

April 07, 2020

Warren Tea Limited: Ratings downgraded to [ICRA]BB- (Negative)/ [ICRA]A4

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based working capital Limits	20.00	24.00	[ICRA]BB- (Negative); downgraded from [ICRA]BB+ (Stable)
Term Loan	19.00	14.06	[ICRA]BB- (Negative); downgraded from [ICRA]BB+ (Stable)
Non-fund based limits	2.64	2.64	[ICRA]A4; downgraded from [ICRA]A4+
Untied limits	-	0.94	[ICRA]BB- (Negative)/ [ICRA]A4, downgraded from [ICRA]BB+ (Stable)/ [ICRA]A4+
Total	41.64	41.64	

*Instrument details are provided in Annexure-1

Rationale

The downward revision in the ratings considers the losses that the company would incur again in FY2020 at the operating level due to the absence of a commensurate uptick in realisation to absorb the increased labour cost. Adjustment for arrear salary and related benefits for the period April 2018 to October 2019 has adversely impacted its profitability in 9M FY2020 and resulted in a net loss of Rs. 8.28 crore compared to net loss of Rs. 5.29 crore in 9M FY2019. Continuing losses over the years led to a significant deterioration in the company's profitability and coverage indicators. The liquidity position of the entity has also weakened significantly over the years due to the cash losses suffered since FY2017. The same is likely to remain weak unless there is a meaningful recovery in tea realisation, given the sizeable debt servicing obligation the entity has in the coming years. ICRA also notes the 21 days lockdown announced by the Government of India (GoI) following the outbreak of COVID-19, which is likely to result in production loss. As a result, the same would have a bearing on the quality and realisation and negatively impact the business profile of all the tea growers in FY2021, including WTL.

Meanwhile, the ratings continue to draw comfort from the company's premium quality tea that commands a higher price over the average market realisation. Besides, comfortable yield of WTL's tea estates mitigates the risks associated with the fixed-cost intensive nature of the tea plantation business to some extent. ICRA has also taken into consideration the sale of one of the tea estates (MoU entered in Q3FY2020) for ~Rs. 19 crore and the expected receipt of the balance sale proceeds of ~Rs.16 crore in FY2021, which would support the company's liquidity position to some extent in the near term.

The ratings, however, also factor in the risks associated with tea for being an agricultural commodity, which depends on agro-climatic conditions and the inherent cyclicity of the fixed-cost intensive tea industry that lead to variability in profitability and cash flows of bulk tea producers like WTL. As Indian tea is essentially a price taker in the international market, low global prices affected domestic realisations to some extent as well. ICRA also notes that WTL's significant exposure in an associate company, which is not value accretive to WTL at present, reduces its overall business returns.

The Negative outlook on the [ICRA]BB- rating reflects ICRA's opinion that the cash accruals from the company's core operations will continue to remain inadequate to service its debt obligations. Accordingly, the liquidity position of WTL would continue to remain poor in the near term, at least.

Key rating drivers and their descriptions

Credit strengths

Superior quality of tea as evident from the significant premium commanded by its produce compared to average market prices - WTL's superior quality of tea in the domestic market resulted in a premium of 36% for its produce compared to the average North Indian tea auction prices in H1 FY2020. WTL's average realisation of tea has decreased in the same period to ~Rs. 199 per kg from ~Rs. 201 per kg in H1 FY2019. However, the top line during the period was supported by higher production of tea of 5.55 Mkg in H1 FY2020 compared to 5.00 Mkg in H1 FY2019.

Comfortable yield of tea estates mitigates risks associated with the fixed-cost intensive nature of bulk tea operations to some extent - The favourable age profile of the bushes results in a comfortable tea estate yield (1,679 kg/hectare in FY2019) of WTL, which directly impacts the cost structure due to the fixed-cost intensive nature of the industry. Although tea production remained at par in FY2019 over the previous year, production of tea increased to 5.55 Mkg in H1 FY2020 compared to 5.00 Mkg in H1 FY2019. Thus, the company's production in FY2020 is likely to be more than FY2019, supporting its topline.

Credit challenges

Sustained deterioration in cost structure due to a significant rise in wage rates, adversely impacting the financial profile - WTL's operating income stood at Rs. 114.01 crore in 9M FY2020, up by ~11% over 9M FY2019, primarily due to an increase in tea production. However, the absence of a commensurate uptick in realisation to absorb the increased labour costs has impacted its profitability, resulting in operating losses of Rs. 3.09 crore in 9M FY2020 compared to an operating profit of Rs. 0.11 crore in 9M FY2019. ICRA notes that tea production in FY2020 is estimated to be higher than FY2019, following the trend in H1 FY2020 production. However; it is expected that average tea realisation for the company is expected to fall in FY2020 compared to FY2019. This is likely to result in significant operating and cash losses for the company given the high cost of production including increased wage rates of tea plantation workers and a hike in fuel expenses. Continuing losses over the years led to a significant deterioration in the company's profitability and coverage indicators. The liquidity position of the entity has also weakened significantly over the years due to the cash losses incurred since FY2017. The same is likely to remain weak unless there is a meaningful recovery in tea realisation, given the sizeable debt servicing obligation that the entity has in the coming years. ICRA also notes the 21 days lockdown announced by the GoI following the outbreak of COVID-19, which is likely to result in production loss. It would also have a bearing on the quality and realisation of tea and negatively impact the business profile of all the tea growers in FY2021, including WTL.

