

PCL Foods Private Limited

February 01, 2019

Summary of rated action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|--------------------------|--------------------------------------|-------------------------------------|------------------------------|
| Fund Based - Cash Credit | NA | 50.00 | [ICRA]BB+ (Stable); Assigned |
| Total | NA | 50.00 | |

*Instrument details are provided in Annexure-1

Rationale

The assigned rating factors in the strategic importance of the Indian market for the parent companies as reflected in the continuous financial support to PCL Foods Private Limited (PCPL) in form of advances, equity infusion, as well as corporate guarantees for bank facilities. ICRA takes comfort from the long and established track record of the Phoenix Group's management and their presence in agro commodity trading for almost two decades. The promoters of the Group have established relationships with their customers and suppliers across different geographies and have been leveraging its benefit, which is evident from the healthy revenue growth in terms of value and volume by the Group as well as PCPL. These factors, coupled with location-specific advantage of presence in a major rice-producing region (Northern India), have enabled the company to register steady revenue growth over the years. PCPL reported sales of Rs. 735.3 crore in FY2018 compared with sales of Rs. 721.7 crore in FY2017. At the consolidated level the Group reported revenues of \$2056.7 million in CY2017 compared with revenues of \$1659.3 million in CY2016. The Group's revenues are diversified across various product segments including Basmati, non-Basmati rice, minerals, sugar, grains, oilseeds, pulses, specialty crops and fresh produces. ICRA notes that PCPL continues to benefit from the strong operational linkages with the parent by virtue of access to information and relationships for sourcing raw material and tradable commodities, benefits from global relationships in food and related industries, access to the knowledge related to commodity flows and alignment of risk management practices with the parent. The Group sourced ~30% and ~80% of the overall non-Basmati rice and Basmati rice volumes respectively traded by it from India in CY2017. The Group is among the top few traders of non-Basmati rice in the world and has an established presence, mainly in the African continent. The ratings take into account the fact that PCPL, along with the Group, manages its price risk and forex risk by entering into suitable derivatives contract to offset the risk. ICRA also notes that there are no term repayments in the company as well as at the Group level in the upcoming years and the management's plans to convert a part of advances given to PCPL into equity in FY2019 will improve its capital structure going forward.

However, ICRA's ratings are constrained by the lack of significant downstream integration at the Group as well as the company level across various products segments which leads to thin and volatile profitability margins. Nonetheless, PCPL's and Phoenix Group's trading operations have witnessed strong growth in the last five years, even though its investments in fixed assets remain low, leading to the lack of significant value addition and low margins. The Group, along with PCPL faces significant inventory price risk as agro products traded by it like rice, pulses and specialty crops cannot be hedged to mitigate the risk due to lack of availability of suitable hedging instruments specific to these commodities. ICRA notes that the overall liquidity profile of the Group remains modest as reflected by high utilisation of its working capital limits with respect to drawing power as its business is working capital intensive in nature. The ratings also factor in the weak coverage metrics at the Group level with Total Debt/OPBDITA of 7.74 times, gearing of 2.56 times and interest coverage of 1.85 times in CY2017. Also, PCPL's profitability remains vulnerable to adverse movements in agro commodity prices with the price risk accentuated by its high inventory holding in the business. PCPL reported low operating margins of -3.47% and net margin of 1.01% in FY2018. The liquidity can be further stretched, especially when commodity prices are rising or are at elevated levels, impacting the Group's ability to take on additional business as its

earnings and cash flows are susceptible to commodity market cycles. Also, the acquisition of Karturi Global Limited is likely to be debt funded, which will further increase the debt levels and further weaken the credit metrics. The ratings are also constrained by the intense competition in the trading business, drastic volatility in the commodity market and, changes in Government policies. ICRA also notes the Group's as well as PCPL's operations, which remain susceptible to the agro-climatic conditions in domestic as well as international markets, impacting the demand and supply of agricultural commodities.

Outlook: Stable

The Stable outlook reflects ICRA's expectation that PCPL will continue to benefit from operational and financial support from its parent, given the strategic importance of the Indian market. The outlook may be revised to Positive if substantial growth in revenues along with improvement in profitability margins and working capital management, leads to strengthening of the financial risk profile. The outlook may be revised to Negative if revenues and cash accruals are lower than expected, or if any major debt-funded capital expenditure or a stretch in the working capital cycle, weakens its liquidity.

