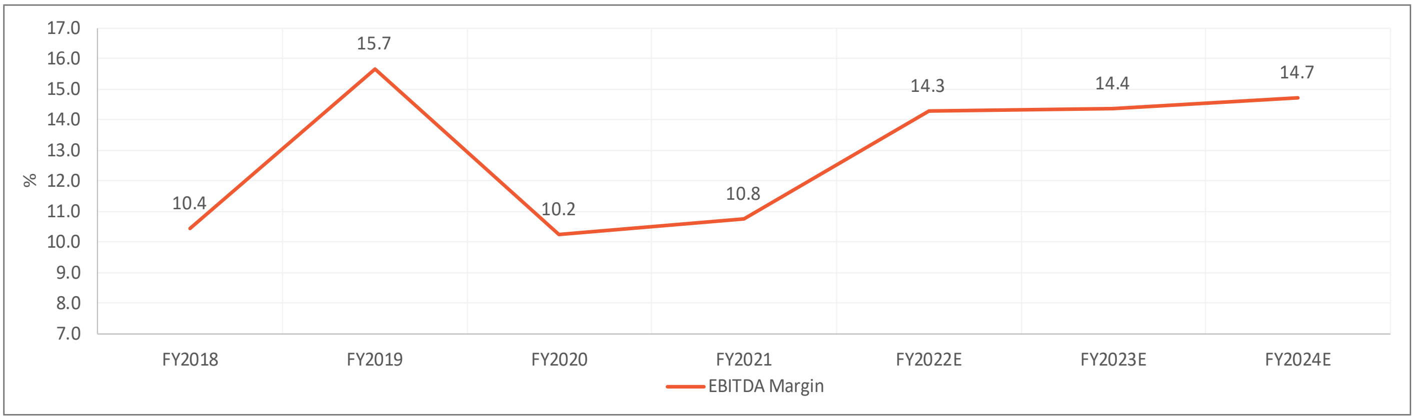
Source: Company; Sharekhan research

The company conducted regular training sessions on TPM and strengthened a kaizen culture, which resulted in notable improvements across the organisation. It encouraged employees to generate new ideas, analyse the root of all problems, and provide out-of-the-box solutions, enhancing overall human productivity along the way. The company has a weekly TPM measuring framework in place and, based on its parameters, can analyse the extent to which employees are fulfilling their responsibilities. Due to the implementation of TPM, breakdowns declined substantially, which will lead to improved EBITDA margin.

EBITDA margin to consistently improve:

DSML's EBITDA margin stood lower at 11% in FY2021 compared to peers at around 14-16%. With increased ethanol sales contribution to 25%+ in FY2024, driving efficiencies through TPM and sweating of existing assets will help DCM's EBITDA margin to improve to 15% by FY2024. Further, the company is focusing on enhancing value of its existing produce by producing country liquor (in response to the government's mandate to supply 18% of the molasses produced by the company to liquor manufacturers), manufacturing high-margin specialty chemicals, and increasing the manufacturing of refined and packaged sugar. This will help EBITDA margin to consistently improve in the medium to long term.

EBITDA margin to rise going ahead

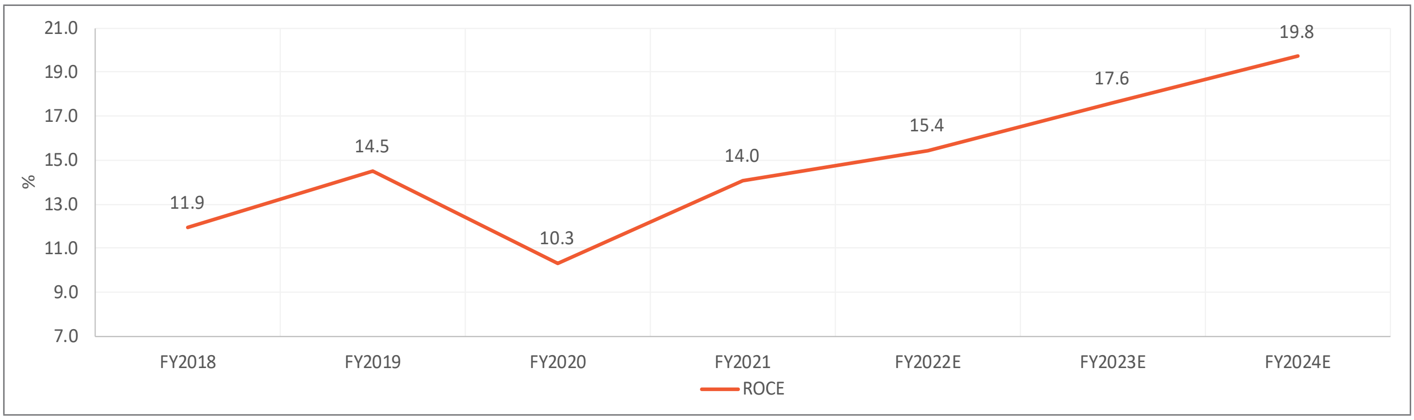


Source: Company; Sharekhan Research

Higher capacity utilisation to aid in improving ROCE

The company intends to freeze major capital expenditure, maximising asset productivity through efficiency-enhancing measures such as TPM, technology, and stronger workflows. DSML is focusing on sweating the crushing capacity across all its units through nominal equipment investments and superior operating practices. The company operated its sugar units at a capacity utilisation of 84% and distillery at 95% during FY2021. There will be an emphasis on crushing for around 200 days each sugar season. Any increase in capacity utilisation leads to higher output and revenue enabling the company to amortise fixed costs and generate superior economies of scale. An increase in capacity utilisation is ROCE-accretive, enhancing organisational value.

