March 16, 2023

Tata Coffee Limited: Long-term rating continues on rating watch with positive implications; short-term rating reaffirmed; rating reaffirmed and withdrawn for commercial paper programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term Fund-based – Cash Credit	150.00	150.00	[ICRA]AA+ rating watch with positive implications; continues on rating watch/ [ICRA]A1+; reaffirmed
Commercial Paper	30.00	-	[ICRA]A1+; reaffirmed and withdrawn
Total	**180.00**	**150.00**	

**Instrument details are provided in Annexure-I*

Rationale

The continuation of the long-term rating under watch with positive implication reflects ICRA's expectations that Tata Coffee Limited's (TCL) operational, financial and managerial linkages with Tata Consumer Products Limited (TCPL; rated [ICRA]AAA(Stable)/[ICRA]A1+) will strengthen upon the implementation of the proposed scheme of arrangement between the companies, which would result in the amalgamation of TCL with TCPL and its subsidiaries. ICRA notes that the shareholders of TCL and TCPL have approved the proposed scheme of arrangement and the matter is pending for approval before the National Companies Law Tribunal (NCLT).

The ratings continue to reflect the healthy operating and financial performances of TCL in 9M FY2023 and ICRA's expectations of sustained performance over the medium term, supported by the company's strong market position and diversified product and customer base. TCL's consolidated operating income grew by ~25% YoY to Rs. 2,127 crore in 9M FY2023 on the back of higher realisations from coffee plantations and the extractions businesses, along with healthy scale-up of the instant coffee operations in Vietnam. TCL's consolidated operating margin contracted by ~400 basis points (bps) YoY to 13.7% in 9M FY2023 primarily on account of input cost pressure in the Eight O'clock Coffee (EOC) business, owing to high South American coffee prices whereas the margin profile of Tata Coffee Vietnam recorded a healthy improvement. ICRA expects TCL's consolidated capital structure is likely to remain comfortable with a gearing of less than 0.5 times with improving coverage metrics over the medium term, supported by healthy accruals and limits capex requirements.

The ratings continue to favourably factor in TCL's diversified nature of operations with presence in roast & ground (R&G) coffee, instant coffee (ICD) and plantation coffee along with a geographically diversified customer base. The ratings also consider the conservative capital structure, both at the consolidated and standalone levels. TCL's status as a subsidiary of TCPL and part of the Tata Group lends significant financial flexibility to the company, which also supports its ratings.

The above strengths are, however, offset to an extent by the company's exposure to agro-climatic risks, notwithstanding the steps taken by the company to mitigate the risks to an extent. The commoditised nature of the instant coffee business, which faces intense competition, along with the sensitivity of TCL's operating margin to volatility in coffee prices, also impact the business risk profile.

ICRA has withdrawn the [ICRA]A1+ rating assigned to the commercial paper (CP) programme of TCL on the basis of the withdrawal request received from the company along with a confirmation that no amount was outstanding against the CP as on the date of the request for withdrawal of the rating.

Key rating drivers and their description

Credit strengths

Diversified business profile with geographically diversified customer base – TCL has a diversified business profile with presence in roast & ground (R&G) coffee, instant coffee (ICD), plantation coffee, tea and pepper, among others. In 9M FY2023, income from the US-based EOC accounted for 53% of the consolidated turnover of the company followed by ICD at 29% and plantation coffee at ~6%, with the balance being accounted for by tea, pepper and allied products. The share of ICD has improved successively over the last three years from ~21% in FY2019 owing to the healthy scale-up of the Vietnam operations. While the performance of ICD and plantation divisions improved in 9M FY2023, EOC faced input cost pressure from high international coffee prices, which led to some moderation in its margins. Exports continue to account for the major portion of TCL's standalone revenue. While green coffee is primarily exported to the premium markets in Europe, instant coffee is exported to multiple geographies including Russia/CIS, the African continent, Europe, the Middle East and Southeast Asia. TCL's established relations with prominent clients enabled the company to avoid any material business disruptions due to the ongoing geo-political conflict in Russia.

