

Sterling Automobiles Private Limited

April 01, 2019

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	3.10	3.10	[ICRA]BBB- (Stable); Reaffirmed
Inventory Funding	21.50	21.50	[ICRA]A3; Reaffirmed
Non-fund Based Limits	0.30	0.30	[ICRA]A3; Reaffirmed
Unallocated	0.10	0.10	[ICRA]BBB- (Stable)/A3; Reaffirmed
Total	25.00	25.00	

*Instrument details are provided in Annexure-1

Rationale

The ratings reaffirmation factors in the extensive experience of the promoters in the automobile dealership business, and the established presence and reputed brand name of Sterling Automobiles Private Limited (SAPL) as one of the authorised dealers for Honda Cars India Limited (HCIL) in Faridabad, operating a large showroom in a favourable location within the city. In addition to the operational benefits that these entail, the promoters and the other Group companies extended financial support to the company in the past in the form of interest-free unsecured loans, which supported its financial risk profile and credit metrics over the years. The ratings also draw comfort from the fact that the company is a part of the Sterling Group (the flagship company being Sterling Tools Limited; rated [ICRA]AA- (Stable)/A1+), which is present across multiple companies in the automotive space.

The ratings, however, continue to be constrained by the company's subdued operating performance in the recent past as reflected by the declining sales volumes. The car sales volumes declined 27% YoY in FY2018 and further by 22% YOY in 6M FY2019. Despite the revival in HCIL's overall domestic sales during the current fiscal, SAPL's revenues have continued to decline on account of the weak pickup in the Faridabad region. Nonetheless, ICRA expects the company to regain its growth momentum following the launch of Honda Civic in FY2019. Further, revenues from the sale of spares, accessories and service charges, which command higher margin, increased to ~21% in FY2018 from ~16.78% in FY2017 of the total revenue. This supported the company's profitability amid declining overall revenues. The ratings also factor in the thin margins and weak bargaining power in the automobile-dealership business, wherein the pricing policies are decided by the principal original equipment manufacturer (OEM). The ratings consider the intense competition in the passenger car market in India and the vulnerability of the company's profits to the inherent cyclicity of the passenger vehicle (PV) industry by virtue of its linkage to the macroeconomic environment. Further, with a single showroom in Faridabad, the company remains exposed to event risks specific to the geography.

Going forward, the acceptance of HCIL's models in the domestic market and the expansion of SAPL's geographic presence would be critical for its revenue growth and de-risking. Hence, these would remain the key rating sensitivities and would be monitored going forward. ICRA also notes that SAPL has extended a corporate guarantee for the working capital facilities of its subsidiary, Sterling Mobikes Private Limited (SMPL), which might result in a possible fund outflow from SAPL in case of SMPL's inability to meet its debt obligations. Hence, the performance of SMPL and the funding requirement from SAPL would also be monitored going forward.

Outlook: Stable

ICRA believes that SAPL's volume and revenue growth during FY2019 would likely remain weak considering the subdued demand trend in Faridabad, where its showroom is located. However, with new models launched by the OEM, there is expected to be some revival in volumes over the medium term. The outlook may be revised to Positive in case of expectations of significant improvement in operating performance, with addition of new outlets to expand geographic presence and offer sizeable revenue growth potential. The outlook may be revised to Negative if further sharp deterioration in sales volumes adversely impacts the company's financial performance.

Key rating drivers

Credit strengths

Key dealer in Faridabad for HCIL, well-established OEM in Indian PV market: SAPL is one of the authorised dealerships for HCIL in the Faridabad market, with a dominant market share in the region. HCIL is the fifth largest player in the domestic PV market, with a 5.2% share in FY2018 (5.4% in 11M FY2019).

Part of the Sterling Group of Companies; business interests in multiple companies in automotive sector: SAPL is owned and managed by the Agarwal family of the Sterling Group, which owns multiple companies in the automotive space, including other automotive dealerships. The flagship company of the Group is Sterling Tools Limited (rated [ICRA]AA-(Stable)/A1+), one of the leading players in the automotive fasteners space in India with a diverse client base.

Extensive track record of promoters in automobile dealership business: SAPL has been an authorised dealer of HCIL's PVs since 2005. The promoters and their relatives have extensive experience in the automobile dealership business. The promoter group operates multiple dealerships for PVs and two-wheelers across North India.

Increase in share of revenues from high-margin spares and service income: The revenues from the sale of spares, accessories and service charges, which command higher margin, increased to ~21% in FY2018 of the total revenue from ~16.78% in FY2017, backed by initiatives undertaken by the company to increase its efficiency. This supported the company's profitability amid declining overall revenues.

Credit challenges

Revenues remain dependent on acceptance of HCIL's models in domestic market; overall underperformance in comparison to principal: SAPL's performance remains closely linked to the performance of HCIL in the domestic market. The company's operating performance remained subdued in FY2018 and in the current year as reflected by declining sales volumes. Despite the revival of HCIL's overall domestic sales during the current fiscal, SAPL's revenues have continued to decline on account of weak pickup in the Faridabad region.

