

January 04, 2024

Kerala Nut Food Co.: Long-term rating downgraded; short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term – Interchangeable*	(7.00)	(7.00)	[ICRA]BB (Stable); downgraded from [ICRA]BB+ (Stable)
Short Term – Fund Based	50.00	50.00	[ICRA]A4+; reaffirmed
Short Term – Interchangeable – Others*	(4.00)	(4.00)	[ICRA]A4+; reaffirmed
Short Term – Interchangeable – Letter of Credit*	(5.00)	(5.00)	[ICRA]A4+; reaffirmed
Total	50.00	50.00	

*Instrument details are provided in Annexure-I; *Sub-limit of Rs. 50 crore short-term fund-based limit

Rationale

The downgrade in the long-term rating takes into consideration the deterioration in Kerala Nut Food Co.'s (KNFC) debt protection metrics, which are likely to remain under pressure in FY2024. ICRA notes that the firm reported losses in FY2023 on account of a sharp drop in cashew kernel prices during the second half of FY2023 against large inventory imported at a relatively higher price. Additionally, due to quality-related issues in an export order, a part of the shipment was returned, which impacted the firm's export orders. Consequently, the firm's working capital intensity increased significantly on the back of inventory build-up, resulting in high interest cost towards elevated working capital limit utilisation. Nevertheless, comfortable receivable cycle and buffer in the firm's bank limits supported its operations in FY2023. The ratings are also impacted by the firm's weakened financial profile, as reflected by stagnant revenues in FY2022 and FY2023, and the firm's vulnerability to volatility in cashew kernel/ RCN prices, which could result in inventory related risks. While the firm is gradually increasing its domestic sales, given the unfavourable export demand, the firm's revenues in FY2024 are likely to remain stagnant with recovery in profitability, as per ICRA's estimates. The ratings also factor in the intense competition from Vietnam in the export market and from numerous processors in the domestic market, which affects the firm's pricing flexibility. Further, any adverse regulatory or quality-related risks could also impact the firm's business as witnessed in FY2023. The ratings also consider the inherent risk associated with partnership firms, including the risk of capital withdrawals, which have been significant in FY2021 and FY2022.

The ratings, however, continue to factor in the extensive experience of KNFC's promoters in the cashew processing industry and established relationship with its customer base, which would continue to support its business, though with limited growth. The ratings continue to derive comfort from the established brand position of KNFC in the cashew processing segment, along with KNFC's established distribution network in the surrounding areas of Karnataka, India. The firm caters to customers in the export market, comprising traders and food processors. The company has a long-term association with its customers in Japan and Europe, from which it gets repeat orders. This apart, the company constantly endeavours to add new customers and enter new geographies, especially in the recent years, when the share of exports declined, and the firm was able to compensate it with an increase in domestic sales. This has helped the firm sustain its top line to some extent. Further, the firm's established track record of procurement from African regions continues to be a key credit positive. The ratings also derive comfort from the adequate liquidity of the firm, which is supported by moderate working capital utilisation and nil repayment obligations.

The Stable outlook on the rating reflects ICRA's opinion that KNFC will continue to benefit from the established market position and customer base developed over the years, through which the firm has been able to garner regular orders.

Key rating drivers and their description

Credit strengths

Experienced promoters in cashew processing industry – The partners of KNFC have more than two decades of experience in the cashew processing industry. Further, the firm has established relationship with its suppliers, resulting in ease of procurement of RCNs.

Established track record with suppliers/customers and a diversified customer base – The firm sells processed cashew kernels mainly to a large and diversified base of wholesalers in the domestic market. Over the past years, it has developed a long-term relationship with several wholesale buyers in the domestic market, which is reflected in regular orders and increasing scale.

Credit challenges

Weakened financial profile with large inventory related risks – The firm's financial profile is marked with a small scale, which has remained stagnant during the recent years and losses in FY2023. Nevertheless, profitability is likely to recover in FY2024, despite stable revenue. The debt protection metrics of the firm deteriorated, as reflected by a gearing of 2.2 times as on March 31, 2023 (0.5 times as on March 31, 2022), due to high working capital borrowings at the year-end. Further, interest coverage and DSCR also declined to -1.1 times and -1.0 times in FY2023 against 1.6 times and 1.6 times in FY2022, respectively. Moreover, the firm is exposed to inventory related risks as witnessed in FY2023 when its working capital intensity increased to around 70% in FY2023 compared to around 45% in FY2022 due to large inventory build-up. However, ICRA believes that subsequent to a likely improvement in profitability in FY2024, moderation in working capital cycle and a reasonable buffer in bank limits would support the firm's operations.

