McLeod Russel India Limited

October 08, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount(Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Term Loan	360.00	360.00	[ICRA]AA-& (Under rating watch with developing implications); reaffirmed
Fund-based Bank Facilities	600.00	491.76	[ICRA]AA-& (Under rating watch with developing implications); reaffirmed
Fund-based Bank Facilities**	200.00	163.92	[ICRA]AA-& / [ICRA]A1+& (Under rating watch with developing implications); reaffirmed
Non-fund-based Bank Facilities	18.80	15.41	[ICRA]A1+& (Under rating watch with developing implications) ; reaffirmed
Commercial Paper Programme	300.00	Nil	[ICRA]A1+& Withdrawn
Total	**1478.80**	**1031.09**	

*Instrument details are provided in Annexure-1

**Fungible with LT facilities

& Under rating watch with developing implications

Rating action

ICRA has reaffirmed the long-term rating assigned to the Rs. 360-crore[1] term loans, Rs. 491.76-crore (reduced from Rs. 600 crore) long-term fund-based bank facilities and Rs. 163.92-crore (reduced from Rs. 200 crore) fund-based working capital limits of McLeod Russel India Limited (MRIL) at [ICRA]AA- (pronounced ICRA double A minus). The Rs. 163.92-crore fund-based working capital limits have also been rated on the short-term scale, for which ICRA has reaffirmed the rating at [ICRA]A1+ (pronounced ICRA A one plus). The rating for the non-fund based bank facilities of the company, of Rs. 15.41 crore (reduced from Rs. 18.80 crore) has also been reaffirmed at [ICRA]A1+[2]. The ratings remain under watch with developing implications.

The [ICRA]A1+ rating assigned earlier to the Rs. 300-crore commercial-paper programme has been withdrawn.

Rationale

The rating action takes into account the proposed sale of certain tea estates by MRIL, the proceeds from which are expected to be used for reduction of debt. Overall, the company has entered into MoUs for the sale of 21 tea estates and 20 factories at a consideration of Rs. 795.61 crore. These estates manufactured 26 mkg of own tea in FY2018 and contributed to around 31% of MRIL’s turnover in FY2018. The estimated EBITDA contribution from the estates, however, is not proportionate to the contribution to revenues. The ratings also continue to favourably factor in the company’s leading position among tea plantation companies in India, and the premium quality of the company’s tea, which fetch higher realisation than industry averages. Considerable non-operating income, which provided substantial support to cash flows in FY2018, and a conservative capital structure, notwithstanding an increase in debt levels in recent years,

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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*

also positively impacted the ratings. However, the ratings also factor in the risks associated with tea for being an agricultural commodity, which is dependent on agro-climatic conditions, as well as the inherent cyclicality of the fixed-cost intensive tea industry that leads to variability in profitability and cash flows of bulk tea producers such as MRIL. While an increase in tea realisations, together with a rise in production from own estates and overall sales volumes, supported the core operating profit margin of the company to some degree in FY2018, the overall performance remained subdued. In Q1 FY2019 as well, operating profits remained low on an absolute basis, notwithstanding some improvement over the corresponding quarter of the previous year. Production costs are expected to be adversely impacted by further increase in the wage rates of tea estate workers going forward as well. ICRA, nonetheless, notes that MRIL's considerable bought-leaf operations, along with the favourable age profile of its tea bushes, mitigates the risks associated with the fixed cost intensive nature of the bulk tea industry to an extent. Moreover, profits from overseas operations have also supported operating profits on a consolidated basis. However, continued high level of exposure to Group companies in FY2018 also had an adverse impact on the ratings. As the loans advanced to the Group companies are largely funded by external debt, MRIL's debt-coverage indicators remained weak on an absolute basis, notwithstanding some improvement during the year.

Outlook: Ratings remain under watch with developing implications

The ratings remain under watch with developing implications, with the timeliness and extent of reduction in debt levels, post conclusion of the sale of the tea estates, remaining a key rating sensitivity. Conclusion of the sale deals is expected post completion of due diligence and other sale formalities. ICRA also notes that the company has planned a buyback of shares to the extent of Rs. 100 crore, which will have some influence on the net reduction in debt levels. ICRA will continue to monitor the developments with regards to the above.

