December 08, 2017

Varun Beverages Limited

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Fund based-Commercial Paper (Proposed)	100.0	[ICRA]A1+; Reaffirmed
Total	**100.0**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) on the Rs. 100.0-crore[1] proposed commercial paper programme of Varun Beverages Limited (VBL or the company)[2].

Rationale

The rating positively factors in the long track record of the promoters, established presence of the company as one of the leading franchisees of PepsiCo and successful acquisition of two more territories (Odisha and part of Madhya Pradesh) from PepsiCo in CY2017, which is expected to bolster VBL's beverage business. While reaffirming the rating, ICRA has also taken into account the strong financial risk profile of VBL supported by healthy growth in operating income (OI), buoyant profitability margins driven by operational efficiencies and inroads into contiguous territories. The rating further factors in VBL's widespread geographical reach (which reduces its dependence on Indian operations alone) and benefits derived from backward integration of operations.

However, the rating is constrained by the vulnerability of VBL's profitability to fluctuations in prices of various raw materials such as sugar, polyethylene terephthalate (PET) resin etc. However, the company has been able to pass on such increases to consumers through hike in the maximum retail price of certain SKUs in the past. VBL's ratings are also susceptible to adverse regulatory changes, modifications in consumer preferences and seasonality as a major portion of revenues is generated in the first half of the year. While reaffirming the rating, ICRA factors in the possibility of VBL extending support to its international subsidiaries.

Key rating drivers

Credit strengths

- **Established track record of promoters; strong market position VBL as one of the leading franchisees of PepsiCo in India -** VBL continues to benefit from the vast experience of its promoters in the bottling industry since the 1960s. Also, the company's strong position in the domestic market as one the largest franchisee of PepsiCo (presence in 18 states and 2 union territories) is a positive.
- **Acquisition of territories to strengthen bottling business -** VBL has further acquired two more territories (Odisha and part of Madhya Pradesh) from PepsiCo in CY2017, which is expected to bolster its bottling business.
- **Stable business model -** The company has a stable business model due to its exclusive franchise agreement with PepsiCo in various states in India and other countries such as Nepal, Sri Lanka, Morocco and Zambia.

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[1] *100 lakh = 1 crore = 10 million*

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

- **Strong financial risk profile –** VBL's strong financial risk profile is indicated by a healthy growth in operating income, buoyant profitability margins over the last few years and strong coverage indicators.
- **Benefits derived from backward integration of operations -** Operational efficiencies and healthy margins led by integrated manufacturing processes as VBL manufactures crown corks, PET pre-forms, corrugated boxes, plastic shells, shrink wrap sheets, and plastic cap closures etc.

Credit weaknesses

- **Vulnerability of operating profitability to fluctuations in prices of various raw materials -** VBL's profitability is vulnerable to fluctuations in the prices of various raw materials such as sugar, concentrate, PET, mango pulp, CO_2 etc. Raw materials form a major part of the cost structure for 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.
- **Vulnerability of profitability to adverse changes in Government regulations or consumer preferences -** VBL's ratings are also susceptible to adverse regulatory changes, modifications in consumer preferences and seasonality as a major portion of revenues is generated in the first half of the year. The demand of aerated beverages is contingent upon the taste and preferences of consumers. Also, with a shift towards a healthy lifestyle, there is a possibility of moderation in demand for aerated beverages. Both these factors can impact the company and thereby affect its ratings.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria

Corporate Credit Rating Methodology

About the company

Incorporated in 1995 by Mr. Ravi Kant Jaipuria, VBL is a franchisee of various carbonated beverages owned by PepsiCo, the major ones being Pepsi, Mountain Dew, 7UP and Mirinda. Apart from carbonated drinks, VBL sells packaged drinking water (Aquafina), and non-carbonated beverages such as Tropicana Slice, Tropicana Frutz and Nimbooz. At present, the company is involved in the distribution of beverages in 18 states and 2 union territories in India. Operations outside India comprise those in Nepal under Varun Beverages (Nepal) Pvt Ltd; in Sri Lanka under Varun Beverages Lanka (Pvt) Ltd; in Morocco under Varun Beverages Morocco SA; and in Zambia under Varun Beverages (Zambia) Ltd.

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.

Key financial indicators (standalone)

	CY2015	CY2016
Operating Income (Rs. crore)	2864	2972
PAT (Rs. crore)	153	187
OPBDIT/ OI (%)	20.2%	23.3%
RoCE (%)	13.7%	14.2%
Total Debt/ TNW (times)	1.50	0.56
Total Debt/ OPBDIT (times)	2.3	1.7
Interest Coverage (times)	4.2	3.9
NWC/ OI (%)	12%	10%

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);
NWC: Net Working Capital

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years
Table

S. No.	Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
				December 2017	February 2017	NA	NA
1	CP (proposed)	Short Term	100.0	[ICRA]A1+	[ICRA]A1+	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

Instrument Details

ISIN No	**Instrument**	**Date of Issuance / Sanction**	**Coupon Rate**	**Maturity Date**	**Amount Rated (Rs. crore)**	**Current Rating and Outlook**
	CP (proposed)	-	-	-	100.0	[ICRA]A1+

Source: the company

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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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