Kaira District Cooperative Milk Producers' Union Limited

January 06, 2023

Ratings

Facilities	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	161.80 (Reduced from 166.80)	CARE AA+; Stable (Double A Plus; Outlook: Stable)	Reaffirmed
Long-term / Short-term bank facilities	120.00	CARE AA+; Stable / CARE A1+ (Double A Plus; Outlook: Stable/ A One Plus)	Reaffirmed
Short-term bank facilities	1,235.00 (Enhanced from 1,230.00)	CARE A1+ (A One Plus)	Reaffirmed
Total bank facilities	**1,516.80** **(₹ One thousand five hundred sixteen crore and eighty lakh only)**		

Details of facilities in Annexure-1.

Detailed rationale and key rating drivers

The ratings assigned to the bank facilities of Kaira District Cooperative Milk Producers' Union Limited (KDUL, the union) continue to be underpinned by its established operations as one of the largest unions of Gujarat Co-operative Milk Marketing Federation Ltd. (GCMMF), which has a leading market position in the organised segment of the Indian dairy industry with well-recognised brands, 'Amul' and 'Sagar', along with good growth prospects for the dairy industry.

The ratings also continue to derive strength from the union's ownership of the brand 'Amul', its growing scale of operations, geographically diversified revenue stream, diversified product portfolio with high share of value-added products to its sales mix, and its presence in the consumer and food products' retail and restaurant business. The ratings also derive strength from the sizeable milk procurement network within and outside Gujarat, presence of a cash flow mechanism towards payment of milk procurement prices, which ensures adequate cushion for debt servicing and its strong liquidity; and the same mechanism is expected to continue going forward.

The long-term rating, however, continues to be constrained by the environment and epidemic-related event risks associated with geographically concentrated milk procurement, exposure to the risks associated with regulatory changes and volatile skimmed milk powder (SMP) prices as well as union's debt-funded capex plans with associated implementation and stabilisation risks.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- Significant growth in the scale of operations through greater geographical diversification of both its sales and sourcing; along with widening of its product profile.

Negative factors – Factors that could lead to negative rating action/downgrade:

- Any adverse changes in the Amul cooperative structure and/ or weakening in the credit profile of GCMMF.
- Any environment and epidemic-related factors in the milk-procuring region of the union having a significant impact on the union's operations for a long term.
- Any adverse changes in the SMP prices or regulations governing dairy industry having material impact on the extent of returns/ milk procurement prices paid to the farmer members on a sustained basis.
- Deterioration in the overall gearing beyond 6x, on a sustained basis.

Detailed description of the key rating drivers

Key rating strengths

Member of the strong apex dairy marketing federation, GCMMF, which has a significant market share in the organised dairy industry in India: KDUL is one of the significant contributing member dairy processing units (DPUs) amongst the 18-member DPUs of GCMMF, as indicated by the 22% contribution to GCMMF's total sales during FY22 (refers to the period April 1 to March 31). GCMMF has established the brands 'Amul' and 'Sagar' as the leading dairy brands in India and facilitates decision making of its member DPUs. GCMMF, through its DPUs, built on a cooperative structure, has a strong milk collection base of more than 36 lakh farmers spread across over 18,565 villages, and the daily milk collection of all member DPUs aggregates around 264 lakh litres per day (LLPD) for FY22 (FY21: 246 LLPD). Furthermore, with a collective milk processing capacity of 390 LLPD, GCMMF commands a prominent market share in pouched milk as well as in various milk products (ranging from 40%-73% market share) in the Indian dairy industry.

Strong pricing power over dairy products: GCMMF, having a prominent market share in the Indian organised dairy industry across various dairy products, possesses strong pricing power for its products and largely heralds the prices of milk and milk products in the country. Furthermore, GCMMF and its DPUs operate on a two-step pricing mechanism, which results in robust

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

cash flows whereby the aim is to pass on remunerative returns to the farmer members by way of milk procurement prices but only after ensuring adequate cushion for meeting its upcoming debt servicing, capital and operational expenses. Considering the inherent strengths of this business model, CARE Ratings expects the said mechanism to sustain going forward.

Growing and geographically diversified operations along with wide product portfolio and presence in retail and restaurant business: KDUL's revenue stream is geographically diversified, with around 45% of its sales being contributed from outside Gujarat. Apart from pouched liquid milk, the union also manufactures a wide range of value-added dairy products, as well as non-dairy products, such as bakery items, with value-added dairy products contributing around 65% of its FY22 sales. Furthermore, its scale of operations witnessed a 20% increase in FY22 to ₹10,335 crore as against FY21 (₹8,600 crore) largely owing to growth of around 15% in the sales of milk, butter, paneer and more than 30% in sales of various other dairy products like ice-cream, ghee, SMP, etc.
Furthermore, the union also has a presence in retail and restaurant business. During FY17, KDUL had commenced its own retail outlet (i.e., Amul Green) and restaurant (i.e., Amul Foodland). It has resorted to online sales for Amul Green via e-commerce giants, which has resulted in increase in its sale. However, the sale of retail and food business presently has lower contribution to the union's sales, though it is expected to pick-up gradually with encouraging response.