Margins exposed to volatility in cashew prices and foreign exchange fluctuations – The procurement of RCN is seasonal with the major portion purchased during April-June period. The prices of cashew kernels and RCNs vary on a daily basis, depending on the international demand-supply scenario, exposing the company's margins to price fluctuations as well as forex risks. Moreover, the availability of RCNs is subject to agro-climatic risks. KNFC's operating margins declined to -5.8% in FY2023 from 3.7% in FY2022 owing to a sharp decline in price realisation. Considering a likely recovery in price realisation in FY2024, the operating margins are likely to improve to around 4%.

Intense competition with low product differentiation and value addition limits pricing flexibility – The firm faces stiff competition from many small units within Karnataka as well as other nearby states, which increased competition. Further, the Indian players face competition from other countries in the export market. The industry is highly fragmented because of the low entry barriers owing to the low capital and technology intensive nature of operations. The industry is highly dependent on labour and is affected by labour shortage issues from time to time. Lack of product differentiation and intense competition restrict its bargaining position and pricing flexibility.

Risks related to partnership nature of the firm – KNFC is exposed to the risks related to a partnership firm, including the capital withdrawal risk. However, no capital withdrawal has been observed in the past three years.

Exposure to changes in trade policies, regulatory changes and quality-related risks – The firm is exposed to risks associated with any adverse change in trade policies and regulations related to import of RCN and export of cashew kernels. Additionally, any quality-related issue, as witnessed in FY2023, could impact its business as well as pricing strength.

Liquidity position: Adequate

KNFC's liquidity profile remains adequate, supported by recovery in profitability, resulting in positive fund flow from operations of nearly Rs. 1.0 crore expected in FY2024 against no major capital expenditure plan or large term loan repayment obligation. Moreover, the average utilisation of the fund-based limits, which stood at 80% in FY2023, is likely to moderate in FY2024, leaving reasonable buffer for any urgent requirement. Additionally, the promoter can infuse unsecured loans in case of any further fund requirement.

Rating sensitivities

Positive factors – The ratings may be upgraded if the firm demonstrates a healthy revenue growth along with an improvement in its profitability, working capital cycle and debt coverage indicators on a sustained basis.

Negative factors – Pressure on the ratings could arise if there is a decline in the firm’s revenue or profitability, leading to weaker coverage indicators on a sustained basis. Moreover, any large capital withdrawal or an increase in the working capital intensity, leading to a deterioration in the liquidity position, could trigger ratings downgrade. Specific credit metrics that could lead to a downgrade of KNFC’s ratings include an interest coverage of less than 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	The ratings are based on the company’s standalone financial profile.

About the company

Established in 1965, Kerala Nut Food Company is primarily involved in the processing of plain cashew kernels from raw cashew nuts (RCNs), which is the major revenue contributor. The firm also operates in other allied activities like trading of cashew kernels and RCNs, and sale of byproducts such as cashew husk. KNFC operates from its 22 manufacturing facilities in Kerala and Tamil Nadu, where it has an aggregate installed capacity to process 77.6 lakh kg/year. The firm is a part of the renowned Kerala-based K. Parameswaran Pillai Group, which was founded in the early part of the 20th century by Late K. Parameswaran Pillai. KNFC is now managed by Dr. Unnikrishnan. The firm employs 2,650 people, most of whom are unskilled labourers.

Key financial indicators (audited)

KNFC Standalone	FY2022	FY2023
Operating income	61.0	63.3
PAT	0.2	-7.9
OPBDIT/OI	3.7%	-5.8%
PAT/OI	0.4%	-12.5%
Total outside liabilities/Tangible net worth (times)	0.7	2.4
Total debt/OPBDIT (times)	4.9	-8.8
Interest coverage (times)	1.6	-1.1

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Source: ICRA Research, Company data

