

March 22, 2021

Dharampal Satyapal Limited: Long-term rating upgraded to [ICRA]AA(Stable); Short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Long-term fund-based cash credit	304.00	304.00	[ICRA]AA(Stable) upgraded from [ICRA]AA-(Stable)
Long-term fund-based term loan	329.5	329.5	[ICRA]AA(Stable); upgraded from [ICRA]AA-(Stable)
Long-term unallocated	61.5	61.5	[ICRA]AA(Stable); upgraded from [ICRA]AA-(Stable)
Short-term non-fund-based	5.00	5.00	[ICRA]A1+ reaffirmed
Total	700.00	700.00	

*Instrument details are provided in Annexure-1

Rationale

The rating upgrade factors in the healthy recovery in Dharampal Satyapal Limited's (DSL or the company) business performance in the recent quarters, following a sharp decline in Q1 FY2021 due to the pandemic, which together with cost rationalisation measures adopted by the company in the recent past, is expected to translate into higher-than-previously envisaged scale, profits and return metrics in FY2021 and FY2022. While the company's turnover is expected to decline in FY2021 vis-à-vis last year, it is partially explained by transfer of confectionery business to a group company from October 2019 onwards. While upgrading DSL's long-term rating, ICRA has also taken a note of the company's sustained robust financial risk profile, characterised by a conservative capital structure, healthy coverage metrics and a strong liquidity position, despite the regular investments in Group entities and other unrelated companies. Further, the ratings continue to draw strength from DSL's strong operational profile, supported by its strong brand presence across India through an established distribution network, and leadership position in the premium pan masala segment. The company enjoys pricing power given its strong brand loyalty among customers and the largely price-inelastic product segment (pan masala), which is exhibited by the successful price hikes implemented by the company in the past. DSL's operational strengths and resulting efficiencies support its large scale of operations and healthy return metrics from core operations. The long-term rating, however, remains constrained by sizeable investments made by DSL in Group entities as well as outside parties, which constrains its overall return metrics (overall ROCE of ~17% in FY2021(E) vis-à-vis ROCE from core operations of ~33% in FY2021(E)). The ratings also continue to be constrained by the vulnerability of DSL's revenues and profits to regulatory risks. Though the company's exposure to regulatory risk has reduced to a certain extent with the transferring of the tobacco business to another Group entity, it remains exposed to regulatory risks associated with the pan masala segment. The risk is heightened by the company's increased revenue dependence on pan masala, following the transfer of its confectionery business in FY2020. The transfer has also heightened the product and brand concentration risk for the company.

The Stable outlook on the [ICRA]AA rating reflects ICRA's expectation that DSL's credit profile will remain robust, supported by healthy profits, low reliance on debt and limited capex/ investments plans.

Key rating drivers and their description

Credit strengths

Business recovery and cost optimisation, expected to lead to better-than-previously envisaged scale, profits and return metrics - DSL's business performance has recovered at a healthy pace in the recent quarters, following a sharp decline in Q1 FY2021 due to the pandemic. This together with the cost rationalisation measures adopted by the company in the recent past, is expected to translate into higher-than-previously envisaged scale, profits and return metrics in FY2021 and FY2022. While the company's turnover is expected to decline in FY2021 vis-à-vis last year, it is partially explained by transfer of confectionery business to a group company from October 2019 onwards.

Leading market position in premium pan masala segment - DSL is the flagship company of the DS Group, which has been in the tobacco and pan masala business for more than 80 years. Over the years, DSL has remained one of the largest players in the Indian pan masala industry through its flagship brand, Rajnigandha. The company's leadership position in the premium pan masala segment supports strong core profitability, as reflected by its core return on capital employed (ROCE) of over 30% in FY2020 and FY2021(E).

Strong pan India distribution network - DSL's market position is supported by its established and strong pan India distribution network (used for all products of the Group). The strength of this widespread distribution network is reflected in the Group's demonstrated ability to push sales of new products and variants. Aided by this network, the DS Group has successfully forayed into new product segments like spices, beverages, mouth fresheners, confectionaries and dairy products (under brands such as Pulse, Catch, Pass Pass, Chingles and Ksheer) over the years, besides maintaining a dominant position in pan masala and tobacco segments (under Rajnigandha, Tulsi and Tansen brands).

Demonstrated pricing power - DSL continues to enjoy pricing power given the strong brand loyalty of its customers and its largely price-inelastic product segment (premium pan masala). This is corroborated by the successful implementation of ~20-22% price hike in FY2018 to withstand the impact of increased tax incidence under the GST regime, following ~40% increase in prices in the preceding three years amid increase in excise duty obligations. Despite the transitory impact on volumes, the company demonstrated its ability to implement price hikes without a prolonged impact on its pan masala sales volumes, which provide comfort. It also implemented a ~6% price hike in February 2020, to absorb the impact of a sharp increase in prices of one of its key raw materials, cardamom. While its pricing power has already been demonstrated, the company's ability to continually do so while maintaining its volumes and healthy profit margins, remains a monitorable.