Key rating drivers:

Credit strengths

Strong parentage: The company enjoys strong operational as well as financial support from its parent companies (Phoenix Commodities Private Limited and Phoenix Global DMCC). PCPL benefits from the extensive global sourcing and logistics network, access to financial support and vast experience in trading various commodities of the parent entities. Support from the parent companies is expected to continue as India is among the strategic and critical growth markets for the Phoenix Group. PCPL is strategically important for the Phoenix Group as it accounted for 20-30% of the overall rice volumes traded by the same in the last three years.

Strong financial linkages with the parent: PCPL receives most of its advances from the parent/Group companies which are long term in nature. Besides, the Group shows explicit commitment by way of issuing a corporate guarantee for the bank facilities of PCPL.

Long track record of management in agro commodity trading industry: The promoters of the Group have a track record of almost two decades in the commodity trading business. Their well-established relationships with clients and suppliers across multiple countries has led to healthy growth in the Group's business.

Diverse product profile of the Group: The Group has a diversified revenue stream as the it trades in a variety of agro products including rice, pulses, grains, oilseeds, sugar and minerals. Its presence across multiple geographies enable sourcing round the year as each geography has a different crop cycle. The Group has an established presence as a rice trader with a healthy market share and established brand presence across Africa.

Easy availability of raw material: PCPL's facilities are suitably located in Haryana, which ensures easy access to the key raw materials – paddy and rice – throughout the year.

Healthy growth in turnover in last few years: The Group's revenue generation crossed \$2 billion in CY2017 at a year-on-year (YoY) growth rate of 24%. The revenue growth was due to an increase in the overall realisations in CY2017 from \$151 per metric tonne to \$193 per metric tonne. PCPL has also reported a YoY growth of 2% in its revenues in FY2018.

Credit challenges

Lack of sufficient downstream integration results in low profitability: The Phoenix Group's vertical integration into key commodities and higher margin downstream products is limited, which makes its margins more volatile across the commodity cycles. Margins in the merchandising businesses are expected to remain relatively thin, except during periods of high crop and other commodity price volatility. This is also reflected in low investments in fixed assets at the Group level, resulting in low value addition and thin profitability margins.

Earnings and cash flows susceptible to volatility in commodity markets and foreign exchange fluctuations: The company and the Group derive most of its sales from trading of agricultural commodities. Given the opportunity-based nature of the trading business, the earnings and the cash flows remain exposed to the volatility in the commodity market cycles and foreign exchange fluctuations.

Modest liquidity profile: High working capital intensity of the business is driven by the requirement to maintain inventory. The limit utilisation of the working capital limits with respect to its drawing power remains high. Given the nature of the business, the company would require additional limits to fund the increasing scale of operations, especially in a rising price trend of commodities.

Average credit risk profile: The Group has a weak credit profile due to thin profitability and an elevated debt level. The Group reported Total Debt/OPBDITA of 7.74 times, gearing of 2.56 times and interest coverage of 1.85 times in CY2017.

Acquisition impact on credit risk profile remains to be seen: The Group is expected to acquire Karturi Global Limited, and the acquisition is expected to be partly debt funded. In that case, the credit metrics of the Group are likely to get further stretched. However, due to the lack of clarity the real impact of such an acquisition remains to be seen.

Intense competition owing to high fragmentation in industry and low product differentiation: The agro trading and processing industry is highly fragmented with numerous organised and unorganised players due to limited entry barriers in the business. Thus, the intense competition in the industry, coupled with the low value-additive nature of operations, exerts pressure on the company's profit margins. However, the company benefits on account of its scale of operations and established track record of the promoters.

Exposure to agro-climatic risks and changes in Government regulations: Given its operations in an agro-based industry, PCPL as well the Group is exposed to agro-climatic risks such as raw material availability, its quality and pricing. Moreover, changes in Government regulations pertaining to the industry can impact the industry dynamics.