Robust milk procurement network with measures undertaken to enhance milk production: KDUL has a strong milk procurement network of 7.13 lakh farmers, who are the ultimate owners of the union and hence ensure stability in milk supply. Besides Gujarat, the union has its own milk-processing plants in Maharashtra (Virar and Pune), Punjab and has leased plants in West Bengal, Punjab, Assam, Bihar and Maharashtra. Milk procurement has witnessed a Year-on-Year (Y-o-Y) growth rate of around 15% over the past two years ended FY22 owing to good milk collection. Also, average milk procurement prices paid to the farmers have witnessed compounded annual growth rate (CAGR) of 7% over the past five years at ₹837.22/kg-fat during FY22. Such remunerative price paid to the farmers over the years is envisaged to help it in sustaining its healthy milk procurement going forward. KDUL also provides various products such as cattle feed and services to its farmer members to enhance milk production and for healthy up-bringing of the cattle.

Good growth prospects for the dairy industry: During FY21, the revenues of the organised dairy sector was affected to an extent owing to the impact of COVID-19 pandemic on the institutional demand. To protect the cooperatives from the COVID-19 pandemic situation and for ensuring regular and remunerative payment to the farmers, the Ministry of Fisheries, Animal Husbandry and Dairying, Government of India, introduced a new scheme 'Interest subvention on Working Capital Loans for Dairy sector'. The scheme made provisions for giving interest subvention of 2% per annum, with an additional incentive of 2% per annum to be given in case of prompt and timely repayment/interest servicing on working capital blocked in SMP, whole milk powder (WMP), white butter and ghee for FY21. However, after the impact of COVID-19 in FY21 and the second wave in Q1FY22, the dairy sector rebounded significantly owing to the strong demand revival of milk and its value-added products. Also, the government is progressively taking initiatives to promote the dairy industry in India, in which inclination towards cattle breeding, clean milk production, dairy development and cattle feed management are included. In this regard, it has implemented the *Rashtriya Gokul Mission* from FY22 to improve productivity and enhance milk production. These schemes aim to improve remuneration for farmers for which an allocation of ₹2,400 crore has been made over the next five years.
In the medium term, the demand for dairy and its allied products is expected to witness healthy demand due to pick-up in demand of value-added products, steady sales of liquid milk and rising retail rates in the year. Over the long-term, the demand outlook is expected to remain favourable due to various factors, such as steady supply of milk with India being world's largest milk producer and government extending various interest subvention schemes / incentives for modernisation of dairy infrastructure to promote its higher production; along with growing demand for milk and milk products backed by increasing population and per capita consumption, increase in expenditure on packaged food, brand awareness and urbanisation. The growth would be primarily driven by increase in the demand for value-added milk products, which is also margin accretive for the players.

Liquidity: Strong
KDUL's liquidity remains strong with the union deriving comfort from sales made on 'cash and carry' basis with daily receipts from GCMMF, while provisional payment to VCS is made on every 10-days' interval, resulting in a lean operating cycle. Moreover, the union also has the flexibility to change the prices paid to the farmers as the funds available with a DPU is passed on to the VCS by way of raw material prices only after retaining a reasonable amount for its debt repayments, capital expenditure and operational expenses during the year. This has also resulted in very negligible utilisation of KDUL's fund-based working capital limits over the past 12 months ended November 2022. Furthermore, it had free cash and bank balance of ₹106.87 crore as on March 31, 2022.

Key rating weaknesses
Debt-funded expansion and up-gradation of its various facilities planned over medium–term: KDUL has been undertaking expansion and up-gradation of its facilities owing to increase in milk supply witnessed over the years and growing demand for value-added dairy products. Presently, the union has envisaged capex towards setting up of automatic milk sampling system, expansion of milk processing and other value-added products at Anand, establishment of an ultra-high temperature (UHT) plant at Khatraj, a new chocolate plant at Mogar, an ice-cream plant at Pune, and expansion of milk processing facilities coupled with value-added products in Punjab and various other capex for machineries for operations at all the facilities. The same, if undertaken, is expected to be pre-dominantly debt funded, which would entail higher requirement of funds for capex and operational expenses. As indicated by the union's management, all these capex plans shall be contingent upon surplus availability and prevalent dairy industry scenario.

Thus, gradual phasing and stabilisation of this capex to optimise the payment of milk prices to the farmers and maintenance of comfortable liquidity in the union shall be crucial from the credit perspective.

