

September 11, 2023

## DS Chewing Products LLP: [ICRA]A(Stable); 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	70.00	70.00	[ICRA]A(Stable); reaffirmed
<b>Total</b>	<b>70.00</b>	<b>70.00</b>	

\*Instrument details are provided in Annexure-I

### Rationale

The rating reaffirmation takes into account ICRA's expectations that DS Chewing Products LLP's (DCPL) will witness a healthy revenue scale up led by recently launched new variant to target the non-premium category, which presents significant market size. The same will be supported by the group's flagship company, Dharampal Satyapal Limited's (DSL's) launch of *pan masala* Mastaba in the same addressable category as both products are mostly consumed in combination. The ratings, continue to draw strength from DCPL's established brand, Tulsi, in the chewing tobacco industry and DCPL's access to a strong distribution and sourcing network under a service agreement with DSL.

The ratings are, however, constrained by ICRA's expectations that DCPL's financial profile will witness a change led by an adverse impact on revenues and profitability, following revision in excise valuation undertaken from FY2023, reflecting the exposure change in Government regulations. Further, the firm has availed loans from related parties to invest in Group companies and venture funds, which has resulted in increasing leverage. In the current fiscal, the firm availed term debt to fund investments in one of its group companies, which is expected to further moderate its coverage indicators and liquidity position. The investments are long-term in nature and primarily towards non-readily tradeable assets and, therefore, have not generated adequate returns at present. Further, the impact of partner capital withdrawals and investments on DCPL's debt coverage metrics and sustenance of the same remains a rating sensitivity. High contingent liabilities in the form of excise tax and GST payments remain a concern and any crystallisation of the same, going forward, remains a key rating monitorable. Nevertheless, while the core business has low capital requirements, ICRA expects the partners to support the firm through infusion of capital in a timely manner, as and when needed, as witnessed in the past. DCPL's reliance on a single brand and a single product segment, along with competition from other players and exposure to regulatory changes are other factors constraining the rating.

The Stable outlook on the rating reflects ICRA's view that DCPL will continue to benefit as part of the DS Group, its strong brand and pan India distribution network. Launch of new Stock Keeping Unit (SKU) to complement the group company's flagship, non-premium *pan masala* variant augurs well for its medium-term growth prospects.

### Key rating drivers and their description

#### Credit strengths

**Established brand in the chewing tobacco industry** – Tulsi is among the leading brands in the domestic premium chewing tobacco industry. Thus, DCPL benefits from the strong brand recall, which augments its ability to charge a premium vis-à-vis other competing brand. Further, the ban on tobacco advertising, imposed more than a decade ago, benefits the firm as it acts as an entry barrier for new brands.

**Strong pan India distribution and sourcing network** – Due to the ban on tobacco advertising, tobacco manufacturers rely on point-of-sale (PoS) advertisement and, hence, having a dedicated distribution network is critical to maintain market share. DCPL benefits from its access to a pan India distribution network of depots, central stockists, distributors, wholesalers and retailers, which is common with other products of the DS Group for brands like Rajnigandha, Pass Pass, Pulse, Catch, etc.

**New SKU launch augurs well for the firm, going forward** –The firm has launched a new SKU variant, which is being sold at Re. 1, and is targeted towards the non-premium segment where there is a huge market opportunity waiting to be tapped. This new variant is expected to be consumed in combination with DSL's latest product, Mastaba. The new variant will be largely volume driven and is expected to aid the firm's revenue growth, going forward.

### Credit challenges

**Loans availed for funding investments in group company leading to pressure on coverage indicators** – The firm's dependence on external debt was primarily towards working capital limits which were used for statutory due payments. However, in current fiscal, the firm availed Rs. 35 crore of term debt to fund investments in one of its group companies in the current fiscal. Further, funding support to subsidiary, 'Gurugram Commerc City Private Limited' (GCPL), to manage its cash flow position including debt obligations (Rs. 80 crore of term debt) pending the ramp up of GCPL's own cash flows, is expected to lead to moderation in coverage indicators in FY2024. GCPL is expected to generate returns in the short to medium term, the timeliness and quantum of the same and associated impact on DCPL's credit profile will be monitorables.

**Vulnerability of tobacco business to Government regulations, recent revised excise valuation impacted profits** - Due to their adverse health effects, tobacco-based products remain susceptible to any changes in Government policies, thus accentuating the product concentration risk. The Government disincentivises tobacco product consumption by levying high taxes and periodically increasing tax rates on their sale. Any adverse change in taxation rates is a key risk for the firm. Apart from taxation, there have been instances of temporary ban on sales of these products in some states. Thus, diversification towards other products remains a rating sensitivity. In FY2023, the firm started paying the excise duty based on revised valuation, i.e., on MRP rather than on the transaction value following a demand raised in June 2021 by the excise department based on the same calculation method. As a result, the firm's net sales witnessed growth, but operating margins declined from ~40% in FY2022 to ~21% in FY2023. While margins were robust in the past, they have now moderated significantly and are expected to remain at similar levels, going forward, primarily owing to higher excise duty incidence as well as launch of high-volume, moderate margin SKU. The crystallisation on contingent liability for the previous periods remains a concern.