Improvement in ROCE in the coming years



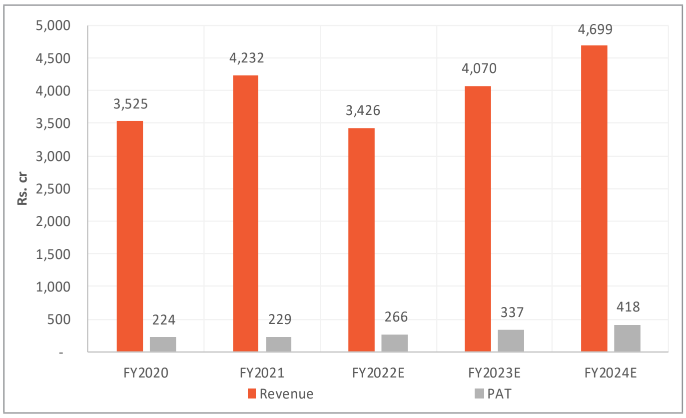
Source: Company; Sharekhan Research

Cumulative FCF to grow by ~Rs. 450 crore; Return profile to consistently improve

Strong earnings growth and improved working capital would help cumulative free cash flow (FCF) to grow by ~Rs. 450 crore over FY2021-FY2024 (despite ~Rs. 600 crore of capex for expansion of ethanol capacity). DSML reduced its debt by Rs. 830 crore over the last two years, aided by better working capital management and no major capex. The company can utilise higher cash flows to further reduce debt by Rs. 300 crore-320 crore in the coming years. Further, it can reward shareholders with higher dividend payout in the long run. Improved profitability and sustained reduction in debt on books would help return profile (RoE/RoCE) to improve substantially to 18.6%/19.8% in FY2024 from 15.7%/14.0% in FY2021.

