Prataap Snacks Limited

Corporate – Food & Food Products

Credit Perspective

October 2019

RATING ACTION

Rating reaffirmed;

Long - term Rating

[ICRA]A+ (Stable)

Short - term Rating

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Total Limits Rated

Rs. 58.00 crore

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Rating Rationale

The reaffirmation of Prataap Snacks Limited's (PSL) rating continues to factor in the well diversified product portfolio across 3 segments including a wide range of snack foods, flavours and SKUs addressing a large consumer base. ICRA also takes note of the significant market share held by PSL in the rings segment (extruded snack). The rating also draws comfort from the integrated sales & distribution network of more than 240+ super stockists and 4,100+ distributors ensuring effective market penetration. ICRA favourably factors in the strategic location of manufacturing facilities across various parts of India which has enabled in lowering the logistics cost, de-risking from concentration in one facility, reducing transit time and improve serve rate. Further, the financial risk profile of PSL remains comfortable aided by low debt levels and capital infusion by Sequoia Capital[1] and IPO proceeds supported the networth position at Rs. 561.36 crore as on March 31, 2019. The same has resulted in healthy gearing of 0.03 times and TOL/ TNW of 0.5 times. Also, coverage metrics remain strong with interest cover of 97.0 times, NCA/ Total debt of 443% and DSCR of 93.3 times in FY2019. The rating also factors in the rich experience of promoters for more than two decades in the snack food industry.

The ratings, however continues to remain constrained by PSL's exposure to stiff competition from branded packaged food players (both multinationals and regional players) in the savoury snack manufacturers. The margins remain vulnerable to adverse movements in raw materials, although operational engineering efforts undertaken by PSL's management has aided in restricting margin contraction. Further, PSL's presence in the food industry has exposed it to brand reputation risks arising out of any consumer product liability claims, product labelling errors, which could impact brand reputation. ICRA also takes note of the new product launches and entry into newer geographies where failure to launch and market new products due to unpredictable consumer preferences might have a material adverse effect on business.

Rating Outlook

The stable outlook reflects ICRA's expectation that PSL will continue to benefit from its established brand equity and report healthy revenue growth and maintain its liquidity position. Further, steady demand for packaged foods driven by increasing affordability, urbanisation, changing lifestyles/customer preferences, and favourable demographics, translate into low business risks for the company.

Scenarios for Rating Upgrade

Sustained growth in revenues and profitability supported by its ability to capture market share with its new product launches and conquer the Gujarat market through its acquisition of Avadh Snacks Private Limited could be triggers for rating upgrade.

Scenarios for Rating Downgrade

Downward pressure on the ratings could emerge in case the revenue growth and cash accruals are lower than expected, or if any major capital expenditure, or stretch in the working capital cycle, weakens the liquidity position.

Key Rating Considerations

Credit Strengths

- Well diversified product portfolio with over 60 products across 3 segments including a wide range of snack foods, flavours and SKUs addressing a large consumer base
- Strong supply chain and distribution network of more than 240+ super stockists and 4,100+ distributors ensuring effective market penetration
- Strategically located manufacturing facilities has enabled in lowering logistics cost, transit time and thereby enhance the serve rate
- Healthy financial risk profile aided by low debt levels and capital infusion by Sequoia resulting in comfortable capital structure and coverage metrics
- Extensive experience of promoters having more than two decades of experience in the snack food industry and have extensive control on the day-to-day operations

Credit Challenges

- Exposure to competition from large multinationals and local/ regional players exerting pricing pressure
- Volatility in margins associated with seasonality of raw materials as reflected by contraction of margins from 8.4% in FY2018 to 7.1% in FY2019
- PSL is exposed to brand reputation risks arising out of any consumer product liability claims, product labelling errors which could impact its brand reputation

Company Profile

Prataap Snacks Limited (PSL) was promoted by Mr. Arvind Mehta, Mr. Apoorva Kumat and Mr. Amit Kumat. PSL commissioned its first manufacturing plant in 2005 for potato chips and subsequently, diversified into other product categories including “extruded snacks” and “namkeens”. Further, it diversified into sweet snack segment in 2018 which constitute to ~2.5% of FY2019 revenues. The company raised Rs. 236 crore through an IPO in September, 2017. PSL acquired Avadh Snacks Private Limited to provide an entry into Gujarat market and recently in July 2019 completed the amalgamation of its wholly owned subsidiary, Pure N Sure Food Bites Private Limited.

