# Deepkiran Foods Private Limited

March 25, 2020

**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 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 growing scale of operations, comfortable capital structure and adequate liquidity, strong debt coverage indicators along with favourable growth prospects for the processed food industry.

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 profile. 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 disruption in its sales in USA due to recent epidemic of Corona Virus
- 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 (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 through spiral freezing technique and has a wider product portfolio, ICPL is primarily focused on export of cut vegetables

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

and fruits through Individual Quick Freezing (IQF) technique. However, during FY19 and 9MFY20, the share of RTE products to the total exports of ICPL has almost doubled as compared with FY18 after the commencement of its new production line.
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, etc. to increase their product offerings.

***Growing; albeit moderate scale of operations along with healthy profitability***
The total operating income (TOI) of the group increased y-o-y by 22% to Rs.333.67 crore during FY19 (refers to the period April to March), with DFPL contributing approximately 61% of the group's TOI, while the balance 39% was contributed by ICPL. The growth in TOI was majorly on account of increase in orders from USA and sales from new markets tapped by the group i.e. Fiji, New Zealand and Singapore. The PBILDT margin of the group remained healthy and increased by 184 bps on y-o-y basis to 21.65% in FY19 primarily on account of increase sales of better margin RTE products by around 150% on y-o-y basis with commencement of new production line by ICPL along with increase in sales realization of majority of products due to firming up of US dollar during FY19. In line, PAT margin of the group also increased by 411 bps to 10.61% in FY19 from 6.50% during FY18. Further, group reported healthy GCA of Rs.56.26 crore during FY19 (Rs.39.18 crore during FY18).
However, during 9MFY20 (refers to the period April to December) the group reported a TOI of Rs.246.69 crore as against Rs.254.25 crore during 9MFY19. The decline in TOI was due to various reasons like marginal dip in orders from USA, decrease in other operating income due to discontinuation of one of the export promotion schemes of the government i.e., Vishesh Krishi Gram Upaj Yojana (V.K.U.Y. license sales) from July 2019 along with weakening of the US dollar in 9MFY20, leading to lower sales realization. However, the said scheme has now again been restarted by government from January 2020. The PBILDT margin also decreased by 567 bps on y-o-y basis to 17.48% due to increase in price of raw materials like milk and corn oil.

***Comfortable capital structure along with healthy debt coverage indicators***
The group has a conservative capital structure indicated by an overall gearing of 0.14x as on March 31, 2019 (0.25x as on March 31, 2019). The debt coverage indicators also remained healthy marked by interest coverage of around 24x and total debt to GCA of 0.67x during FY19. During 9MFY20, DFPL has declared equity dividend of Rs.24.23 crore leading to moderation in tangible net-worth of DFPL from Rs.228.28 crore at FY19 end to Rs.212.96 crore at 9MFY20 end. Despite this, the capital structure of the company remained comfortable with overall gearing of 0.07x as at December 31, 2019 (0.03x 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.

***Substantial addition to manufacturing capacities; albeit minimum reliance on external debt***
During last three years ended March 2019, DFPL has added fixed assets aggregating to Rs.26 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 also undertook two large-size debt-funded expansion plans in a phased manner and its production capacity stood at 17,000 MTPA as on March 31, 2019.The tandoori naan and paratha section commenced full-scale operations from April 2018 and contributed approx. Rs.15.32 crore to TOI during FY19. 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, growing per capita disposable income and discretionary spending along with changing lifestyles of people and time crunch are expected to be driving factors for growth of the processed food industry.

**Key Rating Weaknesses**
***Geographical and customer concentration of its revenue profile***
During FY19 and 9MFY20, USA accounted for approximately 82% and 79% of sales of the group, which exposes the group to risks arising from geographical concentration of its revenue profile. 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 during FY19 and 9MFY20.
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 the availability and pricing of raw materials for processing is susceptible to the vagaries of monsoon. Furthermore, the fruits and vegetables are perishable in nature and its 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 Unit (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.

**Liquidity:** ***Adequate***

The group has adequate liquidity marked by free cash and bank balance of Rs.87.95 crore as on March 31, 2019, which moderated to Rs.74.43 crore as on December 31, 2019 post declaration of dividend of Rs.24.23 crore, indicating substantial financial flexibility. The average utilization of DFPL's fund-based working capital facilities during the trailing 12 months ended December 2019 remained moderate at 68% and the average utilization of ICPL's fund-based working capital facilities during the trailing 12 months ended January 2020 also remained moderate at 73%. Also, the group reported healthy cash flow from operations of Rs.49.19 crore during FY19 (FY18: Rs.55.30 crore). Debt repayment liability also remained low at Rs.13.36 crore and Rs.9.77 crore in FY20 and FY21 respectively, when compared with the cash accruals generated by the group in FY19. The group's current ratio and quick ratio as on March 31, 2019 remained healthy at 3.02x and 2.51x respectively along with comfortable working cycle at 62 days (FY18: 72 days).

**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**
**Criteria for Short Term Instruments**
**Rating Methodology – Manufacturing Companies**
**Rating Methodology – Factoring Linkages in Ratings**
**Financial ratios – Non-Financial Sector**

**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, 2019 is 12,000 MTPA.

| Brief Financials (Rs. crore)- Combined | FY18 (UA) | FY19 (UA) |
|---|---|---|
| Total operating income | 273.35 | 333.67 |
| PBILDT | 54.14 | 72.23 |
| PAT | 17.78 | 35.41 |
| Overall gearing (times) | 0.25 | 0.14 |
| Interest coverage (times) | 15.99 | 23.58 |

*UA: Unaudited*

| Brief Financials (Rs. crore)- DFPL | FY18 (A) | FY19 (A) |
|---|---|---|
| Total operating income | 179.94 | 205.09 |
| PBILDT | 37.43 | 45.18 |
| PAT | 18.04 | 27.20 |
| Overall gearing (times) | 0.07 | 0.04 |
| Interest coverage (times) | 50.76 | 72.51 |

*A: Audited*

As per 9MFY20 provisional financials, the group on a combined basis reported TOI of Rs.246.69 crore with PBT of Rs.25.78 crore vis-à-vis TOI of Rs.254.25 crore with PBT of Rs.41.20 crore during 9MFY19.

**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**

| 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 2019-2020 | Date(s) & Rating(s) assigned in 2018-2019 | Date(s) & Rating(s) assigned in 2017-2018 | Date(s) & Rating(s) assigned in 2016-2017 |
| 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-Jan-19) | 1)CARE A; Stable / CARE A1 (27-Mar-18)<br>2)CARE A; Stable / CARE A1 (13-Apr-17) | 1)CARE A / CARE A1 (05-May-16) |
| 2. | Non-fund-based - ST-BG/LC | ST | 0.50 | CARE A1 | - | 1)CARE A1 (25-Jan-19) | 1)CARE A1 (27-Mar-18)<br>2)CARE A1 (13-Apr-17) | 1)CARE A1 (05-May-16) |

***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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