January 14, 2025

M. K. Shah Exports Limited: Ratings reaffirmed; outlook revised to Stable from Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term – Fund-based - Term loans	104.00	104.00	[ICRA]A(Stable); reaffirmed, outlook revised to Stable from Negative
Long term/Short term – Fund-based-Working capital facilities^	80.50	80.50	[ICRA]A(Stable)/[ICRA]A2+; reaffirmed; outlook revised to Stable from Negative
Long term/Short term – Unallocated limit	5.50	5.50	[ICRA]A(Stable)/[ICRA]A2+; reaffirmed; outlook revised to Stable from Negative
Total	**190.00**	**190.00**	

**Instrument details are provided in Annexure-I; ^Includes cash credit, WCDL, export packing credit*

Rationale

To arrive at the ratings, ICRA has taken a consolidated view of M. K. Shah Exports Limited (MKSEL), M. K. Shah Teas LLP (LLP) and M. K. Shah Realty (MKSR), together referred to as the Group, given the common management, operational and financial linkages and cash flow fungibility among the entities.

The revision in the rating outlook reflects ICRA's expectations that the company's performance will improve in FY2025, supported by a significant rise in orthodox (ODX) tea prices. The performance is likely to remain stable in FY2026 as well. The Group's realisations increased by Rs. 68/kg during April-November 2024, which is expected to support the revenue and profits in the current fiscal and offset the cost impact of crop loss (currently at ~2 lakh kg) in the current tea season. The absence of any wage hikes in the current fiscal is expected to further support the overall profits of the entity. Going forward, MKSEL's cost structure may moderate due to the possibility of wage rate hikes in FY2026; however, the performance is likely to remain stable owing to a firm demand for orthodox tea in the global market.

The ratings continue to factor in MKSEL's established presence as one of the largest producers of ODX tea in India. MKSEL had acquired eight gardens in FY2019 from McLeod Russel India Limited (MRIL), which significantly increased its scale of operations. Going forward, the favourable age profile of the tea bushes and MKSEL's focus on improving productivity are likely to support its cost structure. The consolidated leverage ratio (total debt/OPBDITA) moderated in FY2024 but is likely to improve in the current fiscal, driven by increased profitability and sizeable prepayments on the back of better accruals. At present, MKSEL is entitled to receive a subsidy of Rs. 10/kg from the Assam Government on the production of ODX tea as well as tax exemption on agricultural income. Besides MKSEL, both MKSR and LLP receive interest subsidy on the working capital, supporting the Group's profitability.

The ratings, however, factor in the risks of tea being an agricultural commodity as well as the cyclicality inherent in the fixed-cost intensive nature of the industry that leads to volatility in the profits and cash flows of bulk tea producers such as MKSEL, evident from the impact of the wage hike in October 2023 on the margins. While the wage rates were not revised in the current fiscal, it is expected to increase, impacting the cost structure of the entire industry, including MKSEL. Hence, the quantum of the wage rate increase would be a key monitorable, going forward. The ratings also remain constrained by the company's sizeable financial exposure to Group entities; however, with a ramp-up of operations, adequate revenues will support the

ROCE. Nevertheless, a steady level of non-operating income (rent from real estate properties, interest on capital invested in Group entities etc) supports MKSEL's cash accruals to some extent.

Key rating drivers and their description

Credit strengths

Expected improvement in performance in FY2025 – MKSEL's performance has improved significantly in the current year till date, driven by a sharp rise in ODX tea prices, after a weaker-than-expected performance in FY2024. On a cumulative basis, the average realisations till the 45^{th} sale improved considerably by Rs. 68/kg. The full-year realisations are expected to remain in line, though with some moderation on account of the subdued prices expected in the last quarter of the fiscal. Along with this, the entity maintains high productivity relative to the industry standards that will continue to favour the cost structure. ICRA also estimates the Group's profitability and debt protection metrics to remain comfortable in the medium term.

Favourable age profile of tea bushes and operational efficiency positively impact cost structure – MKSEL's garden costs are largely fixed, in line with that of the industry, with labour costs accounting for a major part of the cost of production. Hence, the profitability of the bulk tea producers is highly correlated to productivity. MKSEL follows sound garden practices and continuous uprooting and fresh plantation, which ensure a favourable age profile of its bushes. Nearly 70% of the bushes are less than 50 years old, supporting the productivity. In FY2021, however, MKSEL's yield was affected by the pandemic and the yield of the acquired gardens was severely impacted by the flood in Upper Assam, pulling down the overall yield to 1,566 kg/hectare in FY2021 from 2,011 kg/hectare in FY2020. Nevertheless, MKSEL's focus on improving the yield, particularly that of the acquired gardens, led to a significant rise in the overall yield to 2,199 kg/hectare in FY2024 from 1,939 kg/hectare in FY2022. In the current fiscal, the productivity remains in line even amid a sizeable crop loss in the national tea market. The sustenance of high yields is likely to mitigate the risks associated with the fixed-cost nature of the industry, favourably impacting the company's cost structure and hence profitability.

