Dodla Dairy Limited

September 20, 2018

Summary of rated instruments

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based- Cash Credit*	72.50	72.50	[ICRA]A+/A1+; Reaffirmed and outlook revised to Positive from Stable
Fund based-Term Loan	46.37	45.00	[ICRA]A+; Reaffirmed and outlook revised to Positive from Stable
Short-term Fund based limits	30.00	30.00	[ICRA]A1+; Reaffirmed
Unallocated Limits	60.63	62.00	[ICRA]A+; Reaffirmed and outlook revised to Positive from Stable
Total	**209.50**	**209.50**	

*Cash credit interchangeable with short-term loans

Rating action

ICRA has reaffirmed the long-term rating assigned to the Rs. 45.0-crore[1] (Rs. 46.37-crore earlier) term loans and Rs.62.0-crore (Rs. 60.63-crore earlier) unallocated limits of Dodla Dairy Limited (DDL)[2] at [ICRA]A+ (pronounced ICRA A plus). ICRA has also reaffirmed long term/short term rating assigned to the Rs. 72.5-crore cash credit facilities at [ICRA]A+/[ICRA]A1+ (pronounced ICRA A one plus) and short term rating assigned to Rs. 30.0-crore short term loans at [ICRA]A1+. The outlook on the long-term rating is revised to Positive from Stable.

Rationale

The revision in outlook is driven by ICRA's expectation of sustained improvement in DDL's liquid milk business over the medium term supported by increased milk procurement by entering into new geographies. Further, the moderation in raw milk prices during current flush season is expected to result in improved profitability. ICRA notes that DDL has filed DRHP with SEBI on August 9, 2018 for an overall issue size of Rs. 500 crore - Rs. 550-crore. The proceeds from primary issuance net of issue expenses are estimated to be in the range of Rs. 135 crore - Rs. 140 crore. Of this, Rs. 86.27 crore is expected to be utilised for prepayment of existing term loans. The remaining Rs. 50 crore – Rs. 55 crore from IPO proceeds are expected to be utilised for purchase of equipment for existing and new facilities and general corporate purposes. ICRA expects DDL's capital structure to improve considerably post IPO on account of networth augmentation and prepayment of debt. The ratings favourably take into account the growth in liquid milk volumes by 15% in FY2018 owing to its entry into newer geographies, expanding customer and milk procurement base. This coupled with significant growth in curd sales, enabled DDL to report 9% growth in Operating Income (OI) in FY2018 to Rs. 1,537.3 crore. The rating draws comfort from the healthy financial profile of the company characterized by robust capital structure with low gearing of 0.4 times, strong debt coverage indicators with interest coverage of 10.2 times, TOL/TNW of 0.7 times and comfortable liquidity position with unencumbered liquid surplus of ~Rs. 78 crore as on March 31, 2018.

[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 the 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 supported by a wide network of bulk coolers and chilling centres helps it maintain a steady source of liquid milk from dairy farmers. The ratings also draw comfort from the favourable growth prospects given the low penetration of the 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, however, are constrained by the commoditised nature of operations, intense competition from organised co-operatives, private sector and unorganised players. Also, the company's vulnerability to external factors such as weather and disease outbreaks impacts the ratings. Given the stiff competition from milk cooperatives – especially in Karnataka and TN (which account for around half of its turnover) – DDL's pricing flexibility in these markets is constrained by its existing high price differential with milk co-operatives in these states. Nonetheless, the company has been largely able to pass on the hike in input costs in the past. Further, the proportion of value added products decreased in overall revenue mix to 29% in FY2018 from 33% in FY2017 due to decrease in sales of butter and ghee as the prices for the same has increased after the implementation of GST. The sustainability of revenues from value-added products remains to be seen.

Outlook: Positive

The revision in outlook factors in the ICRA's expectation of sustained improvement in DDL's liquid milk business over the medium term supported by increased milk procurement by entering into new geographies. Further, the moderation in raw milk prices during current flush season is expected to result in improved profitability. The outlook may be revised to Stable in case of deterioration of debt coverage indicators on account of debt funded capex/ acquisition or if the operational performance is worse than expected. Its capex plans, IPO timelines and the impact of the same on the capital structure will be closely monitored.