**High concentration risk with reliance on single product segment and single brand, coupled with geographical risk**– Despite the business interests of partners across multiple product segments and a wide portfolio of brands, DCPL is reliant on a single product segment, i.e., flavoured tobacco and a single brand, Tulsi. In this context, ICRA notes the firm's venture into manufacturing and exporting *pan masala* under the Group's established brand, Rajnigandha, which is expected to help it diversify its product and brand portfolios as well as geographical presence to some extent.

**Funds withdrawal given partnership constitution of firm and uncertainty on sizeable investments in non-readily tradeable assets** – DCPL's retained cash flows have remained relatively modest in the past, albeit sufficient, as withdrawals by partners have remained high amid minimal funding requirements, compared to the level of profits. In addition, the firm has made investments mostly into non-readily tradeable assets in the past. Continued sizeable incremental investments and/or large funds withdrawals by the partners, which increases the firm's reliance on external debt and affects its liquidity, may affect its credit profile. Prudent management of the level of withdrawals in the future will remain critical for sustaining a comfortable liquidity profile. The partners and promoter group have been infusing capital in the form of unsecured loans primarily to fund a sizeable investment book and ICRA expects the partners to support the firm in case of any need.

### Liquidity position: Adequate

DCPL's liquidity profile remains adequate, supported by adequate fund flow generation from operations, moderate cushion in working capital limits (undrawn fund-based bank facilities averaged at ~Rs. 21 crore in the 11-month period ending July 2023), and free cash and bank balance of ~Rs. 43 crore as on July 31, 2023. The entity has scheduled repayments of Rs. 8.75 crore annually in FY2024 and FY2025. However, the company may have to provide funding support of Rs. 20 crore

to one of its subsidiaries in FY2024. Also, substantial cash outflows in the form of fund withdrawals by partners or other non-current investments, which if not prudently managed, may further impact the firm's liquidity profile adversely. Nevertheless, ICRA expects the partners to support the firm by bringing in unsecured loans in a timely manner, if needed.

## Rating sensitivities

**Positive factors** – The rating could be upgraded, if the firm achieves healthy diversification in its product portfolio, with healthy growth in its scale of operations and profit margins resulting in a sustained improvement in cash accruals, while maintaining healthy debt coverage metrics.

**Negative factors** – The rating could be downgraded, in case of any sustained pressure on the firm's revenues and profitability led by weakening in demand or any adverse changes in the Government's taxation structure. Additionally, DCPL's rating would be prone to a downgrade if there is any sustained moderation in its liquidity profile or if it undertakes sizeable debt-funded investments, witnesses high withdrawals or crystallisation in contingent liability, resulting in an increase in its leverage and a material moderation in its coverage metrics on a sustained basis.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating methodology for entities in the Fast Moving Consumer Goods (FMCG) Industry</a>
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

## About the company

Established in November 2014, DCPL is a Limited Liability Partnership (LLP) firm owned by Mr. Rajiv Kumar and Mr. Ravinder Kumar, who are promoters of the established Dharampal Satyapal (DS) Group. The firm processes and markets flavoured tobacco (*zarda*) under the Tulsi brand. The manufacturing facility of the firm is in Noida, Uttar Pradesh. As the brand is owned by its Group company, DS Sons Private Limited (DSSPL), DCPL pays royalty fee to DSSPL. At present, the company has three manufacturing units in Noida (Uttar Pradesh), Guwahati (Assam) and Kandla (Gujarat).

## Key financial indicators (audited)

Standalone	FY2021	FY2022	FY2023
Operating income	331.7	348.3	401.4
PAT	90.0	82.6	48.9
OPBDIT/OI	46.7%	40.9%	21.2%
PAT/OI	27.1%	23.7%	12.2%
Total outside liabilities/Tangible net worth (times)	6.3	4.5	7.7
Total debt/OPBDIT (times)	0.9	1.2	2.5
Interest coverage (times)	14.2	9.5	5.7

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

Current rating (FY2024)				Chronology of rating history						
Instrument	Type	Amount rated (Rs. crore)	Amount outstanding (Rs. crore)	Date & rating in FY2024			Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	
				11-Sep-23	16-May-23	14-Apr-23			11-Dec-20	19-Oct-20
							-	18-Feb-22		
1	Cash Credit	Long Term	70	-	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)

Source: Company

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Cash Credit	Simple

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 analysing 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 are available on ICRA's website: [Click Here](#)

#### Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	70.00	[ICRA]A(Stable)

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

#### Annexure II: List of entities considered for consolidated analysis – Not Applicable

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### Branches



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