Press Release

Dharwad Mishra Pedha And Food Processing Industry

September 17, 2019

Rating Downgraded and Assigned

Total Bank Facilities Rated*	Rs. 35.00 Cr. (Enhanced from Rs.25.00 Cr.)
Long Term Rating	ACUITE BB+ / Outlook: Stable (Downgraded from ACUITE BBB- /Stable)

** Refer Annexure for details*

Rating Rationale

Acuité has downgraded long-term rating to '**ACUITE BB+**' **(read as ACUITE double B plus)** from **'ACUITE BBB-' (read as ACUITE triple B minus)** on the Rs.25.00 crore and assigned long-term rating of '**ACUITE BB+**' **(read as ACUITE double B plus)** to the Rs.10.00 crore bank facilities of DHARWAD MISHRA PEDHA AND FOOD PROCESSING INDUSTRY (Dharwad Mishra). The outlook is **'Stable'**.

The rating downgrade reflects considerable capital withdrawal by its partners, leading to a significant dip in its net worth, larger than expected capital expenditure leading to deterioration of its financial risk profile. However, the rating continues to benefit from extensive industry experience of the promoters and long track record of operations and steady sales growth in the last few years. The rating also factors in working capital intensity and intense competition in the industry.

Established in 1933, Dharwad Mishra Pedha and Food Processing Industry (Dharwad Mishra), a Dharwad, Karnataka-based partnership firm is engaged in manufacturing of sweets and bakery products. Dharwad was founded by Mr. Avadhbihari Mishra and currently it is being managed by Mr. Ganesh Mishra and Mr. Sanjay Ganesh Mishra. The firm's operations are spread across Karnataka, Maharashtra and Goa.

Analytical Approach

Acuité has considered the standalone business and financial risk profile of Dharwad Mishra to arrive at the rating.

Key Rating Drivers

Strengths

- **Experienced management and long track record of operations**

  Established in 1933, Dharwad Mishra Pedha and Food Processing Industry (Dharwad) has a long operational track record of more than eight decades in the sweets and bakery business. Dharwad has reputed customer base spread across Maharashtra, Karnataka and Goa. About 90 per cent of its revenues are derived from outlets/franchise and remaining10 per cent comes from distributors and agents. Further, the management of Dharwad over the years has also built a healthy relationship with suppliers for procurement of raw materials. Acuité believes that proven long operational track record and longstanding presence of the promoters and reputed brand name is expected to support in improving its business risk profile over the medium term.

- **Steady growth in revenues and profitability**

  Dharwad has reported revenues of Rs.95.82 crore (provisional) in FY2019 as against Rs.77.21 crore in FY2018 and Rs.69.44 crore in FY2017. Over the past four years through FY2019, the revenue growth is at a compound annual growth rate of about 15.61 per cent. This is backed by regular addition of franchisees as well as distributors/agents spread across the territories of Karnataka, Maharashtra and Goa; about 67 per cent, 13 per cent and 18 per cent of total revenues comes from sweets, bread and bakery products and namkeen respectively. Further, the revenue growth is expected to improve to Rs.110 crore - Rs. 140 crore over the medium term supported by recently expanded capacities for foray into new products of batter, instant food mix among others, while increasing the existing capacities for bread, namkeen and chips. To focus on the core business of sweet making, while managing the revenue growth, the firm entered into a logistics arrangement with a third party for distribution of the sweets and bakery products across the locations. This will support in reducing the future capex and operational stress on non-core business of transportation. The firm's operating profitability margins are moderate and stable at about 9.0-10.0 per cent over the past three years through FY2019. Acuité believes that the firm's revenues are expected to improve, while maintaining the margins in line with the past trend.

Weaknesses

- **Moderate financial risk profile**

The financial risk profile of the firm is moderate marked by high gearing (debt-to-equity), total outside liabilities to total net worth (TOL/TNW) as well as moderate debt protection metrics. Gearing and TOL/TNW stood high at 2.42 times and 3.98 times as on 31 March, 2019 (provisional), respectively, and the deterioration is higher-than Acuité's expectations, which was at 0.64 times and 1.84 times as on 31 March, 2018 respectively. Net worth is modest and deteriorated to Rs.14.62 crore as on 31 March, 2019 (provisional) as against Rs.17.21 crore as on 31 March, 2018, due to capital withdrawal by the partners amounting to Rs.4.10 crore in FY2019 (provisional). The withdrawal of capital was to return the money to the investors as the initial stake sale transaction in FY2018, was later found out not materialized. Further, the firm has done aggressive capex to the tune of Rs.13.0 crore in FY2019 higher than expected and continued capex for the last two years amounting to about Rs.22 crore (for construction of building, addition of new and replacement of old machinery) funded out of term debt of Rs.8.0 crore and rest out of internal accruals, which has exerted pressure on the short term working capital besides regular withdrawal of unsecure loans.