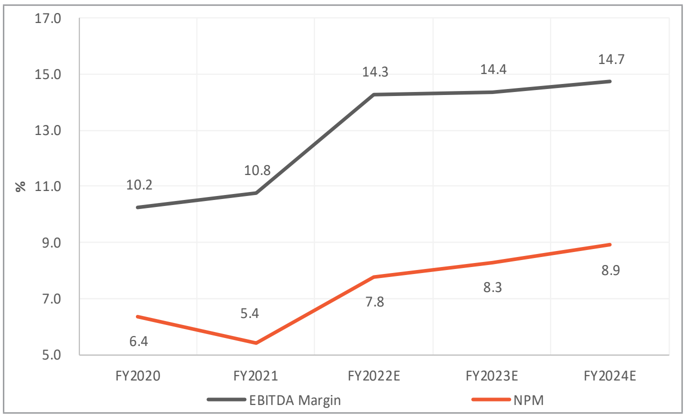
Financials in charts

Steady growth in revenue and PAT



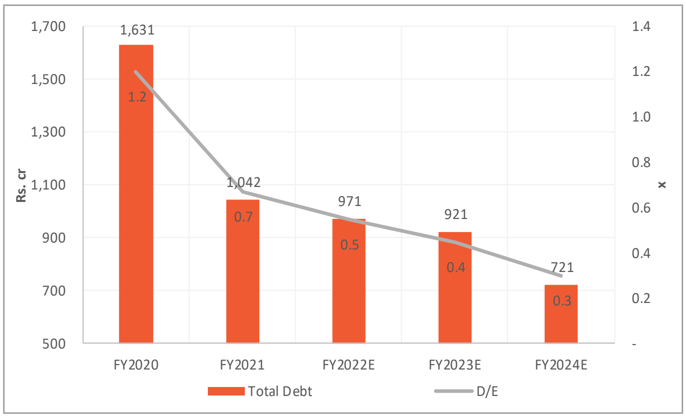
Source: Company, Sharekhan Research

Increased margins going ahead



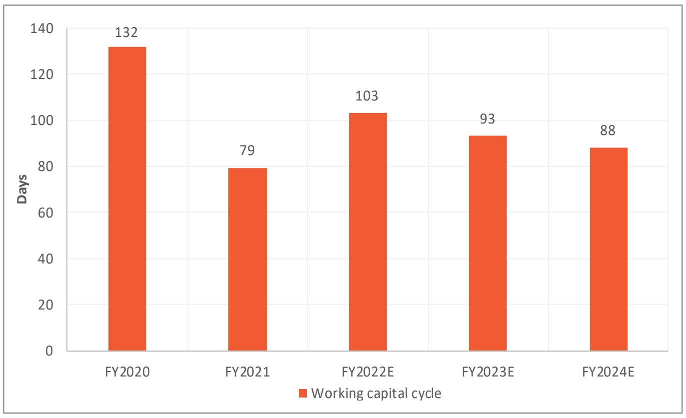
Source: Company, Sharekhan Research

Debt position to improve



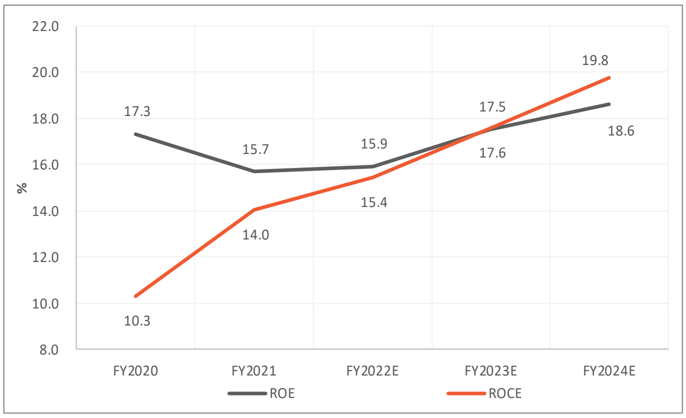
Source: Company, Sharekhan Research

Working capital days to remain stable



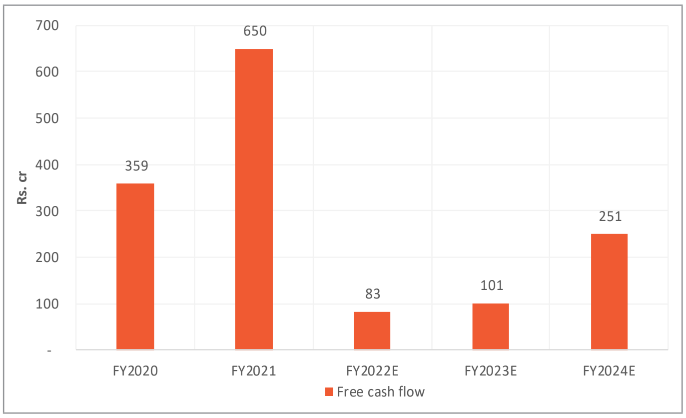
Source: Company, Sharekhan Research

Return ratios to increase



Source: Company, Sharekhan Research

Trend in free cash flows



Source: Company, Sharekhan Research

About company

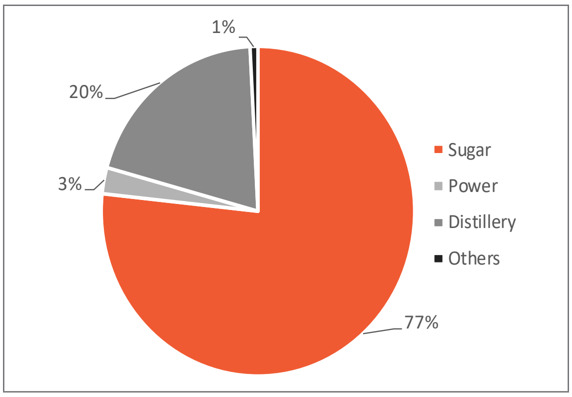
DSML is a prominent player in India's organised sugar business. The company was founded by Lala Ram Narain in 1933 with a cane crushing capacity of 300 tonnes per day (TCD). The company is one of India's oldest integrated sugar companies (engaged in sugar, ethanol, and chemicals manufactured at one end and power generation at the other). Currently, the company has five production facilities in Uttar Pradesh (Dhampur, Asmoli, Meerganj, Rajpura, and Mansurpur) with an aggregate manufacturing capacity of 45,500 TCD. DSML's distillery possesses a capacity of 500 KLPD, including 100 KLPD implemented in January 2022; the power co-generation segment comprises 216.5 MW.

DSML's unit locations and capacities

Capacity	Consolidated	Dhampur	Asmoli	Rajpura	Mansurpur	Meerganj
Sugar crushing (TCD)	45,500	15,000	9,000	8,500	8,000	5,000
Sugar refinery (TPD)	1,700		900		800	
Renewable energy (MW)	216.5 (Surplus ~125)	73	43.5	48	33	19
Distillery (KLPD)	500	250 (including country liquor)	250 (including Hand Sanitizers)	Molasses supplied to Dhampur and Asmoli distilleries		

Source: Company; Sharekhan Research

Revenue mix (FY2021)



Source: Company; Sharekhan Research

Sugar Business

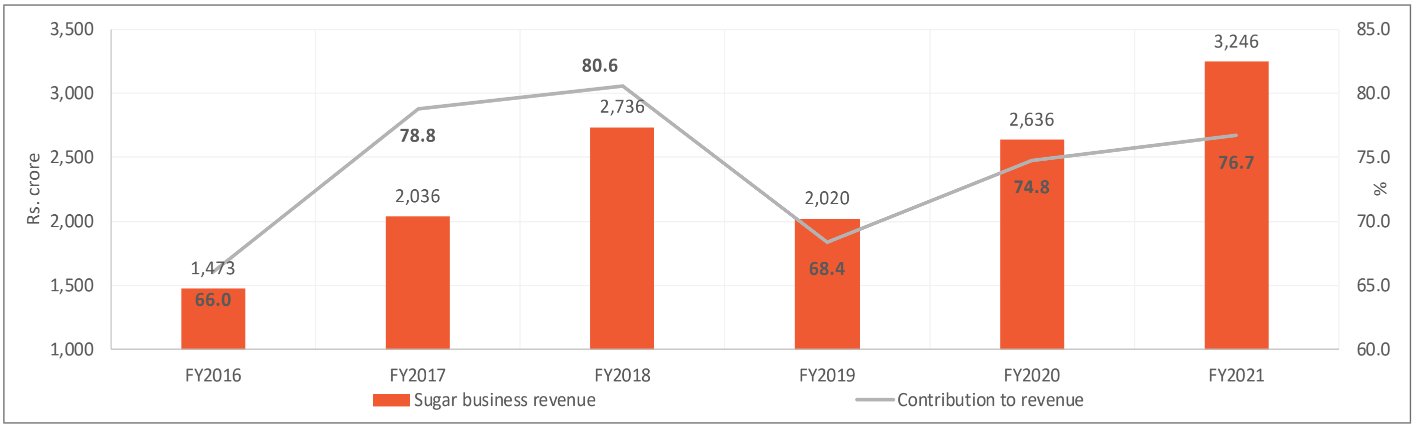
Since its establishment in 1933, DSML has retained its business as one of the leading sugar manufacturers in the country. The company possesses an aggregate cane crushing capacity of 45,500 TCD. The company's manufacturing units (Dhampur, Asmoli, Mansurpur, Rajpura, and Meerganj) are located in the cane rich regions of Uttar Pradesh. The company is engaged in the production of refined (packaged and branded), white, and retail sugar.