BUSINESS RISK PROFILE

Continuous innovation has led to improved product diversification

PSL operates out of two major segments namely – sweet and salty snacks. PSL entered into the sweet snacks segment with the launch of Yum-Pie in FY2018, under Rich Feast brand name. Subsequently, in FY2019 the company launched a new product called cookie cake, yum cake and choco vanilla cake. Owing to the limited potential of cookie cake, PSL has launched mass products in the sweet confectionaries segment like tiffin cakes, cupcakes, etc to cater to the market it is focused and where its existing distribution network could be leveraged for sale of these sweet snacks. PSL has a wide product portfolio of over 60 products across 3 segments, 9 strategically located manufacturing plants, a pan-India network. The same has led to capturing the market share of big giants like Pepsi Co over the past few years. PSL is today one of the top 10 companies in the organised Indian snack industry.

Exhibit 1: Product Mix

Product	Type	SKUs	Target group
Potato Chips	Potato-based	9 flavors	All
Chulbule	Rice grit & corn grit based	7 flavors	Youth & children
Rings, Kurves & Puff	Corn grit based	4 flavors	Children
Namkeen	Gram based	23 varieties	All
Pellet Snacks	Wheat based	2 flavors	Children
Nachos	Corn tortillas	3 flavors	All
Yum-pie	Cake with jam & chocolate	9 flavors	All

Source: Company

Continues to hold its market leadership position in the extruded snacks segment

Extruded food products are mainly corn flour and potato-based or a combination of flours. Northern and Western India are the largest markets for extruded snacks. Both these regions also witness the largest competition in both the organised and unorganised segments. Small pack size is imperative to push sales volumes, especially in the rural markets, where penetration is minimal. Predominantly targeted at the children population, the demand for extruded snacks is expected to increase at a CAGR of 15% over the next five years with an increasing young population, multiple snacking options, growing disposable income and the influence of social media, are expected to support the growth momentum.

Exhibit 2: Revenue Mix

Rs. crore	FY15	FY16	FY17	FY18
Chips	169.9	169.1	215.5	263.8
Extruded Snacks	319.7	498.6	570.3	638.7
Namkeen	60.5	78.1	110.5	106.1
Scrap & Other	8.7	3.1	1.8	2.0
Revenues	**558.8**	**748.9**	**898.1**	**1010.5**

Source: Company

Contract manufacturing to be the main mode of expansion in the salty snack segment

The production process is different across all segments that PSL operates in and the capacities cannot be interchangeably unit across various segments. On an aggregate basis, the installed capacity stood at 80,000 MT and the average utilisation of capacities averaged at ~75%. The focus for expanding is mainly through third party manufacturing (currently has 9 contract manufacturing facilities) as against 5 owned facilities. Two of the units are under exclusive arrangement while others can manufacture any other products in the same plant premises. The third-party manufacturing will be the main mode of expansion in the salty snacks segment under the job work route and PSL intends to set up an additional line in the severely under-penetrated sweet snacks segment in the next three years.

Strong distribution network

Sales through distribution channels remains the primary source of revenues for PSL. The company sells its products through a network of super stockists/distributors located throughout India. The super stockists further sell to the distributors who in turn finally sell to retailers. PSL currently operates through an extensive distribution network comprising over 4,100+ distributors, over 240 super stockists and 79 retail outlets.

