

December 29, 2023

## Valvoline Cummins Private Limited: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term/Short term – Fund-based/Non-fund based limits	50.00	15.00	[ICRA]AA+ (Stable)/ [ICRA]A1+; reaffirmed
Long term – Fund-based limits	100.00	100.00	[ICRA]AA+ (Stable); reaffirmed
Long-term/Short-term - Unallocated limits	-	35.00	[ICRA]AA+ (Stable)/ [ICRA]A1+; reaffirmed
<b>Total</b>	<b>150.00</b>	<b>150.00</b>	

\*Instrument details are provided in Annexure-I

### Rationale

The reaffirmation of the ratings of Valvoline Cummins Private Limited (VCPL) factors in its position as one of the leading players in the lubricant industry, backed by its strong brand presence, technical support from promoter company Valvoline International Inc, a well-entrenched distribution network and a wide product portfolio. These factors, coupled with the captive business of/association with the other promoter company Cummins India Limited (CIL) and the various marketing initiatives undertaken by VCPL, have resulted in a steady volume growth for the company. The ratings also factor in VCPL's comfortable financial profile, characterised by a strong capital structure, its debt-free status, the healthy debt protection metrics and return indicators and an adequate liquidity position. The marketing initiatives and the stable demand prospects for lubricants in India in the near to medium term are likely to keep the volume growth steady for VCPL, going forward.

The ratings, however, are tempered by the highly competitive nature of the industry and the susceptibility of VCPL's profit margins to the volatility in key raw material (base oil) prices and foreign exchange rates, as a sizeable part of the raw material requirement is being met through imports. There has been a substantial increase in base oil prices in the last couple of years which has impacted VCPL's margins. This, coupled with the increased share of the relatively low-margin OEMs, diesel exhaust fluid and the industrial segment in the revenue mix, exerted pressure on the profit margins in FY2023. Additionally, a sizeable proportion of the revenue is generated from the auto sector, exposing it to sectoral concentration risk.

The increased penetration of electric vehicles (EV) can result in some moderation in demand for lubricants in the long term. However, the EV industry in India is still at a nascent stage. The impact of electrification on the commercial vehicle and tractor industries, where VCPL has an established presence, is likely to be limited. Nevertheless, the company remains focussed on enhancing the revenue contribution from other sectors to diversify its revenue mix. ICRA has also taken note of the continued sizeable dividend payout by the company which moderates the net cash accruals, though partly offset by no major capex and other growth plans and its debt-free status.

The Stable outlook reflects ICRA's expectation that VCPL will continue to benefit from a steady demand outlook, its established brand presence and a well-entrenched distribution, enabling the company to generate healthy internal accruals and sustain its liquidity position.

### Key rating drivers and their description

#### Credit strengths

**Established business position, supported by strong brand presence and technical support of promoter Valvoline International Inc.** – VCPL is one of the leading players in the lubricant industry, supported by its strong brand presence, technical support from promoter company Valvoline International Inc, a well-entrenched distribution network and a wide

product portfolio. Valvoline Cummins is among the well-known brands in the Indian lubricant market. VCPL pays a royalty to Valvoline Inc. for the use of the Valvoline brand name and service charge to CIL for its marketing and selling network. Owing to its association with Valvoline International Inc., the company has access to a large database of formulations and enjoys R&D support, which places it favourably to cater to a variety of applications in the lubricant sector in India. Going forward, the impact of the acquisition of the global products business of Valvoline Inc. by Aramco on the Indian business will be monitored.

**Strong marketing and distribution network to cater to retail sales in the domestic market** – In terms of segment-wise sales, the retail segment continues to account for the highest share, both in volume and value terms. The company has developed a well-entrenched distribution network over the years, with around 450 distributors and 55,000-60,000 retailers across the country. VCPL is one of the youngest multinational players in the Indian market, yet it continues to grow at a rate higher than the industry average, supported by various marketing initiatives.

**Large captive business of promoting company, CIL** – VCPL benefits from the sizeable captive business of its promoting company, CIL, which commands a strong market position in the diesel engine market (for power, auto and industrial usage). Moreover, the tie-up of Cummins with other OEMs like Tata Motors has garnered incremental business for VCPL.

**Comfortable financial risk profile** – VCPL registered an operating income of Rs. ~2,150 crore in FY2023 against Rs. 1,694 crore in FY2022, supported by volume growth and higher realisation. The higher realisation was on account of elevated prices of input raw material i.e. base oil and other components. Moreover, the company's capital structure remains comfortable with sizeable net worth and net debt-free status and strong debt protection metrics. However, the margins were impacted in FY2023 (operating margins at 10.3% in FY2023 vis-à-vis 11.4% in FY2022) due to the spike in raw material prices and growth in end-user segments - industrial and OEMs with slightly thin margins. Continued sizeable dividend payouts by the company moderate the net cash accruals, though partly offset by no major capex and other growth plans. The financial profile of the company is likely to remain comfortable, going forward, supported by healthy internal accrual generation and no debt-funded capex.

