The Tobacco Trading Company
May 08, 2018

Rating

<table>
<thead>
<tr>
<th>Facilities</th>
<th>Amount (Rs. crore)</th>
<th>Rating</th>
<th>Rating Action</th>
</tr>
</thead>
<tbody>
<tr>
<td>Long-term Bank Facilities</td>
<td>12.00</td>
<td>CARE B+; Stable (Single B Plus; Outlook: Stable)</td>
<td>Assigned</td>
</tr>
<tr>
<td>Total</td>
<td>12.00</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

(Rupees Twelve crore only)

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The rating assigned to the bank facilities of The Tobacco Trading Company (TTTC) are tempered by small scale of operations and fluctuating total operating income, leveraged capital structure and weak debt coverage indicators, fluctuating profitability margins, working capital intensive nature of operations due to high inventory holding period, vulnerability to government regulations, climatic risks and partnership nature of constitution with inherent risk of withdrawal of capital. The rating, however, derives strength by long track record and experience of the partners for more than two decades in tobacco business, reputed clientele base, favorable location for operating tobacco business and stable outlook of tobacco industry.

Going forward, ability of the firm to increase its scale of operations and improve profitability margins and to manage working capital requirements efficiently would be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Weaknesses

Small scale of operations and fluctuating total operating income

The firm has a track record of twenty five years, however, the total operating income (TOI) of the firm remained low at Rs.16.40 crore in FY17 with a low net worth base of Rs.2.45 crore as on March 31, 2017 as compared to other peers in the industry.

The total operating income of the firm is seen fluctuating during the review period. The total operating income increased from Rs.14.97 crore in FY15 to Rs.19.67 crore in FY16 due to increase in sales volume at the back of repetitive orders from existing customers. However the total operating income declined to Rs.16.40 crore in FY17 due to decline in orders from the new customers.

Leveraged capital structure and weak debt coverage indicators

The capital structure of the firm marked by overall gearing stood leveraged during the review period. The overall gearing of the firm deteriorated from 3.72x as on March 31, 2015 to 5.13x as on March 31, 2017 due to increase in debt levels at the back of increase in utilization of working capital limits and availing unsecured loans from relatives.

The debt coverage indicators marked by interest coverage and TD/GCA remained weak during the review period. The PBILD interest coverage ratio has marginally deteriorated from 1.02x in FY16 to 1.01x in FY17 due increase in interest cost at the back of high utilization of working capital. The TD/GCA has deteriorated from 590.39x in FY 15 to 689.72x in

1Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications
FY17 due to due to increase in debt levels at the back of increase in utilization of working capital limits and availing unsecured loans from relatives.

**Fluctuating profitability margins**

Profitability margins of the firm are seen fluctuating during the review period. The PBILDT margin of the firm has declined from 6.96% in FY15 to 5.81% in FY16 due to increase in raw material cost at the back of presence of stocks which were purchased in FY15 at high cost. However the PBILDT margin increased to 8.64% in FY17 due to increase in selling prices of tobacco. The PAT margin of the firm is fluctuating during review period i.e., in the range of 0.08%-0.11% on account of increase in interest cost at back of increase in utilization of working capital bank facilities as the operations of the firm are working capital intensive owing to trading nature of business.

**Vulnerability of the tobacco business to government regulations and to climatic risks affecting tobacco availability**

Tobacco products form a major source of revenue in the form of taxes to both central as well as state government and hence there are regular modifications in taxation laws/tax rates with respect to the same. Due to the harmful nature of the product, the various state governments have banned Manufacture and sale of various tobacco products under the Food Safety and Standards (Prohibition and Restrictions on Sales) Regulations, 2011 and availability of tobacco is highly susceptible to the factors like area under cultivation, Climatic risk, crop yield. Hence, the profitability margins of the firm are vulnerable to government regulations on tobacco products and availability of tobacco.

**Working capital intensive nature of operations due to high inventory holding period**

The firm has working capital intensive nature of operations due to high inventory holding period. Owing to trading nature of business and availability of tobacco is seasonal in nature (susceptible to climatic risks), the firm has to buy the tobacco depending on availability. Due to market demand fluctuations, the firm holds the inventory till it gets better pricing. Hence the firm has elongated inventory holding period of 332 days in FY17.

As the firm is purchasing Virginia tobacco on auction platforms, the average creditor’s payment period is 1-7 days. The firm receives the payment from its customers within 1-15 days from the date of invoice. The operating cycle of the firm is stood at 329 days in FY17. Average working capital utilization of the firm during the last 12 months period ended 28th February 2018 is 95%.

**Constitution of the entity as a partnership firm with inherent risk of withdrawal of capital**

TTTC, being a partnership firm, is exposed to inherent risk of the partner’s capital being withdrawn at time of personal contingency and firm being dissolved upon the death/retirement/insolvency of the partners. Moreover, partnership firm business has restricted avenues to raise capital which could prove a hindrance to its growth.