Strengths

- **Experience:** The company possesses an experience of over nine decades in sugar manufacturing.
- **Strategic location:** The company's five manufacturing units are located in the cane-rich regions of Uttar Pradesh.
- **Logistics advantage:** The company derives cane from within a 30 km radius from its manufacturing units, moderating logistics costs.
- **Technology:** The company implemented TPM and invested in cutting-edge technologies to enhance productivity.
- **Pioneers:** The company has two sugar refineries (Dhampur and Asmoli), enhancing the proportion of value-added sugar in its product mix.
- **Value addition:** The company has a significant proportion of value-added products in its overall mix, which strengthens its margins.

The company is attractively positioned to sweat resources. The company plans to double cane crushing over five years. DSML will focus on the production of superior quality sugar through complete TPM implementation and will continue to encourage farmers to plant high-yield varieties, improving sugar recovery by reducing cut-to-crush time, enhancing processes, and reducing sugar losses.

Sugar business revenue and revenue contribution



Source: Company; Sharekhan Research

Distillery business

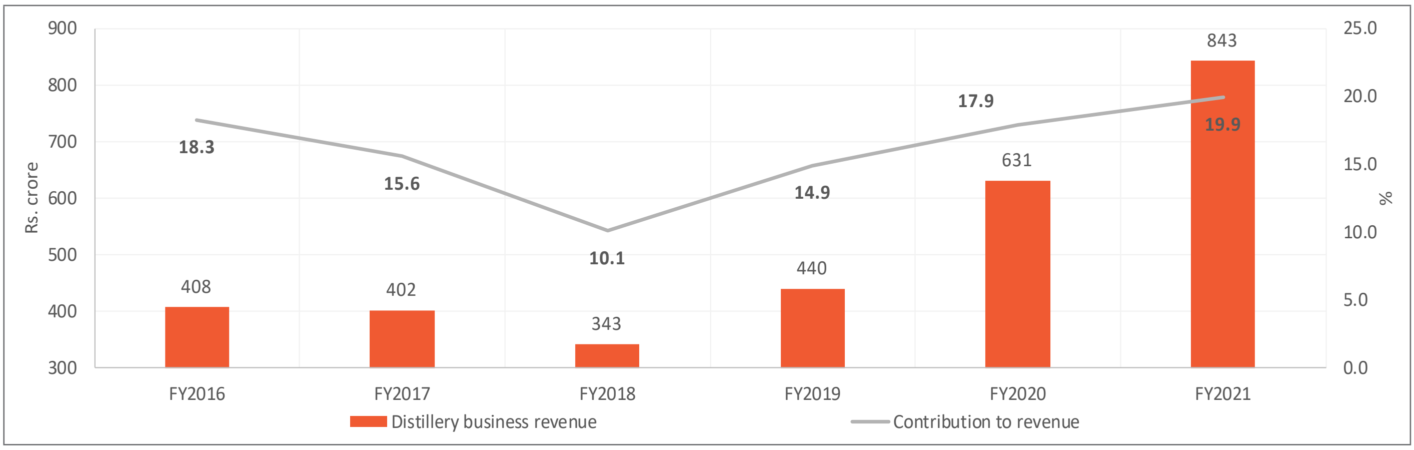
In 1991, DSML ventured into the downstream processing of molasses through the commissioning of its distillery with an installed capacity of 300 KLPD (gradually increased to 500 KLPD). In addition to producing ethanol, distillery manufactures rectified spirit, ENA, special denatured spirit, and ethyl acetate. The government's ethanol blending programme strengthened ethanol offtake by oil marketing companies and utilisation of the company's capacity. The company is one of the largest suppliers of B-Heavy ethanol in Uttar Pradesh.

Strengths

- **Pioneer:** The company was among the first Indian sugar companies to have commenced ethanol production in the 1990s.
- **Size:** The company is one of the largest manufacturers of ethanol and derivative products from sugarcane in India.
- **Relationships:** The company enjoys multi-year partnerships with oil marketing companies.
- **Captive utilisation:** The company utilises molasses in manufacturing ethanol. Captive utilisation stood at 100% in FY2021.

The company plans to commission capacity expansion and increase ethanol production. DSML is poised to supply ethanol produced from cane juice, which, in turn, could increase realisations.

Distillery business revenue and revenue contribution



Source: Company; Sharekhan Research

Co-generation (Power) business

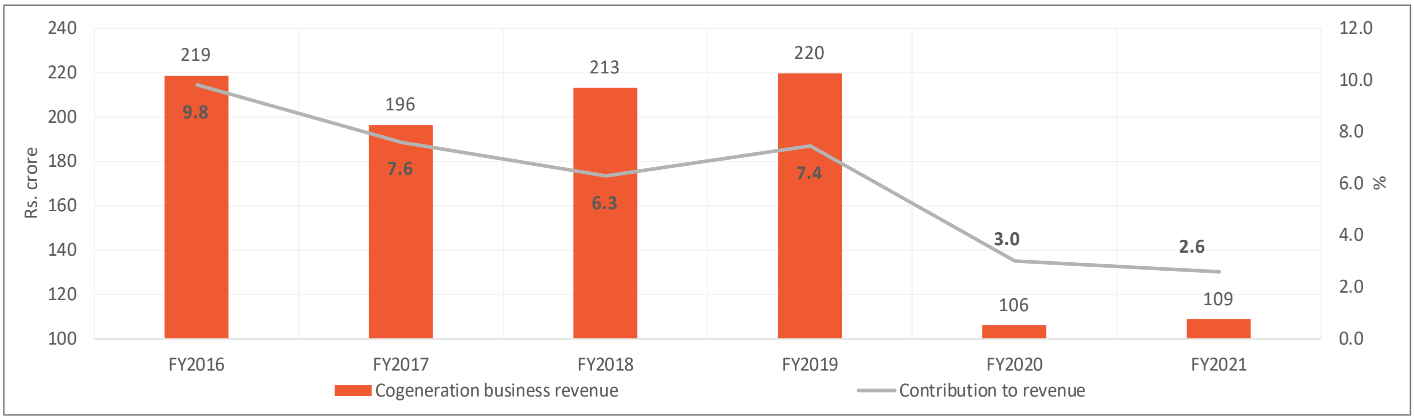
DSML ventured into the business of cogeneration more than two decades ago to enhance the monetisation of bagasse generated from manufacture of sugar. The company was among the first in the Indian sugar industry to install a 105kg/square centimetres boiler and 30 MW turbines, increasing the yield ratio of steam from bagasse. Over the years, the company enhanced its co-generation capacity to 216.5 MW in tranches, one of the largest in India. The company's power generation capacity accounted for 52% of its captive consumption in FY2021, while the rest was channelised for merchant sale to the Uttar Pradesh State Electricity Grid.