Liquidity position

Given the thin profitability as is inherent in the trading and manufacturing of business of agriculture produce, PCPL's cash flows have remained moderate. The company has cash balances to the tune of ~Rs. 10.52 crore (out of which free cash is Rs. 5.16 crore) as on March 31, 2018, highlighting the moderate liquidity position. ICRA further notes that the overall liquidity profile of the Group remains modest as reflected by high utilisation of its working capital limits with respect to drawing power as its business is working capital intensive in nature.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|---|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology Framework for Liquidity Analysis in Corporate Ratings Rating Methodology for Trading Companies |
| Parent/Group Support | The rating assigned to PCL Foods Private Limited factors in the reasonable likelihood of its parent, Phoenix Commodities Private Limited extending financial support to it because of close business linkages between them. There also exists a consistent track record of Phoenix having extended timely financial support to PCL Foods Private Limited in the past, whenever a need has arisen. |
| Consolidation / Standalone | Standalone |

About the company

PCPL, incorporated in 2013, is a wholly-owned subsidiary of Phoenix Commodities Private Limited (Phoenix). Phoenix is the ultimate holding company of the Group and holds ~100% stake in Phoenix Global, DMCC which in turn holds ~100% stake in PCPL. The promoters of PCPL are Mr. Sudip Kumar Basu and Mr. Nitin Navandher (business associates in the Phoenix Group). In March 2014, Phoenix Global, DMCC acquired 99.95% shares of the company. It is involved in trading and manufacturing of agriculture produce like Basmati, non-Basmati Rice, grains and pulses. The rice milling plant of PCPL is located at Taraori, which has a paddy milling capacity of 31,200 metric tonne per annum (MTPA) and sorting capacity of 72,000 MTPA with an additional 2.40 lakh MTPA sorting facility on job work basis at the Kandla Port.

In FY2018, the company reported a net profit of Rs. 7.40 crore on an operating income (OI) of Rs. 735.34 crore on a provisional basis compared with a net profit of Rs. 2.24 crore on an OI of Rs. 721.73 crore in the previous year.

Key financial indicators (PCPL)

| | FY2016 (Audited) | FY2017 (Audited) | FY2018 (provisional) |
|------------------------------|------------------|------------------|----------------------|
| Operating Income (Rs. crore) | 696.08 | 721.73 | 735.34 |
| PAT (Rs. crore) | 0.03 | 2.24 | 7.40 |
| OPBDIT/OI (%) | -1.04% | 0.38% | -3.47% |
| RoCE (%) | 8.71% | 11.36% | 15.22% |
| Total Debt/TNW (times) | 1.52 | 1.37 | 2.45 |
| Total Debt/OPBDIT (times) | -4.14 | 10.86 | -2.82 |
| Interest Coverage (times) | -2.44 | 1.18 | -6.04 |
| NWC/OI (%) | -7% | -6% | 10% |

About the Group

The Phoenix Group, headquartered in Dubai, was established in 1999 by Mr. Gaurav Dhawan as the main promoter. The Group is essentially a commodity trading house and has established presence in more than 18 countries with revenues more than \$2 billion in CY2017. The Group's offices are present in the regions of South-East Asia, South Asia, the Middle East, East Africa, Southern Africa, Central Africa, West Africa, Americas, Australia and Commonwealth of Independent States (CIS) countries. The Group's main trading product portfolio includes products like Basmati, non-Basmati rice, grains, pulses, oilseeds, sugar, and minerals (coal, iron) among others.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

| Instrument | | Current Rating (FY2019) | | | Chronology of Rating History for the past 3 years | | | | |
|------------|---------------|-------------------------|--------------------------|--------------------------------|---|-------------------------|-------------------------|-------------------------|-------------------------|
| | | Type | Amount Rated (Rs. crore) | Amount Outstanding (Rs. crore) | Date & Rating February 2019 | Date & Rating in FY2018 | Date & Rating in FY2017 | Date & Rating in FY2016 | Date & Rating in FY2015 |
| 1 | Fund Based-CC | Long-term | 50.00 | NA | [ICRA]BB+ (Stable) | NA | NA | NA | NA |

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 | Cash Credit | NA | NA | NA | 50.00 | [ICRA]BB+ (Stable) |

Source: PCL Foods Private Limited

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