March 05, 2020

# Skoda Auto Volkswagen India Private Limited: Ratings reaffirmed; rate amount enhanced

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Fund-based/Non-fund Based Facilities | 1,533.00 | 2,607.00 | [ICRA]AA+(Stable)/[ICRA]A1+; for existing amount and assigned to enhanced portion |
| Commercial Paper | 500.00 | 500.00 | [ICRA]A1+; reaffirmed |
| **Total** | **2,033.00** | **3,107.00** | |

**Instrument details are provided in Annexure-1*

## Rationale

The ratings reflect the strong operational and financial support from Volkswagen AG (VW AG, rated A3/Stable/P-2 by Moody's) and other group entities[1] to Skoda Auto Volkswagen India Private Limited (SAVIPL/ the company)—underscoring the importance the parent entity places on the company to develop its Indian operations as manufacturing hub of small and mid-sized cars. Being a wholly-owned subsidiary, SAVIPL has access to the technology and product portfolio of the VW Group, the world's largest passenger car manufacturer by volume (in CY2019). Over the years, VW Group has provided financial support to the Indian operations in the form of equity infusion, unsecured loans and extended credit period, which has supported the liquidity and profitability of the Indian operations. The ratings also favourably factor in the company's strong liquidity profile in the form of sizeable cash surplus, to the tune of Rs 2,000 crore, and the undrawn fund-based approved bank lines of over Rs 4000 crore.

The strength of the ratings is partially offset by SAVIPL's marginal market share in the domestic passenger vehicle (PV) market, the intense competition from incumbents, the thin dealership and service network and the modest product portfolio (especially in the compact/small car segment, which constitute the major share of the overall Indian PV market). ICRA also notes the low local content exposes the company to foreign exchange movement. However, the Group's plans to significantly increase local content and sizeable exports (which acts as natural hedge) allays this concern to an extent.

ICRA takes a note of VW Group's 2.0 strategy announced for the Indian market, wherein the Group will invest EUR 751 million in India over the next three to four years. The investments will be funded through a mix of existing cash surplus, internal accruals and financial support from the promoter group**.** Investment is expected to be deployed towards the launch of four new models on the MQB platform to increase the localisation level, which will help the Group to competitively price the upcoming products. VW Group's strong financial status should help SAVIPL to raise debt at competitive interest rates.

[1] Volkswagen AG and its other subsidiaries/group entities are together referred as VW Group

## Key rating drivers

### Credit strengths

**Strong operational, managerial and financial support from VW Group** - The VW-India[2] entities are the ultimate wholly-owned subsidiaries of VW AG. The VW Group has regularly supported them, both operationally and financially, by equity infusion and/or extended credit period for components supplied by VW Group's other units. ICRA notes that the financial support from the VW Group has supported the company's liquidity position, despite sizeable losses in the initial years of operations. VW Group has announced its India 2.0 strategy for India, wherein the Group will invest EUR 751 million in India over the next three to four years. The investments will be funded through a mix of existing cash surplus, internal accruals and financial support from the promoter group**.**

**VW-India can leverage on superior technological capabilities and wide product portfolio of parent entity i.e. Volkswagen AG** - Being wholly-owned subsidiaries, SAVIPL has access to the technology and product portfolio of the VW Group, the world's largest passenger car manufacturer by volume (in CY2019). However, owing to intense competition from incumbents in the Indian PV industry, SAVIPL was unable to create a meaningful presence in the Indian market. To optimally utilise the production capacity, SAVIPL has started using the Indian unit as the manufacturing hub for small cars and super-compact sedans. At present, exports constitute about 65% of SAVIPL's overall sales (by volume). It exports the Polo and Vento models from the Indian operations. The exports also help the company mitigate the impact of forex volatility, given the sizeable import content in the overall raw material mix.

**Strong liquidity position; regular financial support from VW Group has supported liquidity position of the company -** There is strong liquidity comfort available with the company in the form of undrawn committed and uncommitted banks lines of over Rs 4,000 crore as on January-2020. The company's working capital limit utilisation has been low with average fund-based utilisation of less than 10% over the last one year, thus providing enough room in case of any financial contingency. Moreover, the company's liquidity profile is supported by financial assistance from the VW Group and financial support from the Group companies in the form of extended credit period. In co-operation with the parent company, strategies are implemented to maintain sufficient liquidity. SAVIPL also maintains liquidity equivalent to three months external vendor payments in the form of cash, committed and uncommitted lines

### Credit challenges

**A late entrant in domestic PV market, which is dominated by entrenched players; marginal player in domestic PV market; Strong export growth helped company to mitigate impact of weak domestic sales in last few years**- VW-India is a late entrant in the domestic PV market (which is dominated by incumbents, like Maruti Suzuki India Limited (MSIL) and Hyundai Motors India Limited (HMIL). The overall market share remains marginal at 1.6% for the SAVIPL (VW + Skoda brand) in India.

