

July 15, 2022

Life Line Hatcheries: Ratings assigned

Summary of rating action

| Instrument* | Current Rated Amount (Rs. crore) | Rating Action |
|---------------------------------|----------------------------------|-----------------------------|
| Long-term/ Fund-based term loan | 29.50 | [ICRA]BBB(Stable); assigned |
| Total | 29.50 | |

*Instrument details are provided in Annexure-1

Rationale

While assigning the rating, ICRA has taken a consolidated view of Line Line Feeds India Pvt. Ltd. (LLF) and the promoter's proprietorship firm, Life Line Hatcheries (LLH), collectively referred to in this report as the Group, given their operational synergies, common promoters and the corporate guarantee extended by LLF to LLH.

The rating assigned to the Group factors in its healthy and diversified revenue streams through retail as well as institutional channels, its integrated nature of operations and moderately healthy financial risk profile. The Group has integrated poultry operations including breeder farms, hatcheries, contract farming, chicken processing and retail, enabling the Group to streamline its operations in line with industry trends. ICRA also notes the consistent growth in the overall scale of the Group with revenue growth in FY2022 at a CAGR of ~11% over the past four years, which is also spread across a diverse product portfolio of live bird sales in the wet market, processed and frozen chicken, poultry feeds, hatchable eggs, etc. This has supported a considerable improvement in the overall credit risk profile over the last few fiscals characterised by growing cash accruals and improved net worth supported by healthy return metrics. Moreover, ICRA expects the margins to improve in the long-term with the recent capex undertaken to backward integrate its operations into a soya extraction plant. ICRA also favourably factors in the extensive experience of the promoters in the poultry industry and the established relationships of the Group with its clients and local farmers.

The rating, however, is constrained by Group's exposure to high geographic concentration risk with the entire operation limited in and around Chikmagalur district of Karnataka. Any adverse event or a disease outbreak may adversely impact the overall production levels. The ratings are further constrained by the volatility in the cost of production largely driven by the movements in prices of key raw material, primarily soya bean and maize. Further, the Group has significant debt-funded capex, which is expected to exert pressure on the coverage indicators given that the ramp up of capacity utilisation and returns will take time. The ratings are also constrained by the working capital-intensive nature of operations accentuated by significant ongoing volatility in raw material prices and limited shelf life of the Group's products. Although the Group has some flexibility in converting its live birds into processed or frozen chicken with relatively higher shelf life.

The Stable outlook on the long-term rating reflects ICRA's expectation that the Group's overall scale will continue to grow, and its enhanced integration will enable it to maintain its return metrics.

Key rating drivers and their description

Credit strengths

Experienced promoters at the helm with established relationships with stakeholders – The Group benefits from the more than two decades of its promoter's experience in the poultry industry. The Group and its promoters enjoy goodwill among the local farmers and customers in and around the district of Chikmagalur. The Group also enjoys established relationships with its institutional clients in Karnataka, as well as those from Goa, Tamil Nadu and Kerala.

Integrated poultry operations with diverse product mix – The Group has an integrated range of operations from parent bird breeding and hatchery to processing and own retailing. Thus, the Group has a diversity in its product mix with revenues being derived from live birds, processed and frozen chicken (which together formed 78.7% of its total revenue in FY2022), poultry feed, hatchable eggs, breeder birds, etc. The sales and distribution are supported by an established retail network and institutional sales channel in Chikmagalur, nearby states and exports market (mainly Bhutan). Moreover, the Group sees significantly higher sales from its processed and frozen chicken segment (37.5% and 44.1% in FY2021 and FY2022, respectively) than its peers. Given the flexibility to process large proportion of live birds, the Group remains partly insulated from steep decline in demand prospects or periods of high cost of production, which can depress contribution margins.

Backward integration into soya extraction mill augur wells, going forward – The Group has recently set up a soya extraction plant with a total production capacity of 25,500 MT per annum, which would manufacture de-oiled cakes (DOCs) for the Group's in-house consumption. The soya extraction plant is expected to produce better quality soya DOC, will aid margin expansion and lend flexibility in inventory holding given the higher shelf life of raw material (soya bean) than DOCs.

Moderately healthy financial risk profile, though pressure on debt coverage indicators likely in near to medium term – The Group grew at a CAGR of ~11% from Rs. 315 crore to Rs. 480 crore (provisional figures) over FY2018 and FY2022. Although there was volatility in the profitability, it was healthy over the years with RoCE of 16.8% and operating margin of 11.0% in FY2022. Despite most of the capex being funded by debt, the gearing levels has been moderate and stood at 1.3 times as of March 31, 2022. However, the recent debt-funded capex for the soya extraction plant has moderated the coverage indicators, as reflecting in the Debt Service Coverage Ratio (DSCR) of 1.2 times in FY2022, which deteriorated from 2.8 times in FY2021, led by higher long-term repayment obligations. Another planned capex is for setting up a new hatcheries plant for LLH, which will further increase debt and exert pressure on the coverage indicators in near to medium term. The debt-to-operating profit ratio (TD/OPBIDTA) also remained high at 2.8 times in FY2022, but is expected to improve, going forward, supported by the returns being generated from the ongoing capex and recent backward integration. The Group has already achieved revenue of Rs. 179.50 crore in Q1 FY2023 against Rs. 111.55 crore during the same period in the previous financial year.

