Deepkiran Foods Private Limited

January 07, 2021

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term / Short-term Bank Facilities	17.00	**CARE A; Stable /CARE A1 (Single A; Outlook: Stable/ A One)**	**Reaffirmed**
Short-term Bank Facilities	0.50	**CARE A1 (A One)**	**Reaffirmed**
Total	**17.50 (Rupees Seventeen crore and fifty lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

For arriving at the ratings of Deepkiran Foods Private Limited (DFPL), CARE has taken a combined view of entities promoted by Amin family viz. DFPL and Innovative Cuisine Private Limited (ICPL) (together referred to as a group) due to their managerial (common shareholding & directorships), operational [similar product portfolio i.e. Ready to Eat (RTE) products] and financial linkages (investment of DFPL in ICPL and unsecured loan extended by DFPL).

The ratings assigned to the bank facilities of DFPL continue to remain underpinned by the extensive experience of the promoters in the processed food industry, its state-of-the art manufacturing setup, diversified product offerings, along with assured off-take arrangement with the flagship company of the promoter group - Deep Foods Inc. (DFI; which has an established presence in the processed food industry in the USA). The ratings continue to derive strength from its healthy profitability along with stable scale of operations, comfortable capital structure, strong debt coverage indicators along with favorable growth prospects for the processed food industry. CARE also notes that DFPL has not availed any moratorium on its debt as a Covid relief measure, in line with Reserve Bank of India (RBI) guidelines, on the back of its adequate liquidity.

The ratings, however, continue to remain constrained on account of DFPL's moderate scale of operations, dependence of its raw material sourcing on the vagaries of monsoon along with high customer and geographical concentration of its revenue. The ratings are also constrained on account of fixed price agreement with DFI, which exposes the group's profitability to volatility in raw material prices and foreign exchange fluctuations.

Rating Sensitivities

Positive factors

- Significant growth in scale of operations of the group marked by total operating income (TOI) of Rs.500 crore along-with greater geographical diversification of sales
- PBILDT margin above 25% on sustained basis by managing volatility associated with raw material prices and competitive pressures associated with venturing in to newer geographies
- Improvement in ROCE above 18% on sustained basis

Negative factors

- PBILDT margin falling below 15% on a sustained basis
- Deterioration in overall gearing beyond 0.75 times on sustained basis
- Any significant debt-funded capex undertaken by the company which may result into weakening of its debt coverage indicators (deterioration of TD/GCA beyond 2.5x)

Detailed description of the key rating drivers

Key Rating Strengths

Extensive experience of the promoters in the processed food industry along with assured off-take arrangement

The founder directors of both the entities, Ms Bhagwati Amin and Mr Arvind Amin, possess an experience of more than four decades in the processed food industry through their flagship company i.e., DFI in USA, which was established in 1977. DFI has a well-established production and distribution facility in the USA and owns warehouses across 45 states in USA. DFPL & ICPL have an assured off-take arrangement for their entire production with DFI, which ensures a ready and assured market for the food products manufactured by the group.

Well-established operational set up along with diversified product offerings

DFPL has an operational track record of over a decade and the manufacturing facilities of DFPL and ICPL, located in Gandhinagar and Vadodara respectively, are certified by the United States Food and Drug Administration (USFDA), National Science Foundation (NSF) and ISOQAR – ISO 22000:2005. While DFPL manufactures more than 70 RTE products

[1] *Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

through spiral freezing technique and has a wider product portfolio, ICPL is primarily focused on export of cut vegetables and fruits through Individual Quick Freezing (IQF) technique. However, post commencement of its new production line, during FY19 (FY refers to the period from April 1 to March 31), the share of RTE products to the total exports of ICPL had almost doubled as compared with FY18 and it remained largely stable in FY20.
Further, the group has introduced various new products like green chilli cubes, garlic cubes, ginger garlic cubes, ginger cubes, soaked and boiled moong dal and chana dal, bhakri pizza, various types of parathas, etc. to increase their product offerings in past two years ended FY20.

