Vadilal Industries Limited

July 07, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	112.58	**CARE BBB-; Negative (Triple B Minus; Outlook: Negative)**	**Revised from CARE BBB (Triple B) & Removed from 'Credit watch with negative implications'**
Short-term Bank Facilities	16.72	**CARE A3 (A Three)**	**Revised from CARE A3+ (A Three Plus) & Removed from 'Credit watch with negative implications'**
Total Facilities	**129.30 (Rupees One Hundred Twenty Nine crore and Thirty lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE has removed the ratings assigned to the bank facilities of Vadilal Industries Limited (VIL) from 'Credit watch with negative implications' upon timely publication of its last three quarterly financial results and emergence of clarity on future leadership of the company with past disputes amongst the two main promoters of VIL being largely resolved with their re-appointment as Managing Directors of the company.

The revision in the ratings assigned to the bank facilities of VIL factors cash losses reported by VIL during Q4FY20 (FY refers to the period April 1 to March 31) and expected moderation in its overall financial risk profile during FY21 on the back of coinciding of Covid-19 pandemic induced lockdown with its peak sales season of Q1FY21.

The ratings of the bank facilities of VIL continue to derive strength from the vast experience of the promoters of VIL, its long-standing track record with established operations in ice-cream business, more than a century old presence of the 'Vadilal' brand in the domestic ice-cream market supported by its strong marketing and distribution network, growth in scale of operations backed by expansion of geographical reach both in domestic and export markets along with regular introduction of new flavours/variants in its product basket.

The above rating strengths are, however, tempered by the capital intensive nature of business resulting in relatively high leverage, susceptibility of profitability to volatile raw material prices, seasonality associated with the business and high competition in the ice-cream segment from the organized as well as unorganized segments.

CARE also takes note of the company availing the moratorium granted by its lenders as a Covid relief measure (as permitted by the Reserve Bank of India) for a period of six months from March 2020 to August 2020 for its debt obligations, including interest on working capital facilities.

Outlook: *Negative*

The 'Negative' outlook on the long-term rating of VIL reflects CARE's expectation of VIL incurring cash losses during FY21 amidst significant loss of revenue due to coincidence of Covid-19 induced lockdown with its peak sales season which may lead to pressure on its liquidity and higher reliance on external debt to fund the losses. The outlook may be revised to 'Stable' in case the company is able to turnaround its performance in the remaining part of FY21 and avail its targeted longer tenor debt to liquidate its ad-hoc working capital limits and thereby shore-up its liquidity.

Rating Sensitivities

Positive Factors

- Stabilization of its scale of operations at pre-COVID levels and subsequent growth through greater geographical diversification
- Timely availment of longer tenor debt and liquidation of existing inventory leading to reduction in short term borrowing and improvement in working capital situation; along with maintaining its overall gearing below unity on a sustained basis
- PBILDT margin above 14% on a sustained basis by managing volatility associated with raw material prices along with improvement in its debt coverage indicators
- Improvement in its current ratio beyond 1.20 times

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

Negative Factors

- Inordinate delay in availment of its targeted longer tenor debt of Rs.100 crore beyond the envisaged timeline of September 2020, thereby further impacting its liquidity
- Any materially negative outcome arising from the on-going independent investigation being conducted on the matters referred under the 'Basis for Disclaimer of Opinion' issued by its statutory auditors in their audit reports for the year-ended FY19 and FY20.
- PBILDT margin below 10% on a sustained basis.
- Any significant debt-funded capex which could result in weakening of its debt coverage indicators (deterioration of TD/GCA beyond 5x).

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters

VIL was promoted by Mr. Vadilal Gandhi who started ice-cream business in 1907. Currently, the operations of VIL are managed by the third and fourth-generations of the family i.e. Mr. Rajesh Gandhi, Managing Director, Mr. Devanshu Gandhi, Managing Director and Mr. Kalpit Gandhi, Director and CFO (Son of Mr. Rajesh Gandhi). While Mr. Rajesh Gandhi looks after the overall operations of the company, Mr. Devanshu Gandhi looks after the sales, marketing and distribution functions. Apart from the finance function, Mr. Kalpit Gandhi looks after the plant operations on day to day basis.