Strengths

- **Contemporary technology:** Over the years, the company has invested in state-of-the-art equipment, enhancing efficiency and productivity.
- **Captive utilisation:** The company utilises bagasse in power generation, an eco-friendly resource. Nearly 52% of its power requirement was serviced in-house.
- **Diversified business:** The company's power sales generated 7% of the overall revenue, enhancing revenue visibility.

Going forward, the company intends to invest in installing a new advanced boiler and turbine at Asmoli to generate more power with less steam. DSML intends to maximise efficiency and improve its steam-to-fuel ratio across plants.

Cogeneration business revenue and revenue contribution



Source: Company; Sharekhan Research

Key management personnel

- **Vijay Kumar Goel:** He is the Promoter of the company and the Chairman on board. He has been affiliated with the company and served on the Board since 1960. He has over 58 years of experience in the sugar industry. He has served as the President of the Indian Sugar Mills Association (ISMA).
- **Gaurav Goel:** He is the promoter and Managing Director of the company. He has been affiliated with the company and served on the board since 1994. He is a business management graduate from the American College of London, United Kingdom, and alumni Harvard Business School. He has over 25 years of experience in the sugar industry and has been the President of ISMA and Chairman of Indian Sugar Exim Corporation Limited in 2017-2018.
- **Sandeep Kumar Sharma:** He is the Chief Operating Officer and a whole-time director of the company. He has been associated with the company since 1980 and has over three decades of experience in administration and operations of sugar mills, power generation plants, and chemical plants.

Outlook and Valuation

DSML is currently trading at valuation of 10.5x/8.4x its FY2023E/FY2024E EPS, which is at a discount to some of the close peers. Focus on reducing cyclicality in the business and margin improvement coupled with strengthening of the balance sheet with reduction in debt would help valuation gap versus close peers to reduce in the coming years.

Sector View – Rise in supply for ethanol manufacturing to drive growth

As per ISMA's latest estimates, total sugar production for SY2021-SY2022 based on sugarcane production is estimated at 31.5 million. It is further estimated that due to diversion of sugarcane juice and B-heavy molasses, actual sugar production will drop by 3.4 million tonne. Therefore, estimated sugar production net of diversion is estimated at 28 million tonne, lower than the previous sugar season. The Government of Uttar Pradesh announced the State Advised Price (SAP) for the SS 2021-2022 at Rs. 250/quintal, higher than last season. Accordingly, now the early variety of sugarcane will cost Rs. 350/quintal. A revised ethanol policy, likely minimum support price (MSP) revision, quota-based sugar distribution, and export quota of 6 million tonne will benefit sugar companies in FY2022/FY2023 with stable sugar realisation. Increased international sugar prices would help Indian companies to get better export realisation for their produce. The government is targeting to achieve 20% blending of ethanol by 2025 (10% ethanol blending by 2021-2022), which would largely solve the problem of excess sugar over the medium term.

Company Outlook – Strong growth prospects ahead

The financial performance of DSML was largely influenced by the fortunes of the sugar industry. However, in the past two years, the company has focused on reducing the cyclicality in the industry. The company is focusing on achieving consistent earnings growth and enhancing shareholders' value by focusing on initiatives such as 1) generating more cane from its command areas, 2) driving operating efficiencies through TPM strategy, 3) investing judiciously in scaling up the ethanol business, and 4) deleveraging balance sheet with stable working capital and improved cash flows. Consistent improvement in profitability and reduction in debt will help DSML's earnings to post a 22% CAGR over FY2021-FY2024. Higher FCF generation will help debt to reduce in the coming years.