Healthy profitability; albeit moderate scale of operations
The total operating income (TOI) of the group remained moderate and largely stable at Rs.335.08 crore during FY20, with DFPL contributing approximately 58% of the group's TOI, while the balance 42% was contributed by ICPL. PBILDT margin of the group moderated by 372 bps on y-o-y basis to 17.93% on account of weakening of dollar in FY20 compared to FY19 and increase in price of raw materials like milk, corn oil, multipurpose flour, various vegetables, etc. In line, PAT margin also declined by 231 bps on y-o-y basis to 8.30% in FY20. However, the group reported healthy GCA of Rs.47.37 crore during FY20 (Rs.56.26 crore during FY19).
During H1FY21, the group reported a TOI of Rs.147.52 crore with PBT of Rs.13.90 crore. The group's performance in H1FY21 was impacted due to fixed cost burden on the back of substantial loss of sales during April-May'2020 due to disruptions caused by the outbreak of Covid-19 pandemic. Further, the prices of raw materials had continued to increase in H1FY21 resulting in further moderation in its PBILDT margin to 16.50%. Despite moderation, the profitability of the group continued to remain healthy.

Comfortable capital structure along with healthy debt coverage indicators
The group has a conservative capital structure indicated by an overall gearing of 0.11x as on March 31, 2020 (0.14x as on March 31, 2019). The debt coverage indicators also remained healthy marked by interest coverage of around 35x (PY: 24x) and total debt to GCA of 0.67x during FY20. During FY20, DFPL declared equity dividend of Rs.20.10 crore leading to moderation in tangible net-worth of DFPL from Rs.228.28 crore at FY19 end to Rs.222.15 crore at FY20 end. Despite this, the capital structure of the company remained comfortable with overall gearing of 0.05x as at March 31, 2020 (0.04x as on March 31, 2019) as the company has no external long term debt on its books and has minimum reliance on working capital borrowings to meet its working capital requirement. As indicated by the management, no declaration of dividend to promoters is expected in near future.

Substantial addition to manufacturing capacities; albeit minimum reliance on external debt
During last three years ended March 2020, DFPL added fixed assets aggregating to Rs.33 crore towards automation in its production process which was funded entirely through internal accruals. This automation helps the group to reduce its reliance on manual labour to achieve higher consistency, increase output and operate on an assembly line model. ICPL has also undertaken two large-size debt-funded expansion in a phased manner in near past and its production capacity stood at 17,000 MTPA as on March 31, 2020.The tandoori naan and paratha section commenced full-scale operations from April 2018 and contributed approx. Rs.14.81 crore to TOI during FY20. Considering assured off-take arrangement with DFI and its distribution companies for the entire production, the salability risk is also mitigated to an extent.

Favorable growth prospects for processed food industry
The ethnic Indian and Asian cuisine are becoming more popular amongst the millennial consumers who are more eager to try new food and diversify their eating habits. DFPL and ICPL are well positioned to benefit from this trend with its established range of Indian entrées and its growing range of Asian RTE foods. Increasing working population, bourgeoning urban and young population along with changing lifestyles of people and the paucity of time in a faced-paced world are expected to be driving factors for growth of the processed food industry.

Liquidity: Adequate
The group has adequate liquidity marked by free cash and bank balance of Rs.75.49 crore as on March 31, 2020 post declaration of dividend of Rs.20.10 crore during FY20 which further increased to Rs.83.90 crore as on September 30, 2020 indicating substantial financial flexibility. The average utilization of DFPL's fund-based working capital facilities during the trailing 12 months ended November 2020 remained low at 35% and the average utilization of ICPL's fund-based working capital facilities during the trailing 12 months ended October 2020 remained moderate at 77%. Also, the group reported a healthy cash flow from operations of Rs.38.53 crore during FY20 (FY19: Rs.49.19 crore). The group has repaid its entire term debt obligation by end November 2020 and has no scheduled debt repayments going forward. The group's current ratio and quick ratio as on March 31, 2020 remained healthy at 2.77x and 2.21x respectively along with comfortable operating cycle at 72 days (FY19: 62 days). Also, both DFPL & ICPL have not availed any moratorium on their debt obligations, the option for which was available to them as a Covid-relief measure under RBI's package, on the back of their adequate liquidity.

Key Rating Weaknesses

Geographical and customer concentration of its revenue profile

During FY20 and H1FY21, USA accounted for approximately 79% and 77% of sales of the group, which exposes the group to risks arising from geographical concentration of its revenue. The group has started exports to Canada and Australia (Melbourne) in recent years; however, their contribution to TOI remains low. Furthermore, to mitigate the geographical concentration risk, the group has also started exports to Fiji, New Zealand and Singapore from FY19 onwards.
The customer concentration risk, too, remains high as its entire revenue is earned through sale to its flagship entity and its distribution companies. Any change in the market position of DFI on account of changes in the economic condition in the US market, emergence of new competitors or any adverse regulatory changes governing food trade, etc., could also adversely impact the operations and profitability of the group.

