April 22, 2022

SH Food Processing Private Limited: Ratings Downgraded and 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: Cash credit facilities	3.50	-	-
Long Term: Term loan facilities	38.00	7.50	Downgraded to [ICRA]BB+ from [ICRA]BBB-; Outlook revised to 'Stable' from 'Negative'
Long Term: Unallocated	-	2.50	Downgraded to [ICRA]BB+ from [ICRA]BBB-; Outlook revised to 'Stable' from 'Negative'
Total	**41.50**	**10.00**	

Instrument details are provided in Annexure-1

Rationale

For arriving at the ratings, ICRA has taken a consolidated view of Srinivasa Farms Private Limited (SFPL) along with its subsidiary company, Sh Food Processing Private Limited (SHFPPL), given the business and financial linkages and common management.

The revision in ratings considers the weakening of the company's credit profile as increase in commodity prices and delay in ramp-up of broiler and layer divisions widened the company's operating losses to Rs. 47 crore in 9M FY2022 from Rs. 21 crore in FY2021. Commodity prices are expected to remain firm in the near term, limiting the scope of improvement in margins. However, the company is focussing on improving efficiencies, which along with increase in chicken prices, is expected to mitigate the impact on the margins to an extent. The operating losses have resulted in stretched capital structure and coverage indicators. However, ICRA draws comfort from Rs. 80-90 crore fund infusion from the promoters which have been used to fund the losses and refinance a part of debt. The company's liquidity position remains stretched; however, ICRA notes that timely financial support from promoters is expected to support the company in meeting its working capital requirements and debt obligations. Given the company's operating losses and growth plans, adequate and timely infusion of funds remains a key monitorable. The ratings also remain constrained by exposure to cyclicality inherent in the poultry industry and seasonality in demand and consumption patterns.

The company is setting up a Mega Food Park (MFP) in Prakasam district, Andhra Pradesh and the commissioning of the same has been delayed to FY2023 from Q4 FY2021 (according to earlier plans) on account of delays in execution and funding. A significant part of term loans drawn down towards the MFP construction was also refinanced using the funds infused by the promoters in FY2022.

The ratings derive comfort from SFPL's exclusive pan-India franchise agreement with Hyline International for distribution of its layer breed (W80), and increased acceptability of W80 among the poultry farmers with significant repeat purchases from the layer farmers, supporting the layer breeding operations. The ratings also factor in the vertically integrated nature of the Group's operations with presence in manufacturing of poultry feed, soya de-oiled cake, soya oil, layer and broiler breeding, integration farming and processed chicken (CPP). The ratings consider the Group's established presence spanning more than five decades in the poultry business and favourable long-term demand prospects for the domestic poultry industry, backed by favourable socio-economic factors.

The stable outlook reflects expectation of continued growth in demand for poultry products as well as expectation of promoter funding as and when required.

Key rating drivers and their description

Credit strengths

Vertically-integrated poultry business – The Srinivasa Group has presence across the value chain of the poultry industry including manufacturing of poultry feed, soya processing, breeding of layer and broiler chicks, contract farming, and CPP. Further, the Group has more than five decades of experience in poultry operations. The Group is setting up an MFP, which includes facilities for food grain storage, chicken and egg processing. It would charge users monthly for using the industrial plot and processing infrastructure under SHFPPL, which is a 51% subsidiary of SFPL. The total project cost of MFP is Rs. 115.00 crore. However, the project is expected to be commercialised only in FY2023 (delayed from Q4 FY2021). Moreover, there has been a delay in release of grant for project from Government of Andhra Pradesh.

Exclusive franchise agreement with Hyline International – In August 2017, SFPL entered into a pan-India exclusive franchise agreement with Hyline International, a leading genetic layer breeder in the global market for distribution of layer chicks. Hyline India's market share has increased significantly post its partnership agreement with SFPL on the back of improved market acceptance of W80 layer breed.

Equity infusion promoters to support Group's poultry operations – The promoters have infused ~Rs. 135 crore in the company in the last three years (FY2020 to FY2022) in the form of equity. Further, they have supported additional funding requirements through loans.

