Radico Khaitan Limited

August 13, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating1	Rating Action
Long term Bank Facilities – Fund Based	568.57	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Removed from Credit Watch; Rating reaffirmed at CARE AA-; Stable (Double A Minus; Outlook: Stable)
Short term Bank Facilities – Non Fund Based	60.00	CARE A1+ (A One Plus)	Removed from Credit Watch; Rating reaffirmed at CARE A1+ (A One Plus)
Total Facilities	628.57 (Rs. Six hundred and twenty eight crore and fifty seven lakh only)		
Commercial Paper Issue^	100.00	CARE A1+ (A One Plus)	Removed from Credit Watch; Rating reaffirmed at CARE A1+ (A One Plus)

Details of instruments/facilities in Annexure-1
^ Carved out of working capital limits of the company

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities and CP instrument of Radico Khaitan Limited (RKL) have been removed from credit watch. The ratings were placed on watch as per press release dated March 01, 2019 following the announcement made by the company wherein they informed that the Central Pollution Control Board (CPCB) had made certain observations on Zero Liquid Discharge (ZLD) at their Rampur plant and directed for closure of operations. In May 2019, CPCB revoked the closure directions and provided clearance for the operations of grain based distillery, malt spirit plant & bottling plant. However, CPCB restricted the capacity of the molasses based distillery and directed RKL to comply with further directions post which RKL was to secure written permission from CPCB to restore its installed capacity. In early June, 2019 the CPCB team completed its inspection and CPCB vide its letter dated August 06, 2019 has allowed RKL to restore its manufacturing production of molasses based distillery as per consented capacity.

The ratings of Radico Khaitan Limited (RKL) takes into account the significant improvement in its financial risk profile characterized by enhanced profitability & strengthening of its capital structure and improved liquidity position. This was supported by healthy revenue growth during FY19 (refers to period from April 01 to March 31) on the back of RKL's gain in market share. The ratings also take into account RKL's strong nation-wide presence in the Indian Made Foreign Liquor (IMFL) segment, established brands along with consistent growth in scale of operations. The ratings also factors in the strong parentage, continued benefits of efficiency measures undertaken by the company & the softening of the raw material prices. CARE believes RKL will continue to benefit from its established brand equity and favourable long term volume outlook for the spirits industry combined with changing consumer preferences towards premium brands. The ratings however continue to remain constrained by cyclicality in raw material prices and the company's presence in a highly regulated industry which exposes it to changes in the state policies regarding pricing and sales of country liquor& IMFL.

Going ahead, the ability of the company to maintain its enhanced profitability margins and its comfortable capital structure amidst highly regulated industry environment shall be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Improved financial risk profile: During FY19, company registered net sales of Rs. 2118.31 crore registering growth of 17% over FY18 net sales of Rs. 1812.59 crore. The PBILDT margins improved from 16.32% in FY18 to 17.09% in FY19. The Company's profitability improvement was driven by a combination of higher sales from 'Prestige and above' segment, softening of raw material prices and the management team's ongoing cost optimization initiatives.

Finance cost during the year declined by 48% to Rs. 35.87 crore on account of repayment of borrowings. Therefore, PAT margins improved from 6.81% in FY18 to 8.88% in FY19.

The company has also adopted various cost optimization measures like rationalization of bottle supplies and diversification of supplier base to control costs. These measures along with the company's strategic focus on premium segments are further likely to lead to an improvement in the profitability margins going forward.

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

The overall gearing of the company significantly improved from 0.78x as on March 31, 2017 to at 0.53x as on March 31, 2018 & further to 0.26x as on March 31, 2019, on the back of repayment of term liabilities and increased net-worth. Better profitability during the period improved the PBILDT interest coverage to 10.09x in FY19 (compared to P.Y: 4.31x).

Experienced promoters & reputed name in the industry: RKL, promoted and managed by Khaitan family, has been in the business of liquor manufacturing since 1943 (by the name of Rampur Distillery). In 1998, RKL entered the branded liquor segment with launch of 8PM Whisky. Since then company has launched various successful brands and currently RKL is one of the leading players in the Indian Liquor industry. RKL has a distribution agreement with Suntory (Japan) and E.& J.Gallo Winery (USA) for marketing its premium brands in Indian Market.