Credit challenges

High geographical concentration risk – The entire vertically integrated operations of the Group are largely concentrated in the limited region of Chikmagalur and its nearby districts in Karnataka. While ICRA notes that the group enjoys a strong market position, any adverse turn of natural events or any disease outbreaks in the region, will impact the Group's operations.

Margins remain exposed to volatile feed prices – The feed cost in the poultry sector is one of the key costs and constitutes ~70% of the total cost of production. The feed cost comprises several ingredients, but the primary raw material is soya DOC and maize. The prices of soya bean in FY2022 have been extremely volatile and touched new highs in the months from September to December 2021. The high raw material prices resulted in significantly high cost of production, resulting in weak or negative contribution margins during those periods.

Working capital intensive operations – The operations of the company are working capital intensive (NWC/OI of 27% in FY2022), which have been accentuated in recent times amid rising raw material prices. While there is limited credit period offered and received, The Group's working capital is driven by its high inventory days, which increased to 121 days in FY2022 over 90 days in FY2021. The company's inventory requirements vary in line with the procurement and processing season of its commodities, i.e., soya bean and maize. Moreover, the capex towards the soya extraction plant has also necessitated high working capital requirements, particularly for holding soya bean as well as soya DOC.

Inherent risks in poultry business – The poultry industry is exposed to diseases such as avian influenza (bird flu) outbreaks and the industry has also demonstrated cyclical and seasonality. Further, the poultry industry is fragmented with intense competition leading to pressure on pricing and margins.

Liquidity position: Adequate

The Group’s liquidity is adequate with moderate cushion in cash credit limit utilisation and free cash balances maintained with the bank for contingency. The company is further planning to enhance its limits, which will provide additional flexibility. While there are significant repayments in FY2023, the same are expected to be covered by the projected net cash accruals.

Rating sensitivities

Positive factors – ICRA could upgrade LLF’s rating if there is substantial growth in revenues while maintaining operating margins and improving liquidity. Specific credit metrics that could lead to an upgrade of LLF’s rating include TD/OPBIDTA being lower than 2.3 times on a sustained basis.

Negative factors – Negative pressure on LLF’s rating could arise if there is a sustained decline in revenues and operating margins or deterioration in liquidity. Further, higher than envisaged debt-funded capex or any major withdrawals, resulting in deterioration of coverage indicators may also trigger a downgrade. Specific credit metrics that could lead to rating downgrade include DSCR below 1.5 times on a sustained basis.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|---|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology |
| Parent/Group Support | Not applicable |
| Consolidation/Standalone | Consolidated |

About the company

Life Line Hatcheries (LLH) was founded by Mr. K. Kishore Kumar Hegde in 1995 after the parent company Life Line Feeds India Pvt. Ltd. (LLF) was founded in 1992. LLF is one of the leading poultry companies operating in the broiler segment in Karnataka with its entire operational set up concentrated in Chikmagalur district. In 1985, the promoters started an animal feed distribution dealership through the company, ‘Om Traders’. The company later added table eggs and day-old chicks in its product portfolio. Later, the promoter entered into animal feed manufacturing under the brand name, ‘Nandan’, followed by poultry breeder farming in 1998. Thereafter, the company ventured into value-added products such as processed and frozen chicken, which were sold through the retail chain brand, ‘Life Line’s Tender Chicken’.

LLF’s operations are vertically integrated, with infrastructure facilities ranging from a feed mill, a processing facility, four hatcheries (through LLH), 12 breeder farms, 44 retail outlets, and more than 500 broiler farms.

Key financial indicators (Audited/Provisional)

| Consolidated | FY2020 (A) | FY2021 (A) | FY2022 (Prov.) |
|--|------------|------------|----------------|
| Operating Income (Rs. crore) | 376.2 | 419.9 | 480.0 |
| PAT (Rs. crore) | 8.0 | 19.5 | 22.1 |
| OPBDIT/OI (%) | 8.1% | 11.6% | 11.0% |
| PAT/OI (%) | 2.1% | 4.6% | 4.6% |
| Total Outside Liabilities/Tangible Net Worth (times) | 1.6 | 1.6 | 1.5 |
| Total Debt/OPBDIT (times) | 3.7 | 2.8 | 2.9 |
| Interest Coverage (times) | 3.1 | 4.1 | 4.4 |

Standalone performance, PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation, OI: Operating Income

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

| | Instrument | Current Rating (FY2023) | | | | Chronology of Rating History for the past 3 years | | |
|---|------------|-------------------------|--------------|--------------------|-------------------|---|-------------------------|-------------------------|
| | | Type* | Amount Rated | Amount Outstanding | Date & Rating | Date & Rating in FY2022 | Date & Rating in FY2021 | Date & Rating in FY2020 |
| | | | (Rs. crore) | (Rs. crore) | | - | - | - |
| 1 | Term Loan | Long-term | 29.50 | 0.00 | [ICRA]BBB(Stable) | - | - | - |

Amount in Rs. crore

Complexity level of the rated instrument

| Instrument | Complexity Indicator |
|------------|----------------------|
| Term Loan | Simple |

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's 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 Loans | FY2023 | NA | March 2032 | 29.50 | [ICRA]BBB (Stable) |

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure-2: List of entities considered for consolidated analysis

| Company Name | Ownership | Consolidation Approach |
|----------------------------|-----------|------------------------|
| Life Line Hatcheries | NA* | Full consolidation |
| Life Line Feeds India Pvt. | NA** | Full consolidation |

*Promoter company

**Parent company

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