Long standing track record with an over century-old brand 'Vadilal'

The brand 'Vadilal' has been enjoying a well-known legacy for more than a century in the domestic ice-cream and frozen dessert business. The brand has healthy market share in the states like Gujarat, Rajasthan, UP and Haryana. The product portfolio of VIL's ice-cream and frozen dessert includes more than 150 flavors and varieties in different forms like cups, candies, cones, kulfis, tubs, large packs, etc. Apart from ice-cream and frozen dessert, VIL also ventured into processed food business under the brand 'Quick Treat'. Further, the revenue stream is also moderately diversified geographically as VIL earns nearly 70%-75% of its ice-cream revenue from the states of Gujarat, Rajasthan, Uttar Pradesh and Haryana; whereas balance comes from other states.

Strong marketing and distribution network

VIL [through Vadilal Enterprises Limited (VEL)] has marketing presence in 23 states of India with the support of 63 C&F agents, over 1,200 distributors, more than 55,000 retailers and 290 distribution vehicles. It also offers a wide range of ice-cream and frozen desserts through nearly 300 SKUs (Stock Keeping Units) in leading modern trade outlets like Reliance Fresh, More, Hyper City, D-Mart, Food Bazaar and Star Bazaar, etc. Furthermore, VIL mainly exports its processed food product, frozen dessert and ice-cream to 45 countries across four continents, the key markets include USA, South-East Asian and European countries. During FY19, VIL registered 30% y-o-y growth in export sales and as indicated by the management export sales have shown consistent growth in FY20 as well.

Volume backed consistent growth in scale of operations along with improvement in its profitability during FY19 and FY20

The total operating income (TOI) of VIL which registered a compounded annual growth rate (CAGR) of nearly 8% on a consolidated basis during last three years ended FY20, grew by 6% during FY20 (as per published results on stock exchange) on y-o-y basis alongwith marginal improvement in PBILDT margin by 25 bps on y-o-y basis to 14.51%. The growth in sales was supported by geographical expansion coupled with continuous introduction of new products/flavors and hike in retail prices of some of its products due to significant increase in procurement cost of its key raw material, skimmed milk powder (SMP).

Although, the ice-cream consumption was severely affected in Q1FY21 which is the peak sales season for ice-cream manufacturers, the same is expected to have increased on the back of gradual ramp up of businesses post lifting of lockdown and gradual shift of consumers towards branded ice-cream keeping in mind the safety concerns on the back of recent outbreak of Covid-19 pandemic.

Key Rating Weaknesses

Expected moderation in financial profile and liquidity on the back of significant disruption of business operations during the peak season of Q1FY21 due to outbreak of Covid-19 and subsequent lockdown

Sales and profitability of VIL remain skewed towards Q1 in each financial year due to summer season wherein maximum consumption of ice-cream takes place. During FY20, VIL had funded ~Rs.51 crore of its capex through internal accruals and accordingly, to meet its raw material sourcing requirement during Q3FY20, it had availed ad-hoc limit of ~Rs.54 crore which was envisaged to be repaid from the cash flows of its peak summer season in Q1FY21. However, upon Covid-19 induced lockdown, VIL incurred cash loss during Q4FY20 and has also lost large part of its peak season sales during Q1FY21 and is therefore expected to report cash losses in FY21; thereby impacting its liquidity. At the request of VIL, its

lenders have provided moratorium on servicing of its term loan & working capital limits (including ad-hoc limits) during March 2020 to August 2020, in line with the moratorium available under RBI's Covid-relief package.
VIL has requested its existing lenders to provide Rs.100 crore term loan to be repayable over a period of six years (including moratorium period of one year). This term loan would be essentially utilized to retire ad-hoc limit of ~Rs.54 crore and the balance would be used to meet its expected cash losses during the year, working capital and debt servicing requirements post August 2020. Timely availability of these term loans would be one of the critical rating monitorables.

