

January 10, 2024

Mehsana District Co-Operative Milk Producers' Union Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit/Working Capital Limits	1,570.00	1,570.00	[ICRA]AA+ (Stable); Reaffirmed
Short-term – Non-Fund based Limits	25.00	25.00	[ICRA]A1+; Reaffirmed
Long-term/ Short-term – Unallocated Limits	5.00	5.00	[ICRA]AA+ (Stable)/[ICRA]A1+; Reaffirmed
Total	1,600.00	1,600.00	

*Instrument details are provided in Annexure-I

Rationale

The reaffirmation of ratings for Mehsana District Cooperative Milk Producer's Union Limited (Dudhsagar/ the union) considers the expectation of stable financial performance in the near term, given the established position of the company as a leading dairy processing unit (DPU) under Gujarat Co-operative Milk Marketing Federation (GCMMF)/ Amul, the apex marketing federation with significant pricing power in the domestic market. Dudhsagar reported topline YoY growth of 15% in FY2023 to Rs. 6,833 crore from better realisation and sales volumes. Further, the company is expected to report moderate revenue growth in FY2024 owing to flattish sales realisation in the current fiscal, while the margin is expected to improve on account of lower milk procurement costs due to better availability and lower logistics costs than FY2023. ICRA also notes that the union provides assured inventory off-take to its DPUs.

The ratings also consider the robust procurement setting under the cooperative model in Mehsana (Gujarat), which ensures regular supply of milk to the union by village cooperative societies (VCS). Additionally, Dudhsagar has an arrangement for procuring milk from non-VCS members outside Gujarat, which ensures uninterrupted supply of raw milk throughout the year. Further, the ratings are supported by the DPUs control over milk prices under the cooperative model through dual price payment mechanism wherein milk is purchased at provisional prices from VCS throughout the year and most of the pool price is distributed to farmers at the end of the year, with the union having the flexibility to retain funds.

The ratings, however, remain constrained by the average financial risk profile of the union characterised by modest profitability and net worth base owing to the nature of the dairy cooperative business model wherein most of the operating surplus is passed on to milk producers, leading to limited retention of profits in the business. The adjusted operating margins stood lower at 4.7% in FY2023 over 5.0% in FY2022 owing to higher milk procurement rates amid shortage of milk supply due to lumpy disease impact in FY2023 and rise in logistics costs. Also, Dudhsagar is planning to undertake a sizable debt-funded capex in the near-term to modernise its milk powder division and enhance its production capacities in the ultra-high temperature (UHT) milk, ice cream, yogurt and cottage cheese (*paneer*) categories, which is expected moderate the capital structure and coverage indicators to an extent in the near term.

The ratings also remain constrained by the low utilisation of installed capacities of plants outside Gujarat, which impacts its return indicators to an extent. The ratings continue to factor in the union's exposure to agroclimatic and environment risks, regulatory changes, and disease outbreaks among livestock, which could have a material impact on its dairy operations. ICRA also notes the contingent liabilities pertaining to the buffalo cess of ~Rs. 318.9 crore levied by the State Government of Haryana, as of March 31, 2023. Dudhsagar has challenged the jurisdiction of the state to levy such a cess and the matter is

currently sub judice. Any unfavourable outcome on this matter remains critical from a credit perspective, given the large value at dispute. The issue will remain a monitorable from a rating perspective.

The Stable outlook on the long-term rating reflects ICRA's expectation that Dudhsagar will continue to benefit from its strong milk procurement capability, established dairy operation, and its continued strategic importance to GCMMF. The revenue is expected to witness stable growth over the medium term, while profitability would continue to remain at moderate levels.