Integrated nature of operations – At the standalone level, TCL is a fully-integrated coffee company with its own plantations, curing units, R&G facility and instant coffee production plants. The high levels of integration helps the company in mitigating the impact of volatility in coffee prices and maintaining a stable business profile. TCL's focus on selling high quality value-added and differentiated coffee results in higher realisations compared with market rates. The company maintains a sizeable market share in the premium export markets and is the exclusive supplier of superior quality Arabica beans to Tata Starbucks stores in India.

Healthy capacity utilisation of instant coffee plants and significant ramp-up of the Vietnam operations – TCL operates two instant coffee plants in India in Toopran (freeze-dried plant) and Theni (spray-dried plant) with a combined capacity of ~8,400 MTPA. The domestic ICD capacity utilisation has remained healthy at 90-95% p.a. in the past, except in FY2021 wherein the operations were impacted by the pandemic. The plants continued to operate at healthy utilisation levels in 9M FY2023 with an annualised utilisation of ~99%. The track record of high utilisation enables to company to benefit from operating leverage. The ICD operations in Vietnam (freeze-dried) have recorded a significant ramp-up in FY2022 and 9M FY2023 with capacity utilisation of more than 95%, supported by a healthy order book position. The scale-up has translated into improvement in the operating margin profile of the company, which is expected to aid consolidated performance over the medium term.

Healthy financial flexibility due to its status as a part of the Tata Group – TCL's status as a Tata Group company and a 57.48% subsidiary of Tata Consumer Products Limited imparts considerable financial flexibility to the company. TCL also enjoys significant operational, financial and managerial linkages with its parent. ICRA expects the company to further strengthen its linkages with TCPL upon implementation of the proposed scheme of amalgamation.

Credit challenges

Susceptibility of plantations business to agro-climatic risks – TCL owns and operates plantations of coffee, tea, pepper among other agricultural products. These remain exposed to agro-climatic risks, including pest attacks. While TCL has worked extensively to mitigate such risks, including adequate irrigation facilities, adverse weather conditions could impact the output of the plantations segment. ICRA notes that the tea plantation production in 9M FY2023 was impacted by a pest attack from the tea mosquito bug.

Exposure to volatile coffee prices and foreign exchange rates; commoditised nature of instant coffee business – While the integrated nature of operations mitigates the adverse effects of volatile coffee prices to an extent, the company's overseas operations remain exposed to fluctuations in Arabica coffee prices, which have put pressure on EOC's margins in 9M FY2023. At the standalone level too, TCL remains partly exposed to volatile coffee prices. Moreover, being an export-oriented unit, TCL's operations are also exposed to fluctuations in foreign exchange rates. Nevertheless, TCL's long track record and hedging practices aid in mitigating the risks to an extent. The commoditised nature of ICD business limits the pricing power available to TCL. Nonetheless, a healthy product portfolio, with focus on specialty and premium differentiated coffee along with established relationships with key customers, are expected to continue to support the business profile.

Environmental and social risks

Environmental considerations – TCL remains exposed to physical climate risks as its business is dependent on coffee (both as an input and final product), which is an agricultural commodity. Vagaries of the climate translating into variation in crop output could adversely impact TCL's operations in terms of both availability of raw materials, increase in commodity costs or decline in realisations. The company also remains exposed to changes in environmental norms with respect to treatment of manufacturing residual discharge/waste, which could lead to disproportional upfront capital expenditure. Accordingly, TCL could face operational disruptions if regulatory norms are not complied with.

Social considerations – TCL is exposed to social risks such as compliance (or the lack of it) with health and safety standards besides evolving consumer lifestyle changes. The sector also has prominent dependence on human capital, in terms of direct and indirect employees as well as contractual labour. Being an interplay of manufacturing and services businesses, maintaining healthy employee relationship and retaining talent are essential for disruption-free operations. TCL's products, being eatables, have health implications on consumers and any quality concerns could impact its brand name and lead to additional costs for the company. Further, the company is dependent on plantation workers and local communities and tribes for the productivity of its plantations.

Liquidity position: Strong

TCL's liquidity remains strong, characterised by free cash and liquid investments worth Rs. 329 crore at the consolidated level as on September 30, 2022 (provisional) along with sizeable unutilised working capital limits. The company is expected to generate cash flow from operations in the range of Rs. 250-300 crore p.a. over the next two years. Against this, it has debt repayment obligations worth USD 7.8 million in FY2024 and USD 6.3 million in FY2025. The working capital utilisation of the standalone entity has averaged at 45% over the 11-month period ending November 30, 2022, which provides a comfortable buffer. The company does not have any major growth capex plans over the near term. TCL enjoys substantial financial flexibility owing to its status as a subsidiary of TCPL, which further supports its liquidity profile.