Relatively high leverage due to high capital intensity of the business
Ice-cream manufacturing and distribution industry is capital intensive in nature requiring regular investment in production facilities, innovative products in terms of flavours and packaging, as well as marketing assets like cold storage chain, deep freezers, refrigeration equipped delivery vehicles, push card, etc. During the four years ended FY19, VIL on consolidated basis had incurred capital expenditure of around Rs.103 crore which was funded through term debt of Rs.81 crore and balance through internal accruals. During FY20 also VIL incurred total capex of ~Rs.51 crore largely funded by its internal accruals which stood higher than its earlier estimates. Also, the inherent seasonality associated with the ice-cream business whereby its main raw material (SMP) is largely available during the winter months leads to high working capital utilization as on balance sheet dates. Consequently, despite improvement, the leverage of the company has continued to remain relatively high marked by an overall gearing of 1.18 times as on March 31, 2019 (1.54 times as on March 31, 2018). Also, with a stretch in its creditors due to subdued performance in Q4FY20, VIL's TOL/TNW is expected to have deteriorated as on March 31, 2020.
In order to expand its footprints in Northern and Eastern regions of India, VIL earlier had plans to establish new production facility in East India. Along with that the company also had plans to establish cold storage facilities near its Bareilly plant in Uttar Pradesh. The envisaged cost for these two projects was around Rs.70 crore which the company was planning to fund through term loan of Rs.49 crore and remaining through internal accruals. The execution of these two projects was previously expected to be spread over FY19 and FY20. However, as articulated by the company management, the said capex plans have now been deferred by the company.

Susceptibility of profitability to volatile raw material prices such as Skimmed Milk Powder (SMP) due to its linkages with international markets
The major raw materials for manufacturing of ice-cream are SMP, milk, cream and nuts, which VIL procures from local dairies near its manufacturing units. It also procures palm oil for manufacturing frozen dessert. The prices of key raw materials have increased gradually over the years given the rising demand and constrained supply scenario. Also, each financial year during the period from November to January, the raw material prices are at their lowest due to dynamics of dairy industry; albeit during FY20 the raw material prices (mainly SMP) during the same period stood high on the back lower supply of milk in the industry which has resulted in higher cost of its raw material despite some savings from dip in prices of nuts and palm oil. The higher cost of raw material combined with loss of sales due to Covid-19 impacted its profitability during Q4FY20 and the same is likely to recur during Q1FY21.
Further, during FY19, VIL also earned nearly 17% of net sales from export whereas the company has no imports on the other side. Hence, VIL is exposed to adverse fluctuation in foreign currency exchange rates. However, the company generally enters into forward cover to mitigate the forex risk to some extent.

Seasonality of demand as well as challenges arising from changing consumer tastes and preferences
The sales of VIL are normally concentrated over the summer months, reflecting the seasonality of the business. Hence, the working capital intensity is at its peak level in the last quarter of the financial year as it has to accumulate raw material inventory for meeting the demand for ice cream in the upcoming summer season. The business is also susceptible to changing tastes of consumers requiring investment in fixed assets leading to highly capital intensive operations.

High competition in the ice-cream segment from the organized as well as un-organized markets
Indian ice-cream market is largely dominated by un-organized players with innumerable small and seasonal companies doing the business in various regions. Further, there are large number of big and medium-sized ice-cream companies in India which leads to a highly competitive environment. Although, there is a huge opportunity for industry players since India is one of the fastest growing markets for ice-cream consumption due to its large population and growing per capita income; however, VIL faces high competition from various other established brands like Amul, Havmor, Kwality Walls, Cream Bell, Mother Dairy, Top 'N' Town, Dinshaw's, etc in its various key markets. In addition, Vadilal faces competition from unorganized ice-cream manufactures at local level.

Pending outcome of investigation on certain matters which has formed the basis for issuing of Disclaimer of opinion by its statutory auditors in their audit reports for FY19 and FY20
On account of various disputes between two brothers of the promoter group who were also on the Board of VIL, at various points in time during FY20 some of the independent directors of VIL had resigned from the Board citing hostile

atmosphere in the board meetings which was followed by resignation of the company's statutory auditor along with issuance of disclaimer on their opinion on the accounts for FY19. However, post that, the promoter directors have withdrawn their major counter claims against each other and the quarterly results of the company are also getting published within timelines for the last three quarters. Further, both promoter brothers are re-appointed as Managing Directors of VIL. Also, an external law firm & CA firm are appointed to verify the left out claims of the promoters whose reports are delayed due to Covid-19. Further new statutory auditor of the company for FY20 has also issued disclaimer of opinion in the audit report of FY20 pending outcome of the investigation.