Exhibit 3: Logistics spend

Year	FY2017	FY2018	FY2019
Super stockists	218+	235+	240+
Distributors	3,500+	3,800+	4,100+
Packets sold (mi)	8.8	9.0	11.0
Logistics Cost	72.47	84.35	
% of OI	8.09%	8.07%	

Source: Company

Exposure to competition from large multinationals and local/ regional players

In the organised snacks segment, the market has been historically dominated by major Fast-Moving Consumer Goods (FMCG) companies such as PepsiCo, ITC, Parle Products, etc. PepsiCo, with its Lays' and Kurkure brands, has dominated the chips and extruded snacks market. A large portfolio of products, new flavors, regular new product launches, aggressive advertisements and promotions, celebrity endorsements have been instrumental in PepsiCo gaining dominance in these categories.

In addition to these larger players, the last four to five years have witnessed the aggressive growth of medium-sized companies such as Prataap Snacks. However, failure to launch and market new products due to unpredictable consumer preferences might have a material adverse effect on business.

FINANCIAL RISK PROFILE

Steady improvement in operating income facilitated by both organic and inorganic expansion

The operating income of the company grew from Rs. 172.7 crore in FY2012 to Rs. 1170.60 crore in FY2019 on account of healthy growth in organic as well as inorganic expansion. Organic growth was facilitated by addition of new product segments, geographical diversification and increasing distribution and reach pan India while inorganic expansion was aided by acquisition of Avadh Snacks Private Limited (in Gujarat market) to increase its market share in India's largest snack market and with the acquisition of Pure N Sure Foods private Limited to facilitate its product diversification in the severely under penetrated sweet snacks market.

Operating margins witness contraction in FY2019

The operating profit margins remain constrained on account of (1) increase in potato prices from average realisation of Rs. 13-16/kg which went upwards of Rs. 20/kg; which is ~40% on a YoY basis, (2) increase in palm oil prices on account of higher import duty which increased from 7.5% to 44%. Potato and palm oil constitutes to close to ~20% of raw material costs. Inflationary pressure on the key raw materials led to margin contraction in FY2019.

Going forward, cost cutting measures including increase in trade margins, reduction in grammage, lowering the cost of packaging, reduction in logistics cost and softening of potato prices are expected to lead to improvement in operating margins. Further, increasing share of sweet snacks are expected to provide boost to margins.

Nil debt resulted in strong capital structure with robust debt coverage indicators

As of March 31, 2019, the debt on the books of the company was in the form of short term loans of Rs. 17.87 crore which are for a short duration of ~180 days carrying interest rate ranging between 9-9.25% per annum. Healthy accretion to reserves resulted in net worth of Rs. 561.36 crore as on March 31, 2019. Low debt levels accompanied by equity infusion by Sequoia capital has strengthened the capital structure with gearing of 0.03 times, TOL/ TNW of 0.5 times. Coverage metrics remain strong with interest cover of 97.0 times, NCA/ Total debt of 443% and DSCR of 93.3 times in FY2019.

Working capital intensity remains inherently low

The inherent working capital intensity of the business continues to remain low at 5.6% in FY2019. The inventory days are low due to the perishable nature of raw material and fast-moving finished goods. Strong market position allows the group to enjoy favorable terms with the distributors which are settled within a short duration of ~10 days. PSL also received credit of ~30-45 days from its suppliers.

CAPITAL EXPENDITURE AND FUNDING PLANS

PSL intends to incur Rs. 20-25.0 crore of annual capex towards addition of new sweets line at an estimated capex of Rs. 18.0 crore. Further, there is a consistent need to replace/repair fryers, moulds, etc which results in sizeable maintenance capex for the company.

DEBT REPAYMENT AND LIQUIDITY PROFILE

No repayment obligations

PSL does not have any long-term debt and there are no repayment obligations.

BUSINESS AND FINANCIAL OUTLOOK

PSL will continue to benefit from its established brand equity and report healthy revenue growth. Further, steady demand for packaged foods driven by increasing affordability, urbanisation, changing lifestyles/customer preferences, and favourable demographics, translate into low business risks for the company. Further, PSL's ability to capture market share with its new product launches and conquer the Gujarat market through its acquisition of Avadh Snacks Private Limited is likely to support growth momentum.

