September 15, 2020

Coastal Farms: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loan	23.00	22.65	[ICRA]BB+(Stable); reaffirmed
Fund Based – Cash Credit	27.00	23.70	[ICRA]BB+(Stable); reaffirmed
Unallocated	0.00	3.65	[ICRA]BB+(Stable); reaffirmed
Total	**50.00**	**50.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation considers the moderate credit metrics of Coastal Farms (CF) given the moderate profitability and debt levels. The rating continues to factor in the extensive experience of the promoters in the poultry industry and the firm's established presence in the poultry and feed businesses. The rating derives comfort from the integrated nature of CF's operations with presence across the value chain of breeding to poultry processing, resulting in better operational efficiency.

The rating, however, is constrained by CF's modest scale of operations, which are confined to some particular regions. Further, given the Covid-19 pandemic, the company's sales were impacted from January 2020, though the same have been steadily reviving in the recent few months. Besides, intense competition amid the fragmented industry limits the firm's bargaining power as well as pricing flexibility and exerts pressure on its revenues and margins. However, established relationships with its major customers provide comfort to a large extent. ICRA notes that CF's margins are susceptible to highly volatile broiler realisations due to the seasonal demand of poultry products in India and volatile feed prices, which are driven primarily by agro-climatic conditions. The rating is also constrained by the inherent risks associated with the partnership nature of business, including the risk of capital withdrawal, among others. CF's liquidity remains stretched, as reflected in its continued high working capital utilisation.

The Stable outlook on the [ICRA]BB+ rating reflects ICRA's opinion that CF will continue to benefit from its long track record of operations with the recently commissioned new capacity, revenue diversity across segments and commitment to conservative financial policies.

Key rating drivers and their description

Credit strengths

Extensive experience of the promoters in the poultry industry – CF's promoters have over three decades of experience in the poultry industry. The firm's breeder, hatchery and feed manufacturing units are located in Kushalnagar and Bantwala taluks of Karnataka and it sells products in Karnataka and Kerala. The firm has set up its new integrated chicken processing farm at Barimar, in Bantwala taluk of Karnataka, which commenced operations from February 2020, taking the capacity to 2,000 birds per hour from 500 birds per hour. CF markets its products under the brands, Coastal Feeds, Coastal Wholesome Chicken World and Coastal Hatcheries.

Integrated nature of operations – CF has its presence across the poultry business' value chain viz. breeder farming, hatching, broiler farming, chicken processing and feed manufacturing. Its revenues are spread across segments, which cushioned the impact on poultry sales due to the pandemic and initial speculation associating the Covid-19 with poultry consumption. Feeds accounted for ~35% of the firm's total sales in FY2020, followed by processed chicken (~35%) and broilers (~22%), while the balance comes from others. ICRA notes that the entire requirement for poultry feed is met in-house, enabling the firm to ensure quality and availability of poultry feed.

Financial risk profile characterised by low gearing and moderate debt coverage – Despite the impact on its Q4 FY2020 performance (provisional), CF reported an improvement in operating margins and cash accruals along with stagnant debt, which resulted in moderate debt coverage metrics. While CF's capital structure showed improvement as reflected by Total Debt/Net Worth of 1.0 times as on March 31, 2020 compared to 1.2 times as on March 31, 2019, its interest coverage and DSCR stood comfortable at 3.2 times and 3.0 times, respectively in FY2020. With no major capex plan going forward, ICRA expects the company's capitalisation and debt coverage metrics to remain moderate, supported by a steady operating performance.

Credit challenges

Modest scale of operations – CF's revenues remained at a moderate level of Rs. 92.5 crore in FY2020, lower by 5.7% compared to Rs. 98.0 crore in FY2019 owing to the initial speculation linking the Covid-19 with poultry consumption in Q4 FY2020. The firm has ten chicken retail outlets in various parts of coastal Karnataka, limiting its geographical concentration. The firm's sales were impacted from January 2020 owing to the pandemic, though the same revived in the recent few months. Commencement of a new unit in February 2020 would aid the scale expansion in the long term.

Profitability vulnerable to volatile raw material prices and realisation – Major raw materials required for the feed plant are maize and soya de-oiled cake, prices of which remain volatile due to fluctuation in domestic production. Raw material prices are also dependent on agro-climatic condition, international prices, and demand from the poultry sector, which is susceptible to seasonality in demand. Perishable nature of the products (broiler and processed chicken) and seasonal demand result in volatile realisations. While margins in FY2019 were impacted due to a substantial increase in the prices of maize and soya meal, the same revived in FY2020 partly due to normalisation of prices.

Inherent risk of disease outbreak in the animal husbandry business – Like other entities in the poultry and related businesses, CF is exposed to the inherent industry risk of disease outbreaks like Avian influenza (bird flu). ICRA notes the various bio-security measures adopted by the firm over the years. However, the Covid-19 pandemic has thrown a unique challenge to the industry players as demand was impacted both due to speculation or unwillingness of consumers to buy poultry products as well as the impact of the lockdown on the trade.