Rating sensitivities

Positive factors – The ratings could be upgraded in case of a successful implementation of the proposed scheme of arrangement with Tata Consumer Products Limited.

Negative factors – The ratings may be downgraded if there is any unfavourable movement in coffee prices and/or deterioration in performance of the Eight O'clock business translating into subdued performance of the consolidated entity. Specific credit metrics that could lead to a ratings downgrade include net debt/OPBDITA above 1.75 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Approach – Consolidation Rating Approach – Implicit Support from Parent or Group Policy on withdrawal of credit ratings
Parent/Group support	**Parent: Tata Consumer Products Limited (TCPL; rated [ICRA]AAA(Stable)/[ICRA]A1+)** ICRA expects TCPL to be willing to extent financial support to TCL, should there be a need, given its strategic importance to TCPL and out of its need to protect its reputation. However, ICRA does not foresee any such requirement in the near to medium term.

Analytical Approach	Comments
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of TCL as detailed in Annexure II.

About the company

Tata Coffee Limited (TCL), a 57.48% subsidiary of Tata Consumer Products Limited (TCPL; rated [ICRA]AAA(Stable)/[ICRA]A1+), is a fully-integrated coffee company with coffee plantations, coffee curing facilities, roast & ground coffee facilities and instant coffee production plants. TCL has a total area of ~8,000 hectares (Ha) under coffee cultivation in Karnataka and Tamil Nadu, ~2,400 Ha under tea cultivation and ~1.8 million pepper vines. Its instant coffee business is supported by its manufacturing plants in Toopran (Telangana) and Theni (Tamil Nadu) with an installed capacity of ~8,400 metric tonnes per annum (MTPA). TCL acquired the US-based Eight O'clock Coffee Company (EOC) in June 2006 and commissioned a 5,000 MTPA freeze-dried instant coffee plant in Vietnam in May 2019.

Key financial indicators

TCL Consolidated	FY2021 (audited)	FY2022 (audited)	H1 FY2023 (unaudited)
Operating income	2,263	2,379	1,380
PAT	212	233	212
OPBDIT/OI	17.7%	18.3%	14.4%
PAT/OI	9.3%	9.8%	15.4%
Total outside liabilities/Tangible net worth (times)	1.0	0.8	0.8
Total debt/OPBDIT (times)	2.9	2.3	2.9
Interest coverage (times)	7.5	9.4	7.4

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

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 (Rs. crore)	Amount outstanding as of Dec 31, 2022 (Rs. crore)	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Mar 16, 2023	Apr 05, 2022	Jun 30, 2021	Jun 26, 2020	Jun 19, 2019
1	**Cash Credit**	Long-term/ short-term	150.00	-	[ICRA]AA+ rating watch with positive implications/ [ICRA]A1+	[ICRA]AA+ rating watch with positive implications/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+
2	**Commercial Paper**	Short-term	30.00	-	[ICRA]A1+; reaffirmed and withdrawn	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/short-term fund-based – Cash Credit	Simple
Commercial Paper	Very 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	150.00	[ICRA]AA+ rating watch with positive implications/ [ICRA]A1+
NA*	**Commercial Paper**	NA	NA	NA	30.00	[ICRA]A1+; reaffirmed and withdrawn

*Source: Company; *Unplaced*

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Tata Coffee Limited	100.00% (rated entity)	Full Consolidation
Consolidated Coffee Inc.	50.08%	Full Consolidation
Eight O'clock Holdings Inc.	50.08%	Full Consolidation
Eight O'clock Coffee Company	50.08%	Full Consolidation
Tata Coffee Vietnam Company Limited	100.00%	Full Consolidation

Source: TCL annual report FY2022

ANALYST CONTACTS

Jayanta Roy
+91 33 7150 1120
jayanta@icraindia.com

Kaushik Das
+91 33 7150 1104
kaushikd@icraindia.com

Vipin Jindal
+91 124 4545355
vipin.jindal@icraindia.com

Raunak Modi
+91 22 6169 3368
raunak.modi@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.