Credit challenges

Weak operating performance with significant operating losses impacting the company's debt metrics and liquidity position – The Group has been reporting operating losses since FY2019 due to change in pure-line breeds for layer and broiler segments where production and efficiency parameters took time to stabilize. In FY2022, impact of second wave lockdown and sharp increase in commodity prices has widened the operating losses to ~Rs. 47 crore in 9M FY2022 from Rs. 21 crore in FY2021. With improvement in realisations seen since Q4 FY2022, losses are expected to reduce over the next 12 months but as the commodity prices continue to remain firm, margins are expected to remain under pressure.

Moderate gearing levels and weak coverage indicators – Due to consistent losses, the company's coverage indicators have remained negative since FY2019.

Margins susceptible to raw material price fluctuations – Maize and soya are the two main raw materials for production of feed. Poultry feed is the key cost component for broiler and layer breeding, and integrated farming operations. Prices for soya and maize increased substantially over the last 12 months dampening margins. The operating margins remain susceptible to raw material price volatility and production levels, along with agro-climatic conditions.

Liquidity position: Stretched

The company's liquidity remains stretched as subdued margins and increasing scale are expected to result in negative retained cash flows. Moreover, it has limited free cash balances and negligible buffer in working capital limits. The company has repayment obligations of Rs. 6 crore in FY2023 with capex plans of ~Rs. 30 crore for the mega food park. Timely support from the promoters remains crucial to meet the company's working capital requirements, to fund capex, and to meet debt obligations. Government grant of Rs. 20 crore is expected to support capex funding.

Rating sensitivities

Positive factors – The ratings could be upgraded if healthy growth in revenues, business diversification and improvement in the profitability margins results in improved liquidity position and debt coverage indicators. The specific credit metrics that could result in rating upgrade include OPBITDA/Interest at above 2.8 times on a sustained basis

Negative factors – Pressure on ratings could arise in case a delay in turnaround of operations adversely impacts the company's debt coverage indicators and liquidity position further. Any delay in support from promoters and continued operating losses are also likely to put pressure on its ratings.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology]
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has taken a consolidated view of SFPL, along with its subsidiary company, SHFPPL, given the close business, financial and managerial linkages between the entities.

About the company

Incorporated in 1983, SFPL is a part of the SH Group, which is an integrated poultry player in the domestic market with presence in poultry feed, soya processing, broiler and layer segments. SFPL entered into an exclusive pan-India franchise agreement with Hyline International (Hy-Line W-80) for distribution of layer chicks. The company has also diversified into value-added segments such as processed chicken, liquid egg, etc. SHFPPL was formed to set up an MFP on the demand driven hub-and-spoke model with backward and forward linkages to create a sustainable poultry value chain. The MFP is being set up at Gangavaram village, Prakasam district, Andhra Pradesh on a total area of 53.74 acres and is expected to commence operations in FY2023.

Key financial indicators (audited)

Consolidated	FY2020	FY2021	9M FY2022
Operating Income (Rs. crore)	544.0	636.5	647.4
PAT (Rs. crore)	-112.1	-31.1	-55.4
OPBDIT/OI (%)	-16.6%	-3.3%	-7.4%
PAT/OI (%)	-20.6%	-4.9%	-8.6%
Total Outside Liabilities/Tangible Net Worth (times)	2.1	2.0	
Total Debt/OPBDIT (times)	-1.4	-6.5	-2.3
Interest Coverage (times)	-7.7	-1.9	-5.2

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

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 March 31, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					April 22, 2022	July 29, 2021	Dec 09, 2020	Jan 14, 2020
1	Cash Credit	Long-term	-	-	-	[ICRA]BBB-(Negative)	[ICRA]BBB(Negative)	[ICRA]BBB(Negative)
2	Term Loan	Long term	7.50	7.50	[ICRA]BB+(Stable)	[ICRA]BBB-(Negative)	[ICRA]BBB(Negative)	[ICRA]BBB(Negative)
3	Unallocated	Long term	2.50	-	[ICRA]BB+(Stable)	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term – Term Loan	Simple
Long Term – Fund based/CC	Simple
Long Term Unallocated	Not Applicable

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 analyzing 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, is available on ICRA's 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	Long Term: Term Loan facilities	FY2018	-	FY2029	7.50	[ICRA]BB+ (Stable)
NA	Long Term: Unallocated	-	-	-	2.50	[ICRA]BB+ (Stable)

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Srinivasa Farms Private Limited	Parent of rated entity	Full Consolidation

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