Intense competition in a highly fragmented industry limits bargaining power – Intense competition amid a fragmented industry, which is characterised by the presence of many small and medium-sized players in and around the region, limits CF's overall bargaining power and pricing flexibility. However, the firm's established relationships with its major customers and established brand presence offer comfort to some extent.

Inherent risks associated with the partnership nature of the business – The firm is exposed to the risks associated with partnership firms including capital withdrawal risks that could adversely impact the capital structure. However, the promoters have not withdrawn capital over Rs. 1.0 crore.

Liquidity position: Stretched

CF's cash flows from operations in FY2020 were meagre owing to high working capital requirements on the back of higher stock levels and lower creditors. The firm's liquidity is **stretched** with high working capital utilisation, which leaves limited buffer to meet any contingencies. The firm has an undrawn working capital facility of around Rs. 4.0 crore as on June 30, 2020, which is expected to support the liquidity to some extent going forward. The ability of the firm to scale up and manage operations, which were impacted due to the Covid-19, in a timely manner, would be critical for maintaining a comfortable liquidity profile.

Rating sensitivities

Positive triggers – ICRA could upgrade the ratings if the company scales up its operations while maintaining its profitability on a sustained basis and improving its liquidity profile. Specific credit metric for a rating upgrade would be ROCE of more than 13%.

Negative triggers – Pressure on the ratings could arise if there is a further decline in the scale of operations, leading to a decline in profitability. Any withdrawals by the partners and lower cash accruals, resulting in a tightened liquidity position, could also cause a downgrade. Specific credit metric for a downgrade would be Total Debt/OPBDIT of more than 4 times.

Analytical approach

Analytical Approach	**Comments**
Applicable Rating Methodologies	[Corporate Credit Rating Methodology]
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the standalone financial statements of the rated entity.

About the company

Incorporated in 1997 as a partnership firm, Coastal Farms, is an integrated poultry player based out of Mangalore, Karnataka. The firm is involved in various avenues of poultry business, viz. breeder farming, hatching, broiler farming, chicken processing and poultry and cattle feed manufacturing. Mr. Prakash Shetty, Managing Partner, has over three decades of experience in the industry, and the firm has an established brand presence in the region it operates. The firm's breeder, hatchery and feed manufacturing units are in Kushalnagar and Bantwala taluks of Karnataka and it has ten chicken retail outlets spread across Mangalore and Udupi districts. CF markets its products under the brands, Coastal Feeds, Coastal Wholesome Chicken World and Coastal Hatcheries.

In FY2020, on a provisional basis, the company reported a net profit of Rs. 2.5 crore on an operating income of Rs. 92.5 crore compared to a net profit of Rs. 3.5 crore on an operating income of Rs. 98.0 crore in the previous year.

Key financial indicators (audited)

	FY2019	**FY2020***
Operating Income (Rs. crore)	98.0	92.5
PAT (Rs. crore)	3.5	2.5
OPBDIT/OI (%)	9.3%	13.7%
PAT/OI (%)	11.7%	9.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.2	1.0
Total Debt/OPBDIT (times)	4.6	3.3
Interest Coverage (times)	4.5	3.2

Source: Firm, ICRA research
** Provisional data*

Status of non-cooperation with previous CRA:

CARE in its rationale dated July 29, 2019 stated as follow:

"CARE had, vide its press release dated March 26, 2018, placed the rating(s) of Coastal Farms (COF) under the 'issuer noncooperating' category as COF had failed to provide information for monitoring of the rating. COF continues to be noncooperative despite repeated requests for submission of information through e-mails, phone calls and email dated July 05, 2019, July 09, 2019, July 12, 2019, July 15, 2019 and July 17, 2019 ".

Brickwork Ratings in its rationale dated April 22, 2020 stated as follow:

"Brickwork Ratings downgraded the ratings for the bank loan facilities of Rs 13.50 Crore of Coastal Farms to BWR BB (Stable) Issuer Not Cooperating, based on best available information."

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
					15-Sep-2020	30-May-2019	16-May-2018	-
1	Term Loan	Long Term	22.65	21.9	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	-
2	Cash Credit	Long Term	23.70	-	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	-
3	Unallocated	Long Term	3.65	-	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	-

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan 1	May 2018	NA	May 2026	18.67	[ICRA]BB+(Stable)
NA	Term Loan 2	Feb 2019	NA	Feb 2027	3.98	[ICRA]BB+(Stable)
NA	Cash Credit	NA	NA	NA	23.70	[ICRA]BB+(Stable)
NA	Unallocated	NA	NA	NA	3.65	[ICRA]BB+(Stable)

** Working capital demand loan of Rs. 5 crore is interchangeable with cash credit*

Source: Coastal Farms

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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.

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