Strong financial profile characterised by a comfortable capital structure, healthy debt coverage indicators and a strong liquidity profile - Supported by its healthy profitability, DSL has consistently generated cash accruals greater than the requirement of its core business operations, resulting in low dependence on external borrowings (total debt/OPBDITA of ~0.7 time in FY2021(E)). Together with a strong capital base, this results in a low leverage (total debt/tangible net worth, or TD/TNW, of ~0.1 time as on March 31, 2021(E)), despite its sizeable, regular outflows towards investments in related entities to support the Group's diversification plans as well as other strategic investments in unrelated companies and start-ups. Low leverage coupled with limited debt repayments and healthy profitability results in strong debt metrics as reflected by an interest cover of ~26.1 times and DSCR of ~2.8 times for FY2021(E). In addition, DSL has a strong liquidity profile, characterised by sizeable cash and liquid investment balances and healthy cushion available in working capital limits.

Credit challenges

Brand and product concentration risks - DSL's dependence upon Rajnigandha pan masala sales has remained high, with about 78-80% share in revenues during the last three years. While DSL had expanded its product portfolio in the recent years, to include mouth fresheners, confectionaries and dairy products, shifting its confectionery business to a Group entity from mid-FY2020 has again increased DSL's concentration on the pan masala segment from FY2021 onwards.

Regulatory risks due to adverse health effects of pan masala - Pan masala, due to its adverse health effects, remains susceptible to changes in Government policies related to its sale. The Government disincentivises consumption of pan masala by levying high taxes and periodically increasing tax rates. Thus, the company's ability to pass on the hikes in taxes remains

critical for its sales growth and profits. The company also remains exposed to the risks related to the bans on pan masala, as witnessed in Q1 FY2021, when a temporary ban was imposed by the Government on manufacturing, sale and storage of pan masala and tobacco across India, to contain the spread of coronavirus.

Continuous deployment of cash accruals in diverse ventures with insignificant contribution to profits - Being the DS Group’s flagship company and having strong cash accruals with limited capex requirements, DSL supports the Group’s diversification plans by way of investments in various ventures. Besides, the company has also invested in various unrelated companies and start-ups. As a result, the company has a sizeable investment portfolio (equivalent to ~51% of its net worth in FY2020). As most investments do not generate any significant returns at present, these constrain overall return metrics for DSL. Nevertheless, ICRA draws comfort from the fact that some of these investments are discretionary in nature and subject to the availability of surplus cash flows. Further, the company has primarily funded these investments from internal accruals in the past, with minimal reliance on external borrowings.

Liquidity position: Strong

DSL’s liquidity position remains strong with a comfortable cushion in working capital limits (average undrawn limits of ~Rs. 185 crore vis-à-vis drawing power available in the 6-month period ended January 2021) and healthy free cash and bank balance of ~Rs. 275 crore as on December 31, 2020. Moreover, the company’s demonstrated ability to generate healthy cash flow from operations, together with limited repayment obligations and no material expansion plans, is expected to help it maintain a comfortable liquidity profile, despite the regular funding support to Group entities in the form of incremental investments, loans and advances. ICRA notes that the investments in Group companies are discretionary in nature and any incremental outflows remain dependent upon the surplus liquidity available with the company.

Rating sensitivities

Positive factors – The long-term rating could be upgraded if the company achieves a healthy growth in its scale of operations along with increased diversification across products and brands, and improvement in its return indicators on a sustained basis, while maintaining strong capitalisation and coverage metrics. Further, efficient working capital management which strengthens the liquidity position, could be a positive rating trigger.

Negative factors – The ratings could be downgraded in case of any adverse regulatory developments for *pan masala*, resulting in a sustained pressure on the company’s revenues and profitability as well as a decline in its return indicators. Additionally, DSL’s rating would be prone to a downgrade if it undertakes aggressive debt-funded investments/ acquisitions, or experiences a significant stretch in its working capital cycle, which weakens its liquidity profile and/or results in an increase in its leverage.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for entities in the Fast Moving Consumer Goods (FMCG) Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	While ICRA reviews the standalone as well as consolidated financials of the company, the ratings are primarily based on the standalone business and financial risk analysis, as it is the principal driver for the Group’s credit risk. While doing so, ICRA factors in the already extended as well as expected financial support from the company to various Group entities (including entities other than subsidiaries), in its analysis.

About the company

Incorporated in 1989, DSL is the flagship company of the DS Group, which has been in the tobacco and pan masala business for more than 80 years. DSL manufactures and markets pan masala and dairy products, under the brands—Rajnigandha, Tansen, Ksheer, etc. The company, with its flagship brand (Rajnigandha), is the leading player in the premium pan masala industry in India on the back of its strong brand appeal and widespread distribution network. Pan masala sales accounted for ~78% of the company's standalone revenues in FY2020.

Previously, the company had a presence in other business segments as well. In FY2014, DSL demerged its food, beverage and packaging divisions into separate companies, while also transferring some of its investments in hospitality, real estate and agriculture to new holding companies. From December 2014 onwards, DSL began shifting tobacco manufacturing into a newly-formed Group entity, DS Chewing Products LLP, and in October 2019, the company also shifted its confectionery business to a Group entity, DS Confectionery Products Ltd.

