

January 07, 2020

## Mangalore Ganesh Beedi Works: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund Based - Cash Credit	60.00	60.00	[ICRA]A (Stable); reaffirmed
Short Term - Interchangeable	(0.10)	(0.10)	[ICRA]A1; reaffirmed
<b>Total</b>	<b>60.00</b>	<b>60.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of ratings continues to derive comfort from the firm's financial profile characterised by healthy return on capital employed (RoCE), low gearing and comfortable coverage indicators. The ratings factor in the extensive track record of the partners, established branded presence in South India with strong brand loyalty and wide distribution network of Mangalore Ganesh Beedi Works (MGBW).

However, the ratings are constrained by its high working capital intensity in FY2019 due to high inventory holdings. The ratings factor in the decline in margins owing to an increase in the minimum wage rates of the labourers and a rise in the prices of tendu leaves, one of the key raw materials required for manufacturing *beedi*. The ratings continue to be constrained by MGBW's presence in the highly regulated *beedi* manufacturing industry on the back of health-related concerns. The firm remains exposed to regulatory framework with regards to procurement of tendu leaves, sales and distribution of *beedi*, along with requisite packaging norms. The volumes for *beedi* sales have been declining, over the years, given restrictions on sales promotions, competition from other tobacco products and change in consumer smoking habits. Additionally, the periodic drawings by the promoters continue to limit growth in the firm's net worth.

### Key rating drivers and their description

#### Credit strengths

**Extensive experience of partners in industry** – The firm was incorporated in 1940 and has an extensive track record of operations. The partners have vast experience in handling the operations of the business. Further, the partners have a healthy net worth position and support the funding requirements of the business when required.

**Established brand and strong distribution network in South India** – MGBW is one of the major players in the fragmented *beedi* manufacturing industry and enjoys a strong brand presence in Karnataka, Tamil Nadu and Andhra Pradesh. The firm has been able to maintain its market position in these markets, despite competition from the unorganised *beedi* segment, other tobacco products and restrictions on sales promotions for tobacco products owing to its established distribution network.

**Favourable financial profile** – The firm's financial profile is characterised by a healthy RoCE of 29.71% in FY2019, although the same declined from the previous year. Moreover, it has a comfortable capital structure with a low gearing

of 0.56 times as on March 31, 2019 and comfortable coverage indicators with interest coverage of 3.50 times, Total Outside Liabilities/Tangible Net Worth of 1.31 times and DSCR of 2.60 times in FY2019.

## Credit challenges

**Business vulnerable to Government policies, regulations and growing health awareness** – Being a health hazard, like other tobacco products, the *beedi* industry remains tightly regulated in terms of advertising and tax structure. India's tobacco product manufacturers need to comply with pictorial warnings on packages, which have been potentially affecting volume growth for the industry. Further, the procurement of major raw material i.e. tendu leaves is regulated by the Government.

**Declining volumes coupled with decrease in margins in FY2019** – The firm was impacted by GST implementation as the effective tax rate increased to 28% from 5-6% earlier under the VAT regime. It was able to pass on the increased tax rates only partially to its customers by increasing the *beedi* rates, which impacted its realisation. The volume witnessed ~7% degrowth in FY2019 owing to higher prices, coupled with increasing awareness and anti-tobacco measures. Its profitability remains contingent upon the labour wages scenario and the price of its major raw material i.e. tendu leaves, which is a government-regulated item. The operating margins deteriorated to 13.74% in FY2019 from 23.00% in FY2018 with an increase in the price of tendu leaves, as well as rise in the minimum wages of the labourers.

**High working capital intensity** – The working capital intensity remained high at 35% in FY2019 owing to high inventory levels due to a sharp rise in the prices of tendu leaves, coupled with increased procurement. The yield of tendu leaves in the unit allocated to the firm in FY2018 auctions was higher than anticipated and it had to purchase the increased yield, as was mandated by the terms of the auction.

## Liquidity position: Adequate

The firm's liquidity profile is adequate with cash flow from operations of Rs. 35.75 crore in FY2019, buffer from undrawn working capital limits of 27.62 crore and cash and liquid investments of Rs. 18.24 crore as on March 31, 2019. In relation to these sources of cash, it has minimal outstanding long-term loans with scheduled repayments. It had outstanding short-term loans of Rs. 48.00 crore as on March 31, 2019, which was repaid in November 2019 funded by internal accruals as well as cash flow from reduction in working capital. Further, it has no major capital expenditure requirements in FY2020.

## Rating sensitivities

**Positive triggers** – ICRA could upgrade MGBW's rating if the firm is able to increase its scale of operations and profitability, while increasing its net worth base, supported by limited withdrawals by the partners. Sustained reduction in debt levels, aided by improvement in the working capital cycle, would also be the key for a rating upgrade.

**Negative triggers** – Negative pressure on the firm's rating could arise if there is higher-than-anticipated decline in the revenues or margins. Specific credit metrics that could lead to a downgrade of rating include interest coverage below 3.00 times. Further, substantial withdrawals by the partners, leading to negative retained cash flows may warrant a rating downgrade.

## Analytical approach

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

## About the company

MGBW was established in 1940 by Mr. Madhav Shenoy and Mr. B. Raghuram Prabhu at Bantwal village in South Canara district of Karnataka. At present, the firm is controlled by the Shenoy family with the three brothers – Mr. Jagannath Shenoi, Mr. M. Gopinath Shenoy and Mr. M. Ramanath Shenoy being equal partners. The firm is involved in manufacturing *beedis*, which are sold under the brand – 501 Ganesh Beedi and is one of the largest *beedi* players in the country. Its manufacturing facilities are located in South Canara and old Mysore regions (in Karnataka), Tirunelveli (in Tamil Nadu) and Karimnagar (Andhra Pradesh). Apart from these, it gets some part of the manufacturing done on a job-work basis from Kolkata to cater to North India. While the firm supplies across the country, its revenue is mainly driven from the southern states of Karnataka, Tamil Nadu and Andhra Pradesh.

## Key financial indicators (audited) - Standalone

	FY2018	FY2019
Operating Income (Rs. crore)	519.40	472.23
PAT (Rs. crore)	71.11	27.77
OPBDITA/OI (%)	23.00%	13.74%
RoCE (%)	79.20%	29.71%
Total Outside Liabilities/Tangible Net Worth (times)	1.48	1.31
Total Debt/OPBDITA (times)	1.08	1.43
Interest Coverage (times)	7.47	3.50
DSCR	5.55	2.60

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

**Any other information: None**

## Rating history for last three years

Instrument	Type	Current Rating (FY2020)		Rating 07-Jan 2020	Rating History for the past 3 years		
		Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)		FY2019 04-Dec-2018	FY2018 22-Jan-2018	FY2017 03-Mar-2017
1 Cash Credit	Long Term	60.00	-	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
2 Interchangeable - Bank Guarantee	Short Term	(0.10)	-	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+

*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 No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated(Rs. crore)	Current Rating and Outlook
NA	Cash Credit	-	-	-	60.00	[ICRA]A (Stable)
NA	Interchangeable - Bank Guarantee	-	-	-	(0.10)	[ICRA]A1

Source: Mangalore Ganesh Beedi Works

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