February 06, 2017

Varun Beverages Limited

Instruments*	Amount Rated (Rs. Cr.)	Rating Action
Commercial Paper Programme (Proposed)	100.0	[ICRA]A1+ (Assigned)

Instrument details are provided in Annexure-1

Rating Action

ICRA has assigned its short term rating of [ICRA] A1+ (pronounced ICRA A one plus)[1] to the Rs. 100.0 Cr.[2] commercial paper programme of Varun Beverages Ltd. (VBL).

Rationale

The rating positively factors in the established track record of the promoters and long-term presence of the company as one of the leading bottlers of PepsiCo and successful completion of Initial Public Offer (IPO) in November 2016 which has impacted the financial profile of VBL favourably. While assigning the rating, ICRA also takes into account the strong financial risk profile of VBL as characterised by healthy growth in operating income, buoyant profitability margins over the last few years and comfortable capital structure which has further improved post infusion of equity. The rating further factors in VBL's increasing geographical reach, both domestically and globally along with the benefits derived from backward integration of operations as VBL, on its own, manufactures crown corks, polyethylene terephthalate (PET) pre-forms, storage boxes, shrink wrap sheets, and plastic cap closures etc.

However, the rating is constrained by capital intensive nature of VBL's business, which requires frequent investments in infrastructure on a regular basis. VBL's profitability is also vulnerable to fluctuations in prices of various raw materials such as sugar, PET resin, etc. VBL's ratings are also susceptible to any adverse regulatory changes, changes in consumer preferences and seasonality with a major portion of revenues arising in the first half of the year. While assigning the rating, ICRA also factors the possibility of VBL extending support to its international subsidiaries.

The ability of the company to continue its association with PepsiCo, maintain comfortable capital structure and debt protection metrics and sustain its profitability margins are the key rating sensitivities.

Key rating drivers

Credit Strengths

- Established track record of the promoters and long-term presence of the company as one of the leading bottlers of PepsiCo
- Stable business model of the company due to franchisee bottler agreement with PepsiCo; At present, the company is exclusively engaged in manufacturing and distribution of beverages in 17 States and 2 Union Territories in India
- Strong financial risk profile of VBL as characterised by healthy growth in operating income, buoyant profitability margins over the last few years and comfortable capital structure
- Benefits derived from backward integration of operations as VBL manufactures crown corks, polyethylene terephthalate (PET) pre-forms, storage boxes, shrink wrap sheets, and plastic cap closures etc.
- Successful fund raising through IPO which has been used to repay debt and would therefore result in de leveraging of capital structure and strengthening of debt protection metrics

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

2 100 lakh = 1 crore = 10 million

Credit Concerns

- Capital intensive nature of VBL's business, which requires frequent investments on a regular basis
- Vulnerability of operating profitability to fluctuations in prices of various raw materials
- Vulnerability of profitability to any adverse changes in government regulations or any change in consumer preferences

Description of key rating drivers highlighted above:
VBL continues to benefit from its strong market position domestically. VBL is the largest franchisee bottler of PepsiCo in India having operations in Uttar Pradesh, Rajasthan, Delhi, West Bengal, Haryana, Punjab, Chandigarh, Himachal Pradesh, Uttarakhand, Goa, parts of Madhya Pradesh, three districts of Maharashtra, and North-East India. In February 2015, VBL acquired selling and distribution rights for Punjab, Chandigarh, Himachal Pradesh,

and the remaining parts of Uttar Pradesh, Uttarakhand and Haryana along with four bottling units—one each at Panipat in Haryana, and at Sathariya and Jainpur in Uttar Pradesh and Bazpur in Uttarakhand — on a slump-sale basis from PepsiCo. In 2016, in-line with its philosophy of doing most of the activities in-house, VBL further acquired two co-packing facilities at Sathariya and Phillaur.

VBL's capital structure has strengthened significantly because of funds raised through IPO in November 2016, leading to equity infusion of Rs 667.5 Cr. Most of the IPO proceeds were used to reduce debt. As a result, the promoter shareholding reduced from 100% to around 74.0% as on November 30, 2016. The dilution also includes the equity shares allotted to Standard Chartered Private Equity and AION investments upon conversion of CCDs prior to IPO.

Raw material costs which include components such as sugar, concentrate, PET, mango pulp, Co_2 etc. form a major part of the cost structure of the company. The ability of the company to pass on any increase in its input costs by increasing prices of its products remains critical for its operations. Secondly, the demand of aerated beverages is contingent upon the taste and preferences of consumers. With the growing focus towards a healthy lifestyle, there is a possibility of moderation in demand for aerated beverages. However, given the low penetration and per capita consumption of these beverages in India as against other developed countries and the strong pipeline of healthy beverages (7up Revive, Nimbooz Masala Soda, Tropicana Frutz), there is significant scope for increase in the consumption of these beverages.

Analytical approach
Not Applicable

Links to applicable Criteria
[Corporate Credit Ratings: A Note on Methodology]

About the Company:
Incorporated in 1995 by Mr. Ravi Kant Jaipuria, VBL is a franchisee of various carbonated beverages owned by PepsiCo with the major ones being Pepsi, Mountain Dew, 7up and Mirinda. Apart from carbonated drinks, VBL also sells packaged drinking water - Aquafina, and non-carbonated beverages such as Tropicana Slice, Tropicana Frutz and Nimbooz. At present, the company is engaged in distribution of beverages in 17 States and 2 Union Territories in India. Operations outside India comprise bottling operations in Nepal under Varun Beverages (Nepal) Pvt Ltd; in Sri Lanka under Varun Beverages Lanka (Pvt) Ltd; in Morocco under Varun Beverages Morocco SA; in Zambia under Varun Beverages (Zambia) Ltd; and in Mozambique under Varun Beverages Mozambique Limitada. VBL has 16 domestic production units and 5 production units in its international licensed territories.
VBL raised funds through an IPO in November 2016 with an issue size of 25 million shares, including 10 million shares on offer for sale by the promoters. As a result, the promoter shareholding reduced from 100% to around 74% as on November 30, 2016. The dilution also includes the equity shares allotted to Standard Chartered Private Equity and AION investments upon conversion of CCDs prior to IPO.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

ICRA

Rating History for last three years:
Table: Rating History

S. No.	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years		
		Type	Rated amount (Rs. Crores)	Month - year & rating	Month - year & Rating in FY2016	Month - year & Rating in FY2015	Month - year & Rating in FY2014
				Feb 2017			
1	Commercial Paper	Short term	100	[ICRA]A1+	NA	NA	NA

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

Details of Instruments

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
Commercial Paper (Proposed)	-	-	-	100.00	[ICRA]A1+

Source: VBL

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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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