**Limited product portfolio as compared to competitors; absence of offerings in high volume Mini, Super Compact and Compact Utility Vehicle (UV) segments -** The company's overall product portfolio in the mass-market segment remains limited because of its absence in high volume segments, like compact utility vehicle (UV) and super compact UV segments, in the Indian market. However, planned investment under India 2.0 strategy is expected to be deployed towards the launch of four new models on the MQB platform to increase the localisation level, which will help the Group to competitively price the upcoming products.

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[2] SAVIPL, Skoda Auto India Private Limited (SAIPL) and Volkswagen Group Sales India Private Limited (VGSIPL) are together referred as VW-India. In CY2019, SAIPL and VGSIPL were merged with SAVIPL.

**Thin sales and service network as compared to entrenched players; limited product portfolio in domestic mass market segment and low volume off-take affects profitability of dealers which might impact company's long-term growth prospects** - Despite being a strong brand, VW Group failed to gain any meaningful presence in the domestic PV market, owing to thin sales and service network. Low volume impacts viability of SAVIPL's dealerships, which constrain dealership expansion in semi-urban and rural pockets.

**Low level of localiation content limits pricing flexibility and exposes company's cost structure to foreign exchange volatility - I**ncreased share of imported components continues to impact cost competitiveness of the spare parts. The imported raw materials limit pricing flexibility and expose the company's cost structure to foreign exchange volatility. While the VW and Skoda brands failed to make any meaningful presence in the mass-market segment, the VW Group enjoys a healthy share in the luxury car segment due to healthy demand for the Audi vehicles.

## Liquidity: Strong

The assigned ratings also favourably factor in the company's strong liquidity profile in the form of sizeable cash surplus to the tune of Rs 2,000 crore and undrawn approved bank credit lines in the form committed and uncommitted bank lines of over Rs 4,000 crore. SAVIPL also maintains liquidity equivalent to three months of external vendor payments in the form of cash, committed and uncommitted lines. In co-operation with the parent company strategies are implemented to maintain sufficient liquidity in the company

## Rating sensitivities

**Positive triggers** – Improvement in the credit profile of Volkswagen AG along with improvement in business position of SAVIPL will be crucial for long-term rating improvement. Short-term rating is already at the highest level.

**Negative triggers** – Deterioration in credit profile of Volkswagen AG, substantial deterioration in operational and financial position of SAVIPL or weakening in linkage with the VW group.

## Analytical approach

| Analytical Approach | Comments |
|---|---|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology<br>Rating Methodology for Passenger Vehicle Manufacturers<br>Impact of Parent or Group Support on an Issuer's Credit Rating |
| Parent/Group Support | Parent/Group Company: Volkswagen AG (VW AG, rated A3/Stable by Moody's)<br>ICRA expects VW Group to be willing to extend financial support to SAVIPL, should there be a need, given the importance SAVIPL holds for VW Group for meeting its diversification objectives. SAVIPL and VW Group also share a common name, which in ICRA's opinion would persuade VW Group to provide financial support to SAVIPL to protect its reputation from the consequences of a Group entity's distress. |
| Consolidation/Standalone | For arriving at the ratings, ICRA has combined the financials of SAVIPL along with merged entities i.e. VGSIPL and SAIPL. |

## About the company

Headquartered in Pune, Maharashtra, the Volkswagen Group in India is represented by five brands - Skoda Auto, Volkswagen, Audi, Porsche and Lamborghini. The Indian operations began with the launch of Skoda Auto in 2001. Audi and Volkswagen entered in 2007, while Lamborghini and Porsche were introduced in 2012. SAVIL (erstwhile Volkswagen India Private Limited) has a manufacturing unit in Pune with capacity of 200,000 vehicles per year. The unit currently manufactures Polo, Vento and Ameo vehicles under VW brand and Rapid sedan under Skoda brand.