Liquidity: ***Stretched***
VIL's liquidity stood stretched marked by almost full utilisation of its working capital limits and additional availment of ~Rs.54 crore of ad-hoc working capital limits to fund its raw material sourcing requirement. Total working capital borrowing of VIL increased from Rs.65.64 crore as on March 31, 2019 to Rs.105.54 crore as on March 31, 2020. Upon funding the majority of its capex during FY20 from its internal accruals and simultaneous availment of ad-hoc working capital borrowings along with stretch of its trade creditors, VIL's current ratio stood at 0.98 times as on March 31, 2020. The ad-hoc limits were originally scheduled to be squared up during Q1FY21; however due to Covid-19 induced lockdown, VIL could not retire the same and has availed moratorium on their repayment till August 2020 which has been allowed by its lenders. Post expiry of the bank approved loan moratorium, VIL would be required to repay these ad-hoc limits. Consequently, VIL has approached its lenders for sanction of additional term loans partly towards reimbursement against the large capex already incurred by it from its internal accruals during FY20 as well as for meeting its expected cash loss during FY21 which has arisen from the significant washout of its peak season (i.e. Q1FY21) sales due to the Covid-19 pandemic. Term loan of Rs.16 crore is already sanctioned by a bank; albeit its disbursement is pending. The company also expects to build-up some liquidity through gradual liquidation of its large inventory as of end-FY20 with signs of pick-up in sales with gradual lifting of the lockdown.

Analytical approach: Consolidated
CARE has considered the consolidated financials of VIL for its rating approach due to its strong managerial and operational linkages with its subsidiaries as they are either the marketing arms for the products manufactured by VIL in various geographies outside India or in related diversification. List of entities getting consolidated in VIL is placed at

Annexure-3.

Applicable Criteria:
[Criteria on assigning Outlook and Credit Watch to Credit Ratings]
[Criteria for Short Term Instruments]
[CARE's Policy on Default Recognition]
[CARE's methodology for manufacturing companies]
[Liquidity Analysis of Non-financial sector]
[Financial ratios – Non-Financial Sector]
[Rating Methodology: Consolidation and Factoring Linkages in Ratings]

About the Company
Ahmedabad-based Vadilal Industries Limited (VIL), which was incorporated in 1982, is engaged in manufacturing and distribution of ice-cream under the brand "Vadilal". The brand is named after Mr. Vadilal Gandhi who started ice-cream business in 1907. VIL has two manufacturing facilities for ice-cream, with combined capacity of 350,000 liters per day at Pundhra in Gujarat and Bareilly in Uttar Pradesh as on March 31, 2020. VIL also diversified into the processed food segment in 1991 and has one manufacturing facility for processed food with capacity of 46,200 MTPA at Dharampur in Gujarat. The product portfolio of VIL's ice-cream and frozen dessert includes more than 150 flavors and varieties in different forms like cups, candies, cones, kulfis, tubs, large packs, etc. Apart from ice-cream and frozen dessert, VIL also ventured into processed food business under the brand 'Quick Treat' and product portfolio includes frozen vegetables, ready-to-eat frozen snacks, Indian bread and curries, paneer and flavored milk. On a standalone basis, during FY19, VIL earned around 90% of gross sales from sale of Ice-cream and remaining 10% from processed food segment. Processed foods are mainly exported (nearly 75%).
Furthermore, VIL has also started export of ice-cream mainly to USA through its wholly owned subsidiary, Vadial Industries (Inc), USA and to United Arab Emirates (UAE) through its wholly owned subsidiary Vadilal Gulf (FZE). VIL also provides foreign exchange consultancy services (mainly money changing service) as it is an RBI approved authorized dealer.

