March 21, 2023

ADS Spirits Private Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit	21.00	30.00	[ICRA]A- (Stable); reaffirmed, assigned for enhanced amount
Long-term – Unallocated	39.00	55.00	[ICRA]A- (Stable); reaffirmed, assigned for enhanced amount
Total	**60.00**	**85.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation factors in ICRA's expectation that ADS Spirits Private Limited (ADS) will be able to maintain its healthy financial profile, going forward. Healthy volumetric growth of ADS' Indian made foreign liquor (IMFL) brands as well as country liquor (CL) segment is expected to drive earnings with the company also growing its geographical presence in the IMFL segment. While the company's revenues grew by ~6% and ~20% YoY in FY2022 and 9M FY2023, respectively, aided by increased brand volumes across its liquor segments. ADS' healthy cash accruals and modest reliance on debt has kept credit metrics strong, although an increase in debt levels is expected owing to new office related capex and a growing receivable cycle. The rating also draws comfort from the extensive experience of the promoters in the alcobev industry.

However, the ratings are constrained by the high business risk inherent in the alcobev industry owing to stringent Government controls and regulations, and the lack of pricing power in the CL segment. Further, the company is also exposed to raw material availability and pricing risks, as reflected by the pressure on margins in 9M FY2023. The company's working capital intensity has increased on the back of higher receivables from Government entities. The rating also factors in ADS' concentration on a few states, since it derives most of its revenue from Haryana and Delhi, as well as its high dependence on a single brand, Royal Green, in the IMFL segment. However, the concentration is expected to moderate gradually as it has expanded its footprint in various north-eastern and southern states in the last 2-3 years. ICRA also notes the intensely competitive IMFL segment due to some reputed and numerous regional players, which limits pricing power.

The Stable outlook on the [ICRA]A- rating reflects ICRA's opinion that the company will benefit from its track record in the alcobev industry and the current healthy demand outlook. Moreover, foray into new states will augur well for its earnings growth.

Key rating drivers and their description

Credit strengths

Over two decades of experience of promoters in the industry – The promoters have been involved in the alcobev business for more than two decades. They have an established presence in Haryana, which provides access to retail outlets for selling ADS' own brands, especially IMFL. The company has a pan India presence through the promoters owned bottling units, units taken on lease and tie-ups with other bottlers, which largely cater to ADS' operations.

Healthy volumetric growth in IMFL and CL – ADS has reported healthy volumetric growth in IMFL brands as well as its CL segment. While the entire CL volume growth comes from Haryana, the company has reported strong volume growth in the IMFL segment mainly on account of increased volumes sold by its franchisees. ADS has reported 47.1 lakh cases in 9M FY2023 compared to 41.4 lakh cases in FY2022 in the CL division, while the company has reported 33.7 lakh cases of its IMFL brands (including franchisee) in 9M FY2023 over 35.2 lakh cases in FY2022. Based on own sales growth, which has been primarily led by volumes and to an extent by realisations, the company's revenues grew by ~6% in FY2022 over FY2021. The company earns brand surplus income from its franchisees, whose growth has supported its operating profits.

Strong financial profile and healthy net worth; modest reliance on external debt – ADS has a strong financial profile from reflected by healthy profitability and modest reliance on external debt. Over the years, the company has built a strong net worth led by healthy accretion to reserves. In the past the working capital requirement is being largely funded by the cash generation from business, advances from customer and interest free unsecured loan from promoters, going forward with growing working capital requirements, the company's reliance on bank limits is expected to increase. The company's planned capex for a corporate office will be partly debt funded. Hence, some moderation in credit metrics is expected; however, the same are expected to be comfortable.

Favourable demand outlook for alcobev industry – The demand outlook for the alcobev industry is favourable, led by increasing consumption on account of rising disposable income, urbanisation and changing consumer preferences. With the waning impact of the pandemic, the alcobev industry witnessed a healthy revival in FY2022 which has continued in current fiscal and is poised to continue in the medium term.

Credit challenges

Moderate geographical concentration risk in Haryana and Delhi – ADS has been deriving most of its sales volume from Haryana and Delhi. The company has a distillery in Haryana and its entire CL production is sold in Haryana and is regulated by the Haryana Excise Policy. There has been a significant increase in IMFL brand sales in 9M FY2023; however, ~40-50% of its IMFL volume comes from Delhi. Overall, Haryana and Delhi have been driving a sizeable chunk of the company's revenues, which exposes it to geographical concentration risk. In the last 2-3 years, the company has increased its presence in the eastern and southern markets, which should diversify the revenues to some extent in the medium term.