Debt protection metrics of interest coverage ratio and net cash accruals to total debt (NCA/TD) stood moderate at 2.09 times and 0.13 times, respectively, in FY2019 (provisional) vis-à-vis 2.24 times and 0.40 times in FY2018. The firm reported cash accruals of Rs.4.50 crore for FY2019 and firm's cash accruals are expected in the range of Rs.5 crore- Rs. 7 crore with repayment obligations amounting to Rs.2.50 crore in the medium term. Acuité believes that the financial risk profile is expected to improve marginally; however, it remains moderate on account of modest net worth, modest accretion to reserves, regular capex and moderate accruals to repayment obligations and working capital intensity amid the growing business plans.

- **Moderate working capital management**

Dharwad's operations were efficiently managed with gross current asset (GCA) days of below 100 during FY2017 and 2018. However, with increasing size of operations through franchisee / outlets and penetration into other territories of Maharashtra and Goa the GCA days, it have deteriorated to about 132 days in FY2019 (Provisional); driven by increasing receivables (25-56 days) and inventory levels of (49-63 days), respectively, for past three years. Its creditors are 60 days average for the past three years. Working capital intensive operations and modest net worth led to high utilisation of its bank lines at about 98 per cent over last six months through June 2019. Further, Dharwad is planning to enhance its working capital limits, and timely sanction and availability of working capital limits are critical for the growth in its operations. Acuité believes that Dharwad's operations will continue to be working capital intensive over the medium term, owing to the growing business volumes, diversified territories and foray into new products.

- **Competitive and fragmented industry**

The firm operates in a highly fragmented industry with large number of organised and unorganized players resulting in low bargaining power with customers. The firm's plans of diversifying into new products of batter, instant food mix and its business plans of making at least Rs.20 crore - Rs. 30 crore from these new products amid competition from the existing players is a key rating sensitivity factor.

Liquidity Position

Dharwad's liquidity is stretched marked by moderate working capital intensive operations with fully utilised bank lines, withdrawal of capital and unsecured loans and expected pressure on working capital incremental working capital requirement for the growing operations. Its GCA has deteriorated from about 100 in the past to 132 days in FY2019 and increasing revenues lead to highly utilised bank lines at 98 per cent over past six months through June 2019. Net cash accruals stands at Rs.4.88 in FY 2019 (Prov) with expected cash accruals of Rs 5 crore - Rs. 8 crore over medium term, which should be sufficient against term debt obligation of Rs.2.5 crore over the medium term. Current ratio is at 1.89 times as on March 31, 2019. Acuité believes that the liquidity of Dharwad is expected to improve owing to expected moderation in capex and the firm's plans to go for enhancement in its working capital limits.

Outlook: Stable

Acuité believes that the outlook on Dharwad will remain 'Stable' over the medium term on account of its experienced promoters and long track record of operations. The outlook may be revised to 'Positive' in case of significant improvement in its revenues, while maintaining the profitability and improving its capital structure. Conversely, the outlook may be revised to 'Negative' in case of any stretch in its working capital management or any significant unplanned debt-funded capital expenditure or significant withdrawal of capital leading to deterioration of its capital structure and liquidity.

About the Rated Entity - Key Financials

	Unit	FY19 (Provisional)	FY18 (Actual)	FY17 (Actual)
Operating Income	Rs. Cr.	95.82	77.21	69.44
EBITDA	Rs. Cr.	8.99	7.71	6.64
PAT	Rs. Cr.	1.14	1.16	0.67
EBITDA Margin	(%)	9.38	9.99	9.57
PAT Margin	(%)	1.19	1.51	0.96
ROCE	(%)	15.31	15.85	15.43
Total Debt/Tangible Net Worth	Times	2.42	0.64	8.44
PBDIT/Interest	Times	2.09	2.24	1.76
Total Debt/PBDIT	Times	3.79	1.37	4.23
Gross Current Assets (Days)	Days	132	99	90

Status of non-cooperation with previous CRA (if applicable)

Not Applicable

Any other information

Not Applicable

Applicable Criteria

- Default Recognition - https://www.acuite.in/view-rating-criteria-17.htm
- Manufacturing Entities - https://www.acuite.in/view-rating-criteria-4.htm
- Financial Ratios And Adjustments -https://www.acuite.in/view-rating-criteria-20.htm

Note on complexity levels of the rated instrument

https://www.acuite.in/criteria-complexity-levels.htm

Rating History (Upto last three years)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
29-Jun-2018	Proposed Secured Overdraft	Long Term	25.00	ACUITE BBB- / Stable (Assigned)

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Proposed Secured Overdraft	Not Applicable	Not Applicable	Not Applicable	25.00	ACUITE BB+ / Stable (Downgraded from ACUITE BBB- /Stable)
Proposed Secured Overdraft	Not Applicable	Not Applicable	Not Applicable	10.00	ACUITE BB+ / Stable (Assigned)

Contacts

Analytical	Rating Desk
Srihari Adari Head - Corporate and Infrastructure Sector Ratings Tel: 040-40042327	Varsha Bist Manager - Rating Desk Tel: 022-49294011
srihari.adari@acuite.in Bhavani Sankar Oruganti Senior Analyst - Rating Operations Tel: 040-4004 2327 bhavanisankar.oruganti@acuite.in	rating.desk@acuite.in

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