

June 28, 2024

Neon Motors Private Limited: Ratings reaffirmed; rated amount enhanced; outlook revised to Negative from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	5.00	5.00	[ICRA]BB+(Negative); Ratings reaffirmed, and outlook revised to Negative from Stable
Long-term Fund-based-Cash Credit	87.00	87.00	[ICRA]BB+(Negative); Ratings reaffirmed, and outlook revised to Negative from Stable
Long-term Fund-based- Others	0.00	21.44	[ICRA]BB+ (Negative) assigned
Short-term Non-fund based	6.50	6.50	[ICRA]A4+; Reaffirmed
Long-term/ Short -term – Un allocated	0.06	0.06	[ICRA]BB+(Negative)/[ICRA]A4+; Ratings reaffirmed, and outlook revised to Negative from Stable
Total	98.56	120.00	

*Instrument details are provided in Annexure-I

Rationale

The revision in the outlook on the long-term rating to Negative from Stable considers the likely moderation in Neon Motors Private Limited's (NMPL) credit profile on account of continued low margins and elevated debt levels. NMPL recorded a strong revenue growth of 34% in FY2024 on the back healthy demand in passenger vehicles (PV) and commercial vehicle (CV) segments. However, the company's operating margin remained low at 1.9%, impacted by lower share of spares and service income in the company's revenue mix and initial costs incurred towards new showrooms. Moreover, high working capital requirements with increasing scale and high inventory holding, modest net worth base of the company resulted in elevated debt levels (with sizeable reliance on short-term debt) along with modest coverage metrics. The company's ability to increase its margins, going forward, remains critical to improve its debt metrics.

The ratings, however, favourably factor in the promoters' (a part of the Varun Group) long presence in the dealership industry and NMPL's established position as an authorised dealer Mahindra and Mahindra Limited's (M&M) PVs and CVs and Hyundai Motors India Limited's (HMIL) PVs in 12 districts across Andhra Pradesh (AP) and Telangana. The ratings are further supported by the improving demand for M&M vehicles and the established market position of HMIL in the PV segment. The company has a healthy network with 34 sales and service outlets, 15 service centres and five stockyards across AP and Telangana.

The ratings are, however, constrained by the company's modest capital structure owing to high working capital borrowings, thin margins inherent to the dealership business, and low net worth position. The ratings are further constrained by intense competition in the PV and CV markets in India and limited bargaining power of dealers, with pricing policies decided by the principal OEMs.

Key rating drivers and their description

Credit strengths

Authorised dealer of M&M and HMIL, long experience of the promoter group in dealership industry – NMPL is a part of the Varun Group, which is an established player in the dealership business, operating several dealerships in multiple segments

since 1996. NMPL is an authorised dealer of Mahindra (PV and CV) in Telangana and AP and that of HMIL (PV) in Telangana. The healthy market share of HMIL and increasing acceptance of M&M along with NMPL's increasing share in these OEM's sales are expected to aid the top line of the company.

Extensive network in AP and Telangana – The company has 34 sales and service facilities, 15 service centres and four stockyards across Telangana and Andhra Pradesh. The company also plans to start a R-Outlet and service bodyshop in FY2025.

Credit challenges

Modest financial risk profile – The financial profile of NMPL is modest, characterised by a gearing of 13.6 times as on March 31, 2024, given the low net worth and high working capital debt and sizeable reliance on short-term debt. The company's operations are working capital intensive, given the requirement to hold high inventory. Besides, elevated inventory levels with increasing scale of operations resulted in high reliance on working capital borrowings. Moreover, the company continues to rely on high-cost short-term debt from financial institutions to fund a part of its capex and working capital requirements, despite Rs. 20-crore long-term funds infused by the promoters (as non-convertible preference shares) in FY2024. High reliance on short-term debt enhances the refinancing risk, as indicated by debt service coverage ratio [DSCR] (including short-term debt) of 0.55 times in FY2024, while DSCR, excluding short-term debt, stood at 1.5 times. Moreover, the company's thin margins owing to lower proportion of spares and service income in the revenue mix also impact its debt metrics. Hence, increase in the margins and net worth remains crucial for improvement in credit metrics.

