

McLeod Russel India Limited

May 06, 2019

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	360.00	360.00	Revised from [ICRA]A(Negative) to [ICRA]BBB- (Negative)
Fund-based Bank Facilities	491.76	491.76	Revised from [ICRA]A(Negative) to [ICRA]BBB- (Negative)
Fund-based Bank Facilities**	163.92	163.92	Revised from [ICRA]A(Negative)/[ICRA]A2+ to [ICRA]BBB- (Negative)/[ICRA]A3
Non-fund-based Bank Facilities	15.41	15.41	Revised from [ICRA]A2+ to [ICRA]A3
Total	1031.09	1031.09	

*Instrument details are provided in Annexure-1

**Fungible with LT facilities

Rationale

The rating revisions factor in further deterioration in MRIL's liquidity profile due to a slower-than-anticipated progress on asset monetisation and continued pressure on the profitability of the core tea operations of the company. While ICRA notes that a majority of the proceeds from the sale of the second tranche of tea estates has been received recently with a delay, MRIL's overall leveraging remains high. The high exposure to weak Group companies has been largely funded by short-term debt, thus further aggravating the tight liquidity position and exposing the company to significant refinancing risks. The company also has sizeable repayment obligations of its long-term debt in the near term, which would keep its liquidity position under stress, notwithstanding the receipt of the garden sale proceeds recently. Going forward, input costs pressure is expected to keep the operating profitability (OPM) of the company under pressure, despite the cost-control exercises undertaken. Trend in tea prices relative to costs and timely fruition of further deleveraging plans of the company and group would be important factors determining the overall financial risk profile. The ratings continue to favourably factor in MRIL's leading position among tea plantation companies in India, and the premium quality of its tea, which fetches higher realisation than industry averages. Moreover, profits from overseas operations, although reduced in the current year, have supported operating profits on a consolidated basis. However, the ratings also factor in the risks associated with tea for being an agricultural commodity, which depends on agro-climatic conditions, as well as the inherent cyclicity of the fixed-cost intensive tea industry that leads to variability in profitability and cash flows of bulk tea producers such as MRIL. In 9M FY2019, the improvement in tea prices was not commensurate with the increase in wage costs, which adversely impacted the operating profitability of most of the organised bulk tea players in North India, including MRIL. ICRA, nonetheless, notes that MRIL's considerable bought-leaf operations, along with the favourable age profile of its tea bushes, mitigate the risks associated with the fixed cost intensive nature of the bulk tea industry to an extent.

Outlook: Negative

The Negative outlook underpins ICRA's expectation that input cost pressure would continue to impact the operating profitability and cash flows from operation, which along with higher debt level (on account of exposure to Group companies) would keep coverage indicators depressed and liquidity stretched. The outlook could be revised to Stable in case of a significant increase in prices, relative to costs, thus leading to healthy operating profitability and/or higher-than-expected reduction in exposure to Group companies, leading to a lower debt burden. The quantum and timeliness of the reduction in debt would be a key rating sensitivity. Revision in outlook to Positive looks unlikely at present.

Key rating drivers

Credit strengths

Status of being one of the largest bulk tea producers in domestic markets, notwithstanding reduction in scale; 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 standalone 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. MRIL has sold 21 gardens in India, which is expected to reduce almost ~32 mkg of total production, while the African stake sale will reduce almost 5 mkg of tea production, thus reducing the global production to around ~80 mkg, going forward. Notwithstanding the reduction, MRIL still remains one of the largest bulk tea producers from India.

Superior quality of tea produced by MRIL; high productivity and bought-leaf operations reduce risks associated with the fixed-cost intensive nature of operations to some extent - The superior quality of tea fetches a premium over industry averages both in the domestic as well as in the export markets. The average realisation of MRIL's produce fetches a premium over auction averages, indicating superior quality of teas produced. The favourable age profile of MRIL's tea bushes, with around 72% of the Indian bushes below 50 years of age, helps record a healthy tea estate yield. This directly impacts the cost structure because of the fixed-cost intensive nature of the industry. Though the operating cost has increased primarily owing to increase in wages, ICRA understands that the company has taken major cost-reduction initiatives to reduce the overall impact of the same and the benefits are expected in the current year itself. Nonetheless, increase in input costs would continue to keep the profitability under pressure. A large bought-leaf operation, which aids in better absorption of fixed overheads, reduces the overall fixed cost intensity of the bulk tea business.

Credit challenges

Slower than anticipated progress on asset monetisation - The company has made slower-than-expected progress on its asset monetisation plans that has delayed the planned deleveraging of its balance sheet to an extent. While ICRA notes that a majority of the proceeds from the sale of the second tranche of tea estates has been received with a delay, MRIL's overall leveraging remains high.

Tightness in liquidity position- Delay in asset monetisation, loss making tea operations and significant debt repayment in the near term would keep liquidity position tight as per ICRA's estimates.