Valuation – Re-initiate coverage with Buy assigning a PT of Rs. 692

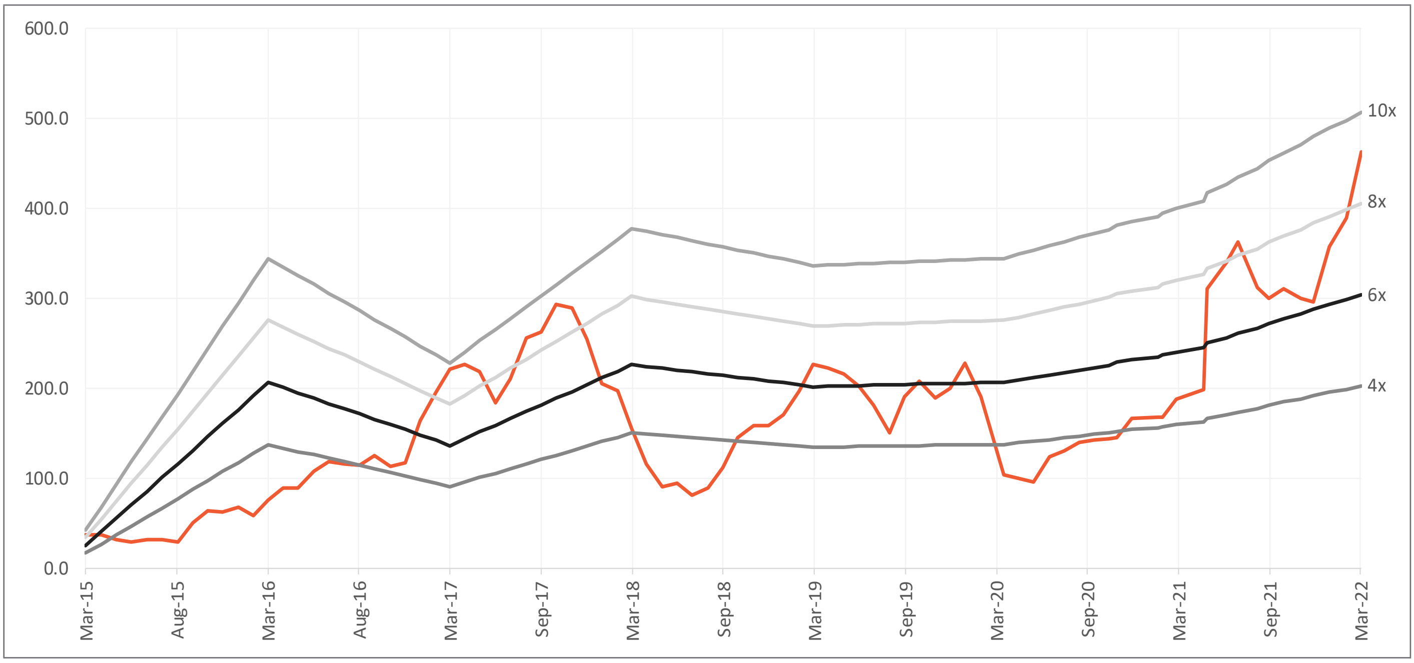
DSML is focusing on creating value for shareholders by strengthening the non-commodities business to achieve consistent earnings growth with higher EBITDA margins. The stock is currently trading at valuation of 10.5x/8.4x its FY2023E/FY2024E EPS, which is at a discount to some of the close peers. Strong earnings visibility, improving margin profile, and strengthening of the balance sheet would help the valuation gap with close peers to reduce in the coming years. Hence, we are re-initiating coverage on the stock with a Buy recommendation, assigning a PT of Rs. 692 (valuing the stock at 11x its FY2024E EPS, which is at 27% discount to the target multiple of Balrampur Chini Mills [BCML]).

Peer Comparison

Particulars	P/E (x)			EV/EBITDA (x)			RoCE (%)		
	FY21	FY22E	FY23E	FY21	FY22E	FY23E	FY21	FY22E	FY23E
Balrampur Chini	21.6	20.1	15.8	18.3	17.9	19.9	15.7	16.5	19.0
Triveni Engineering	26.9	19.6	16.4	16.0	13.4	11.2	17.7	20.3	22.2
Dhampur Sugar	15.4	13.3	10.5	9.9	9.1	7.5	14.0	15.4	17.6

