Amreli District Co-operative Milk Producers' Union Limited

February 21, 2022

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term/Short-term Bank Facilities	50.00	**CARE AA-; Stable / CARE A1+ (Double A Minus; Outlook: Stable / A One Plus)**	**Assigned**
Total Facilities	**50.00 (Rupees fifty crore only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Amreli District Cooperative Milk Producers' Union Limited (AMR dairy, the Union) derive strength from it being one of the unions of the 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 such as 'Amul' and 'Sagar'; along with stable growth prospects for the dairy industry. The ratings further derive strength from measures underway to enhance milk procurement, growing share of value-added products, 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 is, however, constrained by the moderate capacity utilisation of its recently-enhanced milk processing capacity, environment and epidemic-related event risks associated with geographically-concentrated milk procurement and exposure to risks associated with regulatory changes and volatile skimmed milk powder (SMP) prices.

Rating Sensitivities

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

- Significant growth in 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 or 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 the dairy industry, having a material impact on the extent of returns/milk procurement prices paid to the farmer members on a sustained basis.
- Deterioration in overall gearing beyond 4x 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

AMR dairy is one of the members of the Dairy Processing Units (DPUs), among the 18-member DPUs of GCMMF under the three-tier 'Amul structure'. GCMMF is the apex marketing federation in the structure and AMR dairy sells 100% of its products to GCMMF, which in turn, sells it to the end-users.

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 36 lakh farmers spread across more than 18,565 villages, and the daily milk collection of all member DPUs aggregated to around 246 lakh litres per day (LLPD) for FY21 (refers to the period from April 1 to March 31). Furthermore, with a collective milk processing capacity of 390 LLPD, GCMMF commands a prominent market share in pouched milk and in various milk products (ranging from 40-73% market share) in the Indian dairy industry.

Strong pricing power over dairy products due to GCMMF's leading market position, coupled with presence of a mechanism for payment of milk procurement prices, which ensures adequate debt-servicing coverage

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

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

Stable growth prospects for the dairy industry
During FY21, the revenue of the organised dairy sector was affected to an extent, owing to the impact of the COVID-19 pandemic on the institutional demand. With the surge of the second wave, bulk demand for milk and other dairy products from hotels, restaurants and cafes, sweet marts and tea stalls witnessed contraction. This led to diversion of milk from dairy farmers who were supplying milk to private dairies and unorganised players to the organised dairy co-operatives, which resulted in an increased quantity of milk sourced. The fall in institutional demand was offset to some extent by the increased consumption by households, while the excess milk sourced was converted into SMP and butter, resulting in surplus stock of the same.
In order to help the dairy sector to liquidate inventory of SMP, there were two major measures announced by the government. Firstly, the Ministry of Fisheries, Animal Husbandry and Dairying, Government of India, had 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 till March 31, 2026. Secondly, the Government of Gujarat, through the National Dairy Development Board (NDDB), announced a subsidy with a ceiling of Rs.50 per kg of SMP with a maximum budget allocation of Rs.150 crore for the entire scheme, which was valid for a period of six months from July 01, 2021 to December 31, 2021.
SMP prices have witnessed an improving trend in the current year (FY22), which should help the sector liquidate the higher inventory of SMP. Also, the Union Budget 2022-23 announced a reduction in direct tax liability for cooperatives, which should enhance the income of cooperative societies and help in boosting rural demand.
In the medium-term, the demand for dairy and its allied products is expected to witness healthy demand with lower restrictions, as compared to the earlier COVID-19 wave, and also an increase in household consumption. 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 the world's largest milk producer and the 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 primarily be driven by the increase in demand for value-added milk products, which is also margin-accretive for the players.

Liquidity: **Strong**
The liquidity of the Union is strong, with the Union deriving comfort from sales made on a 'cash-and-carry' basis with daily receipts from GCMMF, while provisional payment to VCS is made on an interval of every 10-days, resulting in a comfortable operating cycle (31 days in FY21). 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. The average utilisation of AMR dairy's fund-based working capital limits stood moderate, at 63%, for the last 12-months ended December 31, 2021.