Established brands with pan India Presence: RKL's portfolio currently includes four millionaire brands namely 8PM whisky, Contessa Rum, Old Admiral Brandy and Magic Moments Vodka. Apart from this it distributes other successful brands like Whytehall whisky and Brihans range of brands acquired inorganically. In June 2010, RKL launched new brands 'After Dark' and 'Eagles dare' whisky and in May 2012, launched Florence, a super-premium brandy, in the state of Tamil Nadu. In FY13, it launched super premium vodka, Verve along with its flavoured version on pan India basis. Continuing with its trend of launching newer brands, RKL launched a new readymade drink "Electra" during FY15 and three new brands in FY17 under the aegis of Pluton premium bay rum, Rampur single malt and Regal Talons Premium whisky.Recently, RKL launched Jaisalmer Indian Craft Gin, a product in the luxury segment. This brand is positioned in the fast-growing white spirits segment globally. Further in FY19 launched premium variant of 8PM whisky – 8PM Premium Black and a superior variant of Morpheus brandy – Morpheus Blue.

Strong hold in defence segment: RKL is one of the largest players in the defence market where its most famous brand is 'Contessa' rum. Two more brands 'After Dark Whisky' and 'Morpheus Brandy' have been approved to supply to Canteen Store Department (CSD). There are stringent conditions for entering into CSD segment leading to entry barriers for new players.

High Entry Barriers: Liquor policies governing its production and sale are entirely controlled by respective State governments. With all the alcohol consuming States/Union Territories having their own regulations and entry-exit restrictions, it is very difficult for new entrants to get licenses thus providing a competitive advantage to existing players. However, the States have been reasonably flexible in granting expansion of existing capacity to meet demands. This acts in favour of incumbents as new players find it difficult to start.

Spirits Industry in India: Positive Outlook: As per Euromonitor, IMFL volume is expected to reach 339 million cases in CY2022. During the CY2018-2022 period IMFL sales volume is expected to grow at a CAGR of 2.6%. During the same period IMFL industry value is expected to grow by 5.8% making a case for the ongoing premiumization trend. Overall vodka industry volume is expected to grow by 4.2% CAGR and value by 9.7% during the CY2018-2022 period. Radico Khaitan is extremely well positioned with the market leading share in this segment with its Magic Moments brand.
Growing disposable incomes, increasing rural consumption, greater acceptance of social drinking and a higher proportion of the young population entering the drinking age, are all factors that make India one of top markets for global spirit companies. These demographics also support the case for the growth of aspirational brands and premium products. Consumer needs and preferences are evolving and they are now more focused on quality, convenience, value proposition and personalization to suit their styles and values. India has a young demographic profile with a median age of 28 years and around 67% of the population is within the legal drinking age. These two indicators represent significant growth opportunities for the industry. The youth segment is expected to redefine consumption growth given their access and exposure to mobiles and the internet. This consumer group is more focused on the customer experience offered by a product, in particular its brand and design.

Key Rating Weaknesses
Highly regulated industry: Liquor industry is highly regulated in India with each state controlling the production, sales and duty structure independently. As a result, there are difficulties in transfer of production from one state to another along with huge burden of duties and taxes. The state controls the licenses for production, distributorship and retailing also.
Cyclicality in raw material prices: ENA (Extra Neutral Alcohol) forms a major component of the raw materials required for the Company's product portfolio and hence commodity price volatility remains one of the key considerations. ENA is produced from the byproduct molasses in the sugar manufacturing process or from grains. Lower than anticipated sugarcane production and/or any sharp rise in prices of molasses or ENA will have an impact on the Company's profitability. ENA prices may also increase due its alternative use in ethanol blending and a more attractive price offered by the petrochemical industry. However, the Company's capability to shift to a grain-based distillery insulates it against any significant increase in prices of molasses. The margins are highly susceptible to the volatility in the price of molasses and grains. Raw material prices are governed by various factors including the supply of molasses and grains which is in turn dependent upon production,

government regulations, demand from other sectors like biodiesel, etc. However, the company maintains a sizable inventory of molasses which insulates it against short and medium term fluctuations in molasses prices. The Company has a capacity to store 3 months' equivalent of its molasses requirements. Further, RKL has flexibility to shift its production between grains and molasses with change in prices of each.

Liquidity Analysis

Liquidity: Strong - RKL has a strong liquidity position with healthy cash accruals and moderate working capital cycle. The liquidity profile is further supported by the availability of sufficient bank limits for company's working capital requirements. The company continues to maintain a moderate working capital cycle of 60-70 days as it needs to maintain inventory at various warehouses and provide advances to bottlers to fund operations for its bottling units. For the company's own requirements along with the aforementioned loans, the company has available adequate working capital lines, which the company used at an average utilization level of 56% for 12 months ended April 2019. This provides sufficient liquidity buffer for the company's funds requirements. Additionally, RKL maintained a comfortable current ratio of 1.54 times as on March 31, 2019. Scheduled debt repayments for FY20 stand at Rs. 13.77 crore, as against gross cash accruals of Rs. 242.41 crore in FY19.