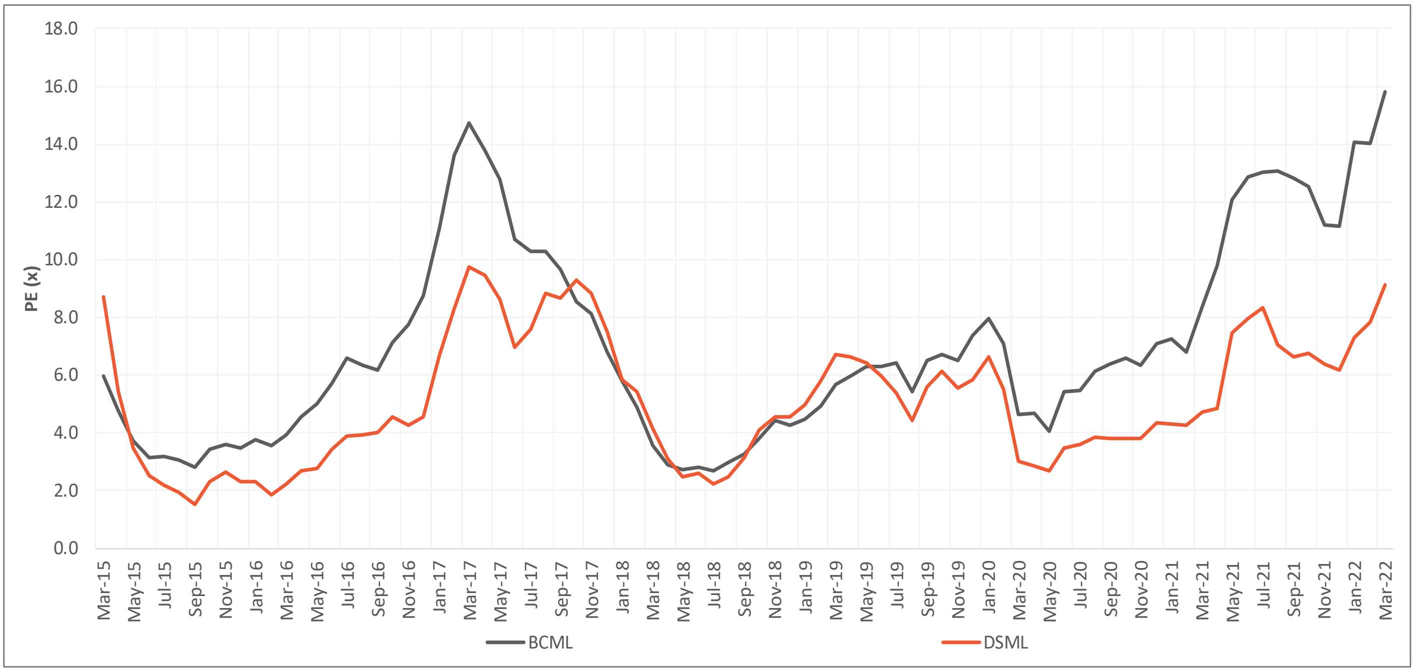
Source: Company, Sharekhan estimates

One-year forward P/E (x) band



Source: Sharekhan Research

Valuation gap: BCML vs. DSML



Source: Sharekhan Research

Key Financials

Statement of Profit and Loss Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Total Revenue	**3,525.1**	**4,231.5**	**3,426.3**	**4,069.7**	**4,699.3**
% y-o-y growth	19.3	20.0	-19.0	18.8	15.5
Raw Material Cost	2,755.6	3,300.6	2,545.7	3,044.1	3,508.0
Employee Cost	140.7	147.1	151.5	156.1	160.8
Other Expenses	267.6	328.4	239.8	284.9	338.3
Total Operating Cost	**3,163.9**	**3,776.1**	**2,937.1**	**3,485.1**	**4,007.1**
EBITDA	**361.2**	**455.4**	**489.2**	**584.6**	**692.2**
% y-o-y growth	-21.9	26.1	7.4	19.5	18.4
EBITDA Margin (%)	10.2	10.8	14.3	14.4	14.7
Other Income	31.1	17.5	8.0	10.0	10.0
Interest & Other Financial Cost	100.6	79.9	60.4	56.8	49.3
Depreciation	76.0	77.7	79.0	84.5	90.1
Profit Before Tax	**215.7**	**315.3**	**357.8**	**453.4**	**562.8**
Tax Expense	-8.4	86.2	92.0	116.5	144.6
Adjusted PAT	**224.0**	**229.1**	**265.9**	**336.9**	**418.2**
% y-o-y growth	-10.7	2.3	16.0	26.7	24.1
NPM (%)	6.4	5.4	7.8	8.3	8.9
Exceptional Items	-	-	-	-	-
Reported PAT	**224.0**	**229.1**	**265.9**	**336.9**	**418.2**

Source: Company; Sharekhan estimates

Balance sheet Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Equity Capital	66.5	66.5	66.5	66.5	66.5
Reserves & Surplus	1,295.2	1,493.6	1,711.5	2,000.3	2,354.6
Net Worth	**1,361.7**	**1,560.1**	**1,777.9**	**2,066.8**	**2,421.0**
Deferred Tax Liabilities (Net)	0.0	33.7	33.7	33.7	33.7
Total Borrowings	**1,630.7**	**1,041.9**	**971.0**	**921.0**	**721.0**
Capital Employed	**2,992.6**	**2,635.6**	**2,782.6**	**3,021.5**	**3,175.7**
Net Block	1,634.7	1,611.7	1,732.7	1,898.2	1,958.1
Capital WIP	6.8	21.2	25.0	15.0	15.0
Goodwill	2.9	2.5	2.8	2.8	2.8
Investment	2.3	2.6	2.6	2.6	2.6
Current Assets	**2,222.5**	**1,832.8**	**1,800.3**	**2,004.8**	**2,217.9**
Inventories	1,604.9	1,293.6	1,314.2	1,449.5	1,609.3
Sundry Debtors	343.2	296.7	262.8	312.2	360.5
Cash and Bank Balance	9.9	72.4	44.1	47.3	33.8
Fixed Deposits with Bank	6.5	7.8	0.0	0.0	0.0
Loans & Advances	12.6	10.9	12.5	12.5	12.5
Other Current Assets	245.4	151.5	166.7	183.3	201.7
Less: Current Liabilities & Provisions	**876.6**	**835.2**	**780.7**	**901.9**	**1,020.7**
Trade Payables	606.3	599.0	523.0	620.6	713.6
Other Current Liabilities & Provisions	270.2	236.2	257.7	281.3	307.1
Net Current Assets	**1,345.9**	**997.7**	**1,019.6**	**1,102.9**	**1,197.2**
Total Assets	**2,992.6**	**2,635.6**	**2,782.6**	**3,021.5**	**3,175.7**

Source: Company; Sharekhan estimates

Cash flow statement

Rs cr

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Operating cash flow before working capital changes	300.1	306.8	344.9	421.3	508.3
Changes in working capital	145.2	412.0	-58.0	-80.1	-107.7
Cash flow from operating activities	**445.2**	**718.8**	**286.9**	**341.2**	**400.5**
Cash flow from investing activities	**-79.3**	**-70.2**	**-196.3**	**-240.0**	**-150.0**
Cash flow from financing activities	**-369.2**	**-586.0**	**-118.9**	**-98.0**	**-264.0**
Net change in cash and cash equivalents	**-3.3**	**62.6**	**-28.3**	**3.2**	**-13.4**
Opening cash balance	13.2	9.9	72.4	44.1	47.3
Closing cash balance	**9.9**	**72.4**	**44.1**	**47.3**	**33.8**

