Mahindra Logistics Limited

March 16, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Working Capital Facilities	50.00	50.00	[ICRA]AA (Stable); Reaffirmed
Non-Fund Based Working Capital Facilities	5.00	15.00	[ICRA]A1+; Reaffirmed
Total	**55.00**	**65.00**	

* Instrument Details are provided in Annexure-1

Rating action

ICRA has reaffirmed the long-term rating of [ICRA]AA (pronounced ICRA double A) assigned to the Rs. 50.00 crore[1] long-term, fund-based working capital facilities of Mahindra Logistics Limited ('MLL' or 'the company')[2]. ICRA has also reaffirmed the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) assigned to the Rs. 15.00 crore (enhanced from Rs. 5.00 crore) short-term, non-fund based working capital facilities of MLL. The outlook on the long-term rating is Stable.

Rationale

The reaffirmation of ratings takes into account the strong parentage of MLL as a subsidiary of Mahindra & Mahindra Limited (M&M, rated [ICRA]AAA (stable)/A1+), MLL's established presence in the supply chain management (SCM) segment with M&M being an anchor customer, the increasing client diversification in the SCM business, the leadership position it enjoys in the people logistics (people transport solutions or PTS) business because of its first mover advantage, and the strong financial risk profile of the company as indicated by robust profitability, nearly fully equity-funded capital structure and healthy liquidity position. ICRA notes that the company continues to follow an asset light business model, which is positive, especially in a declining business environment. ICRA also notes that the company has successfully completed its initial public offering (offer for sale by existing investors), to provide partial exit to the private equity (PE) investor (Kedaara Capital).

MLL is positioned as a key intermediary in M&M's automotive and farm equipment business by providing end-to-end supply chain solutions. The strong business linkage with the Mahindra Group ('the group') particularly M&M, in the SCM segment provides MLL with the requisite experience, volumes and a stable business avenue. MLL's SCM business is currently largely focused on the automotive segment, in line with its large dependence on the parent group for business. While MLL has also developed a strong client base outside the group, its current dependence on the group remains high at 54% (PY: 63%) of total revenues for FY2017.

The operating margins of MLL remain thin given the asset-light business model employed by the company, wherein it continues to be a business aggregator and executor. The changing business mix in the SCM segment in favour of higher margin warehousing and line feeding businesses, as against its traditional transportation business, has been aiding improvement in operating margin over the past few years. While the profit margins are relatively better in the PTS

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[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications.*

business, the business remains vulnerable to competition from a large number of unorganised players. Improving scale and profitability of its subsidiaries is also aiding improvement in consolidated operating margins. Profitability–as measured by Return on Capital Employed (ROCE)–has been strong, despite thin margins, owing to its asset light business strategy. The capital structure of the company remains strong–debt free on a standalone basis since FY2013 and low debt levels on a consolidated basis. MLL continues to enjoy superior liquidity, as reflected by sizeable cash and bank balance and liquid investments aggregating to Rs. 116.24 crore as on March 31, 2017, and largely unutilised bank lines of Rs. 48.00 crore.

Outlook: Stable

ICRA believes that MLL will maintain its current comfortable capital structure and profitability, while aiming to grow the topline aggressively. ICRA expects the working capital intensity to remain at the current elevated levels, as the outside the group business is expected to grow at a faster pace. The outlook may be revised to positive if the operating profit margins improve to more than 3% on a sustained basis, while also maintain the current working capital intensity levels. A reduction in working capital intensity, resulting in release of considerable amount of capital, will also be a rating positive. The outlook may be revised to negative in case of any large debt funded acquisition that may suppress profitability and adversely impact the capital structure.

Key rating drivers

Credit strengths

Strong financial flexibility by being a part of Mahindra Group; strong business linkages with the Group in the SCM segment provides requisite volumes and stable business avenue

The group began the logistics business as a division of M&M, before spinning it off as a wholly owned subsidiary of M&M in FY2009. While MLL was initially focused on meeting the SCM requirements of the group companies, it subsequently diversified its client base beyond the group. It continues to cater to almost entire supply chain requirements of M&M. It derived ~54% of its FY2017 revenues from the group. In addition to the business linkages and strong business volumes, MLL, being a part of Mahindra Group, derives flexibility in tapping the banking and financial markets in case of funding requirements.

Asset light business model provides operational flexibility, especially in declining business environment

MLL follows an asset light strategy; the vehicles are hired from transport companies on contractual basis. MLL ties up all its warehousing requirement on a lease basis. Such a policy results in very low capital expenditure requirements and hence, low fixed costs. While the policy affects the margins negatively due to higher operating costs, it provides flexibility during industry down-cycle and helps reduce volatility in return on capital employed (RoCE).