In FY2020, the company reported a net profit of Rs. 379.5 crore on an operating income of Rs. 3,592.6 crore, compared to a net profit of Rs. 412.6 crore on an operating income of Rs. 3,664.0 crore in the previous year.

Key financial indicators (audited)

NIEL	FY2019	FY2020
Operating Income (Rs. crore)	3,664.0	3,592.6
PAT (Rs. crore)	412.6	379.5
OPBDIT/OI (%)	21.9%	18.2%
PAT/OI (%)	11.3%	10.6%
Total Outside Liabilities/Tangible Net Worth (times)	0.3	0.3
Total Debt/OPBDIT (times)	0.2	0.7
Interest Coverage (times)	49.2	23.1

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 (FY2021)			Chronology of Rating History for the past 3 years						
	Type*	Amount Rated (Rs. crore)	Amount Outstanding as of Dec 31, 2020 (Rs. crore)	Date & Rating		Date & Rating in FY2020	Date & Rating in FY2019		Date & Rating in FY2018	
				22-Mar-21	27-Oct-2020	26-Jul-2019	14-Dec-2018	6-Apr-2018	28-Jun-2017	10-Apr-2017
1 Cash Credit	LT	304.00	--	[ICRA]AA (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
2 Term Loans	LT	329.5	311.0	[ICRA]AA (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
3 Unallocated	LT	61.5	--	[ICRA]AA (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
4 Short-term Non-fund Based	ST	5.00	--	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-	-
5 Long-term/ Short-term Interchangeable	LT/ST	-	--	-	-	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	-
6 Short-term Fund-based	ST	-	--	-	-	-	-	-	[ICRA]A1+	[ICRA]A1+
7 Long-term Non-fund Based	LT	-	--	-	-	-	-	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
8 Commercial Paper	ST	-	--	-	-	-	-	Withdrawn	[ICRA]A1+	[ICRA]A1+
9 NCD	LT	-	--	-	-	-	-	Withdrawn	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)

*LT: Long-term; ST: Short-term

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 [click here](#)

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	Cash Credit	NA	NA	NA	304.00	[ICRA]AA (Stable)
NA	Term Loans	FY2017	NA	FY2022	329.5	[ICRA]AA (Stable)
NA	Unallocated	NA	NA	NA	61.5	[ICRA]AA (Stable)
NA	Short-term Non-fund Based	NA	NA	NA	5.00	[ICRA]A1+

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	DSL Ownership	Consolidation Approach
Divyansh Powergen Private Limited	100.00%	Full Consolidation
Divyansh Hotels and Resorts Private Limited	100.00%	Full Consolidation
Nilanchaal Cement Private Limited	100.00%	Full Consolidation
Divyansh Cement and Infrastructure Private Limited	100.00%	Full Consolidation
Hillside mines and Minerals Private Limited	100.00%	Full Consolidation
Mount Mines and Minerals Private Limited	100.00%	Full Consolidation
Sandarbh Foods Private Limited	100.00%	Full Consolidation
DS Confectioner Limited	100.00%	Full Consolidation
Abhisar Buildwell Private Limited	100.00%	Full Consolidation
Avichal Buildcon Private Limited	100.00%	Full Consolidation
DS Luxury Retail Limited	100.00%	Full Consolidation
Bharat Broadcasting Company Limited	100.00%	Full Consolidation
Best Broadcasting Company Limited	100.00%	Full Consolidation
DS Dairy and Agri Projects Limited	100.00%	Full Consolidation
DS Dairy Farming Limited	100.00%	Full Consolidation
DS Cattle Farms Limited	100.00%	Full Consolidation
DS Agronomy Limited	100.00%	Full Consolidation
DS Agri and Cattle Farms Limited	100.00%	Full Consolidation
DS Agrarian Estates Limited	100.00%	Full Consolidation
DS India Agri and Dairy Limited	100.00%	Full Consolidation
DS Gross Dairy Products Limited	100.00%	Full Consolidation
Den Pee Kagaz Udyog Private Limited	100.00%	Full Consolidation
Prive Luxury Limited	100.00%	Full Consolidation
Snow White Dairy Products Limited	100.00%	Full Consolidation
DSL Global Pte. Limited	100.00%	Full Consolidation
DS Businesses AG	100.00%	Full Consolidation
Hotel Hirschen AG	100.00%	Full Consolidation
Abiba Buidtech and Consulting Pvt. Ltd.	100.00%	Full Consolidation
Ultimate Farming Pvt. Ltd.	100.00%	Full Consolidation
Rishika Agrodevelopers Pvt. Ltd.	100.00%	Full Consolidation
DS Farms and Estates Limited	100.00%	Full Consolidation
Kolkatta Hotels Limited	99.99%	Full Consolidation
DS (Assam) Hospitality Limited	97.56%	Full Consolidation
Hotel Walzenhausen AG	77.62%	Full Consolidation
Kamakhya Oil Company	70.00%	Equity Method
Legend Fly Private Limited	50.00%	Equity Method
Seven R Hotels Private Limited	42.70%	Equity Method

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