Key rating drivers

Credit strengths

Status of being one of the largest bulk tea producers globally, with a geographically diversified production base – MRIL produced around 89 mkg of tea in FY2018, accounting for almost 7% of the total domestic tea production. The consolidated production of around 118 mkg accounted for approximately 5% of the global production of black tea. The stand-alone production increased by around 5% during the year, and consolidated production, by around 3%. The globally diversified production base of the consolidated entity, with gardens in India, Uganda, Rwanda and Vietnam mitigates the risks arising from adverse agro-climatic conditions to some extent, although exposure to geo-political risks remains.

Superior quality of tea produced by MRIL; high productivity and bought-leaf operations reduce the risks associated with the fixed-cost intensive nature of operations to some extent - The tea produced by MRIL are known for their quality, both in the domestic as well as in the export markets, fetching a premium over industry averages. The favourable age profile of MRIL's tea bushes, with around 72% of the Indian bushes being below 50 years of age, results in the company recording a high tea estate yield. This directly impacts the cost structure due to the fixed-cost intensive nature of the industry. Moreover, the inclusion of bought-leaf operations, which aids in better absorption of fixed overheads, in the company's sales mix also reduces the overall fixed cost intensity of the bulk tea business.

Considerable non-operating income and high profits from overseas operations, which provided substantial support to cash flows in FY2018, and a conservative capital structure; notwithstanding the increase in debt levels in recent years – While the operational performance of MRIL's plantation business has weakened considerably in recent years, with the muted increase in realisations unable to compensate for the substantial increase in costs – particularly wages, cash flows have been supported by considerable non-operating income. In FY2018, the company received Rs. 154 crore of special dividend from its wholly-owned subsidiary, Boreilli Tea Holdings Plc (UK) (BTHL), as repatriation of partial proceeds from the sale of treasury stock held by BTHL. This, together with interest and other non-core income led to a net cash accrual of around Rs. 119 crore during the year on a standalone basis. NABARD deposits built up over the past years led to a healthy bank balance as well, which supports the overall liquidity position of the company, notwithstanding some decline in the quantum of balances in the past few years. Cash flows were even stronger on a consolidated basis, with overseas operations generating an operating profit of around Rs. 138 crore, leading to consolidated net cash accruals of Rs. 291 crore. The capital structure also remained conservative on both standalone and consolidated basis, notwithstanding an increase in standalone debt levels in the recent years. Consolidated debt levels were lower than the previous years, with operating profits and partial proceeds from the sale of treasury stock being used to pare debt. ICRA notes that cash flows in FY2019 are also expected to be supported by the non-operating income in the form of proceeds from the sale of tea estates.

Credit challenges

Continued pressure on core operating profitability during FY2018, notwithstanding some improvement over the previous year – While an increase in tea realisations, together with a rise in tea production from own estates and overall sales volumes, supported the core operating profit margin of the company to some degree, the operating profitability of the company remained muted at 1% on a standalone basis during FY2018. Production costs were adversely impacted by higher wages, power and fuel costs. The increase in tea realisations was inadequate to compensate for the rise in costs. This, together with increased debt levels, resulted in continued pressure on debt coverage indicators as well, notwithstanding some improvement over FY2017 levels. In Q1 FY2019 also, operating profits remained low on an absolute basis, despite some improvement over the corresponding quarter of the previous year. Production costs are expected to be adversely impacted by further increase in the wage rates of tea estate workers going forward as well. However, ICRA notes that on a consolidated basis, the company reported an operating profit of Rs. 168 crore in FY2018, supported by healthy profitability from overseas operations.

Largely debt-funded exposure to Group companies increases the overall debt levels and results in pressure on debt coverage – The total debt in FY2018 increased considerably, primarily due to additional bank borrowing made to fund loans to group companies. Enhanced debt levels, together with the consequent rise in interest costs, exerted pressure on debt protection metrics. Going forward, ICRA notes that the receipt of proceeds from the proposed sale of certain tea estates would be likely to result in a reduction in debt levels and consequently an improvement in debt coverage indicators.

Risks associated with tea for being an agricultural commodity as well as the inherent cyclicality of the fixed-cost intensive tea industry - Tea production depends on agro-climatic conditions, which subject it to agro-climatic risks. Moreover, tea estate costs are primarily fixed with labour-related costs, which are independent of the volume produced, accounting for around 50% of the production cost. This leads to variability in profitability and cash flows of bulk tea producers such as MRIL.