Broad customer base with presence among established companies in each industry segment

Though MLL derived ~54% of its FY2017 revenues from the group, the revenue concentration to the group has reduced over the years (~63% in FY2016). MLL has been focusing on strengthening its presence with the other original equipment manufacturers in the automotive space and diversify its presence into other industry verticals (like pharmaceuticals, FMCG and e-commerce industries). MLL has, over the past four years, added several new customers in the non-automotive segment, resulting in diversification of customer profile.

Leadership position in PTS business, with first mover advantage

By virtue of being an early entrant into the people movement service, a growing requirement for the information technology (IT) and IT enabled services (ITeS) companies, MLL has established a leading position in the PTS business. MLL has a moderately diversified customer base, with it deriving ~46% of its PTS segment revenue in FY2017 from the top five customers. Though a majority of the segment revenues is derived from IT / ITeS companies, these are reputed companies in the industry and have been giving continued business.

Healthy capital structure and liquidity with negligible utilisation of working capital limits owing to healthy cash accruals and PE infusion

The capital structure of the company remains strong–debt free on a standalone basis since FY2013 and low debt levels on a consolidated basis (gearing of 0.1x as of March 31, 2017). MLL continues to enjoy superior liquidity, as reflected by sizeable cash and bank balance and liquid investments aggregating to Rs. 116.24 crore as on March 31, 2017, and largely unutilised bank lines of Rs. 48.00 crore. The capital structure and the liquidity profile have been supported by the Rs. 100.00 crore PE infusion by Kedaara Capital in FY2015. The liquidity, however, has reduced over the past two years due to increase in working capital intensity (as measured by NWC/OI of 6% in FY2017 as against 4% in FY2016 and 1% in FY2015), as the new businesses demanded higher credit period. ICRA expects MLL to maintain the working capital intensity at current levels.

Credit challenges

Concentration of SCM business on automotive (auto) industry exposes the company to high industry cyclicality

MLL's SCM segment derived ~68% of its FY2017 consolidated revenues from auto industry, thus exposing the business to cyclicality inherent in the automotive industry. However, with MLL deriving majority of the segmental revenue growth over the past four years (FY2014-FY2017) from non-automotive industry, its concentration towards the auto industry has decreased from ~77% of SCM revenues in FY2016. This has been achieved on account of focus on non-Mahindra Group business, which is primarily in non-automotive segment. Going forward, the business from e-commerce companies is expected to grow substantially, leading to increase in share of non-automotive segment.

Operates in a very competitive business, dominated by a large number of unorganised players

MLL faces competition from the unorganised logistics service providers in the SCM business and local travel operators in the PTS business. This is negative especially in an environment of declining business volumes and cost-control by the end customers.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

Corporate Credit Rating Methodology

About the company:

Mahindra Logistics Limited (MLL), currently a 61.05% subsidiary of Mahindra & Mahindra Limited (M&M), is a third party logistics (3PL) provider, primarily operating in SCM and PTS. The company commenced operations from December 2000 as a division of M&M to handle the captive logistics and supply chain needs of the Group. Subsequently, the division began operating for external clients across the country. MLL was spun off as a 100% subsidiary of M&M, with effect from April 01, 2008. MLL is head-quartered in Mumbai, with 15 offices and over 4,900 employees (on roll) across India.

During FY2014 and FY2015, Kedaara Capital, a PE investor, infused Rs. 200.00 crore in the company through a combination of primary and secondary investments. MLL concluded its IPO in November 2017 and has got listed in the Bombay Stock Exchange and the National Stock Exchange. As of December 31, 2017, Kedaara Capital, along with Normandy Holdings Limited, held 9.40% stake in equity share capital.

As per audited financials for FY2017, MLL, on a consolidated basis, reported a profit after tax (PAT) of Rs. 46.10 crore on an operating income (OI) of Rs. 2,668.68 crore, as against a PAT of Rs. 35.87 crore on an OI of Rs. 2,064.11 crore during FY2016.

Key financial indicators (audited; consolidated)

	FY2016	FY2017
Operating Income (Rs. crore)	2,064.11	2,666.68
PAT (Rs. crore)	35.87	46.10
OPBDIT/ OI (%)	2.54%	2.86%
RoCE (%)	19.18%	19.95%
Total Debt/ TNW (times)	0.09	0.10
Total Debt/ OPBDIT (times)	0.54	0.45
Interest coverage (times)	39.82	21.89
NWC/ OI (%)	4%	6%

Source: MLL

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2018)				Chronology of Rating History for the past 3 years		
					Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding as on December 31, 2017 (Rs. crore)	March 2018	December 2016	December 2015	November 2014
1	Fund-Based Limits	Long Term	50.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Non-Fund Based Limits	Short Term	15.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

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 – Cash Credit	NA	NA	NA	50.00	[ICRA]AA (Stable)
NA	Non-Fund Based – Bank Guarantee / Letter of Credit	NA	NA	NA	15.00	[ICRA]A1+

Source: MLL

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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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