**Key Rating Strengths**

**Long track record and experience of the partners for more than two decades in tobacco business**

The Tobacco Trading Company (TTTC) was established in 1992 as a partnership firm, initially by Mrs.G.Saraswathi, Mr.V.Lakshmi Narayana, Mr.G.Maheswara Rao, Mr.V.Malakondaiah, Mr.V.Hanumantha Rao and Mr.U.Navakrishna. Later the firm was reconstituted in the year 1997 and Mrs.G.Saraswathi, Mr.G.Vasu Babu and Mr.G.Jaya Prakash Narayan are the partners in the reconstituted firm. Mr.G.Vasu Babu is a graduate by qualification and has more than 20 years of experience in same line of business. Further, Mr.G.Jaya Prakash Narayan is a qualified graduate and has experience of more than 20 years in the same line of business. The above factors helped the firm in approaching tobacco boards for purchasing tobacco in auction platforms and to establish relationship with customers.

**Reputed Clientele base and favorable location for doing tobacco business**
The firm has reputed client base like ITC Limited (CRISIL AAA; Stable/ CRISIL A1+ reaffirmed on October 24, 2017), Alliance One Industries Private Limited, Premier Tobacco Packers who are into the business of selling cigarettes and exporting tobacco related products. The firm has ease of approaching the suppliers of tobacco as the firm is having its administrative office cum godown at Tangutur (Andhra Pradesh) which is located in the major tobacco growing area in Andhra Pradesh.

**Stable outlook of tobacco industry**

Cigarettes currently represent one of the most popular forms of tobacco, accounting for nearly 90% of the global tobacco sales value. The global cigarette market today represents a multi-billion dollar market and according to IMARC group, its total revenues reached values worth US$ 816 Billion in 2017, representing a CAGR of around 7% during 2009-2017. Despite falling volumes in developed markets as a result of an increasing awareness on the harmful effects of cigarette smoking, manufacturers have been able to increase value growth. Factors driving the cigarette market include a continuous increase in the prices of cigarettes and an increasing popularity of premium products. Another major factor driving the growth is the rising consumption of cigarettes in developing countries. Owing to the aforementioned reasons, the outlook for tobacco industry looks stable for the medium term.

**Analytical Approach:** Standalone

**Applicable Criteria**

- Criteria on assigning Outlook to Credit ratings
- CARE’s Policy on Default Recognition
- Financial ratios – Non-Financial Sector
- Rating Methodology - Wholesale Trading

**About the firm**

Andhra Pradesh based, The Tobacco Trading Company (TTTC) was established in 1992 as a partnership firm, by Mrs.G.Saraswathi, Mr.V.Lakshmi Narayana, Mr.G.Maheswara Rao, Mr.V.Malakondaiah, Mr.V.Hanumantha Rao and Mr.U.Navakrishna. Later the firm was reconstituted in the year 1997 and Mrs.G.Saraswathi, Mr.G.Vasu Babu and Mr.G.Jaya Prakash Narayan are the partners in the reconstituted firm. The Tobacco Trading Company (TTTC) is an authorized licensed dealer in tobacco registered with Tobacco Board for trading of Virginia tobacco. VTT is mainly engaged in trading of Virginia tobacco. The firm purchases the raw material i.e., Wet Virginia tobacco through the competitive bidding process conducted by Tobacco Board (TB) at Andhra Pradesh location. The TB collects the tobaccos from farmers, who are licensed holder to grow any particular tobacco. Further, these tobaccos are put in tender process. After successfully winning the tender, the firm processes the Virginia tobacco manually by separating the tobacco leaves, with the help of local contractual workers. After separation of tobacco leaves, the firm outsources the process like threshing. Threshing process involves conditioning of tobacco with heat and moisture, and finally re-drying the Virginia tobacco. The processing unit for separation of tobacco leaves is located at Tangutur which is 20 km away from Ongole, where tobacco is one of the major crops.

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<th>Brief Financials (Rs. crore)</th>
<th>FY16 (A)</th>
<th>FY17 (A)</th>
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<tbody>
<tr>
<td>Total operating income</td>
<td>19.67</td>
<td>16.40</td>
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<tr>
<td>PBILDT</td>
<td>1.14</td>
<td>1.42</td>
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<tr>
<td>PAT</td>
<td>0.02</td>
<td>0.02</td>
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<tr>
<td>Overall gearing (times)</td>
<td>4.14</td>
<td>5.13</td>
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<tr>
<td>Interest coverage (times)</td>
<td>1.01</td>
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A-Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not applicable

Rating History for last three years: Please refer Annexure-2

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.

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**For detailed Rationale Report and subscription information, please contact us at www.careratings.com

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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the company at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

Annexure-1: Details of Instruments/Facilities

<table>
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<tr>
<th>Name of the Instrument</th>
<th>Date of Issuance</th>
<th>Coupon Rate</th>
<th>Maturity Date</th>
<th>Size of the Issue (Rs. crore)</th>
<th>Rating assigned along with Rating Outlook</th>
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<td>-</td>
<td>12.00</td>
<td>CARE B+; Stable</td>
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Annexure-2: Rating History of last three years

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<thead>
<tr>
<th>Sr. No.</th>
<th>Name of the Instrument/Bank Facilities</th>
<th>Current Ratings</th>
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<tr>
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<td></td>
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<td>Amount Outstanding (Rs. crore)</td>
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<td>1.</td>
<td>Fund-based - LT-Cash Credit</td>
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## CONTACT

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