Thin profit margins owing to dealership nature of operations and intense competition from other automobile dealers: Inherent to the automobile-dealership business, with the commission structure decided by the principal, the profit margins have been thin for SAPL. In addition, intense competition in the Delhi/NCR region owing to the presence of major HCIL dealers and other OEMs exerts pressures on the sales volumes and margins of the company. Nonetheless, it has been able to manage its margins on the back of steady service income.

Exposure to adverse event risk specific to the area: The company operates a single integrated showroom in Faridabad, Haryana, which exposes it to regulatory risks and adverse event risk specific to the mentioned region. With high concentration of sales in the said region, any weakening of the region’s economy or any regulatory change is likely to have an adverse impact on SAPL’s revenues.

Modest financial risk profile: The financial risk profile of the company remains modest with gearing of 2.28 times and TOL/TNW of 2.87 times as on March 31, 2018. The coverage metrics also remained modest in the same year. Moreover, ICRA notes the corporate guarantee extended by SAPL to its subsidiary – Sterling Mobikes Private Limited (SMPL). SMPL reported weak financial performance as reflected by cash losses in FY2018. Though SMPL’s repayments in FY2018 were met through incremental unsecured loans from directors, any support from SAPL to fund the cash losses and debt servicing requirements of its subsidiary would be a key monitorable.

Liquidity position

SAPL’s liquidity position remains comfortable as reflected by positive free cash flows in the last two fiscals and healthy cash balance of Rs. 2.43 crore as on March 31, 2018. Its average working capital utilisation remained moderate at 48% of the sanctioned limits for the 10 months ended January 2019.

Analytical approach

	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Automotive Dealerships
Parent/Group Support	Not applicable
Consolidation / Standalone	Consolidated; For arriving at the ratings, ICRA has consolidated the financials of Sterling Mobikes Private Limited with SAPL (as mentioned in Annexure-2) given the close business, financial and managerial linkages among them.

About the company

Sterling Automobiles Private Limited (SAPL) owns and operates an automobile dealership under the brand Classic Honda. Incorporated in October 2005, the company is an authorised dealer of Honda Cars India Limited. The company operates a single integrated facility in Faridabad, with infrastructure to provide sales, service and spares (3S) to the customers. The showroom, spread over a total area of 12,856 square yards, is one of the largest Honda dealerships in India in terms of area. SAPL is a part of the Sterling Group of Companies, which operates multiple entities in the automotive space. The flagship company of the Group is Sterling Tools Limited, which is one the leading players in the automotive fasteners space in India with a diverse client base.

Key financial indicators (audited) – Standalone

	FY2017	FY2018
Operating Income (Rs. crore)	130.12	96.19
PAT (Rs. crore)	1.13	1.30
OPBDIT/OI (%)	2.82%	3.49%
RoCE (%)	10.74%	11.53%
Total Debt/TNW (times)	3.56	2.28
Total Debt/OPBDITA (times)	6.08	5.14
Interest Coverage (times)	2.14	2.19

Key financial indicators (audited) – Consolidated

	FY2017	FY2018
Operating Income (Rs. crore)	212.54	162.18
PAT (Rs. crore)	1.29	-2.81
OPBDIT/OI (%)	3.23%	1.18%
RoCE (%)	22.88%	1.28%
Total Debt/TNW (times)	4.75	6.36
Total Debt/OPBDITA (times)	5.97	19.24
Interest Coverage (times)	2.03	0.62

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 (FY2020)			Chronology of Rating History for the Past 3 years		
			Rated amount	Amount outstanding	Month-year & Rating	Month- year and Rating in		
			(Rs. crore)		April 2019	FY2019	FY2018	FY2017
					-	March 2018	December 2016	
1	Term Loan	Long Term	3.10	2.14	[ICRA]BBB-(Stable)	-	[ICRA]BBB-(Stable)	[ICRA]BBB-(Stable)
2	Inventory Funding	Short Term	21.50	-	[ICRA]A3	-	[ICRA]A3	[ICRA]A3
3	Non-fund Based Limits	Short term	0.30	-	[ICRA]A3	-	[ICRA]A3	[ICRA]A3
4	Unallocated	Long term/ Short Term	0.10	-	[ICRA]BBB-(Stable)/A3	-	[ICRA]BBB-(Stable)/A3	[ICRA]BBB-(Stable)/A3

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
-	Term Loan	June 15, 2015	Base Rate + 1.3%	FY2023	3.10	[ICRA]BBB- (Stable)
-	Inventory Funding	-	-	-	21.50	[ICRA]A3
-	Non-fund Based Limits	-	-	-	0.30	[ICRA]A3
-	Unallocated	-	-	-	0.10	[ICRA]BBB- (Stable)/A3

Source: SAPL

Annexure-2: List of entities considered for consolidated analysis:

Company name	Ownership	Consolidation approach
Sterling Mobikes Private Limited	Managerial control	Full consolidation

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