Daikin Airconditioning India Private Limited (Revised)

October 09, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating*	-	-	[ICRA]AA+; Outlook revised to 'Positive' from 'Stable'
Proposed Fund-based Bank Facilities	100.0	100.0	[ICRA]AA+; Outlook revised to 'Positive' from 'Stable'
Total	**100.0**	**100.0**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed its Issuer Rating of [ICRA]AA+ (pronounced ICRA double A plus) on Daikin Airconditioning India Private Limited (DAIPL). The outlook on the Issuer Rating has been revised to Positive from Stable. ICRA has also reaffirmed its long-term rating of [ICRA]AA+ on the Rs. 100.0-crore† proposed bank facilities of DAIPL‡. The outlook on the long-term rating is also revised to Positive from Stable.

Rationale

ICRA's ratings continue to draw comfort from DAIPL's strong parentage, and the high level of operational and financial linkages with its parent, Daikin Industries Limited (DIL;§ rated A3 with Positive outlook by Moody's). This ensures access to technology and technical expertise of the parent company, which has a diversified global footprint, with strong position in major markets.

The revision in outlook is driven by the positive demand prospects for the Indian room air-conditioning (RA) industry, given its limited level of penetration, which would be the growth driver for the company, in the near to medium term. ICRA has also taken note of DIL's focus on emerging markets such as India, Bangladesh, Nepal, Sri Lanka and Africa, which would further strengthen its commitment towards DAIPL, as the latter would also be catering to the African market. This would ensure long-term revenue visibility for DAIPL as the growth potential in African countries is also strong. ICRA has favourably factored in the company's state-of-the art manufacturing facility in Neemrana, Rajasthan with a capacity to produce 1.5 million units of RAs on an annual basis. Strong manufacturing base in India with increasing localisation would help to partially mitigate the impact of volatility in the foreign exchange rates and upward revision in the import duty on imported

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** With effect from Sep 1, 2017, ICRA has aligned the symbols and the definitions of ratings pertaining to the Issuer Rating Scale with that of the Long-Term Rating Scale. The change in the symbol is not to be construed as a change in the credit rating. Please refer to ICRA's website for more details*

† 100 lakh = 1 crore = 10 million

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

§ Daikin Industries Limited (DIL), a Japanese company and global leader in the air conditioning segment, has an outstanding rating of A3 from Moody's.

ACs. Furthermore, DAIPL is planning to set up a new facility in the other parts of India in the next five years, at an estimated capex of Rs. 700 crore, which would be funded entirely by internal cash accruals.

ICRA's ratings also factor in DAIPL's strong market position in the Indian AC market, with a strong brand and its reputation for high-end energy-efficient products such as inverters, ACs and variable refrigerant volumes (VRVs), supported by its assorted product profile. ICRA has also taken cognisance of the company's strong and expanding pan-India distribution network, and its ongoing efforts to penetrate new geographies for exports.

ICRA notes that the growth in sales volumes of various products along with consistent increase in the localisation and the company's focus on premium positioning, have supported its profitability in the past couple of years. DIAPL's improving profitability, combined with its unleveraged capital structure, has resulted in robust credit metrics.

The rating strengths are partially offset by the intense competition in the Indian AC market, volatility in volumes due to weather conditions and the vulnerability of the company's profitability to adverse movement in exchange rates. The hedging by DAIPL of about 80-90% of the foreign currency exposure through forward contracts reduces the forex risk to a large extent.

Going forward, in addition to the operating and financial performance of DAIPL, any rating action on the parent's credit rating will be a key rating sensitivity.

Outlook: Positive

The Positive outlook reflects ICRA's belief that DAIPL will continue to benefit from its strong parentage and the extensive experience of its management in the AC industry. The outlook may be revised to 'Stable' if the topline of the company declines along with reduction in profitability. Any change in the rating or outlook on DIL's ratings from Moody's, may also lead to a revision in the ratings of DAIPL.

Key rating drivers

Credit strengths

Strong parentage with 99.99% stake of Daikin Industries Limited (DIL, Japan) – DAIPL has strong relationship with DIL (its parent company), in terms of transfer of technology, knowhow, supply chain linkages as around 28% of material is supplied by DIL or its subsidiaries while the rest of the material is supplied by vendors. DIL also has a representation in the board of directors of DAIPL and also provides regular training to DAIPL's employees.

Strong market presence with healthy market share in the room air-conditioning industry in India – DAIPL has a sizable market share in the Indian room air-conditioning industry in FY2018. The company's topline growth has remained robust in the past couple of years. The company continues to remain the market leader in the VRV segment in FY2018, while it maintains sizable market share in the inverter Room ACs.

Wide spread dealer network throughout India and aggressive marketing efforts supporting the top-line growth – DAIPL has a sales and distribution network of over 6000 channel partners and 27 warehouses (including five mother warehouses). The company has over 600 service partners and over 400 Daikin Solution Plazas (exclusive showrooms of Daikin).