Key rating drivers and their description

Credit strengths

Established market position driven by important standing in cooperative value chain of GCMMF – Dudhsagar is one of the leading unions among the 18 milk unions under GCMMF and has an aggregate milk processing capacity of up to 50 lakh litres per day (LLPD). Dudhsagar contributed ~12.6% to GCMMF's total income during FY2023. Through its unions, GCMMF has built a cooperative structure with a strong milk collection base of over 35 lakh farmers from more than 18,500 villages. It commands a significant market share in the Indian dairy industry and largely controls the prices of milk and milk products in India. Dudhsagar, hence, derives significant financial flexibility as part of the GCMMF cooperative structure. Further, under the cooperative model, GCMMF's DPUs maintain control over raw milk prices by the dual price payment mechanism wherein milk is purchased at provisional prices from VCS throughout the year and most of the pool price is distributed to farmers at the end of the year; although the union has the flexibility to retain funds.

Established milk procurement system from VCS under cooperative model alongside milk procurement arrangement with non-VCS members outside Gujarat de-risk milk availability issues – Dudhsagar has an established milk procurement system under its cooperative model in Mehsana, which ensures regular supply of milk to the district union by VCS. Also, Dudhsagar has an arrangement for procuring milk from non-VCS members outside Gujarat, which ensures uninterrupted supply of raw milk throughout the year.

Geographically diversified presence with two dairy processing units in North India – Dudhsagar owns six dairy plants in and around Mehsana with a combined processing capacity of 25 LLPD, along with two plants in Haryana (Manesar and Dharuhera) with a capacity of 10 LLPD and 15 LLPD, respectively. The union also owns chilling plants across Rajasthan, Haryana and Uttar Pradesh in addition to its processing facilities. Dudhsagar's geographically diversified presence provides operational flexibility in terms of a diversified revenue stream and a strong milk procurement arrangement.

Favourable dairy industry growth prospects – The Indian dairy industry is expected to continue to grow on the back of steady supply of milk, with the country being the world's largest milk producer. Increase in demand for milk and milk products due to rising disposable income and increasing health consciousness are other positive demand factors.

Credit challenges

Moderate financial risk profile; planned debt-funded capex to keep coverage numbers under check in near to medium term – Despite its long operational history, its large scale of operations and a strong business risk profile, Dudhsagar has an average financial risk profile characterised by a relatively moderate net worth, leverage capital structure, modest operating profitability level and consequent moderate coverage indicators. The union follows a business model, wherein the price differential for their milk supply is paid to members at the end of the year, which provides them with strong flexibility over the surplus pay-outs after looking at all their payment obligations, including debt and capex. Further, Dudhsagar is planning a large debt-funded capex of Rs. 650 crore for modernising its powdered milk facilities and expanding its UHT capacity at the Mehsana plant, while expanding its capacity for ice cream, yogurt and *paneer* at its Haryana plants. The same will be largely debt-funded and are expected to be completed by mid-FY2025. Though the same is expected to improve operational efficiencies and increase capacities, the coverage metrics are expected to remain under check in the near to medium term. However, healthy financial flexibility and adequate liquidity from the assured off-take from GCMMF supports its credit profile.

Below optimum utilisation of milk processing capacities of plants located outside Gujarat – Dudhsagar's plants in Haryana have been operating below their optimum capacity, at ~26-35% of their installed processing capacity for many years now. The

capacity utilisation of the plants also varies from the production schedule given by GCMMF to the union. At an aggregate level, the union’s capacity utilisation has been moderately utilised during the year, which remained at 55% in FY2023 over 58% in FY2022.

Exposure to volatile product prices and regulatory changes along with external factors like weather and disease outbreaks

– The union is exposed to risks related to agro-climatic factors, such as droughts and disease outbreaks, leading to increase in cattle diseases, which may adversely impact milk production and have a significant material impact on its dairy operations. The same was witnessed in FY2023 with the emergence of the lumpy disease that had affected milk supply.