Experienced promoters and established presence as one of the largest producers of ODX tea in India – MKSEL, incorporated in 1999, is one of the largest ODX (orthodox) tea producers in India. The promoters have a vast experience in the tea plantation sector and the export market. After the acquisition of eight tea estates from MRIL in FY2019, MKSEL's scale of operations has increased substantially. At present, it manufactures only ODX tea with an area under cultivation of 8,460 hectares (as of FY2024) spread across 13 tea gardens in Assam compared to 2,513 hectares and five tea estates in FY2018 (prior to the acquisition). In FY2024, MKSEL's production stood at 18.6 million kg (Mkg) and accounted for around 18% of the overall ODX tea produced in India.

In the current fiscal, MKSEL's tea production till November 2024 stood at 18.2 Mkg vis-à-vis 18.4 Mkg during the same period in the last fiscal. The superior quality of MKSEL's ODX tea commands a significant premium over the North Indian auction averages. In addition to sales through auction houses and private parties, MKSEL exports a portion of its produce. In this season, the entity has also started to sell through private auctions, resulting in some cost savings. A major portion of the Group's export is routed through LLP, which procures tea from MKSEL. Additionally, tea exports through the realty entity - MKSR - supported the overall export volumes in the last fiscal.

Conservative capital structure – MKSEL availed a sizeable amount of long-term debt (Rs. 115 crore) to acquire gardens from MRIL in FY2019, and its working capital borrowing also increased with the scaling up of operations. However, the company's consolidated capital structure remained conservative, reflected in a gearing of 0.5 times as on March 31, 2024. The consolidated debt level is likely to decline due to the prepayment of term loans (around Rs. 20 crore prepaid in the last fiscal), supported by the healthy accruals in the current fiscal. Reduction in debt and improved profits are likely to strengthen the consolidated debt coverage metrics, going forward.

Credit challenges

Risks of tea being an agricultural commodity and inherent cyclicality of fixed-cost intensive tea industry – Tea production depends on agro-climatic conditions, making it vulnerable to agro-climatic risks. Moreover, most of the tea estate costs are fixed, with manpower expenses accounting for a major portion of the production cost. Given the fixed-cost intensive nature of the tea business, the yield of the gardens and the out-turn ratio (defined as black tea produced to green leaf consumed) directly impact the cost structure and hence the profitability of bulk tea players, including MKSEL.

Profitability and cost structure vulnerable to wage rate hikes in the near term – MKSEL's operating margins had suffered significantly in the last fiscal (FY2024) because of the subdued realisations and wage rate revisions. The basic daily wages for tea estate workers in Assam increased by Rs. 18 per manday from October 2023, which pushed up the cost of made tea by ~Rs. 9-10/kg. However, a sharp rise in MKSEL's realisations in the current fiscal would offset the impact of the cost inflation to an extent. Nonetheless, the likely increase in wage rates in the coming fiscal is likely to adversely impact the cost structure of the bulk tea industry, including MKSEL, in the medium term and the quantum of the increase would remain the key monitorable, going forward. Any sharp hike without a commensurate increase in realisation will adversely impact the margins and coverage metrics of the entities in the bulk tea industry.

Realisation in domestic market remains vulnerable to export market performance and exposes entity to concentration risks– Exports play a vital role in maintaining the overall demand-supply of the tea market, especially in the case of MKSEL, owing to its pure-play ODX nature of operations (ODX varieties are primarily exported). So, healthy export prices become crucial for maintaining auction realisations as the buyers in these auctions also eventually sell the tea in the export market itself. Volatility in the export of orthodox tea to Iran and other West Asian markets from India keeps the Indian orthodox tea prices vulnerable, exposing the Group's overall profitability to the performance of the export market. Further, the company operates all its 13 tea estates in Assam and focuses only on the production of the orthodox variety. This exposes MKSEL to geographical as well as product concentration risk. However, the entity's high yields and the robust demand for orthodox varieties arising from a global supply constraint (owing to continued weak production in Sri Lanka) are expected to mitigate these risks in the near to medium term.

Sizeable investment in Group entities – MKSEL's investment in the Mauritius-based wholly-owned subsidiary, Vaksana Holdings (which acquired a 70% stake in a tea estate in Congo in FY2014 through step-down subsidiaries), stood at Rs. 24.6 crore (Rs. 6.0-crore equity and balance redeemable preference shares) as on March 31, 2024. The return from the investment in Vaksana Holdings has remained nil so far. Lack of commensurate returns from the investments in Group entities and a sizeable capital invested for the acquisition of tea estates from MRIL in FY2019 along with muted market conditions have adversely impacted MKSEL's consolidated ROCE, which stood at 3.9% in FY2024. Nevertheless, the ROCE is likely to improve significantly in the current fiscal, aided by a healthy operating profit and firm realisations.

Liquidity position: Adequate

The company's liquidity position is likely to remain adequate. The consolidated cash flow from operations declined in FY2024 to Rs. 4.65 crore owing to a drop in realisation and increase in wage rates. However, the cash flow from operations is expected to improve in FY2025, supported by buoyant ODX prices. Its debt repayment obligation stands at Rs. 9.6 crore for FY2025 but would increase to Rs. 12.5 crore in FY2026 and FY2027 due to a ballooning repayment structure. However, a sizeable term loan prepayment (around Rs. 30 crore) in the current fiscal would reduce the overall debt service obligation in the near-to-medium term. Further, the entity has no major capex plan, going ahead, supporting the liquidity.

