

Mohan Meakin Limited

September 27, 2018

Summary of rated instruments

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|-----------------------------------|-----------------------------------|----------------------------------|--|
| Long-term: Fund Based/Cash Credit | 65.00 | 65.00 | [ICRA]BBB- (Stable); upgraded from [ICRA]BB (Stable) |
| Long-term: Fund Based/Term Loan | 10.00 | - | - |
| Short-term: Non-fund Based | 10.00 | 5.00 | [ICRA] A3, upgraded from [ICRA] A4+ |
| Long-term/Short-term: Unallocated | 15.20 | 5.00 | [ICRA]BBB-(Stable)/A3, upgraded from [ICRA]BB (Stable)/ [ICRA] A4+ |
| Total | 100.20 | 75.00 | |

*Instrument details are provided in Annexure-1

Rating action

ICRA has upgraded the long-term ratings on Rs. 75-crore bank facilities of Mohan Meakin Limited (MML) to [ICRA]BBB- (pronounced ICRA triple B minus) from [ICRA]BB (pronounced ICRA double B). The short-term ratings have been upgraded to [ICRA]A3 (pronounced ICRA A three) from [ICRA]A4+ (pronounced ICRA A four plus). The outlook on the long-term rating is Stable.

Rationale

The ratings upgrade takes into account the improvement in MML's performance in FY2018, which has continued in Q1 FY2019 as well. The company reported healthy revenue growth of ~13% aided by increased sales volume in FY2018. This was despite the implementation of the Goods and Services Tax (GST) from July 1, 2017 and de-stocking in line with the Supreme Court directive on closure of all liquor retail outlets within 500 meters of highways across the country from April 1, 2017. This apart, the company's capital structure strengthened due to increased accretion to reserves, which resulted in low gearing levels. Further, while ICRA notes the significant contribution of extraordinary income to the company's accruals; various cost-reduction initiatives undertaken by MML, along with product price increases in various states, improved the operating margins in FY2018. ICRA also takes note of the recent policy changes in Uttar Pradesh which will aid the company going forward. The ratings also derive strength from MML's operating track record of over 15 decades in the Indian liquor industry and the established brand presence of its flagship brand – Old Monk – in the rum segment. The ratings also take into account the company's pan-India presence through its own manufacturing units in the North and franchisee bottling arrangements that cater to other regions.

The ratings, however, are constrained by the company's average operational profile as reflected by low capacity utilisation of the manufacturing facilities due to its vintage. This has resulted in subdued margins for the company. The ratings also factor in the concentration risks arising out of high dependence on a single brand – Old Monk – for most of its sales, and limited presence of the company in other product categories. Additionally, the margins remain exposed to any fluctuation in raw material prices given the increased reliance on outside purchase of spirits. The ratings are also

constrained by the high business risk inherent in the liquor industry owing to high taxes and stringent Government controls and regulations, and limited pricing power.

Notwithstanding these concerns, ICRA expects the company to keep benefitting from its established brand presence and favourable long-term volume outlook for the Indian-made foreign liquor (IMFL) industry due to increase in per capita income as well as changing lifestyles. MML has planned capital expenditure of Rs.10-15 crore for upgrading its beer unit during FY2020. Given that a substantial portion of the same is expected to be funded through internal accruals, ICRA expects MML's capital structure and coverage metrics to remain comfortable going forward. The company's ability to grow its operating income (OI) and profitability in a regulated market would remain the key rating sensitivities.

Outlook: Stable

The Stable outlook reflects ICRA's expectation that MML will continue to benefit from the extensive management industry experience, established brand equity, and favourable long-term volume outlook for the industry. Additionally, an expectation of pick-up in volumes as a fallout of the new excise policy in Uttar Pradesh augurs well for the company's growth prospects over the short to medium term. The outlook may be revised to Positive if the company is able to demonstrate a sustained improvement in revenues and profitability. The outlook may be revised to Negative if cash accruals are lower than expected, or if there is material deterioration in margins, or if any major debt-funded capital expenditure, or stretch in the working capital cycle weakens liquidity. Any unforeseen regulatory change will also be a key rating sensitivity.

Key rating drivers

Credit strengths

Experienced management; reputation in industry: The management has extensive experience in the liquor manufacturing industry. The Mohan family took over the company's operations in 1949, and since then the company has been one of the well-known players in the Indian liquor industry.

Established brands with pan-India presence: The company has an extensive operational track record and an established presence in the domestic IMFL market through its flagship brand, Old Monk. Under the IMFL segment, MML's portfolio currently includes brands like Old Monk, Golden Eagle, Solan No. 1 etc. The company has a pan-India distribution network through its own manufacturing units in the North and franchisee bottling arrangements that cater to other regions.

Moderate financial risk profile: MML has moderate financial risk with comfortable gearing levels. Steady accretion to reserves has strengthened the company's net worth, resulting in gearing of 0.53 times as on March 31, 2018. The company's subdued profit margins result in moderate coverage indicators as reflected by interest coverage of 2.79 times for FY2018. MML has an efficient working capital cycle, with Net Working Capital (NWC)/Operating Income (OI) ratio of 10% in the same year.