Contingent liabilities largely pertaining to Haryana Murrah Buffalo Cess – The union has a sizable contingent liability pertaining to the Haryana Buffalo Cess. The said milk cess was started in 2001 by the State Government of Haryana under the Haryana Murrah Buffalo and Other Milch Animals Breed (Preservation and Development of Animal Husbandry and Dairy Development Sector) Act, 2001. The cess is applicable to milk processing plants in the state. The contingent liability due to the cess as of the end of FY2023 stood at ~Rs. 318.9 crore (P.Y., ~Rs. 243.0 crore). Dudhsagar has challenged the jurisdiction of the state to levy such a cess and the matter is currently sub judice. Any unfavourable outcome on this matter remains critical from a credit perspective, given the large value at dispute.

Liquidity position: Adequate

Dudhsagar has adequate liquidity since it is paid by GCMMF on a daily basis and suppliers are paid every 10 days. Further, the average working capital utilisation remained at ~68% of the drawing power and ~18% of the sanctioned limits over the last 12 months ending in October 2023, resulting in requisite cushion in terms of unutilised limits. Dudhsagar has moderate repayment obligations of ~Rs. 58 crore in FY2024; although expected to increase from FY2025 due to its new debt-funded capex plans. Overall, ICRA expects Dudhsagar to comfortably meet its near-term commitments through internal accruals. Dudhsagar passes back the surplus to farmers at the end of the year in the form of price differences, which stood at Rs. 375 crore in FY2023. This is provided from the surplus after meeting all obligations of the union, which provides much needed flexibility to the company.

Rating sensitivities

Positive factors – Any near to medium term rating upgrade is constrained, given the almost sole dependence of Dudhsagar on GCMMF for product off-take and brand positioning.

Negative factors – Downward pressure on the rating could emerge if there is significant drop in sales as well as realisations leading to reduction in profitability, impacting return and coverage indicators, or any material weakening of the liquidity position. Downward pressure could also emerge if there is a weakening of the credit profile of GCMMF or reduced strategic importance of the union for GCMMF.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	The rating assigned to Dudhsagar factors in the high likelihood of GCMMF extending financial support to it because of the cooperative structure and GCMMF being the apex marketing federation for all unions in Gujarat. Further, most of Dudhsagar’s sales is routed through GCMMF and, hence, given the close business linkages between them, ICRA expects GCMMF to be willing to extend financial support to Dudhsagar to protect its reputation from the consequences of a union’s distress.
Consolidation/Standalone	Standalone

About the company

Incorporated in 1960, Dudhsagar is a co-operative district producers' milk union established under the three-tier cooperative structure of Gujarat, known as 'Anand Pattern' or 'Amul Structure'. Dudhsagar procures milk from around 1,240 member VCS of around 6.1 lakh farmers, who hold the entire shareholding in Dudhsagar Dairy. It had a total milk processing capacity of 50 LLPD as on March 31, 2023, from its dairy plants in Gujarat and Haryana.

Key financial indicators (audited)

Dudhsagar Standalone*	FY2022	FY2023
Operating income	5,923	6,833
PAT	340	394
OPBDIT/OI	5.0%	4.7%
PAT/OI	5.7%	5.8%
Total outside liabilities/Tangible net worth (times)	2.9	2.5
Total debt/OPBDIT (times)	2.6	1.2
Interest coverage (times)	5.2	6.3

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2024)			Chronology of rating history for the past 3 years			
		Amount rated (Rs. crore)	Amount outstanding as of March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	
				Jan 10, 2024	Oct 25, 2022	Jul 29, 2021	Apr 02, 2020	
1 Fund-based – Cash Credit/Working Capital Limits	Long term	1570.00	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	
2 Non-Fund based Limits	Short term	25.00	-	[ICRA]A1+	[ICRA]A1+	-	-	
3 Unallocated Limits	Long term and short term	5.00	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	-	-	
4 Term Loans	Long term	-	-	-	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Cash Credit/Working capital Limits	Simple
Short -term – Non- Fund based Limits	Very Simple
Long-term/ Short -term – Unallocated Limits	Not Applicable

