October 30, 2017

Dodla Dairy Limited

Summary of rated instruments

Instrument*	Rated Amount (in Rs. crore)	Rating Action
Term loans	46.37 (reduced from 77.94 earlier)	[ICRA]A+ (Stable); Reaffirmed
Cash credit^	72.50	[ICRA]A+ (Stable)/[ICRA]A1+ Upgraded short-term rating from [ICRA]A1
Short-term fund-based Limits	30.00	[ICRA]A1+ Upgraded from [ICRA]A1
Unallocated limits	60.63 (increased from 7.06 earlier)	[ICRA]A+(Stable) Reaffirmed
Total	**209.50 (enhanced from 187.50)**	

^Cash credit interchangeable with short term loans
*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the long-term rating assigned to the Rs. 46.34-crore[1] (reduced from Rs. 77.94-crore) term loans and Rs. 60.63-crore (enhanced from Rs. 7.06-crore) unallocated limits of Dodla Dairy Limited (DDL/Dodla)[2] at [ICRA]A+ (pronounced ICRA A plus). ICRA has upgraded the ratings assigned to the Rs.72.50-crore cash credit facilities of DDL to [ICRA]A+/[ICRA]A1+ (pronounced ICRA A one plus) from [ICRA]A+/[ICRA]A1 (pronounced ICRA A one). Furthermore, ICRA has upgraded the short-term rating assigned to the Rs. 30.00 crore short term loans of DDL to [ICRA]A1+ from [ICRA]A1. The outlook on the long-term rating is Stable.

Rationale

The upgrade in short-term rating reflects DDL's strong liquidity position as reflected by adequate cushion in working capital limits and high unencumbered liquid surplus. Further, majority of the capex undertaken in FY2017 was funded through internal accruals resulting in lower than anticipated debt levels and consequently resulting in better than expected debt coverage and leverage indicators in FY2017. The ratings favourably take into account DDL's ability to sustain its growth momentum supported by continuously expanding its milk procurement base and improving its product mix towards higher proportion of value-added product sales. DDL's liquid milk volumes witnessed healthy growth of 13% in FY2017 owing to entry into new geographies and expanding customer base. This coupled with significant growth in value-added products mainly driven by curd sales enabled DDL to report 19% growth in Operating Income (OI) in FY2017 at Rs.1411.47 crore. In line with ICRA expectations, there was moderation in the operating profitability to 6.26% from 8.16% in FY2016 on account of increase in the raw milk procurement cost per litre with no commensurate increase in liquid milk realisation. However, the cash accruals continue to remain robust.

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[1] *100 lakh = 1 crore = 10 million*
[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications.*

The ratings continue to factor in the well established position of ***Dodla*** brand and its diversified presence across the districts of Andhra Pradesh (AP), Karnataka and parts of Tamil Nadu (TN) and Telangana. DDL's established procurement base among dairy farmers supplemented by a wide network of bulk coolers and chilling centres provides the company a steady source of liquid milk. The ratings also draw comfort from the favourable growth prospects given the low penetration of organised sector in the dairy industry. DDL's entry into newer geographies and its ability to develop value-added products are crucial for sustaining the current growth momentum.

The ratings are, however, constrained by the commoditised nature of operations; high competition from organised co-operatives, private sector and unorganised players; and its vulnerability to external factors such as weather and disease outbreaks. Given the high competition from milk cooperatives especially in Karnataka and Tamil Nadu, which account for around half of DDL's turnover, DDL's pricing flexibility in these markets are constrained given the existing high price differential between the milk co-operatives and DDL in these states— although the company has been largely able to pass on the hike in input costs in the past.

DDL plans to setup a new dairy processing unit in Rajahmundry at an estimated cost of Rs. 65-70 crore crore, proposed to be funded through internal accruals. Further, the company intends to add one lakh litre per day of processing capacity every year through inorganic growth and set up the requisite procurement network to support the raw milk requirement at the new plants. Given the healthy internal accrual generation, ICRA expects the capital structure to continue to remain at existing levels.

Going forward, the ability of the company to maintain its profitability through sustained improvement in procurement base of milk, thereby limiting its dependence on SMP; successfully enter newer geographies and complete new Rajahmundry plant within budgeted costs and timelines would be the key rating sensitive factors. Dodla would remain exposed to event risks such as climatic vagaries and epidemics.

Key rating drivers

Credit strengths

- **Established brand in southern India:** Dodla brand is well established in liquid milk segment in southern India with a wide network of more than 6,000 dealers/direct selling agents and its diversified presence spread across districts of AP, Karnataka and parts of TN and Telangana combined with favorable growth prospects given the low penetration of organised sector in the dairy industry
- **Healthy growth in OI:** DDL's liquid milk volumes witnessed healthy growth of 13% in FY2017 owing to entry into new geographies and expanding customer base. This coupled with significant growth in value-added products mainly driven by curd sales enabled DDL to report 19% growth in Operating Income (OI) in FY2017 at Rs.1411.47 crore.
- **Wide procurement base:** DDL's established procurement base among dairy farmers supplemented by a wide network of bulk coolers and chilling centres provides the company a steady source of liquid milk.