Price volatility and availability risk associated with its agro-based raw materials

The group procures raw materials (agro-based commodities) from the open market and does not have any fixed price contracts with its suppliers. Agro based commodities exhibit seasonality and availability & pricing of raw materials for processing is susceptible to the vagaries of monsoon. Furthermore, the fruits and vegetables are perishable in nature and their demand is more or less uniform throughout the year which gives rise to the need for cold storage. On the other hand, sale prices to DFI are fixed in advance on arm's length basis considering the prevailing trend of raw material pricing and other overheads. Hence, the company's profitability is exposed to any major adverse movement in the prices of raw materials during the year. However, the assured off-take arrangement with DFI at mutually decided rates considering the cost structure insulates DFPL and ICPL from any major price variations.

Susceptibility of its profitability to foreign exchange fluctuation risk

DFPL and ICPL are 100% Export Oriented Units (EOU) with entire sales in overseas markets, primarily USA, while the raw materials are mainly procured indigenously and accordingly, the group is exposed to any sudden movements in the foreign exchange rate. However, DFPL uses bill discounting facility and ICPL uses packing credit loan in foreign currency (PCFC) for its working capital requirements, which insulates the companies from exchange rate volatility risk to a certain extent. Also, the group takes forward contracts to hedge the foreign currency exposure partially.

Analytical approach: Combined. Combined view of DFPL and ICPL has been taken due to their managerial (common shareholding & directorships), operational (similar product portfolio i.e. RTE) and financial linkages (investment of DFPL in ICPL).

Applicable Criteria:

Criteria on assigning 'outlook' to Credit Ratings
CARE's Policy on Default Recognition
CARE's methodology for manufacturing companies
Financial Ratios – Non-Financial Sector
Rating Methodology – Notching by factoring linkages in Ratings
Criteria for Short Term Instruments
Liquidity Analysis of Non-Financial Sector Entities

About the Company

Gandhinagar-based Deepkiran Foods Private Limited (DFPL) was established in 1998 by the US-based Amin family. The Amin family has presence in the processed food industry through their flagship company i.e., Deep Foods Inc. (DFI), which is headquartered in USA. DFI manufactures and markets a range of frozen Indian food products through its distribution companies in USA, Canada and Australia. DFPL started commercial production in 2002. The company manufactures and exports its entire production of processed and Ready-to-Eat (RTE) food products to multiple regional units of DFI and its distribution companies in the USA, Canada and Australia. The installed capacity as on March 31, 2020 stood at 12,000 MTPA.

Brief Financials (Rs. crore) - Combined	FY19 (UA)	FY20 (UA)
Total operating income	333.67	335.08
PBILDT	72.23	60.08
PAT	35.41	27.80
Overall gearing (times)	0.14	0.11
Interest coverage (times)	23.58	35.00

UA: Unaudited (derived by combining the standalone audited financials of DFPL and ICPL)

Brief Financials (Rs. crore) - DFPL	FY19 (A)	FY20 (A)
Total operating income	205.09	194.44
PBILDT	45.18	33.92
PAT	27.20	18.18
Overall gearing (times)	0.04	0.05
Interest coverage (times)	72.51	34.77

A: Audited

As per H1FY21 provisional financials, the group on a combined basis reported TOI of Rs. 147.52 crore with PBT of Rs. 13.90 crore.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Annexure - 1: Details of Facilities / Instruments

Name of the Instrument/ Bank Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT/ ST-Bills discounting/ Bills purchasing	-	-	-	17.00	CARE A; Stable / CARE A1
Non-fund-based - ST-BG/LC	-	-	-	0.50	CARE A1

Annexure - 2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT/ ST-Bills discounting/ Bills purchasing	LT/ST	17.00	CARE A; Stable / CARE A1	-	1)CARE A; Stable / CARE A1 (25-Mar-20)	1)CARE A; Stable / CARE A1 (25-Jan-19)	1)CARE A; Stable / CARE A1 (27-Mar-18) 2)CARE A; Stable / CARE A1 (13-Apr-17)
2.	Non-fund-based - ST-BG/LC	ST	0.50	CARE A1	-	1)CARE A1 (25-Mar-20)	1)CARE A1 (25-Jan-19)	1)CARE A1 (27-Mar-18) 2)CARE A1 (13-Apr-17)

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT/ ST-Bills discounting/ Bills purchasing	Simple
2.	Non-fund-based - ST-BG/LC	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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