DFM Foods Limited

December 04, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	86.26	CARE BBB; Negative	Revised from CARE BBB+; Stable
Long Term / Short Term Bank Facilities	20.00	CARE BBB; Negative / CARE A3+	Revised from CARE BBB+; Stable / CARE A2

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

CARE Ratings Limited (CARE Ratings) has revised the ratings on the bank loan facilities of DFM Foods Limited (DFM) from 'CARE BBB+; Stable/CARE A2' to 'CARE BBB; Negative/CARE A3+'. The rating revision reflects continued weakness in the business risk profile. Over the past two fiscals through FY23, the company's high growth strategy through incurring significant marketing expenses towards brand building and go-to-market expenses along with high employee costs led to operating losses, and thus, weakened the debt coverage metrics of the company along with liquidity. However, in Q1FY24, the company had reported operating profit after a hiatus of five quarters on the back of restrained marketing expenditure, reversal from earlier strategy. Earlier, CARE Ratings had reaffirmed the ratings following the expectation of revival in overall business risk profile gradually over the quarters. However, despite the significant market expenditure incurred over the past two fiscal years, the company's turnover is under pressure with net sales declining by 17.5% in H1FY24 year on year (Y-o-Y). The company also posted muted PBILDT level and losses at PAT level in Q2FY24 on the back of de-growth in sales and increased marketing and remuneration expenditure, particularly, as a result of a one-time overlap period (July to October) of two CEOs in the company. Continued weakness in the turnover may lead the company to incur more costs to stop ceding the market share. Furthermore, the continued losses may further impact the liquidity position of the company to support upcoming term loan obligations. In H2FY24, the company's 'repayment obligations are about Rs.8 crore while in FY25 the company's term loan principal repayment of Rs.25 crore is falling due. Furthermore, as no equity infusion is envisioned in the medium term, improvement in the business risk profile is key to generate sufficient liquidity to keep meeting the ongoing operational expenses as well as to service its debt.

The ratings, however, continues to derive its strength from DFM's established brand name, market position, and its stronghold over the Northern region of the country, supported by its wide distribution network. Despite the losses, the company continues to have a comfortable capital structure, supported by efficient working capital management.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors:

- Substantial rise in gross cash accruals (GCA) with increase in scale of operations and/or improvement in profitability to more than ₹40 crore on a sustained basis.
- Improvement in profitability, leading to strengthening of the debt coverage metrics with profit before interest, lease rentals, depreciation, and taxation (PBILDT) interest coverage at least 3x and total debt (TD) to GCA below 4x sustainably.
- Significant equity infusion covering the losses and strengthening the overall gearing to below 0.25x on a sustained basis.

Negative factors:

- Any debt-funded programme in the short term, resulting in an increase in the overall gearing by more than 1x on a sustained basis along with moderation in the liquidity position.
- Continued deterioration in the business risk profile i.e., either continued de-growth in turnover or continued losses or both.

Analytical approach: Standalone

Outlook: Negative

The 'Negative' outlook signifies any continued pressure on sales and/or continued loss may further deteriorate the liquidity position of the company and thus may trigger negative rating action.

Conversely, improvement in operating profitability and/or substantial improvement in the liquidity profile may lead to revision of outlook to 'Stable'.

Detailed description of the key rating drivers:

Key strengths

Strong brand name with an established market position in Northern India and wide distribution network

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

DFM introduced 'CRAX' (the company's flagship brand) in 1984, and with continued branding and marketing efforts, has established itself as a strong brand name in the Indian snacks segment for over three decades. The company enjoys a high brand recall value, offering more than 21 distinct products in the snacks and *namkeen* segment. Initially, DFM focused on the children's market with its flagship product, Crax Rings, and a well-executed strategy of including in-pack gifts. However, the company has strategically diversified its product portfolio over time to reduce its dependence on this segment and cater to a wider demographic. This diversification includes the introduction of *namkeen* and, more recently in FY22, chips, marking a shift towards a broader customer base. In FY23, it further expanded its product portfolio to launch Crax Pipes and added variations to its existing products. This expansion strategy is a testament to DFM's commitment to leveraging its established brand and consolidating its market position. It has a demonstrated presence in Northern India and is actively pursuing expansion efforts in the East zone with a distribution network of more than 1,200 distributors pan-India.

