Indigo Paints Private Limited

February 06, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long term Bank Facilities	20.04	**CARE BBB+; Stable (Triple B Plus; Outlook: Stable)**	**Revised from CARE BBB; Stable (Triple B; Outlook: Stable**
Long/Short-term bank facilities	20.00	**CARE BBB+; Stable/CARE A3+ (Triple B Plus; Outlook: Stable/A Three Plus)**	**Revised from CARE BBB; Stable/CARE A3+ (Triple B; Outlook: Stable/A Three Plus**
Total	**40.04 (Rs. Forty crore and Four lakh only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the long term ratings to the bank facilities of Indigo Paints Private Limited (IPPL) takes into account the volume driven growth in scale of operations and consequent improvement in profitability from better cost absorption during FY19 (refers to a period from April 1 to March 31) and 9MFY20 (refers to a period from April 1 to December 31).

The ratings also take note of the IPPL's comfortable capital structure and debt coverage indicator, along with its adequate liquidity position from sufficient cash and liquid investments and moderate utilization of bank lines.

The ratings further, continues to derive strength from its experienced and qualified promoters, improving track record with dealership network setup across major states and funding support in the form of compulsory convertible preference shares (CCPS) from its private equity investor.

CARE Ratings also takes a note of the synergies derived from acquisition of Hi-Build Coatings Private Limited (HBCPL) and the completed capital expenditure at IPPL's Jodhpur facility.

The rating strengths are however constrained by the moderate scale of operations and profitability as compared to established players and intense competition from them which limits the operational flexibility and pricing power of the company. Further, the ability of the company to continue investing in capacities, including backward integration and supply chain will be crucial for the overall financial risk profile.

Rating Sensitivities

Positive Factors

- The ability of the company to improve its operating profit with PBILDT margins in the range of 14% - 18% on a sustained basis
- Deriving envisaged benefits from completed capital expenditure
- Total Debt to Cash flow from operations below 1x on sustained basis

Negative Factors

- Lower than 11% - 12% PBILDT margin on sustained basis
- Weakening of interest coverage ratio below 12x - 13x on sustained basis
- Delay or postponement of IPO coinciding with debt funded capex, impacting the overall gearing ratio beyond 0.70x

Detailed description of the key rating drivers

Key Rating Strengths

Long established track record and experienced promoters

The company has a long track record of more than a decade in the paint industry. The company is spearheaded by Mr. Hemant Jalan, in the capacity of managing director (MD). Mr. Jalan is a chemical engineer from IIT Kanpur, MS in chemical engineering from Stanford University and MBA from Chicago University. Prior to starting IPPL, he was CEO of a large copper

[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

smelting project of the Vedanta Group. Mr. Jalan is involved in day-to-day operations of the company. The senior management is ably assisted with a second tier management which brings in high degree of operational expertise. The day-to-day operations of the company are managed by a team of qualified and experienced professionals. Further, Sequoia has 2 members on the board and is represented by Ms. Sakshi Chopra and Mr. Ravi Shankar Venkataraman Ganapathy Agraharam, both of who are well qualified and experienced.

Established distribution network across major states along with proximity to raw material sources

IPPL has a range of decorative paints including emulsions (regular exterior emulsions, regular interior emulsions), acrylic laminate, metallic emulsion, tile coat, bright ceiling coal, roof coat emulsion, floor coat emulsion, polymer putty, primers (WT Cement Primer, Exterior wall primer, Wood Primer, Red oxide Metal Primer), cement paints and distemper (acrylic distemper) amongst others. The sales in the decorative segment are mostly retail sales and are largely made through dealers. IPPL has an established supply chain strategically spread across 23 states and caters to requirements through 33 depots servicing 6844 regular dealers' as on March 31, 2019 vis-à-vis 5972 dealers as on March 31, 2018. Further, the company has strategically located manufacturing facilities at Jodhpur – Rajasthan (Decorative paints), Kochi (Kerala) and Pudukkottai (Tamil Nadu) with depots spread across North, North East, South, East, Central and Western part of India. The depots store inventory to the tune of 1-1.5 month to cater to the dealer demand.

