

December 05, 2019

## ADS Spirits Private Limited: Ratings upgraded

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term: Fund Based/Cash Credit	13.50	21.00	[ICRA]BBB+ (Stable); upgraded from [ICRA]BBB (Stable)
Long-term: Fund Based/Term Loan	25.00	4.03	[ICRA]BBB+ (Stable); upgraded from [ICRA]BBB (Stable)
Long-term: Unallocated	21.50	34.97	[ICRA]BBB+ (Stable); upgraded from [ICRA]BBB (Stable)
<b>Total</b>	<b>60.00</b>	<b>60.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The rating upgrade factors in the sustained improvement in ADS Spirits Private Limited's (ADS) operational performance and financial profile in FY2019. The company's net revenues grew by ~24% YoY to Rs. 391.9 crore in FY2019, aided by increased sales volumes on the back of diversification into new markets of the Indian-made foreign liquor (IMFL) segment. Moreover, the increased proportion of IMFL sales (in the overall revenue profile) supported margin improvement in FY2019. It also helped in efficient absorption of fixed overheads following an increase in the business scale. The upgrade also factors in the company's adequate liquidity position backed by sizeable accruals against repayments, and continued infusion of unsecured loans from promoters to support the business growth. Though the bank lines remain highly utilised, the incremental accruals will aid the growing working capital needs going forward. Despite the higher level of debt, the company's financial profile remained comfortable on the back of healthy profitability and steady accruals, as reflected by gearing of 0.92 times as on March 2019, interest coverage of 7.34 times, NCA/TD<sup>1</sup> of 39.56% and DSCR<sup>2</sup> of 5.26 times in FY2019. ICRA also notes that the demand outlook for the liquor industry remains favourable, driven by the demographic profile, changing lifestyles and improving disposable income that supports the company's growth prospects, as reflected in the healthy operating income (OI) growth over the past few years. The rating also draws comfort from the extensive experience of the promoters in the liquor industry, and their continued support to the company in the form of unsecured loans which kept the dependence on external borrowings low.

However, the ratings continue to be constrained by the high business risk inherent in the liquor industry owing to high taxes and stringent Government controls and regulations, and the lack of pricing power in the country liquor (CL) segment. ICRA also notes the intensely competitive IMFL segment due to the presence of some reputed and numerous regional players posing stiff competition, which limits the pricing power. Further, the company is exposed to raw material availability and pricing risk, which is heightened by the current uptick in ENA<sup>3</sup> prices, and the company's

<sup>1</sup> NCA/TD: Net Cash Accruals to Total Debt

<sup>2</sup> DSCR: Debt Service Coverage Ratio

<sup>3</sup> ENA: Extra Neutral Alcohol

increased reliance on purchase of ENA from outside. Though the company maintained its operating margins despite pressure in FY2019, its ability to do so on a consistent basis remains imperative. The ratings also factor in the concentration risks arising out of the company's high dependence on a single brand – Royal Green – for most of its sales, and limited presence in other product categories. ADS's ability to grow its OI and profitability in a regulated market would remain the key rating sensitivity. Any significant withdrawal of advances from its Group company resulting in an increase in debt levels will be a key monitorable. Any unforeseen regulatory change will also be a key rating sensitivity.

The Stable outlook on the [ICRA]BBB+ rating reflects ICRA's expectation that ADS will continue to benefit from the extensive experience of the promoters in the industry and favourable long-term volume outlook for the industry.

## Key rating drivers and their description

### Credit strengths

**Over two decades of experience of promoters in industry:** The promoters have been involved in the alcohol business for more than two decades. The promoters have an established presence in liquor retailing in Haryana, which provides access to retail outlets for selling the products under the company's brands, especially IMFL.

**Expansion in scale of operations with improvement in product mix:** With an increase in sales volumes following geographic diversification, ADS's OI and profitability have consistently improved. Further, over the last two years the company has increased its geographical footprint by entering into bottling agreements with distilleries in Jharkhand, Telangana, Odisha, etc. The company's revenues registered a healthy YoY growth of 24% to Rs. 391.9 crore in FY2019, while its operating profitability strengthened to 15.25% in the same fiscal. Healthy scale up of operations along with continued focus on the more margin accretive IMFL segment supported margin expansion in FY2019.

**Comfortable financial risk profile:** The company's capital structure remained satisfactory with improvement in the overall gearing levels (0.92 times as on March 31, 2019 vis-à-vis 1.05 as on March 31, 2018) due to steady accretion to reserves and continuous repayment of term debt. The coverage indicators were also comfortable as reflected by interest coverage of 7.34 times and DSCR of 5.26 times for FY2019.