Comfortable capital structure supported by efficient working capital management

In FY23, on account of losses incurred due to sustained advertising and global trade management (GTM) expenses, the capital structure of the company moderated yet remained comfortable, supported by DFM's efficient operational cycle. The company held an average of 26 days of inventory, collected payments within an average of four days, and had an average creditor period of 47 days, resulting in a negative operating cycle of 18 days. This efficient model allowed them to collect cash and settle supplier payments before needing to pay for inventory, providing a notable financial cushion against a falling net worth from the operating losses. As on March 31, 2023, the debt-to-equity ratio stood at 0.80x (PY: 0.66x) and the overall gearing ratio stood at 0.98x (PY: 0.79x). This is expected to continue over the medium term considering scheduled repayment of term loans.

Key weaknesses

Geographical concentration risk, leading to moderate scale of operations

DFM predominantly derives 78-80% of its revenue from the Northern region of the country, followed by the Eastern, Western, and Southern regions. This has led to its scale of operations remaining moderate with a total operating income (TOI) of ₹586.08 crore in FY23 (FY22: ₹554.45 crore), despite incurring significant marketing expenses over the last two fiscal years through FY22. However, in August 2023, the company commercialised a new manufacturing plant in the East zone with an installed capacity of 5,100 metric tonne per annum (MTPA), exhibiting favourable potential for increased revenue from this region. Furthermore, the company is strategically reducing its dependence on any single region and product by adopting a multi-product, multi-channel, and multi-geography approach under its new management. Yet, the company's net sales dropped by 17.5% in H1FY24 y-o-y to Rs.256 crore. The company's turnover may moderate in FY24, however, the scale of operations would remain moderate.

Susceptible operating margins due to cost fluctuations and intense competitive

The primary raw materials (palm oil, corn grit, suji, and packaging materials) constitute more than 60% of the total costs. The pricing of these materials is influenced by various factors, including geographical and climatic conditions, global market prices, and domestic supply and demand dynamics. Consequently, the company's profitability is susceptible to fluctuations in raw material prices and inflationary pressures. However, DFM has been able to maintain a gross margin of 36-40% in the last five years through FY23, attributed to the company's brand equity, the implementation of various cost-control measures, and through pricing improvement. The company improved its gross margin from 36% in FY22 to 38% in FY23.

The company also faces significant competition from both, well-established large companies and emerging small regional players that have proliferated nationwide, intensifying competition within the industry. Although DFM operates at a moderate scale, having an established brand name positions DFM favourably in comparison to its competitors.

Weak debt coverage ratios on account of operational losses

In FY22 and FY23, the company's capital structure moderated due to continued spending on marketing expenses to support high turnover growth strategy. These expenditures did not yield the expected revenue levels, resulting in losses at both, the PBILDT and profit-after-tax (PAT) levels, resulting in weak debt coverage metrics, i.e., interest coverage and total debt to PBILDT. In current fiscal as well, the company's debt coverage metrics may remain weak considering expectation of modest operating profitability.

Liquidity: Adequate

The liquidity position of DFM is adequate as marked by adequate combination of GCA and cash and bank balance for FY24 against its repayment obligations. As on September 30, 2023, the company had free funds of Rs. 23.34 crore including current investments of Rs 11.27 crore in the form of mutual funds. Against this the company has debt repayments of around Rs. 8 crore in the subsequent two quarters, i.e., Q3FY24 and Q4FY24. Further, the company has term loan principal repayment of Rs.25 crore in FY25. In FY23, the company utilised 63% and 42% of its working capital limits comprising cash credit (CC) plus overdraft (OD) and bill discounting limits, respectively. The company's negative working capital cycle further enhances its cash flow generation capabilities, as it expands its operations but constrains its current ratio, which was at 0.64x, and quick ratio at 0.45x in FY23.