Auto dealership business characterised by intense competition, thin margins and weak bargaining position – The dealership business is characterised by thin margins and low bargaining power of the dealer, as margins on vehicles are determined by the principal. The inherently low value addition and intense competition in the auto dealership business have resulted in low operating margins for the company. Although the company is an authorised dealer of M&M and HMIL, its sales and profitability remain susceptible to intense competition from other dealers of M&M and HMIL as well as other OEMs in the regions. The dealers have to pass on additional benefits to customers to increase sales owing to intense competition, which impacts their profitability to an extent. The share of margin-accretive spares and service income has low contribution in the company's overall sales.

Liquidity position: Adequate

The liquidity of Neon Motors is adequate with a buffer of ~Rs. 11 crore in its working capital limits and cash balance Rs. 8.2 crore as on March 31, 2024 against repayment obligations of Rs. 1.5-2.0 crore and capex plans of ~Rs. 5.0 crore in FY2025. The company also has short-term loans of Rs. 19.8 crore as on March 31, 2024, which are expected to be refinanced.

Rating sensitivities

Positive factors – The outlook on the long-term rating could be revised to Stable from Negative if a healthy increase in margins leads to improved debt metrics. The ratings could be upgraded if there is a sustained increase in its scale of operations, leading to a growth in earnings and improved net worth.

Negative factors – The ratings could witness a downward revision if any material decline in the earnings results in a deterioration in the company's debt metrics. Further, a stretched working capital cycle, impacting the liquidity position of the company, can trigger ratings downgrade. A specific credit metric that could lead to ratings downgrade is DSCR less than 1.3 times, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology-Automobile Dealerships
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of NMPL

About the company

Neon Motors Private Limited was set up in 2012 as an automobile dealer (passenger vehicles and commercial vehicles) for Mahindra and Mahindra Limited in Vishakhapatnam, Andhra Pradesh. The company further expanded to Hyderabad (Telangana) and added additional dealership (passenger vehicles) of Hyundai Motors India Limited. As on date, the company has 34 sales and service outlets, 15 service centres and four stockyards, spread across 12 districts of Andhra Pradesh and Telangana.

Key financial indicators (audited)

NMPL	FY2023	FY2024*
Operating income	707.3	947.6
PAT	1.6	0.8
OPBDIT/OI	1.8%	1.9%
PAT/OI	0.2%	0.1%
Total outside liabilities/Tangible net worth (times)	14.5	16.3
Total debt/OPBDIT (times)	9.2	8.6
Interest coverage (times)	1.9	1.5

Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore

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	Type	Current rating (FY2025)		Chronology of rating history for the past 3 years			
		Amount rated (Rs. crore)	Amount outstanding as of March 31, 2024 (Rs. crore)	Date & rating in FY2025	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
				June 28, 2024	March 27, 2023	-	-
1 Term loans	Long term	5.00	3.63	[ICRA]BB+ (Negative)	[ICRA]BB+(Stable)	-	-
2 Fund-based Cash Credit	Long term	87.00	-	[ICRA]BB+ (Negative)	[ICRA]BB+(Stable)	-	-
3 Fund based Cash Credit	Long term	21.44	-	[ICRA]BB+ (Negative)	-	-	-
4 Non-Fund based-BG	Short term	6.50	-	[ICRA]A4+	[ICRA]A4+	-	-
5 Unallocated Limits	Long term/Short term	0.06	-	[ICRA]BB+(Negative)/ [ICRA]A4+	[ICRA]BB+(Stable)/ [ICRA]A4+	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term Loan	Simple
Long-term fund based- Cash Credit	Simple
Long-term fund based- Inventory funding	Simple
Short term- Non Fund based-Bank Guarantee	Very Simple
Long-term/ Short -term – 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	Term Loan-I	FY2022	NA	FY2028	2.50	[ICRA]BB+(Negative)
NA	Term Loan-II	FY2023	NA	FY2029	2.50	[ICRA]BB+(Negative)
NA	Cash Credit	NA	NA	NA	108.44	[ICRA]BB+(Negative)
NA	Bank Guarantee	NA	NA	NA	6.50	[ICRA]A4+
NA	Unallocated limits	NA	NA	NA	0.06	[ICRA]BB+(Negative)/[ICRA]A4+

Source: Company

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

Annexure II: List of entities considered for consolidated analysis: NA

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