

May 21, 2020

Skoda Auto Volkswagen India Private Limited: [ICRA]A1+ assigned to the enhanced Commercial Paper Programme

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based/Non-fund Based Facilities	2,607.00	2,607.00	[ICRA]AA+(Stable)/[ICRA]A1+; Outstanding
Commercial Paper	500.00	1,500.00	[ICRA]A1+ Assigned/ Outstanding
Total	3,107.00	4,107.00	

*Instrument details are provided in Annexure-1

Rationale

The ratings reflect the strong operational and financial support from Volkswagen AG¹ (VW AG) and other group entities² of 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 a 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, the VW Group has provided financial support to its Indian operations—through equity infusion, unsecured loans and extended credit period—which has supported the liquidity and profitability of its Indian arm. The ratings also favourably factor in the company's strong liquidity profile in the form of sizeable cash surplus of over Rs. 800 crore, and the undrawn fund-based approved bank lines (combining committed as well as uncommitted lines) of over Rs. 4,500 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 constitutes the major share of the overall Indian PV market). ICRA also notes that the low local content exposes the company to foreign exchange movement. However, SAVIPL's plans to significantly increase local content and sizeable exports (which acts as natural hedge) allays this concern to an extent.

ICRA currently has a Negative outlook for multiple automotive segments including PVs and commercial vehicles (CVs). The novel coronavirus pandemic and consequent nationwide lockdown has significantly impacted economic activity and disrupted the supply chain. ICRA expects volume declines across most automotive segments during FY2021, ranging from high single-digit to mid double-digit. These estimates, however, would be revisited over the next two to three months as greater clarity emerges. ICRA also notes various relief measures provided by the Government and the RBI, including loan moratorium, which would help buffer the impact on the economy to an extent. The situation is still evolving and ICRA will continue to monitor it closely over the next few quarters and take appropriate rating action, wherever required.

¹ Volkswagen AG is rated A3 (currently under review) by Moody's

² Volkswagen AG and its other subsidiaries/group entities are together referred to as the VW Group

Key rating drivers

Credit strengths

Strong operational, managerial and financial support from VW Group – VW India³ entities are the ultimate wholly-owned subsidiaries of VW AG. The VW Group has regularly supported them, both operationally and financially, through 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. The VW Group has announced its India 2.0 strategy, 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 its Indian unit as the manufacturing hub for small cars and super-compact sedans. In FY2020, exports constituted about 65% of SAVIPL's overall sales (by volume). It exports the Polo and Vento models from its 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 cash and liquid investments of over Rs. 800 crore, along with undrawn committed and uncommitted banks lines of over Rs. 4,500 crore as of March 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 an 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 1.5% for SAVIPL (VW + Skoda brand) in India during FY2020.

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 UV and super compact UV segments, in the Indian market. However, planned investment in its India 2.0 strategy is expected to be deployed to launch four new models on

³ SAVIPL, Skoda Auto India Private Limited (SAIPL) and Volkswagen Group Sales India Private Limited (VGS IPL) are together referred to as VW India. In CY2019, SAIPL and VGS IPL were merged with SAVIPL.

the MQB platform to increase the localisation level, which will help the Group to competitively price its upcoming products.

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, the VW Group failed to gain any meaningful presence in the domestic PV market, owing to its thin sales and service network. Low volume impacts the viability of SAVIPL's dealerships, which constrain dealership expansion in semi-urban and rural pockets.

Low level of localisation content limits pricing flexibility and exposes company's cost structure to foreign exchange volatility - Increased share of imported components continues to impact cost competitiveness of the company's 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 its Audi vehicles.

Liquidity: Strong

The assigned ratings favourably factor in the company's strong liquidity profile in the form of a sizeable cash surplus of over Rs. 800 crore and undrawn approved bank credit lines in the form committed and uncommitted bank lines of over Rs. 4,500 crore. In cooperation with the parent company, strategies are implemented to maintain sufficient liquidity in the company. SAVIPL's management shares that it will always maintain liquidity equivalent to three months of external vendor payments and debt obligations in the form of cash, committed and uncommitted lines.

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 Rating Methodology for Passenger Vehicle Manufacturers Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	Parent/Group Company: Volkswagen AG (VW AG, rated A3 (ratings under review) by Moody's) ICRA expects the VW Group to be willing to extend financial support to SAVIPL, should there be a need, given the importance that SAVIPL holds for the VW Group meeting its diversification objectives. SAVIPL and the VW Group also share a common name, which in ICRA's opinion would persuade the 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 the merged entities, VGS IPL and SA IPL.

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 of the VW brand, and the Rapid sedan from the Skoda brand.

The Group also had other entities, SA IPL and VGS IPL, which were merged with SAVIPL, the merger becoming effective from October 05, 2019. SAVIPL (erstwhile SA IPL) runs an assembling facility at Aurangabad (Maharashtra), where it assembles Skoda (Octavia, Kodiaq and Superb), Volkswagen (Passat and Tiguan) and Audi (A4, A6, Q5, Q7) brands. It has a capacity to produce 41,180 cars per annum. VGS IPL 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 (FY2021)			Chronology of Rating History for the Past 3 Years				
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding* (Rs. crore)	Date & Rating 21 May 2020	Date & Rating in FY2020 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
1	Fund-based/Non-fund Based Facilities	2,607.00	453.57	[ICRA]AA+ (Stable) and [ICRA]A1+	[ICRA]AA+ (Stable) and [ICRA]A1+	[ICRA]AA+ (Stable) and [ICRA]A1+	[ICRA]AA+ (Stable) and [ICRA]A1+	[ICRA]AA+ (Stable) and [ICRA]A1+	[ICRA]AA+(Negative) and [ICRA]A1+
2	Commercial Paper	1500.00	500.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-	-

Source: The company; *: Amount outstanding as on April 30, 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	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	-	-	-	1500.00	[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 VGS IPL are merged with SAVIPL, and the merger became effective from October 05, 2019

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