Key rating drivers

Credit strengths

Healthy growth in OI: DDL's liquid milk volumes witnessed a growth of 15% in FY2018 backed by increase in sales volume by 10% to 28.34 crore liters (CL) coupled with improved average realizations by 4.7%. This coupled with significant growth in curd dales, enabled DDL to report 9% growth in OI in FY2018 to Rs.1,537.3 crore.

Established brand in southern India and favourable growth prospects: The Dodla brand is well established in the liquid milk segment of southern India and has diversified presence across the districts of AP, Karnataka and parts of Tamil Nadu and Telangana combined with favourable growth prospects given the low penetration of the organised sector in the dairy industry.

Robust capital structure and coverage indicators: The rating draws comfort from the healthy financial profile of the company characterized by robust capital structure with low gearing of 0.4 times, strong debt coverage indicators with interest coverage of 10.2 times, TOL/TNW of 0.7 times and comfortable liquidity position with unencumbered liquid surplus of ~Rs. 78 crore as on March 31, 2018.

Established procurement network: DDL's wide procurement base ensuring regular supply of milk at competitive prices from farmers, supplemented by a wide network of bulk coolers and chilling centres. At present, the company has 11 plants with a milk processing capacity of 12.55 LLPD, 51 milk chilling centres and 15 bulk milk coolers in an around its procurement area.

Credit challenges

Stiff competition from other players: This business has commoditised nature of operations with strong competition from organised co-operatives, private diaries and unorganised players and its vulnerability to external factors such as weather and disease outbreaks.

Decrease in revenues from value-added products: The proportion of value added products decreased in overall revenue mix to 29% in FY2018 from 33% in FY2017 due to decrease in sales of butter and ghee as the prices for the same has increased after the implementation of GST. The sustainability of revenues from value-added products remains to be seen.

Little control over procurements costs: The company has little control over the procurement costs of liquid milk as these are impacted by intense competition from state-owned milk co-operatives and other private dairies and low switching costs for farmers. 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, Dodla Dairy Limited (DDL) is promoted by Mr. D. Sesha Reddy and Mr. D. Sunil Reddy. The company is involved in processing and sale of milk and milk products under the Dodla brand with a market presence predominantly in four southern states viz. Andhra Pradesh, Karnataka, Tamil Nadu and Telangana. In July 2017, TPG Dodla Dairy Holdings Pvt. Ltd. acquired 27% stake in Dodla. At present, the promoters hold 73% stake and the remaining 27% stake is held by TPG Dodla Dairy Holdings Pvt. Ltd. DDL has 11 processing and packaging units with a processing capacity of 12.55 lakh litres per day. DDL has filed DRHP with SEBI on August 9, 2018 with expected list by end of Q3 FY2019.

Key financial indicators

	FY2017 Audited	**FY2018 Audited**
Operating Income (Rs. crore)	1410.0	1537.3
PAT (Rs. crore)	45.9	50.6
OPBDIT/OI (%)	6.2%	6.8%
RoCE (%)	21.7%	19.5%
Total Debt/TNW (times)	0.5	0.4
Total Debt/OPBDIT (times)	1.6	1.2
Interest coverage (times)	10.8	10.2

Source: DDL

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating September 2018	Chronology of Rating History for the past 3 years: Date & Rating in FY2018 October 2017	Date & Rating in FY2017 December 2016	Date & Rating in FY2017 May 2016	Date & Rating in FY2016 April 2015
1	Term Loan	Long Term	45.00	45.00	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Cash Credit	Long Term/ Short Term	72.50	72.50	[ICRA]A+ (Positive)/A1+	[ICRA]A+ (Stable)/A1+	[ICRA]A+ (Stable)/A1	[ICRA]A- (Positive)/A2+	[ICRA]A- (Stable)/A2+
3	Short-term fund-based	Short Term	30.00	30.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A2+	[ICRA]A2+
4	Unallocated limits	Long Term	62.00	62.00	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)

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: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan	February 2015	9.75%	October 2021	45.00	[ICRA]A+(Positive)/A1+;
NA	Cash Credit	-	8.00%	-	72.50	[ICRA]A+(Positive);
NA	Short-term Fund-based	-	-	-	30.00	[ICRA]A1+
NA	Unallocated limits	-	-	-	62.00	[ICRA]A+(Positive)

Source: DDL

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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