Lava International Limited

April 06, 2022

Ratings

Facilities/Instruments	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	250.00 (Enhanced from 189.50)	CARE BBB+; Stable (Triple B Plus; Outlook: Stable)	Revised from CARE BBB; Stable (Triple B; Outlook: Stable)
Short Term Bank Facilities	650.00 (Reduced from 710.50)	CARE A2 (A Two)	Revised from CARE A3+ (A Three Plus)
Total Bank Facilities	**900.00 (Rs. Nine Hundred Crore Only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Lava International Limited (Lava) factors in improved operational performance during 11MFY22 (refers to the period from April 1 to February 28), healthy order book position from government authorities, expanding global footprints through acquisition of a Panama based company to cater to Latin American market and addition of new customers with higher revenue visibility. The ratings also continue to derive strength from its experienced promoters and management team, comfortable financial risk profile, wide distribution network and streamlined business operations with established R&D team which help them adapt faster to changing technology. The ratings, however, are constrained by elongated operating cycle, continued reliance on third-party suppliers for its majority of raw material requirement, its exposure to foreign currency transactions and stiff competition in Indian mobile handset market.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Sustained improvement in scale of operations beyond Rs 3,000 crore with PBILDT margin above 6.50%
- Improvement in working capital cycle below 50 days.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Sustained decline in scale of operations with PBILDT margin below 5.00% and ROCE below 6%.
- Increase in working capital cycle beyond 150 days
- Elongation in the collection period and delay in the recovery from long outstanding debtors adversely impacting the overall liquidity.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters and management term

Lava is promoted by Mr. Hari Om Rai, Mr. Shailendra Nath Rai, Mr. Vishal Sehgal and Mr. Sunil Bhalla. Mr. Hari Om Rai, Chairman and the Managing Director (MD) of the company is co-chairing the task force for "Make in India" program of the Government of India. All the promoters are part of the Board of Directors of the company having background in engineering and management studies with wide experience in varied fields. The board is ably supported by a team of highly qualified and experienced professionals from telecom and consumer durable industry.

Wide distribution network and streamlined business operations

Lava has a well-established distribution model and support-service network consisting of 1,100+ distributors, who further distribute products to 1,10,000+ retailers and micro-distributors across India along with 20 carrying & forwarding agents providing sales and distribution support. It's after sales service network is spread all around the country with over 800 + professionally managed service centres focused on transparency and quality of service. Due to strong distribution channel, feedback about the models reaches to R&D team fast, helping them adapt to changing design and technology trend.

Improvement in scale of operations during FY22 along with improved profitability

During 9MFY22 (refers to the period from April 1 to December 31), the company has recorded total operating income (TOI) of Rs 1,459 crore with PBILDT margin of 4.80% and till Feb 2022, company has booked turnover of Rs 1880 crore with PBILDT margin of approx. 6%. The company has received orders worth Rs 926 crore from Gujarat and Uttar Pradesh state government, out which, company has executed approx. Rs 80 crore in FY22 and from January 2022, company has started supplying of feature phones to Motorola in their own brand under royalty arrangement due to which scale has improved.

The total operating income of the company declined by ~16% y-o-y from Rs. 1,942.92 crore in FY20 to Rs. 1,623.32 crore in FY21 on account of decline in sales volume of feature and smart phone segment. The continued intense competition from Chinese players also contributed to significant decline in the sales of the company and plummeting market share over the past few years.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Despite decline in turnover, PBILDT margin of the company improved from 5.08% in FY20 to 6.22% in FY21 owing to significant reduction in cost of material consumed and reduction in fixed overheads such as employee cost, resultantly, PAT margin of the company also improved from 1.28% in FY20 to 2.55% in FY21.
The company has recently acquired a Panama based Chinabird Centroamerica S.A. (CBCA) under share swap arrangement, engaged in supplying of mobile phones under the brand name of BMobile and Azumi to Tier1 mobile carriers and large retailers like Telcel, Claro, Telefonica, Tiga, Walmart, Digicel etc. The increase in the total operating income on the back of the acquisition aiding the company to expand its reach, order book of Rs 850 crore from government authorities, increase in existing business and sustainability of margins will remain a key monitorable as incremental sales will also give incentive of 4%-6% under Production Linked Incentive (PLI) scheme launched by Government of India.