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	Fund-based – Cash Credit/Working Capital Limits	NA	NA	NA	1570.00	[ICRA]AA+ (Stable)
NA	Non-Fund based limits	NA	NA	NA	25.00	[ICRA]A1+
NA	Unallocated limits	NA	NA	NA	5.00	[ICRA]AA+ (Stable)/ [ICRA]A1+

Source: Company

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

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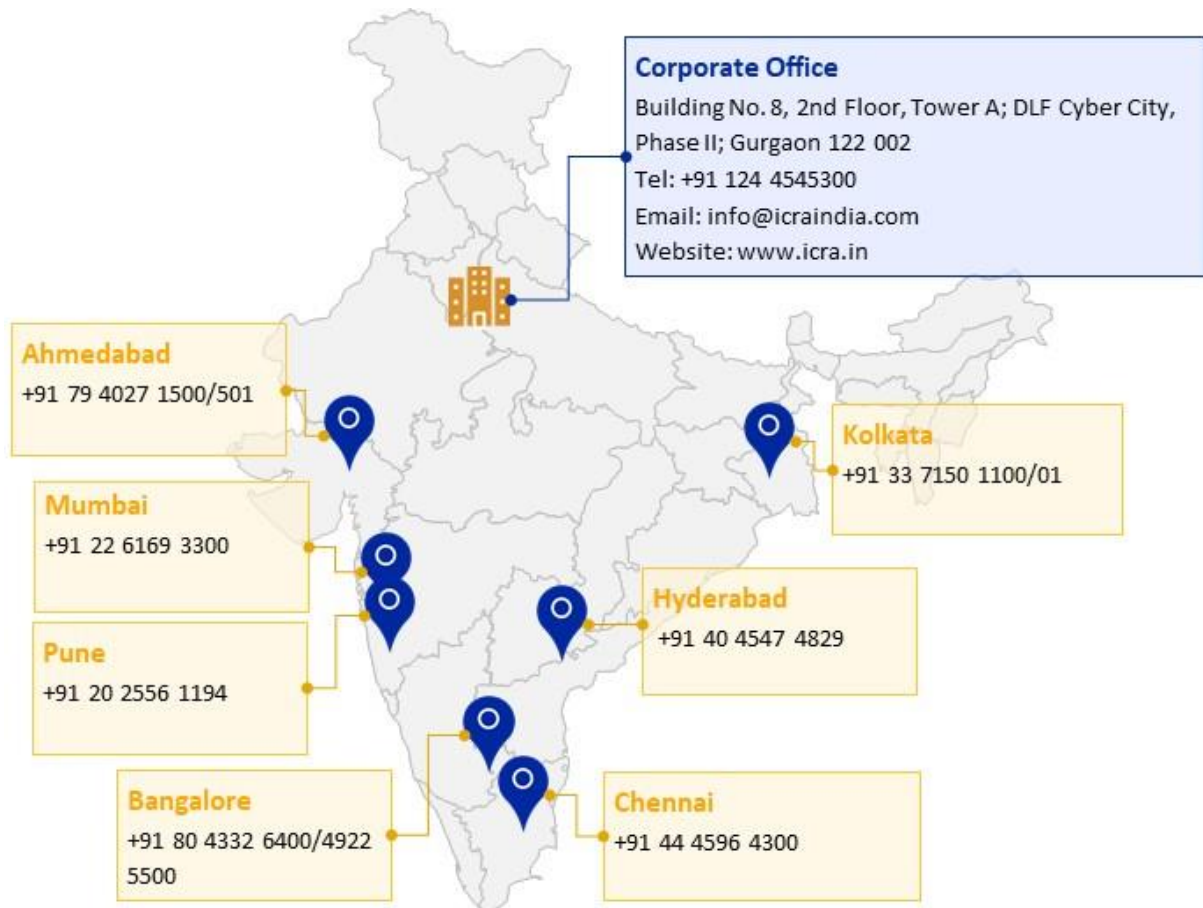
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Branches



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