Key Rating Weaknesses
Low milk procurement base and moderate utilisation of enhanced milk processing facility along with limited product profile; albeit gradually growing share of value-added products
The Union enhanced its milk processing capacity from 2 LLPD to 3.20 LLPD during FY20; albeit its milk procurement has not immediately increased in proportion to it, and hence, the capacity utilisation remained moderate at 43% during FY21. Although its milk procurement network has largely remained stagnant over the past four years, the Union is making efforts to increase the same. Out of 646 villages in the Amreli district, AMR dairy has, as of now, covered around 490 villages. The Union is hence making efforts to expand its milk procurement network by reaching maximum villages of the Amreli district, and thus, enhance its milk procurement. AMR dairy's milk procurement network comprised of 720 VCS with 34,574 farmer members in FY21, who hold the entire shareholding in AMR dairy and ensure smooth and steady supply of milk to the Union. It also provides cattle-feed at concessional rates to its members' VCS to enhance the milk productivity.
The average milk procurement price paid to its farmer members stood at Rs.629 per kg fat during FY21. However, it derives significant benefit from being part of the GCMMF structure, whereby, the entire sales of the Union are to GCMMF. During FY21, AMR dairy's sales constituted around 1% of GCMMF's TOI for FY21. With GCMMF's industry leadership position in the organised domestic dairy industry, the milk procurement and sales of AMR dairy is also expected to gradually increase.
The Union's product profile includes ghee, curd, lassi and buttermilk, apart from packaged milk. Over the last four years ended FY21, the share of value-added products has witnessed an improving trend, and it increased from 19% in FY18 to 26% in FY21. The Union is already in the process of adding capacities for manufacturing ice-cream and paneer, which should also help in passing on more remunerative prices to the farmers. AMR dairy has envisaged to incur a capex of around Rs.28 crore during FY22-FY24 towards setting up an ice-cream plant of 15,000 litres per day and a paneer plant of 2 tonne per day. The capex is expected to be funded by the government grant of around Rs.13.50 crore and the balance through internal accruals/bank borrowings.

Exposure to environmental and epidemic-related event risks associated with geographically concentrated milk procurement
DPUs, including the AMR dairy, are exposed to 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. With respect to AMR dairy, it collects its entire milk from its milk shed area in Gujarat, and hence, the Union remains exposed to risks associated with concentrated milk procurement.

Exposure to inherent regulatory changes and volatile SMP prices
The Indian dairy industry remains exposed to inherent risks associated with regulatory changes, such as change in government incentives/ban on export of dairy products (mainly SMP), and demand for signing of free trade agreements (FTAs) by surplus milk-producing countries such as Australia and New Zealand to gain access to the Indian dairy market. Furthermore, the demand for dairy analogues, which are used as a substitute for milk and milk fats, also pose challenges to some extent, as they are look-alike dairy products and provide significant cost-cutting opportunities. Also, the sector remains exposed to volatility in SMP prices, which are largely determined by the domestic and international demand-supply dynamics, along with export competitiveness of Indian players. This apart, the industry also remains fragmented with the presence of a large number of players. Nevertheless, GCMMF, by virtue of its dominant position in the industry, is largely able to mitigate such challenges.

Analytical Approach: Standalone, with group support
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 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 member-farmers for their milk supply. Hence, the credit risk of such cooperative sector entities is assessed based on 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 of Default Recognition
Rating Methodology – Manufacturing Companies
Criteria for Short Term Instruments
Financial Ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Rating Methodology: Notching by factoring linkages in Ratings

About the Union
Incorporated in 2002, AMR dairy is a cooperative DPU established under the three-tier dairy cooperative structure of Gujarat, known as 'Anand Pattern' or 'Amul Structure'. The Union procures milk from around 729-member VCS consisting of around 34,574 lakh farmers, who hold the entire shareholding in AMR dairy. It had a total milk processing capacity of 3.20 LLPD, as on March 31, 2021, at its milk processing unit in Amreli, Gujarat. Apart from milk processing capacity, it also has capacities for manufacturing value-added products like curd, ghee, lassi, buttermilk. It also has a cattle feed plant at Amreli, with an installed capacity of 300 tonne per day.

Brief Financials (Rs. crore)	FY20 (A)	FY21 (A)	8MFY22(Prov.)
Total operating income	215.94	268.33	174.94
PBILDT	3.99	22.03	17.83
PAT	0.66	9.55	10.86
Overall gearing (times)	0.53	0.38	0.33
Interest coverage (times)	1.62	8.26	14.62

A: Audited, Prov.: Provisional

Status of non-cooperation with previous CRA: Not applicable
Any other information: Not applicable

Rating History for last three years: Annexure-2

Covenants of rated instrument/facility: Not applicable

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

Annexure-1: Details of Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based-LT/ST		-	-	-	50.00	CARE AA-; Stable / 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 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Fund-based-LT/ST	LT/ST*	50.00	CARE AA-; Stable / CARE A1+				

* 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/ST	Simple

Annexure 4: Bank Lender Details for this Company

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

Note on complexity levels of the rated instrument: CARE Ratings Ltd. 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 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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