Comfortable capital structure and debt coverage indicators
The financial risk profile of the company stood comfortable characterized by improved overall gearing and healthy debt coverage indicators. As on March 31, 2021, the overall gearing of the company stood at 0.25x (PY: 0.26x). The interest coverage ratio improved to 4.24x as on March 31, 2021 (PY:3.33x) on account reduction in interest expense. Further, the total debt to Gross cash accruals (GCA) ratio moderated and stood at 5.95x as on March 31, 2021 (PY: 5.43x) on account of lower scale of operations.

Key Rating Weaknesses
Elongated operating cycle
The operating cycle of the company elongated to 157 days as on March 31, 2021 (PY: 112 days) on account of debtors outstanding of more than six months amounting to Rs 664 crore (after adjusting provisions created) (PY: 551.22 crore) thereby leading to elongated average collection period of 181 days as on March 31, 2021 (PY: 146 days). These debtors comprise of multiple retailers under accessories segment which were impacted due to COVID-19 led disruptions. Though, in current year, company recovered approx. Rs 100 crore from these debtors, however, recoverability of the remaining amount remains a key monitorable. The company has to maintain the minimum levels of inventory to meet delivery schedules as it imports majority of its raw materials and thus the company needs to stock up the requisite inventory, therefore, the company has inventory days of around 2 to 2.5 months. Though, payable days of the company remained around 3 months as approx. 40% of the total creditors are backed by LC having usance of 90 days.

Reliance on third-party suppliers for its majority of raw material requirement
Lava is dependent on the third-party suppliers for its raw material requirements. As per the earlier business model of the company, it did not manufacture the products but only assemble the Semi Knocked Down units (SKDs) to produce Completely Built Units (CBUs). However, with recent developments in the manufacturing capacities of company, it has increased its focus on manufacturing handsets in India and to obtain raw material locally. Despite that, majority of sourcing is being made through third-party vendors located in China/Hong-Kong, which exposes the company to inherent risks of dependence on third parties and imports. Going forward, the reliance of the company on supplier for raw material is expected to reduce and shall remain a key monitorable.

Foreign exchange exposure
Lava is exposed to foreign exchange rate risk on account of import of SKDs from OEM partners based in China/Hong Kong. As a policy, the company maintains buffer (of 2%-3%) in prices for any adverse forex movement; further, based on the management's insights and market information, the company enters into hedging to cover part of its foreign exchange risk. Due to the currency fluctuations company reported loss on foreign exchange transactions of Rs. 5.70 crore during FY21 (PY: Gain of Rs. 2 crore). Furthermore, the company tends to pass-on the increase in cost by increasing the price of the handsets. But due to increased competition in the industry Lava remains exposed to risks related to foreign exchange fluctuations.

Changing trend in Indian mobile handset market
The Indian mobile handset industry is marked by high level of competition with the market being highly price sensitive and value driven. The industry is fragmented with a large number of both domestic and foreign players operating in the market, which has led to stiff price competition. The online channel sale contributed 55% in FY21. Further, as more players are setting up manufacturing units in India post growing Government of India support through various initiatives and schemes, the production is expected to rise and hence the exports. Given the nature of industry, LAVA continues to remain exposed to various ecosystem challenges that include increasing competition, volatile exchange rates, technology obsolesce risk, product failures, IP conflicts. The ability of LAVA to effectively manage these issues shall remain a key rating sensitivity.

Industry Outlook:
With rising per capita income level globally, demand for mobile phones has been increasing which is evident from the increased penetration of mobile phones across the different markets and also the growing subscription witnessed across mobile services and data. The low cost 4G network has not only increased the subscription base, but also the sale of smartphones and 4G enabled feature phones, which is evident from the domestic sales increasing in these last few years. According to F&S, India's mobile phone subscription market is projected to grow from 1,181 million subscriptions for the financial year 2021 to an estimated 1,369.1 million subscriptions for the financial year 2026 at a CAGR of 3.0%. The total global export market is estimated at USD 248 billion in 2020 and around 200 countries import mobile phones across the world4. India's export market with a contribution of USD 3.1 billion contributing to 1.26% of the total global market by value is next only to China and Vietnam. Globally, top five companies (Samsung, Apple, Huawei, Oppo and Vivo) account for nearly 80% of the total revenues

in 2020. All these companies are currently having presence in India with their assembly units, but the base of these companies is still in China and Vietnam, which is expected to shift to India in the years to come. With the help of various government initiatives and more companies setting up their manufacturing units, India is witnessing an enormous growth in the export market. UAE, Russia, South Africa, Turkey, Netherland and USA are the key export destinations. India has a potential to export around USD 100 billion value of mobile phones and USD 40 billion value of components by the year 2025**.**