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current rating (FY2024)			Chronology of rating history for the past 3 years			
	Type	Amount rated (Rs. crore)	Amount outstanding as on March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
				Jan 04, 2024	Nov 07, 2022	Dec 28, 2021	Mar 22, 2021
1 Interchangeable	Long-term	(7.00)	--	[ICRA]BB (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)
2 Fund Based	Short-term	50.00	--	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A3
3 Interchangeable - Others	Short-term	(4.00)	--	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A3
4 Interchangeable - Letter of credit	Short-term	(5.00)	--	[ICRA]A4+	[ICRA]A4+	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Interchangeable	Simple
Short-term – Fund based	Simple
Short-term – Interchangeable – Others	Simple
Short-term – Interchangeable – Letter of credit	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 are available on ICRA's website: [Click Here](#)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash credit*	NA	NA	NA	(7.00)	[ICRA]BB (Stable)
NA	EPC/PCFC	NA	4.6%	NA	50.00	[ICRA]A4+
NA	FBD*	NA	NA	NA	(4.00)	[ICRA]A4+
NA	Letter of credit*	NA	NA	NA	(5.00)	[ICRA]A4+

Source: Firm, *Sub-limits of Rs. 50 crore short-term fund-based limit, Interchangeable

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

Annexure II: List of entities considered for consolidated analysis: Not applicable

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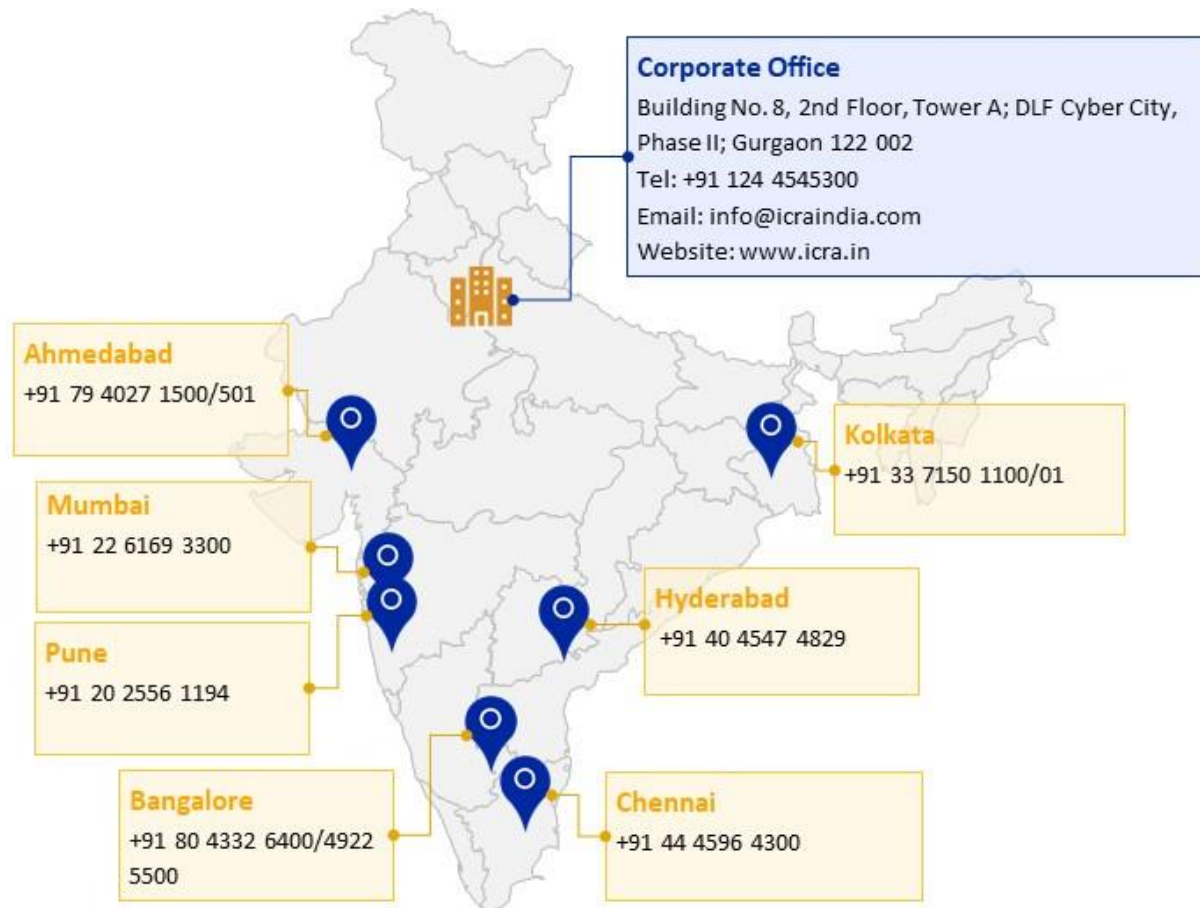
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