Favourable financial profile with unlevered capital structure, comfortable liquidity with efficient working capital management – The company's financial profile remained healthy with unlevered capital structure and comfortable liquidity. The company's healthy cash accruals are expected to keep the liquidity at comfortable levels in the near-medium term.

Capital expenditure plan for expansion of manufacturing capacity to 3.0 million units would help in reducing the import dependence to a large extent – DAIPL has planned a total capex of Rs. 700.00 crore over the next five years on doubling of its plant capacity to 3.0 million units RAs from 1.5 million units of RAs as at March 31, 2018. The increase of manufacturing base in India will help in reducing its import dependence and also prevent any impact of foreign currency volatility and increase in import duty (hike in import duty on imported ACs).

Favorable outlook for the AC industry in India given the low penetration – The increasing urbanisation and rising standard of living is fast making air-conditioners (AC) a requirement across India, the segment is still considered one of the least penetrated consumer durable segments, with about 5-7% penetration of the total market.

Credit challenges

Cyclical demand and dependence on other variables such as urban and rural electrification – The demand for room air-conditioners is also dependent on real estate activities, availability of electricity, and up-front cost of acquisition. All these factors could restrict the volumetric growth in the near to medium term.

Susceptibility to weather conditions – Sales volumes are also susceptible to weather conditions; inherent seasonality in the business due to intensity of summer.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.** ICRA has also considered the implicit support of, Daikin Industries Limited (DIL) (rated A3 with 'Positive' outlook by Moody's). ICRA has also considered the following rating methodologies.

Links to applicable criteria:

Impact of Parent or Group Support on an Issuer's Credit Rating
Corporate Credit Rating Methodology
Approach for Financial Ratio Analysis
Liquidity Analysis of Entities in the Non-Financial Sector

About the company

Daikin Airconditioning India Private Limited (DAIPL), a wholly-owned subsidiary of Daikin Industries Limited, is involved in manufacturing and selling room air-conditioners, variable refrigerant volumes (VRVs), and chillers under the 'Daikin' brand. DAIPL was incorporated in April 2000 as a joint venture (JV) between DIL and the SIEL Limited, with DIL holding an 80% stake in the JV. Later, DIL acquired a 100% stake in the company and it became a wholly-owned subsidiary of DIL. Initially, DAIPL serviced the Indian market through imports from Daikin's facilities in Japan, Thailand and Malaysia. In 2009, the company commenced production at its manufacturing unit at Neemrana, Rajasthan, with the production of chillers. Later, it also started manufacturing VRVs and HFC-32 refrigerant high wall split ACs and packaged ACs at its plant. The manufacturing plant is spread across 40 acres and has around 2,800 employees as at August'2018. Currently, the company has a sales and distribution network of over 6,000 dealers and 27 warehouses (including five mother warehouses). In addition, it has over 600 service partners and over 400 Daikin Solution Plazas (exclusive showrooms of Daikin). The company plans to double its manufacturing capacity in the next five years, with the new capacity scheduled to commence operations in a phased manner in next five years at other parts of India.

In FY2018, DAIPL reported a net profit of Rs. 150.3 crore on an operating income (OI) of Rs. 3194.3 crore compared with a net profit of Rs. 97.8 crore on an OI of Rs. 2840.4 crore in the previous year.

Key financial indicators

	FY2016 IndAS	FY2017 IndAS	FY2018 IndAS
Operating Income (Rs. crore)	2369.0	2840.4	3194.3
PAT (Rs. crore)	54.8	97.8	150.3
OPBDIT/OI (%)	4.5%	6.5%	8.8%
RoCE (%)	10.6%	19.3%	26.4%
Total Debt/TNW (times)	0.0	0.0	0.0
Total Debt/OPBDIT (times)	0.0	0.0	0.0
Interest Coverage (times)	4.8	4.9	5.9

(Source: DAIPL's annual report)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the Past 3 Years	
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating October-18	Date & Rating in FY2018 August-17	Date & Rating in FY2017 September-16
1	Issuer Rating	Long Term	-	-	[ICRA]AA+ (Positive)	Ir AA+ (Stable)	Ir AA+ (Stable)
2	Fund based-Proposed limit	Long Term	100.0	Nil	[ICRA]AA+ (Positive)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)

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
NA	Issuer Ratings	-	-	-	-	[ICRA]AA+ (Positive)
NA	Fund Based-Proposed	-	-	-	-	[ICRA]AA+ (Positive)

Source: ICRA

Corrigendum

Document dated October 9, 2018 has been corrected with revisions as detailed below:

- Revision on page number 2, under credit strength segment: The words "approved by DIL" after the sentence "DAIPL has strong relationship with DIL (its parent company), in terms of transfer of technology, knowhow, supply chain linkages as around 28% of material is supplied by DIL or its subsidiaries while the rest of the material is supplied by vendors" has been deleted. Some grammatical changes have also been made in the section.
- Revision on page number 3, under about the company section: The word "SIEL Limited" has replaced the word "Usha Shriram Group"

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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.

For more information, visit www.icra.in

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