Rating sensitivities

Positive factors – Healthy profitability and cash accruals along with the reduction of debt on a sustained basis will be the key factors for an upgrade. A decline in the consolidated total debt/OPBDITA to less than 1.5 times on a sustained basis may also trigger an upgrade.

Negative factors – ICRA may downgrade the ratings if the consolidated profitability and cash accruals deteriorate significantly, or if any sizeable debt-funded capex/acquisition adversely impacts the consolidated leverage and liquidity. Specific triggers for a downgrade will be a consolidated interest coverage of less than 4.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Tea
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated the financials of MKSEL with its Group entities, M. K. Shah Teas LLP and M. K. Shah Realty (as mentioned in Annexure II), given the close business, financial and managerial linkages among them

About the company

M. K. Shah Exports Limited, incorporated in 1992, was promoted by the Late Mukundray Shah. The company is an ODX tea producer and has 13 tea estates in Assam with 8,388 hectares of land under cultivation (as of FY2022), including eight tea estates acquired from McLeod Russel India Limited in July 2018. In 8M FY2025, MKSEL manufactured 18.2 Mkg tea vis-à-vis 18.6 Mkg in FY2024 and recorded sales volume of 10.18 Mkg in 8M FY2025 from 18.9 Mkg in FY2024. The full-year volumes are expected to remain similar.

In July 2019, the promoters had set up M. K. Shah Teas LLP, in which MKSEL is a partner. Since then, most of the tea exports of the Group have been routed through this LLP. However, exports to a few countries like Iran, Germany, Japan etc. are made directly by MKSEL, as per the clients' requirement. MKSEL sells tea to the LLP, which is finally exported, and the LLP provides advances for the same to MKSEL, thus having strong operational and financial linkages.

In FY2024, the company started tea business in partnership entity, M. K. Shah Realty. Earlier, this entity was into real estate leasing and had LRD loans which were paid off in FY2024 with support from MKSEL. The operations here are similar to the LLP entity in which tea is bought from MKSEL and exported.

Key financial indicators

MKSEL	Standalone		Consolidated^	
	FY2023	FY2024	FY2023	FY2024
Operating income	463.8	442.0	478.2	452.3
PAT	39.1	5.6	43.4	9.1
OPBDIT/OI	14.8%	8.1%	15.6%	9.0%
PAT/OI	8.4%	1.3%	9.1%	2.0%
Total outside liabilities/Tangible net worth (times)	0.8	0.7	0.8	0.7
Total debt/OPBDIT (times)	2.7	4.7	2.9	5.1
Interest coverage (times)	5.3	2.6	6.2	2.7

*PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; ^ICRA estimates; Amount in Rs. crore; *Provisional results*
Source: Company, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2025)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Date & rating in FY2025		Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022
				Jan 14, 2025	May 28, 2024	-	Mar 20, 2023	Apr 18, 2022	Apr 07, 2021
1	Fund-based - Term loans	Long term	104.00	[ICRA]A (Stable)	[ICRA]A (Negative)	-	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)
2	Fund-based - Working capital facilities*	Long term/ Short term	80.50	[ICRA]A (Stable) /[ICRA]A2+	[ICRA]A (Negative) /[ICRA]A2+	-	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A- (Stable)/ [ICRA]A2+	-
3	Unallocated limit	Long term/ Short term	5.50	[ICRA]A (Stable) /[ICRA]A2+	[ICRA]A (Negative) /[ICRA]A2+	-	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A- (Stable)/ [ICRA]A2+	-
4	Fund-based - Working capital facilities	Long term	-	-	-	-	-	-	[ICRA]A- (Positive)
5	Fund-based- Working capital facilities	Short term	-	-	-	-	-	-	[ICRA]A2+

**Includes cash credit, WCDL, export packing credit*

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term – Fund-based - Term loans	Simple
Long term/Short term – Fund-based - Working capital facilities*	Simple
Long term/Short term – Unallocated limit	Not applicable

**Includes cash credit, WCDL, export packing credit*

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	**Long term – Fund-based - Term loan**	Sep-2018	-	Dec-2028	74.00	[ICRA]A (Stable)
NA	**Long term – Fund-based - Term loan**	Jun-2021	-	Dec-2028	30.00	[ICRA]A (Stable)
NA	**Long term/Short term – Fund-based - Working capital facilities***	-	-	-	80.50	[ICRA]A (Stable)/[ICRA]A2+
NA	**Long term/Short term – Unallocated limit**	-	-	-	5.50	[ICRA]A (Stable)/[ICRA]A2+

*Source: Company; *Includes cash credit, WCDL, export packing credit*

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

Annexure II: List of entities considered for consolidated analysis

Company Name	MKSEL Ownership	Consolidation Approach
M. K. Shah Teas LLP	15% (as on March 31, 2024)	Full Consolidation
M. K. Shah Realty	15% (as on March 31, 2024)	Full Consolidation

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