Favourable demand outlook: India's spirit industry is expected to record the second-fastest growth globally. At present, the Indian alcohol industry is characterised by per capita consumption of 5.1 litres per annum, which is considerably lower than the Asian per capita average of 20.9 litres. The industry's growth is expected to be supported by favourable demographics, rising disposable incomes and urbanisation. These growth drivers are expected to support the company's revenues.

High entry barriers and strong hold in defence segment: While the highly regulated nature of the industry with substantial Government controls on advertising and taxes restrict growth to a certain extent, the same creates entry barriers for new players, thereby favouring incumbents. MML is also one of the suppliers of branded IMFL to the Canteen Stores Department (CSD), which has significant business barriers to entry. About 20% of the company's revenues are through sale to the CSD.

Credit challenges

Weak operational profile reflected by low capacity utilisation: The company's operational profile remains weak as reflected by low capacity utilisation due to plants of relatively older vintage, which has in turn resulted in high production costs. As a result, the margins have remained low in the past.

Exposure of profitability margins to volatility in raw-material prices: The company's margins remain dependent on price trends of major raw materials like molasses and grains. The raw material prices are governed by various factors, including the supply of molasses and grains, which is in turn dependent upon production, Government regulations, demand from other sectors like biodiesel etc.

Highly regulated nature of industry: MML remains exposed to changes in pricing by state governments. Strong government controls, ban on advertising, varying tax structures in different states pose challenges and restrict growth of the industry; demonetisation and de-stocking on account of ban on liquor sale near highways from April 1, 2017 affected the sales volumes of the industry in FY2018.

Project risks associated with large capital expenditure plans in Hathras, UP: The company had taken land on lease at Hathras, UP from UPSIDC¹; however proper possession of the same has not been received. ICRA will continue to monitor the progress on the possession of the land, and any further capex on it and its impact on the company's financial profile.

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

MML was initially established in 1855 by Mr. Edward Dyer, who established the first brewery in India. In 1949, Late Mr. Narendra N. Mohan took over the operations of the company. MML owns brands such as Old Monk in the rum segment and Meakin 10000, Asia 72, and Golden Eagle in the beer segment. MML has two manufacturing facilities to manufacture beer, spirit, and food products (largely grain flakes) at Mohan Nagar in UP and Kasauli/Solan in Himachal Pradesh (HP). In addition, it has bottling plants at Mohangram in Punjab and Solan in HP.

¹ Uttar Pradesh State Industrial Development Corporation

Key financial indicators (audited)

| | FY2017 | FY2018 |
|------------------------------|--------|--------|
| Operating Income (Rs. crore) | 464.77 | 523.68 |
| PAT (Rs. crore) | 4.79 | 15.53 |
| OPBDIT/OI (%) | 3.07% | 3.54% |
| RoCE (%) | 19.82% | 35.36% |
| Total Debt/TNW (times) | 1.19 | 0.53 |
| Total Debt/OPBDIT (times) | 3.43 | 1.62 |
| Interest Coverage (times) | 1.56 | 2.79 |

OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortisation; PAT: Profit after Tax; RoCE: Return on Capital Employed; TNW: Tangible Net worth; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress); Source: Financial statements of MML; ICRA research; The company started reporting in Ind AS from FY2017

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

| SNo | Name of Instrument | Type | Current Rating (FY2019) | | | Chronology of Rating History for the Past 3 years | | |
|-----|--------------------|----------------------|-------------------------|--------------------|-----------------------------|---|-----------------------------|----------------------|
| | | | Rated amount | Amount outstanding | Month-year & Rating | Month- year and Rating in | | |
| | | | | | | (Rs. crore) | September 2018 | July 2017 |
| 1 | Cash Credit | Long Term | 65.00 | - | [ICRA]BBB-(Stable) | [ICRA]BB (Stable) | [ICRA]BB-(Stable) | [ICRA]B+ |
| 2 | Term Loan | Long Term | - | - | - | [ICRA]BB (Stable) | [ICRA]BB-(Stable) | [ICRA]B+ |
| 3 | Non-fund Based | Short Term | 5.00 | - | [ICRA]A3 | [ICRA] A4+ | [ICRA] A4 | [ICRA] A4 |
| 4 | Unallocated | Long Term/Short Term | 5.00 | - | [ICRA]BBB-(Stable)/[ICRA]A3 | [ICRA]BB (Stable)/[ICRA] A4+ | [ICRA]BB-(Stable)/[ICRA] A4 | [ICRA]B+ / [ICRA] A4 |

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 Name | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---------|-----------------|-----------------------------|-------------|---------------|--------------------------|----------------------------------|
| - | Cash Credit | - | - | - | 65.00 | [ICRA]BBB- (Stable) |
| - | Non-fund Based | - | - | - | 5.00 | [ICRA]A3 |
| - | Unallocated | - | - | - | 5.00 | [ICRA]BBB- (Stable)/ [ICRA]A3 |

Source: MML

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