Assumptions/Covenants

Not Applicable

Environment, social, and governance (ESG) risks

Not Applicable

Applicable criteria

[Policy on default recognition](#)
[Financial Ratios – Non financial Sector](#)
[Liquidity Analysis of Non-financial sector entities](#)
[Rating Outlook and Credit Watch](#)
[Short Term Instruments](#)
[Manufacturing Companies](#)
[Policy on Withdrawal of Ratings](#)

About the company and industry

Industry classification

Macro Economic Indicator	Sector	Industry	Basic Industry
Fast Moving Consumer Goods	Fast Moving Consumer Goods	Food Products	Other Food Products

DFM was established in 1983 and is engaged in the business of manufacturing, distributing, and marketing packaged foods. As on September 30, 2023, the company's total installed capacity is 57,000 MTPA, including the capacity added by the Kolkata plant (5,100 MTPA). The installed capacity for the snacks segment is 54,000 MTPA, whereas the installed capacity for *namkeen* is 3,000 MTPA. DFM is currently promoted by Advent International – a global private equity (PE) firm. As on September 30, 2023, the company has invested $78 billion in over 415 private equity investments across 42 countries and has an asset under management of more than $92 billion, as on June 30, 2023.

Brief Financials (₹ crore)	March 31, 2022 (A)	March 31, 2023 (UA)	H1FY24 (UA)
Total operating income	554.45	586.08	256.70
PBILDT	-15.22	-34.15	5.80
PAT	-24.76	-61.38	-5.50
Overall gearing (times)	0.78	0.98	-
Interest coverage (times)	-1.71	-3.77	1.61

A: Audited UA: Unaudited; Note: 'the above results are latest financial results available'

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 rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/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		-	-	31-03-2027	51.26	CARE BBB; Negative
Fund-based - LT-Working Capital Limits		-	-	-	35.00	CARE BBB; Negative
Fund-based/Non-fund-based-LT/ST		-	-	-	20.00	CARE BBB; Negative / CARE A3+

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 2023-2024	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
1	Fund-based - LT-Term Loan	LT	51.26	CARE BBB; Negative	1)CARE BBB+; Stable (12-Sep-23)	1)CARE BBB+; Stable (23-Dec-22) 2)CARE A; Negative (03-Jun-22)	1)CARE A; Negative (14-Feb-22) 2)CARE A; Stable (25-Nov-21) 3)CARE A; Stable (05-Nov-21)	1)CARE A; Stable (24-Nov-20)
2	Fund-based/Non-fund-based-LT/ST	LT/ST*	20.00	CARE BBB; Negative / CARE A3+	1)CARE BBB+; Stable / CARE A2 (12-Sep-23)	1)CARE A2 (23-Dec-22) 2)CARE A1 (03-Jun-22)	1)CARE A1 (14-Feb-22) 2)CARE A1 (25-Nov-21) 3)CARE A1 (05-Nov-21)	1)CARE A1 (24-Nov-20)
3	Fund-based - LT-Working Capital Limits	LT	35.00	CARE BBB; Negative	1)CARE BBB+; Stable (12-Sep-23)	1)CARE BBB+; Stable (23-Dec-22)	1)CARE A; Negative (14-Feb-22) 2)CARE A; Stable	1)CARE A; Stable (24-Nov-20)

						2)CARE A; Negative (03-Jun-22)	(25-Nov-21) 3)CARE A; Stable (05-Nov-21)	

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities
Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Term Loan	Simple
2	Fund-based - LT-Working Capital Limits	Simple
3	Fund-based/Non-fund-based-LT/ST	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please click here

Note on the 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.

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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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