**Favourable demand outlook:** India's liquor 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.

### Credit challenges

**Exposure of profitability margins to volatilities of raw material prices:** The company's margins remain dependent on price trends of major raw materials like grains and packing materials. The recent increase in the cost of key inputs is expected to keep the margins under check in FY2020. This apart, the product prices for a particular financial year are decided at the beginning of the year itself by the respective state government. Hence, the company's ability to pass on any raw material price increase during the year remains limited. Nonetheless, the company's continued focus on premium IMFL is expected to mitigate the impact to an extent.

**Intense competition and highly regulated nature of industry:** ADS' revenues will continue to be impacted by increasing competition in the domestic IMFL market from global players as well as regional players. In addition, ADS 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 the industry's growth.

**High working capital requirements:** In line with the increase in scale of business, the working capital requirements of the company have increased. It has been fully utilising its working capital limits. Also, the company has funded its working capital requirement through customer advances, primarily from the promoter group company as well as unsecured loans from promoters. Any major deviation in working capital parameters may lead to a tight liquidity position.

### Liquidity position: Adequate

The company's liquidity is adequate with positive fund flow from operations and a modest working capital cycle. The company does not have any additional capex plans, which along with modest repayment obligations in the medium term, is expected to support its liquidity position. However, with an increase in scale of business and distribution network, the company's working capital funding requirements are likely to increase. This in turn which could result in some reliance on external debt. The company's ability to avail timely limit enhancement commensurate to its scale of business remains imperative.

### Rating sensitivities

**Positive triggers:** ICRA could upgrade the rating if the company demonstrates a sustained improvement in revenues and profitability, which leads to an improvement in credit metrics. An improved working capital cycle, leading to a better financial risk profile, could also trigger a rating upgrade. In addition, significant reduction in outside liabilities resulting in TOL/TNW below 1.50 times on a sustained basis could support an upward change in rating.

**Negative triggers:** Further increase in working capital intensity, leading to significant reliance on external debt and material deterioration of debt protection metrics could lead to a ratings downgrade. Any weakening of its liquidity position or a decline in the current ratio below 1 times on a sustained basis could lead to downward revision in the rating. Over and above, any unforeseen and unfavourable regulatory change or a large, debt-funded capital expenditure or acquisition may also warrant a rating action.

### Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group Support	Not applicable
Consolidation/Standalone	Not applicable

### About the company

ADS Spirits Private Limited (ADS) was incorporated in 2010. The company operates a 60-kilo litre per day (KLPD) grain-based distillery in Jhajjar, Haryana for manufacturing ENA, which is the main ingredient for manufacturing CL and IMFL. The company commenced operations in March 2013. It also manufactures and bottles CL and IMFL (whisky and vodka), which are retailed under its own brands in Haryana. The plant has capabilities to manufacture distilled wet grain solvent

(DWGS) at its facility. In addition, the company has a 2.5-MW captive coal-based power plant, which in addition to meeting the entire power requirement of the manufacturing unit, supplies steam for the manufacturing process.

### Key financial indicators (audited):

	FY2018	FY2019
Operating Income (Rs. crore)	315.25	391.90
PAT (Rs. crore)	17.78	31.97
OPBDITA/OI (%)	13.54%	15.25%
RoCE (%)	34.98%	41.00%
Total Outside Liabilities/Tangible Net Worth (times)	3.00	2.40
Total Debt/OPBDIT (times)	1.63	1.51
Interest Coverage (times)	6.59	7.34
DSCR (times)	2.77	5.26

### Status of non-cooperation with previous CRA: Not applicable

### Any other information: None

### Rating history for past three years

SNo	Name of Instrument	Type	Current Rating (FY2020)			Chronology of Rating History for the Past 3 years		
			Rated amount (Rs. crore)	Amount outstanding	Month-year & Rating December 5, 2019	Month- year and Rating in		
						FY2019	FY2018	FY2017
					October 29, 2018	September 28, 2017	September 5, 2016	
1	Cash Credit	Long Term	21.00	-	[ICRA]BBB+ (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)
2	Term Loan	Long Term	4.03	4.03	[ICRA]BBB+ (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)
3	Unallocated	Long Term	34.97	-	[ICRA]BBB+ (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)

Amount in Rs. Crore

### 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](http://www.icra.in)

### Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	Cash Credit	-	-	-	21.00	[ICRA]BBB+ (Stable)
-	Term Loan	FY2014	-	FY2022	4.03	[ICRA]BBB+ (Stable)
	Unallocated	-	-	-	34.97	[ICRA]BBB+ (Stable)

Source: ADS

### Annexure-2: List of entities considered for consolidated analysis: Not applicable

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