Liquidity: Adequate
Lava's liquidity position has remained adequate as reflected by comfortable current ratio of 1.82x as on March 31, 2021. The company had free cash & bank balance of Rs. 57.83 crore as on March 31, 2021 (PY: Rs. 47.80 crore). The average working capital utilization of the company stood moderate at ~58% during the last 12 months trailing ending January, 2022. The operating cycle of the company elongated to 157 days as on March 31, 2021 (PY: 112 days) on account of higher collection period. The company has projected gross cash accruals of Rs. 103.88 crore against which it has a total debt repayment obligation of Rs. 11.96 crore in FY23. The company has envisaged capex of Rs 50 crore under PLI scheme for backward integration and expansion in its existing business in FY23 and FY24 which is projected to be funded in 70:30 debt-equity ratio. The company's healthy cash accruals and un-utilized working capital limits provides sufficient cushion against funds mismatches, if any, as well as any adverse market scenarios**.**

Analytical approach: Standalone

Applicable Criteria
Policy on default recognition
Financial Ratios – Non-financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Manufacturing Companies

About the Company
Incorporated in 2009, Lava is promoted by Mr Hari Om Rai, Mr Sunil Bhalla, Mr Shailendra Nath Rai and Mr Vishal Sehgal. The company is engaged into designing, manufacturing, assembling, trading and distribution of mobile handsets, tablets and accessories under the brands 'Lava' and 'Xolo'. The company has set-up assembling unit in Noida (Uttar Pradesh) with the total production capacity of around 48 million handsets per annum as on March 31, 2021. Lava also has 4 SMT lines with a capacity of around 9 million circuits per annum. It has a wholly-owned subsidiary Lava International (H.K.) Limited (Lava HK) based in Hong Kong through which the company exports mobile handsets to Bangladesh, Nepal, Thailand, Indonesia, Dubai Singapore etc. As per consolidated financials of FY21, company reported turnover of Rs 5519 crore in FY21 (PY: Rs 5280 crore) with PBILDT margin of 4.49% (PY: 3.74%).

Brief Financials (Rs. crore)	31-03-2020 (A)	31-03-2021 (A)	9MFY22(UA)
Total operating income	1,942.92	1,623.32	1459.00
PBILDT	98.63	100.93	70.02
PAT	24.81	41.44	28.33
Overall gearing (times)	0.26	0.25	NA
Interest coverage (times)	3.33	4.24	NA

A: Audited; UA: Unaudited
Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Non-fund-based-Short Term		-	-	-	650.00	CARE A2
Fund-based - LT-Cash Credit		-	-	-	165.00	CARE BBB+; Stable
Fund-based - LT-Term Loan		-	-	June 26	85.00	CARE BBB+; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Non-fund-based-Short Term	ST	650.00	CARE A2	-	1)CARE A3+ (25-Mar-21) 2)CARE A3+ (11-May-20)	-	1)CARE A2 (31-Dec-18)
2	Fund-based - LT-Cash Credit	LT	165.00	CARE BBB+; Stable	-	1)CARE BBB; Stable (25-Mar-21) 2)CARE BBB; Stable (11-May-20)	-	1)CARE BBB+; Stable (31-Dec-18)
3	Fund-based - LT-Term Loan	LT	85.00	CARE BBB+; Stable	-	1)CARE BBB; Stable (25-Mar-21) 2)CARE BBB; Stable (11-May-20)	-	1)CARE BBB+; Stable (31-Dec-18)

* Long Term / Short Term

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not Applicable

Annexure 4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Fund-based - LT-Cash Credit	Simple
2	Fund-based - LT-Term Loan	Simple
3	Non-fund-based-Short Term	Simple

Annexure 5: Bank Lender Details for this Company
To view the lender wise details of bank facilities please **click here**

Note on complexity levels of the rated instrument: CARE Ratings Ltd. has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About CARE Ratings Limited:
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With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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