The group also had other entities i.e. SAIPL and VGSIPL, which are merged with SAVIPL and the merger became effective from October 05, 2019. SAVIPL (prior name SAIPL) has an assembling facility at Aurangabad (Maharashtra); it assembles Skoda brands (Octavia, Kodiaq and Superb), Volkswagen brands (Passat and Tiguan) and Audi brands (A4, A6, Q5, Q7). It has a capacity to produce 41,180 cars per annum. VGSIPL was the sales and marketing arm for the Volkswagen, Audi, Porsche and Lamborghini brands in India.

## Key financial indicators (audited)

| SAVIPL (formerly known as VIPL) (Standalone) | FY2018 | FY2019 |
|---|---|---|
| Operating Income (Rs. crore) | 8761.5 | 7053.0 |
| PAT (Rs. crore) | 120.1 | 198.1 |
| OPBDIT/OI | 9.3% | 9.2% |
| RoCE | 10.9% | 7.9% |
| | | |
| Total Debt/TNW (times) | 0.9 | 0.6 |
| Total Debt/OPBDIT (times) | 2.4 | 2.1 |
| Interest Coverage (times) | 5.1 | 5.1 |

*OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress)*

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

## Any other information: None

## Rating history for last three years

| | | Current Rating (FY2020) | | | | Chronology of Rating History for the Past 3 Years | | | | |
|---|---|---|---|---|---|---|---|---|---|---|
| | Instrument | Type | Amount Rated (Rs. crore) | Amount Outstanding* (Rs. crore) | Date & Rating 05-Mar 2020 | Date & Rating in FY2020 09 Dec 2019 | Date & Rating in FY2019 21 Dec 2018 | Date & Rating in FY2019 13 Apr 2018 | Date & Rating in FY2018 01 May 2017 | Date & Rating in FY2017 19 Jan 2016 |
| 1 | Fund-based/Non-fund Based Facilities | Long Term/ Short Term | 2,607.00 | 952.75 | [ICRA]AA+ (Stable) and [ICRA]A1+ | [ICRA]AA+ (Stable) and [ICRA]A1+ Outstanding | [ICRA]AA+ (Stable) and [ICRA]A1+ | [ICRA]AA+ (Stable) and [ICRA]A1+ | [ICRA]AA+ (Negative) and [ICRA]A1+ | [ICRA]AA+(Negative) and [ICRA]A1+ |
| 2. | Commercial Paper | | 500.00 | 150.00 | [ICRA]A1+ | [ICRA]A1+ assigned | - | - | - | - |

*Source: The company; *: Amount outstanding as on 03rd March 2020.*

## 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 |
|---|---|---|---|---|---|---|
| - | Fund-based/Non-fund Based Facilities | - | - | - | 2,607.00 | [ICRA]AA+(Stable)/[ICRA]A1+ |
| - | Commercial Paper | - | - | - | 500.00 | [ICRA]A1+ |

*Source: The company*

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

| Company Name | Ultimate Ownership** | Consolidation Approach |
|---|---|---|
| Skoda Auto Volkswagen India Private Limited | 100.00% | Full Consolidation |
| Volkswagen Group Sales India Private Limited | 100.00% | Full Consolidation |
| Skoda Auto India Private Limited | 100.00% | Full Consolidation |

***Ultimate ownership of VW AG; SAIPL and VGSIPL are merged with SAVIPL, and the merger became effective from October 05, 2019*

## ANALYST CONTACTS


**Subrata Ray**
+91 22 6114 3408
subrata@icraindia.com

**Ashish Modani**
+91 20 6606 9912
ashish.modani@icraindia.com

**Pavan Rajkumar Agrawal**
+91 20 6606 9916
pavan.agrawal@icraindia.com


## RELATIONSHIP CONTACT


**L Shivakumar**
+91 22 6114 3406
shivakumar@icraindia.com


## MEDIA AND PUBLIC RELATIONS CONTACT


**Ms. Naznin Prodhani**
Tel: +91 124 4545 860
communications@icraindia.com


## Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

## About ICRA Limited:

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## ICRA Limited


**Corporate Office**
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

**Registered Office**
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

**Branches**

| | |
|---|---|
| Mumbai | + (91 22) 24331046/53/62/74/86/87 |
| Chennai | + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294, |
| Kolkata | + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008, |
| Bangalore | + (91 80) 2559 7401/4049 |
| Ahmedabad | + (91 79) 2658 4924/5049/2008 |
| Hyderabad | + (91 40) 2373 5061/7251 |
| Pune | + (91 20) 2556 0194/ 6606 9999 |