Investment by private equity - Sequoia Capital India

IPPL has received investments amounting to Rs.140 crore from Sequoia Capital (SC) in three tranches in the form of CCPS'. The first tranche amounted to Rs.30 crore (FY15), second and third tranche was for Rs.20 crore and Rs.90.00 crore respectively, thereby strengthening the company's capital structure. The exit period to the Private Equity investor falls due between August, 2019 and August, 2020. The three viable exit options are, through an IPO, secondary sale or where IPPL would arrange a buyer for the equity securities held by SC. The company is expected to go public and has planned for an IPO in the near future providing an opportunity for SC to exit and funding capital expenditure going ahead. *Going forward, any change in the exit route of SC or delay in IPO coinciding with debt funded capex, both impacting the overall gearing ratio will remain crucial to the financial risk profile of the company.*

Growth in revenue and profitability

IPPL's constant efforts to improve its market share through aggressive brand building activities have resulted in substantial sales growth over the years. The company has been increasingly installing tinting machines at dealer locations which has further supported the volume growth. The total operating income (TOI) has seen a y-o-y growth of approximately 35% and stood at Rs.561.28 crore vis-à-vis. Rs.415.75 crore during FY18. Further, the PBILDT has seen a significant growth from Rs.24.25 crore in FY18 to Rs.53.36 crore in FY19. *Sustained improvement in topline and profitability, above industry average will be the key rating sensitivity.*

Comfortable capital structure and debt coverage indicators

The capital structure continued to remain comfortable with an overall gearing and debt equity ratio at 0.50x and 0.29x as on March 31, 2019 as against 0.30x and 0.11x as on March 31, 2018. During FY19, the company availed a term loan which was utilized towards construction of Jodhpur facility (completed in December 2020). The same has led to moderation in capital structure of the company. However, with improved scale and profitability the debt coverage indicators, viz Total Debt to GCA (TDGCA) stood at 1.22x during FY19 (PY: 1.83x) and improvement in profitability as led to an interest coverage of 13.69x during FY19 vis-à-vis 6.37x in FY18. *Further improvement in the debt coverage matrices is the key rating sensitivity.*

Key Rating Weaknesses

Modest scale and moderate profitability margins

IPPL registered a 367 bps improvement in its PBILDT margin during FY19 which stood at 9.51% vis-à-vis 5.83% in FY18. Consequently, the company reported a PAT margin of 3.80% during FY19 as against 0.62% during FY18. The growing scale of operations and improved realizations has enabled better cost absorption which in turn has favorably affected profitability. However, despite the growth in scale of operations remains modest. The same restrict IPPL's operational flexibility and limits the bargaining power with customers and suppliers. Further, the profitability margins remain moderate in comparison to industry averages. Advertisement and sale promotion expenditure is one of the major costs for the company and is expected to remain high. IPPL had been spending heavily on brand building and advertisements, which in the past had resulted in operating losses. The company has signed MS Dhoni (for three years 2018-2020) as their brand ambassador and is also the title sponsor for Pro Kabaddi Team (U-Mumba, for two years ending 2020). *The ability of the company to sustain its volume growth above the industry average, on the backdrop of competition from large established players will be crucial for the overall financial risk profile.*

Risk associated with volatility in raw material price

The key raw material of IPPL comprises of binders, fillers, different variants of cement etc. which is largely procured from domestic market. IPPL operates in an industry where the raw material cost is one of the major cost drivers and one of the major components to impact operating margin. Further, the raw materials like pigments, solvents, Tio2, and resins are derivatives of crude oil. The volatility in the crude oil prices also has a direct impact on the raw material cost. The ability of IPPL to manage inventory efficiently and be able to pass on the volatility in the prices of raw material to its customers, is critical for managing the profitability of the company.

Intense competition from organized and unorganized companies

IPPL manufactures products and operates in an industry which comprises of several large and established players along with many unorganized and local players operating in local states. The paint industry is characterized by low entry barriers and low level of product differentiation. However, setting up the distribution channel is a challenge to new entrants in the market. Thus, brand recall and advertisement is important to increase retail sales. The top five Indian paint manufacturers hold more than 60% of the market share. Therefore pricing, branding and distributorship network is the important for the company to garner customers. The ability of the company to continue investing in capacities and brand building will be critical to withstand competition from large established players.