Exposure to environmental and epidemic-related event risks associated with geographically concentrated milk procurement: DPUs, including KDUL, are exposed to the environmental risks (such as outbreak of epidemic/ bovine diseases) associated with concentration in milk collection; since most of their milk procurement is from one district and its surrounding villages. KDUL has built up its milk procurement network outside Gujarat with non-member VCS in Kolkata, Pune, Mumbai, Chennai, Assam, Bihar and Punjab and contribution of the same to total milk procurement has increased from 20% in FY19 to 26% in FY22. However, majority of its total milk procurement in FY22 continued to be from its own milk shed area in Gujarat (i.e., around 72%), hence, the union remains exposed to the risks associated with concentrated milk collection. Recently, there has been overall decline in availability of milk due to lumpy skin disease in animals albeit KDUL has very negligible impact of the same.

Analytical approach: Standalone with group support.

The milk suppliers (farmer owners) are at the base of the dairy cooperative structure. Profit is not a motive of organisations working under this structure and maximum returns to these dairy farmers are passed on by way of milk procurement prices after ensuring retention of a reasonable amount for their debt repayment, capital and operational expenses. Furthermore, the Amul dairy cooperative structure has a robust cash flow mechanism, wherein the Marketing Federation (GCMMF) releases funds to its DPUs through a two-step price payment mechanism during the year, and DPUs make payments to VCS, which in-turn distribute payment to the member farmers for their milk supply. Hence, the credit risk of such cooperative sector entities is assessed based on the sustainability and growth of the structure, stability of the milk supply base, trend in milk procurement and that of the average annual milk procurement prices paid to the dairy farmers, along with reach of its distribution network and the strong brand of 'Amul' created by the federation.

Applicable criteria

Criteria on assigning 'outlook' and 'credit watch' to credit ratings
CARE's policy on default recognition
Rating methodology - Notching by factoring linkages in ratings
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating methodology - Short term instruments
Rating methodology - Manufacturing companies

About the company

Incorporated in 1964, KDUL is the first dairy cooperative of the three-tier 'Amul Model' or 'Anand Pattern' and is popularly known as 'Amul Dairy' after its brand name. After the establishment of KDUL, the 'Amul Model' of having farmers (milk suppliers) at its base was replicated throughout the country, giving birth to other similar cooperative unions.

KDUL procures milk from 1,259-member VCS consisting of 7.13 lakh farmers, which hold the entire shareholding in KDUL. It is one of the largest amongst the 18 member DPUs of GCMMF with a total milk processing capacity of 68.85 LLPD as on March 31, 2022, across its dairy plants located in Gujarat, Maharashtra, West Bengal, Punjab, Assam and Bihar. Apart from milk processing, KDUL also manufactures other value-added milk-based products, including butter, cheese, paneer, ghee, curd and ice-cream.

Brief Financials (₹ crore)	FY21 (A)	FY22 (A)	8MFY23 (Prov.)
Total operating income	8,600	10,335	7,589
PBILDT	206	201	NA
PAT	32	37	NA
Overall gearing (times)	1.92	1.38	NA
Interest coverage (times)	4.47	6.73	NA

A: Audited; Prov.: Provisional; NA – Not available; Financials are classified as per CARE Ratings' standards.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Not applicable

Complexity level of various instruments rated for this company: Please refer Annexure-3

Annexure-1: Details of facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term loan	-	-	-	September 2026	161.80	CARE AA+; Stable
Fund-based - ST-Bank overdraft	-	-	-	-	580.00	CARE A1+
Non-fund-based - LT/ ST-BG/LC	-	-	-	-	120.00	CARE AA+; Stable / CARE A1+
Term loan-Short term	-	-	-	-	655.00	CARE A1+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - ST-Bank overdraft	ST	580.00	CARE A1+	-	1)CARE A1+ (02-Nov-21)	1)CARE A1+ (04-Jan-21)	1)CARE A1+ (09-Mar-20) 2)CARE A1+ (01-Apr-19)
2	Non-fund-based - LT/ ST-BG/LC	LT/ST*	120.00	CARE AA+; Stable / CARE A1+	-	1)CARE AA+; Stable / CARE A1+ (02-Nov-21)	1)CARE AA+; Stable / CARE A1+ (04-Jan-21)	1)CARE AA+; Stable / CARE A1+ (09-Mar-20) 2)CARE AA+; Stable / CARE A1+ (01-Apr-19)
3	Fund-based - LT-Term loan	LT	161.80	CARE AA+; Stable	-	1)CARE AA+; Stable (02-Nov-21)	1)CARE AA+; Stable (04-Jan-21)	1)CARE AA+; Stable (09-Mar-20) 2)CARE AA+; Stable (01-Apr-19)
4	Term loan-Short term	ST	655.00	CARE A1+	-	1)CARE A1+ (02-Nov-21)	1)CARE A1+ (04-Jan-21)	1)CARE A1+ (09-Mar-20) 2)CARE A1+ (01-Apr-19)

*Long term/Short term.

Annexure-3: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based - LT-Term loan	Simple
2	Fund-based - ST-Bank overdraft	Simple
3	Non-fund-based - LT/ ST-BG/LC	Simple
4	Term loan-Short term	Simple

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

Annexure-4: Bank lender details for this company
To view the lender wise details of bank facilities please click here

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About CARE Ratings Limited:

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With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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