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

Links to applicable criteria:

Rating Methodology for Entities in the Indian Bulk Tea Industry

About the company:

McLeod Russel India Limited (MRIL), the tea plantation company of the Kolkata-based B.M. Khaitan Group, was originally incorporated as Eveready Company India Private Ltd. on May 5, 1998. MRIL was formed after the demerger of the bulk-tea business from Eveready Industries India Ltd. (EIIL) with effect from April 1, 2004. MRIL has acquired several other companies like Williamson Tea Assam in FY2006, Doom Dooma Tea Company in FY2007 and Moran Tea in FY2008. These acquisitions helped MRIL increase the number of tea estates to 53 in India, with the total land under tea cultivation being 33,723 hectares (Ha). MRIL also acquired tea estates through its subsidiaries in Vietnam (three tea estates and seven factories), Uganda (six tea estates and five factories) and Rwanda (two tea estates and two factories) between CY2009 and CY2014, which took the total production to around 118 Mkg on a consolidated basis during FY2018. In the recent past, MRIL has sold one tea estate in the Dooars, and is proposing to sell 21 more, of which 18 are in Assam and three in Dooars. Post conclusion of the sale, the company would have 31 tea estates with a capacity to manufacture around 42 mkg of tea from own leaves. MRIL is primarily a producer of CTC tea, which accounts for around 96% of the total tea production.

In FY2018, on a standalone basis, the company reported a net profit of Rs. 67.3 crore on an operating income of Rs. 1597.8 crore, compared to a net profit of Rs. 30.5 crore on net sales of Rs. 1,388.7 crore in the previous year. On a consolidated basis, the entity reported a net profit of Rs. 219.2 crore in FY2018 on the back of an operating income of Rs. 2055.1 crore, against a net profit of Rs. 64.5 crore on net sales of Rs. 1772.1 crore in the previous year.

Key financial indicators (audited)

Standalone

	FY2017	FY2018
Operating Income (Rs. crore)	1483.07	1597.78
PAT (Rs. crore)	30.52	67.26
OPBDIT/OI (%)	2.2%	2.2%
RoCE (%)	6.0%	10.6%
Total Debt/TNW (times)	0.58	0.67
Total Debt/OPBDIT (times)	24.72	28.31
Interest coverage (times)	0.26	0.20

Source: Annual Reports of Company
Note:
1.The above table includes profit on compulsory acquisition of land by Government received in FY2017 and FY2018 as part of operating revenue; however, while assigning the rating, ICRA has considered the same as non-operating income
2. Financial numbers have been revised post publication of the last press release (dated June 08, 2018) based on the detailed financial schedules of the Annual report for FY2018, which has now been published

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 October 2018	Date & Rating June 2018	Chronology of Rating History for the Past 3 Years: Date & Rating in FY2018 August 2017	Date & Rating in FY2017 August 2016	Date & Rating in FY2016 August 2015
1	Term Loan	Long Term	360.00	349.41*	[ICRA]AA- &	[ICRA]AA- &	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA+ (Stable)
2	Fund-based Bank Facilities	Long Term	491.76	NA	[ICRA]AA- &	[ICRA]AA- &	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA+ (Stable)
3	Fund-based Bank Facilities**	Long Term/Short Term	163.92	NA	[ICRA]AA- &/ [ICRA]A1+ &	[ICRA]AA- &/ [ICRA]A1+ &	[ICRA]AA (Negative)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+
4	Non-fund-based Bank Facilities	Short Term	15.41	NA	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Commercial Paper Programme	Short Term	Nil	Nil	Withdrawn	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

**As on March 31, 2018, excluding installments payable within 31-Mar-19*

& Under rating watch with developing implications

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	Mar, 2015 – Sep, 2017	NA	FY2020-FY2024	360.00	[ICRA]AA- &
NA	Fund-based Bank Facilities	NA	NA	NA	491.76	[ICRA]AA- &
NA	Fund-based Bank Facilities**	NA	NA	NA	163.92	[ICRA]AA- &/ [ICRA]A1+ &
NA	Non-fund-based Bank Facilities	NA	NA	NA	15.41	[ICRA]A1+ &
NA	Commercial Paper Programme	NA	NA	NA	Nil	Withdrawn

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Source: MRIL

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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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