Industry Outlook

In FY19, the paint industry has expanded at the rate of 12% in volume terms and about 15% in value terms. Going forward, the growth shall be dependent on a number of factors like disposable income in the hands of public, urbanisation, economic development, regular monsoons, raw material prices, growth in the infrastructure and recovery in the real estate & automobile segment. Consequently, CARE believes that the credit profile of paint companies which invest in innovation, R & D and manage their inventory & supply chain efficiently are likely to enjoy an edge over others.

The domestic paint industry is estimated to be a Rs.50,000 crore industry with the decorative paint category constituting almost 75% of this market. The domestic paint industry still continues to have a sizeable 30-35% share of unorganized players which primarily cater to the low end of the product basket.

Liquidity: Adequate

The liquidity of the company is adequate characterized by sufficient cushion in accruals vis-à-vis repayment obligations and moderate cash and liquid investments of Rs.26.85 crore as on March 31, 2019. The companies bank limits are utilized to the extent of 48% supported by above unity current ratio. Further, with comfortable gearing levels and negligible utilisation of bank lines, the issuer has sufficient gearing headroom, to meet its incremental working capital needs over the next one year.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
Criteria for Short Term Instruments
CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
Rating Methodology : Manufacturing Companies

About the Company

Indigo Paints Private Ltd (IPPL) is a company incorporated in the year 2000 with its registered office based out of Pune, Maharashtra and its manufacturing facilities are based out of Jodhpur, Rajasthan, Kochi in Kerala and Pudukkottai in Tamil Nadu. IPPL is engaged in manufacturing and sales of decorative paints including exterior emulsions, interior emulsions, acrylic laminate, metallic emulsion, tile coat, bright ceiling coal, roof coat emulsion, floor coat emulsion, polymer putty, primers (WT

Cement Primer, Exterior wall primer, Wood Primer, Red oxide Metal Primer), cement paints and distemper (acrylic distemper). The company sells the various products under the brand name “Indigo”. The company has a total installed capacity of 2,05,800 metric tons per annum (MTPA) ending FY19

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)	9MFY20 (UA)
Total operating income	415.76	561.29	471.42
PBILDT	24.25	53.36	47.33
PAT	2.57	21.35	16.32
Overall gearing (times)	0.30	0.50	0.44
Interest coverage (times)	1.90	7.50	8.33

A: Audited; UA: Unaudited

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

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT/ ST-Cash Credit	-	-	-	20.00	CARE BBB+; Stable / CARE A3+
Fund-based - LT-Term Loan	-	-	April 2024	20.04	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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT/ ST-Cash Credit	LT/ST	20.00	CARE BBB+; Stable / CARE A3+	-	1)CARE BBB; Stable / CARE A3+ (04-Jan-19)	1)CARE BBB-; Stable / CARE A3 (28-Feb-18) 2)CARE BBB-; Stable / CARE A3 (28-Apr-17)	1)CARE BBB- / CARE A3 (Under Credit Watch) (26-Apr-16)
2.	Fund-based - LT-Term Loan	LT	20.04	CARE BBB+; Stable	-	1)CARE BBB; Stable (04-Jan-19)	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities

Name of the Instrument	Detailed explanation
A. Financial covenants	
I Margins of Fund based limits	Margin of 25% on all inventory and book debts
Ii Unsecured loans from promotes/group entities	The company during the tenure of the bank loan to not, without prior permission from the bank - Undertake any further capex expect being funded by companies own resources - Repay any subordinated loans from the directors/promoter group - Invest in, extend any advance, loans, to any group company, associate, subsidiary, any other third party
iii. Other	- Minimum DSCR of 2x to me maintained at all times. - Current ratio >= 1.33x - Term debts/Net cash Accruals not to exceed 3x
	- Minimum networth of Rs.120.5 crore to be maintained - TOL/TNW <=1.5x - Net FA / Term debt >=1.2x
B. Non-financial covenants	
I Submission of Annual and Quarterly financial statements	Two copies of audited balance sheet to be submitted not later than 180 days from the close of a financial year
ii Submission of stock and debtors statement	Quarterly financial statements to be submitted 60 days from the date end of the quarter Annual financial statements - Provisional results within 90 days of financial year end - Audited results within 180 days of financial year end
iii Change in ownership/shareholding	Any change in shareholding or management control will be with prior consent from the banker

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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About CARE Ratings:

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