Risks associated with tea for being an agricultural commodity - The profitability and cash flows of bulk tea producers like WTL remain volatile owing to the risks associated with tea for being an agricultural commodity, which depends on agro-climatic conditions as well as the inherent cyclicity of the fixed-cost intensive tea industry. Additionally, given that Indian tea is essentially a price taker in the global market, low international prices may impact the domestic realisations to an extent.

Significant investment/advances in an associate company, which are not value accretive to WTL at present - ICRA also notes that WTL has invested/advanced around Rs. 31.47 crore to an associate company till FY2019, which accounted for around 40% of the company's tangible net worth as on March 31, 2019. As the same is not value accretive to WTL at present, it adversely impacted the business returns.

Liquidity position: Poor

WTL's liquidity position is poor, as reflected by significant cash losses incurred by the company from FY2017 to FY2019, which is likely to continue in FY2020 as well. This, along with increased debt servicing obligations in the near to medium term may aggravate the company's cash flow position. Further, high utilisation of the working capital facilities also leaves

low cushion for the company for any additional working capital requirements. The sale of one of the tea estates will support the liquidity position in the short term, subject to timely receipt of the same.

Rating sensitivities

Positive triggers - ICRA may revise WTL's long-term rating outlook if the entity demonstrates a significant growth in production and realisation, thereby improving the operating profits as well as the liquidity profile on a sustained basis.

Negative triggers - Pressure on WTL's ratings may arise in case of weakening of the financial risk profile owing to a drop in production and if the realisation does not improve enough to recover increasing labour costs, and /or if the company is unable to receive sale proceeds of one of its tea estates in a timely manner.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Indian Bulk Tea Industry
Parent/Group Support	Not Applicable
Consolidation / Standalone	The ratings are based on the standalone financials of the company

About the company

Warren Tea Limited (WTL) owns seven tea gardens across a cultivable area of around 4,119 HA under the leadership of Mr. Vinay K. Goenka. The gardens are located in the Upper Assam region, primarily in Dibrugarh and Tinsukia districts. The company's tea production stood at 6.91 Mkg in FY2019 with the CTC variety comprising a major portion of the company's tea. Further, the company has entered a Memorandum of Understanding (MOU) for sale of one of its tea gardens.

In 9M FY2020, the company reported a net loss of Rs. 8.28 crore on an operating income of Rs. 114.01 crore compared to a net loss of Rs. 5.29 crore on an operating income of Rs. 102.80 crore in 9M FY2019. In FY2019, the company reported a net loss of Rs. 15.92 crore on an operating income of Rs. 118.51 crore. An actuarial gain of Rs. 5.23 crore on employee obligation during the year led to a lower loss of Rs. 12.48 crore at the total comprehensive income (TCI) level.

Key financial indicators

	FY2018 (Audited)	FY2019 (Audited)	9MFY2019 (Unaudited)	9M FY2020 (Unaudited)
Operating Income (Rs. crore)	119.15	118.51	102.80	114.01
PAT (Rs. crore)	-7.89	-15.92	-5.29	-8.28
OPBDIT/OI (%)	-3.88%	-14.57%	0.11%	-2.71%
RoCE (%)	-6.26%	-18.44%	-	-
Total Debt/TNW (times)	0.35	0.47	-	-
Total Debt/OPBDIT (times)	-7.22	-2.29	-	-
Interest coverage (times)	-1.23	-4.28	0.04	-0.80

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2021)			Rating History for the Past 3 Years				
		Type	Amount Rated	Amount Outstanding as on November 30, 2019	Rating	FY2020	FY2019		FY2018
					7-Apr-2020	22-Apr-2019	04-Jan-2019	07-Dec-2018	10-Jan-2018
1	Fund based limits	Long Term	24.00	NA	[ICRA]BB- (Negative)	[ICRA]BB+ (Stable)	[ICRA]BBB (Negative)	[ICRA]BBB (Negative)	[ICRA]BBB+ (Stable)
2	Term loan	Long Term	14.06	14.06	[ICRA]BB- (Negative)	[ICRA]BB+ (Stable)	[ICRA]BBB (Negative)	[ICRA]BBB (Negative)	[ICRA]BBB+ (Stable)
3	Non-fund based limits	Short Term	2.64	NA	[ICRA]A4	[ICRA]A4+	[ICRA]A3+	[ICRA]A3+	[ICRA]A2
4	Unallocated limits	Long Term/Short term	0.94	NA	[ICRA]BB- (Negative)/ [ICRA]A4	-	-	-	-

Amount in Rs. crore

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	Fund based working capital limits	NA	NA	NA	24.00	[ICRA]BB- (Negative)
NA	Term Loan I	Oct-2016	-	July 2021	3.50	[ICRA]BB- (Negative)
	Term Loan II	Dec-2016	-	Feb 2023	6.50	[ICRA]BB- (Negative)
	Term Loan III	Nov-2017	-	Feb 2023	4.06	[ICRA]BB- (Negative)
NA	Non-fund based limits	NA	NA	NA	2.64	[ICRA]A4
NA	Unallocated limits	NA	NA	NA	0.94	[ICRA]BB- (Negative)/ [ICRA]A4

Source: Warren Tea Limited

ANALYST CONTACTS

Mr. K Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Mr. Sujoy Saha
+91 33 7150 1184
sujoy.saha@icraindia.com

Mr. Sandipan Kumar Das
+91 33 7150 1190
sandipan.das@icraindia.com

Mr. Nitesh Bahety
+91 33 7150 1186
nitesh.bahety@icraindia.com

RELATIONSHIP CONTACT

Mr. Jayanta Chatterjee
+91 80 4332 6401
jayantac@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

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For more information, visit www.icra.in

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

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