(Rs. Crore)

Brief Financials -VIL (Consolidated)	FY19 (A)	FY20*
Total operating income	576.69	608.89
PBILDT	82.22	88.35
PAT	33.36	41.38
Overall gearing (times)	1.18	0.98
PBILDT Interest coverage (times)	5.84	5.29

A: Audited
**as per published abridged financial results on the stock exchange*

Status of non-cooperation with previous CRA: Rating assigned by CRISIL to the fixed deposit instrument of the company continued to remain under 'Issuer not cooperating' category vide its press release dated December 18, 2019 in absence of requisite information.

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/ Bank Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	48.13	CARE BBB-; Negative
Non-fund-based - LT-Bank Guarantees	-	-	-	5.30	CARE BBB-; Negative
Non-fund-based - ST-Letter of credit	-	-	-	7.18	CARE A3
Fund-based - LT-Term Loan	-	-	February, 2025	59.15	CARE BBB-; Negative
Fund-based - ST-EPC/PSC	-	-	-	9.54	CARE A3

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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Cash Credit	LT	48.13	CARE BBB-; Negative	-	1)CARE BBB (Under Credit watch with Negative Implications) (27-Dec-19) 2)CARE BBB (Under Credit watch with Negative Implications) (26-Sep-19) 3)CARE BBB (Under Credit watch with Negative Implications) (22-Aug-19) 4)CARE BBB+ (Under Credit watch with Developing Implications) (10-Jun-19)	1)CARE BBB+; Stable (12-Sep-18)	1)CARE BBB+; Stable (28-Aug-17)
2.	Non-fund-based - LT-	LT	5.30	CARE BBB-;	-	1)CARE BBB (Under	1)CARE	1)CARE

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
	Bank Guarantees			Negative		Credit watch with Negative Implications) (27-Dec-19) 2)CARE BBB (Under Credit watch with Negative Implications) (26-Sep-19) 3)CARE BBB (Under Credit watch with Negative Implications) (22-Aug-19) 4)CARE BBB+ (Under Credit watch with Developing Implications) (10-Jun-19)	BBB+; Stable (12-Sep-18)	BBB+; Stable (28-Aug-17)
3.	Non-fund-based - ST-Letter of credit	ST	7.18	CARE A3	-	1)CARE A3+ (Under Credit watch with Negative Implications) (27-Dec-19) 2)CARE A3+ (Under Credit watch with Negative Implications) (26-Sep-19) 3)CARE A3+ (Under Credit watch with Negative Implications) (22-Aug-19) 4)CARE A2 (Under Credit watch with Developing Implications) (10-Jun-19)	1)CARE A2 (12-Sep-18)	1)CARE A2 (28-Aug-17)
4.	Fund-based - LT-Term Loan	LT	59.15	CARE BBB-; Negative	-	1)CARE BBB (Under Credit watch with Negative Implications) (27-Dec-19) 2)CARE BBB (Under Credit watch with Negative Implications) (26-Sep-19) 3)CARE BBB (Under Credit watch with Negative Implications)	1)CARE BBB+; Stable (12-Sep-18)	1)CARE BBB+; Stable (28-Aug-17)

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
						(22-Aug-19) 4)CARE BBB+ (Under Credit watch with Developing Implications) (10-Jun-19)		
5.	Fund-based - ST-EPC/PSC	ST	9.54	CARE A3	-	1)CARE A3+ (Under Credit watch with Negative Implications) (27-Dec-19) 2)CARE A3+ (Under Credit watch with Negative Implications) (26-Sep-19) 3)CARE A3+ (Under Credit watch with Negative Implications) (22-Aug-19) 4)CARE A2 (Under Credit watch with Developing Implications) (10-Jun-19)	1)CARE A2 (12-Sep-18)	1)CARE A2 (28-Aug-17)

Annexure-3: List of entities getting consolidated in VIL

Sr. No.	Name of the Entity	Subsidiary / Associate / Joint Venture	% Shareholding by VIL as on March 31, 2019
1.	Vadilal Industries (USA) Inc	Subsidiary	100.00
2.	Vadilal Industries Pty Ltd.	Subsidiary	100.00
3.	Vadilal Gulf (FZE)	Subsidiary	100.00
4.	Vadilal Cold Storage	Subsidiary	98.00

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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