Credit challenges

- **High competition from other players:** This business has commoditised nature of operations with high competition from organised co-operatives, private sector and unorganised players and its vulnerability to external factors such as weather and disease outbreaks.
- **Sustainability of revenues from value added products:** Proportion of value added products in the overall revenue mix improved during FY2017 to 33% from 30% in FY2016; however the sustainability of the same remains to be seen.
- **Little control over procurements costs:** The company has little control over the procurement costs of liquid milk as these are driven by high competitive intensity from state owned milk cooperatives and other private dairies and low switching costs for the farmers. Particularly in Karnataka and TN which account for around half of DDL's turnover, the pricing flexibility for the company is constrained given the existing high price differential between the milk co-operatives and DDL's consumer pack price.

Analytical approach

For arriving at the ratings, ICRA has applied its rating methodologies as indicated below:

Links to applicable Criteria

[Corporate Credit Rating Methodology]

About the company

Incorporated in 1995, DDL is promoted by Mr. D. Sesha Reddy and Mr. D. Sunil Reddy and is engaged in processing and sale of milk and milk products under Dodla brand with a market presence predominantly in four southern states viz. Andhra Pradesh, Karnataka, Tamilnadu and Telangana. In July 2017, TPG Dodla Dairy Holdings Pvt Ltd acquired 27% stake in Dodla (23% from Black River Asset Management and 4% from promoters). Currently, promoters hold 73% and remaining 27% is held by TPG. DDL has eleven processing and packaging units with a processing capacity of 11 lakh litres per day.

Key financial indicators (audited)

Particulars	FY2016	FY2017
Operating Income (Rs. crore)	1182.37	1411.47
Net Profit (Rs. crore)	35.58	44.39
OPBITDA/OI (%)	8.16%	6.26%
RoCE (%)	27.80%	21.72%
Total Debt / Tangible Net worth (times)	0.45	0.47
Total Debt / OPBITDA (times)	1.13	1.54
Interest Coverage (times)	9.58	11.01
NWC/OI (%)	3%	3%

Source: DDL; OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress); NWC: Net Working Capital

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years
Table

<table>
<tr><th rowspan="2">S. No.</th><th rowspan="2">Name of Instrument</th><th colspan="3">Current Rating</th><th colspan="4">Chronology of Rating History for the past 3 years</th></tr>
<tr><th>Type (Long Term/ Short Term)</th><th>Rated amount (Rs. crore)</th><th>Month - year & rating</th><th colspan="2">Month – year & Rating in FY2017</th><th>Month – year & Rating in FY2016</th><th>Month - year & Rating in FY2015</th></tr>
<tr><td rowspan="2">1</td><td rowspan="2">Cash Credit</td><td rowspan="2">Long Term/ Short Term</td><td rowspan="2">72.5</td><td>October 2017</td><td>December 2016</td><td>May 2016</td><td>April 2015</td><td>April 2014</td></tr>
<tr><td>[ICRA]A+ (Stable)/A1+</td><td>[ICRA]A+ (Stable)/A1</td><td>[ICRA]A- (Positive)/A2+</td><td>[ICRA]A- (Stable)/A2+</td><td>[ICRA]A- (Stable)/A2+</td></tr>
<tr><td>2</td><td>Term loan</td><td>Long Term</td><td>46.37</td><td>[ICRA]A+ (Stable)</td><td>[ICRA]A+ (Stable)</td><td>[ICRA]A- (Positive)</td><td>[ICRA]A- (Stable)</td><td>[ICRA]A- (Stable)</td></tr>
<tr><td>3</td><td>Short-term fund-based</td><td>Short Term</td><td>30.0</td><td>[ICRA]A1+</td><td>[ICRA]A1</td><td>[ICRA]A2+</td><td>[ICRA]A2+</td><td>[ICRA]A2+</td></tr>
<tr><td>4</td><td>Unallocated</td><td>Long Term</td><td>60.63</td><td>[ICRA]A+ (Stable)</td><td>[ICRA]A+ (Stable)</td><td>[ICRA]A- (Positive)</td><td>[ICRA]A- (Stable)</td><td>[ICRA]A- (Stable)</td></tr>
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Complexity level of the rated instrument:
ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1

Details of Instruments

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. crore)	Current Rating and Outlook
Term Loan	-	10.4%	October 2021	46.37	[ICRA]A+ (Stable)
Cash Credit	-	8.5%	-	72.50	[ICRA]A+ (Stable)/A1+
Short-term fund-based	-	-	-	30.00	[ICRA]A1+
Unallocated	-	-	-	60.63	[ICRA]A+ (Stable)

Source: DDL

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