High working capital intensity led by elevated receivable cycle – In line with the increase in scale of business, the working capital requirements of the company have increased. As most of the debtors are from state corporations, the risk of debtors turning bad remains low; however, the delays in recoveries elongate the working capital cycle. The change in liquor retail policy in Delhi from private to government control, has also resulted in a sharp rise in debtors days in 9M FY2023. The receivable build-up beyond six months also remains a concern and typically the working capital limit utilisation is high at month ends. In the past, this has necessitated regular long-term fund infusion in the form of unsecured loans from promoters, while the company is expected to enhance its limits further in the near term.

Vulnerability to changes in raw material prices – ADS' margins remain exposed to volatile raw material prices, particularly for broken rice for the distillery, glass bottles for IMFL and coal/husk prices for its captive power plant. The input price has increased significantly in 9M FY2023 compared to FY2022; hence operating profit margin (OPM) has declined to 17.1% in 9M FY2023 from 20.1% in FY2022. The ability of the company to receive commensurate price increase approvals and support its margins thus remains crucial.

Intense competition in highly regulated alcohol industry – The liquor industry is intensely competitive due to numerous small players. It is a highly regulated industry with the state government controlling the sales and distribution, making the company susceptible to changes in Government policies. Any change in Government policies with respect to production and distribution of liquor, taxation, and state excise duty or any material changes in the duty structure may impact the liquor industry and, subsequently, the company.

Liquidity position: Adequate

ADS's liquidity is **adequate**, aided by healthy cash flow from operations and moderate cushion in the cash credit limit. The company is generating ~Rs. 80-90 crore net cash from business, which is sufficient to take care of the proposed capital expenditure of Rs. 65-70 crore and additional working capital requirements due to absence of any long-term debt repayments. The promoters have also been providing funding support by way of interest free unsecured loans. Moreover, the company is in the process of enhancing its cash credit limits, which lends comfort. The company is likely to take a Rs. 24.5-crore term loan for capex, which will be repaid in two years. The existing cash generation from business will be sufficient for loan repayment. The company has not maintained any sizeable free cash at present.

Rating sensitivities

Positive factors – The ratings may be revised upwards if the company reports sustained scale-up in operations through greater diversification of its product profile and geographical spread, while maintaining healthy profitability and debt metrics.

Negative factors – Downward pressure on the rating will emerge if there is a high reliance on external borrowings, resulting in deterioration in debt metrics, or if lack of commensurate and timely returns from capacity expansion impacts the coverage metrics and causes any weakening in the overall liquidity position on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not applicable
Consolidation/Standalone	Standalone financial profile of ADS

About the company

ADS Spirits Private Limited was incorporated in 2010. The company operates a 60-KLPD grain-based distillery in Jhajjar, Haryana, for manufacturing extra neutral alcohol (ENA), which is the main ingredient for manufacturing CL and IMFL. The company commenced operations from March 2013. It also manufactures and bottles CL and IMFL. In addition, the company has a 2.5-MW captive coal/husk-based power plant, which alongside meeting the entire power requirement of the manufacturing unit, supplies steam for the manufacturing process. While CL is only sold in Haryana, its IMFL is sold in Haryana, Delhi and other states as well. The company has franchisee arrangements across the other states wherein the IMFL brands are manufactured and bottled.

Key financial indicators (audited)

ADS Standalone	FY2021	FY2022	9M FY2023*
Operating income	546.1	576.3	530.6
PAT	79.3	78.1	61.2
OPBDIT/OI	21.5%	20.1%	17.1%
PAT/OI	14.5%	13.6%	11.5%
Total outside liabilities/Tangible net worth (times)	0.8x	0.6x	0.7x
Total debt/OPBDIT (times)	0.4x	0.7x	0.9x
Interest coverage (times)	241.0x	188.7x	125.0x

*Source: Company, *provisional financial submitted by management*
PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amounts in Rs. Crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore) *	Date & rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021	Date & Rating in FY2020
				Mar 21, 2023	Feb 14, 2022	Sep 30, 2021	June 29, 2020	Dec 5, 2019
1 Cash Credit	Long Term	30.00	-	[ICRA A- (Stable)	[ICRA A- (Stable) Removed from ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable) ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
2 Term Loan	Long Term	-	-	-	-	[ICRA]BBB+ (Stable) ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
3 Unallocated	Long Short	55.00	-	[ICRA A- (Stable)	[ICRA A- (Stable) Removed from ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable) ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)

Source: Company,

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term Fund-based – Cash Credit	Simple
Long-term – Unallocated	NA

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	30.00	[ICRA]A- (Stable)
NA	Unallocated	NA	NA	NA	55.00	[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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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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