Exposure to Group companies increases the overall debt levels and puts pressure on debt coverage – Although MRIL used the proceeds from the sale of gardens to reduce debt, however, contrary to ICRA's expectation, the total debt outstanding still remains high on account of increased exposure to Group companies. ICRA notes that the company has plans to reduce its debt over the short term; however, continued exposure to Group companies, would keep MRIL's borrowings elevated at least over the short term.

Significant deterioration in financial risk profile- Pressure on core operating profitability persists as depressed tea prices not adequately compensating for the increase in wage costs, notwithstanding the cost-reduction initiatives taken by the company. In 9M FY2019, there was a considerable decline in operating profitability of the company. The performance of the overseas operations in CY2018 was also adversely impacted owing to subdued tea prices in the African market. Though non-operating income is likely to support the net profitability to an extent, input costs pressure is expected to keep the profitability of the company under pressure.

Risks associated with tea for being an agricultural commodity as well as the inherent cyclicity 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.

Liquidity position

MRIL's liquidity position remains stretched with deterioration in its core operating profitability and continued high exposure to Group companies. The delay in asset monetisation, loss making tea operations and significant debt repayment in the near term would keep liquidity position tight as per ICRA's estimates. Quantum and timeliness of deleveraging, for the company as well as the group, would be the key factor influencing the overall liquidity position going forward.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Indian Bulk Tea Industry
Parent/Group Support	Not applicable
Consolidation / Standalone	For arriving at the ratings, ICRA has analysed MRIL's consolidated financials comprising domestic operations as well as overseas operations through a wholly-owned subsidiary, Borelli Tea Holdings Limited, along with other stepdown subsidiaries mentioned in Annexure 2.

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. (EIL) 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 33,723 hectares (Ha) of total land under tea cultivation. 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 in FY2018. In the recent past, MRIL has sold 12 tea estates in Assam region and has signed an MoU to sell more estates, both in Assam and in Dooars. Post conclusion of the sale, the company would have a capacity to manufacture around 42 mkg of tea from its 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. 1,597.8 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. 2,055.1 crore against a net profit of Rs. 64.5 crore on net sales of Rs. 1,772.1 crore in the previous year. In 9M FY2019, the company reported a net profit of Rs. 314 crore on an operating income of Rs. 1,134 crore on a standalone basis.

Key financial indicators (audited)

Consolidated financials

	FY2017	FY2018
Operating Income (Rs. crore)	1806.29	2055.13
PAT (Rs. crore)	64.45	219.15
OPBDIT/OI (%)	2.8%	8.2%
RoCE (%)	7.3%	15.2%
Total Debt/TNW (times)	0.58	0.60
Total Debt/OPBDIT (times)	18.76	6.59
Interest coverage (times)	0.37	0.93

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Current Rating (FY2020)						Chronology of Rating History for the Past 3 Years				
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating May 2019		Date & Rating in FY2019 March 2019	Date & Rating in FY2019 October 2018	Date & Rating in FY2019 June 2018	Date & Rating in FY2018 August 2017	Date & Rating in FY2017 August 2016
1 Term Loan	Long Term	360.00	350.00	[ICRA]BBB- (Negative)		[ICRA]A (Negative)	[ICRA]AA- &	[ICRA]AA- &	[ICRA]AA (Negative)	[ICRA]AA (Stable)
2 Fund-based Bank Facilities	Long Term	491.76	NA	[ICRA]BBB- (Negative)		[ICRA]A (Negative)	[ICRA]AA- &	[ICRA]AA- &	[ICRA]AA (Negative)	[ICRA]AA (Stable)
3 Fund-based Bank Facilities**	Long Term/ Short Term	163.92	NA	[ICRA]BBB- (Negative)/ [ICRA]A3		[ICRA]A (Negative)/ [ICRA]A2+	[ICRA]AA- &/ [ICRA]A1+ &	[ICRA]AA- &/ [ICRA]A1+ &	[ICRA]AA (Negative)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+
4 Non-fund-based Bank Facilities	Short Term	15.41	NA	[ICRA]A3		[ICRA]A2+	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+	[ICRA]A1+

& 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]BBB-(Negative)
NA	Fund-based Bank Facilities	NA	NA	NA	491.76	[ICRA]BBB-(Negative)
NA	Fund-based Bank Facilities**	NA	NA	NA	163.92	[ICRA]BBB-(Negative)/ [ICRA]A3
NA	Non-fund-based Bank Facilities	NA	NA	NA	15.41	[ICRA]A3

Source: MRIL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Borelli Tea Holdings Limited	100.00%	Full Consolidation
Phu Ben Tea Company Limited*	100.00%	Full Consolidation
McLeod Russel Uganda Limited*	100.00%	Full Consolidation
Gisovu Tea Company Limited*^	60.00%	Full Consolidation
McLeod Russel Middle East DMCC*	100.00%	Full Consolidation
McLeod Russel Africa Limited*	100.00%	Full Consolidation
Pfunda Tea Company Limited*^	90.00%	Full Consolidation

*These are step-down subsidiaries of Borelli Tea Holdings Limited. ^in the current financial year, the group has signed MoU to divest their entire stake in Gisovu Tea Company Limited and 50% of their stake in Pfunda Tea Company Limited.

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