Exhibit 4: Financial outlook

Parameters	ICRA's Comments
Revenue Growth	Revenue growth of 15% over the next three years.
Profitability Indicators	OPM expected to remain at current levels
Repayment Obligations	Nil
Capital Expenditure Plans	Capex rate to remain high at around Rs. 25.0-30.0 crore per year To be funded by largely by internal accruals
Leverage and Coverage Indicators	Capital structure (TD/TNW) likely to remain strong with low dependence on debt Coverage indicators to remain robust
Working Capital Intensity	Working capital intensity to remain low which is inherent of business
Retained Cash Flows	To remain at current levels

Source: PSL, ICRA research

PROMOTER AND MANAGEMENT PROFILE

The promoters of the PSL have more than two decades of experience in the snack food industry and have extensive control on the day-to-day operations in the business. Promoters hold ~23.04% stake in the business.

ANNEXURE I: Key FINANCIAL Indicators

	Standalone			Consolidated		
In Rs. crore	**FY2017**	**FY2018**	**FY2019**	**FY2017**	**FY2018**	**FY2019**
Operating Income (OI)	894.0	1029.9	1068.9	895.7	1044.7	1170.6
Growth in OI (%)	18.1%	15.2%	3.8%		16.6%	12.0%
OPBDITA	42.2	89.3	74.4	43.9	95.0	83.2
Profit After Tax (PAT)	894.0	1029.9	1068.9	20.6	44.2	44.6
Net Cash Accruals (NCA)	38.3	81.8	74.7	36.9	76.8	79.2
OPBDITA/OI (%)	4.7%	8.7%	7.0%	4.9%	9.1%	7.1%
PAT/OI (%)	2.4%	4.7%	4.3%	2.3%	4.2%	3.8%
ROCE (%)	8.1%	17.4%	10.7%	15.5%	16.7%	9.8%
Short-term Debt	26.9	7.5	17.6	26.9	7.5	17.9
Long-term Debt	26.9	0.0	0.0	38.7	0.0	0.0
Total Debt	**53.8**	**7.5**	**17.6**	**65.6**	**7.5**	**17.9**
Tangible Net Worth (TNW)	244.1	530.5	574.1	237.7	519.5	561.4
Total Debt/TNW	0.2	0.0	0.0	0.28	0.01	0.03
Total Debt/OPBDITA	1.3	0.1	0.2	1.49	0.08	0.21
Interest Coverage	9.2	30.9	96.3	9.6	32.7	97.0
TOL/TNW	0.6	0.3	0.3	0.7	0.3	0.5
NCA /TD (%)	71.3%	1093.5%	424.8%	56.3%	1027.5%	443.0%
DSCR (excl STD/prepayments)	3.7	4.3	97.7	9.1	14.7	93.3
Working Capital Indicators						
Debtor Days	6	7	10	6	7	10
Creditor Days	41	51	38	41	53	38
Inventory Days	40	40	39	42	43	51
NWC/OI (%)	2.8%	1.4%	4.7%	0.6%	1.0%	5.6%
Cash Flow Analysis						
Fund Flows from Operations	34.2	71.2	60.5	35.9	76.8	68.2
Retained Cash Flows	60.8	92.3	38.9	30.7	71.4	24.4
Free Cash Flows	12.9	37.2	7.2	(251.9)	21.6	(262.0)

Source: PSL, ICRA research;

ANNEXURE II: Details of Rated Facility

Exhibit 5: Details of PSL's Bank Limits Rated on Long-term Scale

Bank limits	Amounts (Rs. crore)	Rating
Unallocated	58.00	[ICRA]A+ (Stable)
Total	**58.00**	

Links to Applicable Criteria:
[Corporate Credit Rating Methodology]

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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.

For more information, visit www.icra.in and www.icraresearch.in

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