Source: Company; Sharekhan estimates

Key ratios

Particulars	FY2020	FY2021	FY2022E	FY2023E	FY2024E
Margins & tax rate (%)					
GPM	21.8	22.0	25.7	25.2	25.4
EBITDA Margin	10.2	10.8	14.3	14.4	14.7
NPM	6.4	5.4	7.8	8.3	8.9
Tax rate	-3.9	27.3	25.7	25.7	25.7
Cost matrix (% of revenue)					
Raw material cost	77.0	76.2	72.5	73.0	72.9
Excise duty	1.2	1.8	1.8	1.8	1.8
Employee cost	4.0	3.5	4.4	3.8	3.4
Other expenses	3.3	2.9	2.8	2.8	2.8
Consumption of stores, spares & other manufacturing expenses	1.5	1.3	1.0	1.0	1.2
Repair & Machinery	1.2	1.3	1.3	1.3	1.3
Selling expenses	1.6	2.2	2.0	2.0	2.0
Total operating cost	**89.8**	**89.2**	**85.7**	**85.6**	**85.3**
Growth ratios (y-o-y %)					
Revenues	19.3	20.0	-19.0	18.8	15.5
Operating profit	-21.9	26.1	7.4	19.5	18.4
PBT	-32.4	46.2	13.5	26.7	24.1
Adjusted PAT	-10.7	2.3	16.0	26.7	24.1
Reported PAT	-10.7	2.3	16.0	26.7	24.1
Per share (Rs.)					
CMP	532	532	532	532	532
Adjusted EPS	33.7	34.5	40.0	50.7	62.9
Cash EPS	45.2	46.2	51.9	63.4	76.5
Book value per share (BVPS)	204.9	234.8	267.6	311.0	364.3
DPS	6.0	6.0	6.0	6.0	8.0
Valuation ratios (x)					
P/E	15.8	15.4	13.3	10.5	8.4
Price / Book value (BV)	2.6	2.3	2.0	1.7	1.5
EV / EBITDA	14.3	9.9	9.1	7.5	6.1
EV / Sales	1.5	1.1	1.3	1.1	0.9
Market cap / Sales	1.0	0.8	1.0	0.9	0.8
Working capital (days)					
Inventory days	166	112	140	130	125
Debtors Days	36	26	28	28	28
Creditors Days	70	58	65	65	65
Operating cash cycle	**132**	**79**	**103**	**93**	**88**
Financial ratios					
Debt / Equity (x)	1.2	0.7	0.5	0.4	0.3
Dividend Payout Ratio (%)	21.4	20.9	18.1	14.2	15.3
RoE (%)	17.3	15.7	15.9	17.5	18.6
RoCE (%)	10.3	14.0	15.4	17.6	19.8

Source: Company; Sharekhan estimates

About company

DSML is a prominent player in India's organised sugar business. The company was founded by Lala Ram Narain in 1933 with a cane crushing capacity of 300 TCD. The company is one of India's oldest integrated sugar companies (engaged in sugar, ethanol, and chemicals manufactured at one end and power generation at the other). Currently, the company has five production facilities in Uttar Pradesh (Dhampur, Asmoli, Meerganj, Rajpura, and Mansurpur) with an aggregate manufacturing capacity of 45,500 TCD. DSML's distillery possesses a capacity of 500 KLPD; the power co-generation segment comprises 216.5 MW.

Investment theme

DSML is one of the largest sugar companies in India with integrated facilities of 45,500 tonnes per day (cane crushing capacity), distillery capacity of 500 KLPD, and co-generation capacity of 216.5 MW. The company is focusing on achieving consistent earnings growth and enhancing shareholders' value by focusing on initiatives such as 1) generating more cane from its command areas, 2) driving operating efficiencies through the TPM strategy, 3) investing judiciously in scaling up the ethanol business, and 4) deleveraging balance sheet with stable working capital and improved cash flows. Consistent improvement in profitability and reduction in debt will help DSML's earnings to post a 22% CAGR over FY2021-FY2024.

Key Risks

- Decline in sugar production would impact the company's revenue and acts as a key risk to our earnings estimates.
- Change in the government's policies towards ethanol blending would affect the company's profitability.

Additional Data

Key management personnel

Vijay Kumar Goel	Chairman
Gaurav Goel	Managing Director
Sandeep Kumar Sharma	Chief Operating Officer
Susheel Kumar Mehrotra	Chief Financial Officer
Aparna Goel	Company Secretary & Compliance Officer

Source: Company Website

Top 10 shareholders

Sr. No.	Holder Name	Holding (%)
1	Anil Kumar Goel	9.00
2	Seema Goel	3.70
3	Dimentional Fund Advisors LP	1.01
4	Frank Russell Company	0.16
5	Acadian Asset Management LLC	0.14
6	WisdomTree Investments Inc	0.13
7	Grantham Mayo Van Otterloo & Co LLC	0.09
8	State Street Corp	0.04
9	American Century Cos Inc	0.02
10	Kulkarni Suchet	0.01

Source: Bloomberg

Understanding the Sharekhan 3R Matrix

Right Sector	
Positive	Strong industry fundamentals (favorable demand-supply scenario, consistent industry growth), increasing investments, higher entry barrier, and favorable government policies
Neutral	Stagnancy in the industry growth due to macro factors and lower incremental investments by Government/private companies
Negative	Unable to recover from low in the stable economic environment, adverse government policies affecting the business fundamentals and global challenges (currency headwinds and unfavorable policies implemented by global industrial institutions) and any significant increase in commodity prices affecting profitability.
Right Quality	
Positive	Sector leader, Strong management bandwidth, Strong financial track-record, Healthy Balance sheet/cash flows, differentiated product/service portfolio and Good corporate governance.
Neutral	Macro slowdown affecting near term growth profile, Untoward events such as natural calamities resulting in near term uncertainty, Company specific events such as factory shutdown, lack of positive triggers/events in near term, raw material price movement turning unfavourable
Negative	Weakening growth trend led by led by external/internal factors, reshuffling of key management personal, questionable corporate governance, high commodity prices/weak realisation environment resulting in margin pressure and detoriating balance sheet
Right Valuation	
Positive	Strong earnings growth expectation and improving return ratios but valuations are trading at discount to industry leaders/historical average multiples, Expansion in valuation multiple due to expected outperformance amongst its peers and Industry up-cycle with conducive business environment.
Neutral	Trading at par to historical valuations and having limited scope of expansion in valuation multiples.
Negative	Trading at premium valuations but earnings outlook are weak; Emergence of roadblocks such as corporate governance issue, adverse government policies and bleak global macro environment etc warranting for lower than historical valuation multiple.

Source: Sharekhan Research

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