Analytical approach:
Standalone

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

About the Company
RKL is engaged in manufacturing of Rectified Spirit (RS), Extra Neutral Alcohol (ENA), Country Liquor and IMFL. The company has one of the largest distilleries in India at Rampur with molasses based distilling capacity of 75 million litres per annum and grain-based distillation capacity of 27 million litres per annum. The company also has tie-ups with 23 bottling units spread across the country in addition to its five own bottling units. In Maharashtra, RKL has tied up with its JV Radico NV (36% shareholding) for bottling operations. The company has three distilleries and one JV (Radico NV Distilleries Maharashtra – 36% stake – two distilleries) with total capacity of 157 million liters. RKL has developed its entire brand portfolio over the years. The Company launched ten new brands over the past decade. Of these new brands, nine brands are in the premium category. RKL currently has four millionaire brands in terms of number of cases sold in their portfolios which are 8PM Whisky, Contessa Rum, Old Admiral Brandy and Magic Moments Vodka.
Central Pollution Control Board (CPCB) had made certain observations on Zero Liquid Discharge (ZLD) at their Rampur plant and directed for closure of operations. In May 2019, CPCB revoked the closure directions and provided clearance for the operations of grain based distillery, malt spirit plant & bottling plant. However, CPCB restricted the capacity of the molasses based distillery and directed RKL to comply with further directions post which RKL was to secure written permission from CPCB to restore its installed capacity. In early June, 2019 the CPCB team completed its inspection and CPCB vide its letter dated August 06, 2019 has allowed RKL to restore its manufacturing production of molasses based distillery as per consented capacity.
In Q1FY20 RKL has reported a growth of about 22% in its total operating income to Rs. 626.90 crore (Q4FY19: Rs. 513.58 core) from the previous quarter. The PBILDT & PAT margins improved by 171 basis point & 114 basis points to 16.36% (Q4FY19: 14.65%) & 8.74% (Q4FY19: 7.60%) respectively. The interest coverage also improved to 13.91x (Q4FY19: 9.75x).

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	1812.59	2118.31
PBILDT	295.85	362.01
PAT	123.45	188.06
Overall gearing (times)	0.53	0.26
Interest coverage (times)	4.31	10.09

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

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
Non-fund-based-ST-BG/LC	-	-	-	60	CARE A1+
Fund-based-Long Term	-	-	-	475	CARE AA-
Term Loan –Long Term	-	-	Dec 2021	31.25	CARE AA-
Term Loan-Long Term (Proposed)	-	-	-	62.32	CARE AA-
Commercial Paper	-	-	7-364 days	100.00	CARE A1+

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.	Non-fund-based - ST-BG/LC	ST	60.00	CARE A1+	1)CARE A1+ (Under Credit watch with Developing Implications) (05-Jul-19)	1)CARE A1+ (Under Credit watch with Developing Implications) (01-Mar-19) 2)CARE A1+ (17-Sep-18) 3)CARE A1 (06-Apr-18)	-	1)CARE A1 (23-Jan-17)
2.	Fund-based-Long Term	LT	475.00	CARE AA-; Stable	1)CARE AA- (Under Credit watch with Developing Implications) (05-Jul-19)	1)CARE AA- (Under Credit watch with Developing Implications) (01-Mar-19) 2)CARE AA-; Stable (17-Sep-18) 3)CARE A; Stable (06-Apr-18)	-	1)CARE A; Stable (23-Jan-17)
3.	Term Loan-Long Term	LT	93.57	CARE AA-; Stable	1)CARE AA- (Under Credit watch with Developing Implications) (05-Jul-19)	1)CARE AA- (Under Credit watch with Developing Implications) (01-Mar-19) 2)CARE AA-; Stable	-	1)CARE A; Stable (23-Jan-17)

						(17-Sep-18) 3)CARE A; Stable (06-Apr-18)		
4.	Commercial Paper	ST	100.00	CARE A1+	1)CARE A1+ (Under Credit watch with Developing Implications) (05-Jul-19)	1)CARE A1+ (Under Credit watch with Developing Implications) (01-Mar-19) 2)CARE A1+ (25-Dec-18) 3)CARE A1+ (11-Sep-18) 4)CARE A1 (06-Apr-18)	-	1)CARE A1 (23-Jan-17)

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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