## Credit challenges

**Highly competitive industry** – The lubricant oil industry is characterised by the presence of a few large players, including oil marketing companies (OMC), other relatively large players and a number of unorganised players, which limits the pricing flexibility of the industry participants. However, VCPL continues to benefit to some extent because of its strong brand presence and the technical support from Valvoline International Inc., enabling it to earn healthy margins.

**Industry growth moderated by technological developments; increased penetration of EVs can result in moderation of sales** – The lubricant industry's growth has been impacted by technological developments that have reduced the frequency of lubricant change and sump sizes. However, VCPL's marketing and R&D initiatives have enabled it to outpace the industry growth. Increased penetration of EVs can also result in some moderation in demand for lubricants. However, the EV industry in India is still at a nascent stage and its impact on lubricant sales is not expected to be material in the medium term.

**Vulnerability of profitability to fluctuations in raw material prices and foreign exchange risks** – VCL's major raw material is base oil (a derivative of crude oil) and 55-60% of the requirement is met through imports from recognised vendors. This exposes the profitability to fluctuations in crude oil prices and forex rates. The product prices for some consumer segments, however, cannot be revised immediately to absorb the price volatility due to market forces. This was also evident in recent quarters wherein the base oil prices firmed up considerably due to pandemic-related disruption and the ongoing Russia-Ukraine war, leading to a moderation in VCPL's margins. However, base oil prices are expected to settle down, going forward, rendering stability to the company's margins.

**Sales susceptible to slowdown in auto sector** – A sizeable part of the revenue is generated from the auto sector, making the company vulnerable to any slowdown in this sector. While the long-term outlook for the automotive sector remains strong, VCPL's growth will continue to be linked to any intermittent demand fluctuations from the automotive segment.

## Liquidity position: Adequate

VCPL's liquidity is adequate, supported by healthy internal accrual generation, free cash balances/liquid investments (~Rs. 51.6 crore as of March 31, 2023) and undrawn bank lines as the utilisation of fund-based limits remains nil. While the dividend payout is expected to remain high, in line with the past trend, it is not expected to weigh down on the company's liquidity as it does not have any long-term debt repayment liability or any major capex plans over the medium term.

## Rating sensitivities

**Positive factors** – The ratings could be upgraded if there is a significant growth in VCPL's scale along with increased product diversification to the non-automotive segment and expansion in market share. The ratings may also be revised upwards if the company is able to maintain healthy profitability amid a comfortable capital structure and liquidity on a sustained basis.

**Negative factors** – A sizeable decline in VCPL's revenue and profitability and stretching of the working capital cycle may exert pressure on the liquidity position and trigger a downgrade. Any sizeable debt-funded capex could also lead to a downgrade.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

## About the company

Valvoline Cummins Private Limited (VCPL) was incorporated in 1994 and promoted by Valvoline International Inc. in a joint venture with Cummins India Limited in which the partners hold 50% equity each. VCPL is engaged in the distribution and marketing of automotive lubricants, transmission fluid, gear oil, hydraulic lubricants, automotive chemicals, specialty products, greases and cooling system products. Since its inception, the company had outsourced manufacturing to a toll blender in Mumbai. However, with the setting up of its own manufacturing facility at Ambarnath in Maharashtra in 2013, the company shifted its entire production to this unit. The company was converted from a limited company to a private limited company with effect from October 14, 2015.

## Key financial indicators (audited)

VCPL Standalone	FY2022	FY2023
Operating income	1,695.9	2,151.2
PAT	135.6	156.3
OPBDIT/OI	11.4%	10.3%
PAT/OI	8.0%	7.3%
Total outside liabilities/Tangible net worth (times)	1.1	1.4
Total debt/OPBDIT (times)	0.0	0.0
Interest coverage (times)	75.3	92.4

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

Instrument	Type	Current rating (FY2024)		Chronology of rating history for the past 3 years			
		Amount rated (Rs. crore)	Amount outstanding as on March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
				Dec 29, 2023	Oct 31, 2022	Aug 27, 2021	Apr 27, 2020
1 Fund-based/Non-fund based limits	Long term /Short-term	15.00	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+
2 Fund-based limits	Long term	100.00	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	-
3 Non-fund based limits	Short-Term	-	-	-	-	[ICRA]A1+	[ICRA]A1+
4 Unallocated limits	Long term /Short-term	35.00	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	-	-	-

### Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term/Short term – Fund-based/Non-fund based limits	Simple
Long term – Fund-based limits	Simple
Unallocated limits	Not Applicable

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	Fund-based/Non-fund based limits	NA	NA	NA	15.00	[ICRA]AA+(Stable)/[ICRA]A1+
NA	Fund-based limits	NA	NA	NA	100.00	[ICRA]AA+(Stable)
NA	Unallocated limits	NA	NA	NA	35.00	[ICRA]AA+(Stable)/[ICRA]A1+

Source: Company

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

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