Press Release

Bhagwati Products Limited

April 11, 2019

Rating Downgraded Outlook Revised

Total Bank Facilities Rated*	Rs. 850.00 Cr.
Long Term Rating	ACUITE BBB / Outlook: Negative (Downgraded from ACUITE A-/Stable)
Short Term Rating	ACUITE A3+ (Downgraded from ACUITE A2+)

* *Refer Annexure for details*

Rating Rationale

Acuité has downgraded the long-term rating to '**ACUITE BBB**' **(read as ACUITE triple B)** from **'ACUITE A-' (read as ACUITE A minus)** and short term rating to **'ACUITE A3+' (read as ACUITE A three plus)** from **ACUITE A2+ (read as ACUITE A two plus)** to the Rs. 850.00 crore bank facilities of Bhagwati Products Limited (BPL). Acuité has revised the outlook to **'Negative'** from **'Stable'**.

The downward revision in rating is on account of a sharp deterioration in operating performance which is expected to continue over the medium term on account of the significant competitive intensity in BPL's area of operations. BPL has been facing pressures on its key product segment i.e. mobile phones. It has attempted to derisk its revenue profile by diversifying into other product categories like solar panels, batteries, power banks, Air-conditioners, sound bars among others. However, a significant traction in these segments is yet to be demonstrated. BPL's revenues for 9M FY2019 (Provisional) stood at Rs. 705.00 crore as against Rs. 1818.67 crore for 9M 2018 (Provisional) and Rs. 2,174.15 crore for FY2018. The company witnessed a significant revenue decline across its major product categories i.e. mobile phones, LED TVs and solar panels in the current year. The operating margin (EBITDA margin) of BPL has also declined to 1.13 per cent for 9M FY2019 (Provisional) as compared 4.42 per cent during 9M FY2018 (Provisional) and 3.65 per cent for FY2018.

The revision in the outlook is based on Acuité's expectation that, the business profile of BPL is expected to be under stress over near to medium term. Any further deterioration in the revenues or operating measures will impart a further downward bias to the rating.

Delhi based, BPL (the erstwhile Bhagwati Cookies & Wafers Limited (BCWL)) was previously engaged in manufacturing and trading of edible products such as biscuits, cakes, pastries and electronic products (batteries, chargers, Bluetooth). In December 2011, Micromax Informatics Limited (MIL) acquired 80 per cent stake in BCWL and the name was changed to Bhagwati Products Limited (BPL). BPL is engaged in the assembling of mobile handsets, LED TVs, power banks and chargers among others, mainly for MIL. BPL derives more than 90 percent of its revenues from MIL. BPL's manufacturing facilities are located at Rudrapur (Uttarakhand), Hyderabad, Bhiwadi (Rajasthan), Greater Noida and Indore.

Analytical Approach

Acuité has considered the standalone business and financial risk profile of BPL to arrive at the rating.

Key Rating Drivers

Strengths

- **Experienced promoters and management team**

BPL is promoted by Mr. Rajesh Agarwal (holding 29.44 per cent stake), VRS & Associates (holding 60.00 per cent stake which is a partnership firm of Mr. Rahul Sharma, Mr. Sumeet Kumar and Mr. Vikas Jain) and SMK & Associates (holding 10.55 percent stake which is partnership firm of Mr. Mukesh Gupta and family). Mr. Rajesh Agarwal (Chairman of BPL), Mr. Rahul Sharma, Mr. Sumeet Kumar and Mr. Vikas Jain are also co-promoters of MIL. The promoters of BPL have background in engineering with an average experience of more than a decade each in the information technology and telecommunications industry. Mr. Mukesh Gupta, who is the Managing Director in BPL, is an alumnus of IIT Delhi and was instrumental in product development and marketing initiative in 'Microtek Inverters'. The Management of BPL is supported by a team of experienced and qualified professionals who are involved in the day to day operations.

- **Prudent capital structure**

Historically, BPL has been able to maintain a conservative financial risk profile marked by healthy net worth and low gearing. The net worth of BPL increased to Rs.345.48 crore as on March 31, 2018 as against Rs.314.82 crore in the previous year on account of retention of profits. BPL has followed a conservative financial policy in the past, as reflected by its peak gearing of just 0.25 times over the last three years through 2016-18. The Total debt of Rs.63.79 crore as on March 31, 2018 includes Rs.36.26 crore of term loans from bank and Rs.27.52 crore working capital borrowings. The gearing has improved to 0.18 times as on 31 March, 2018 as compared to 0.25 times as on March 31, 2017. Acuité believes that BPL's declining profitability and consequently the lower ploughback of earnings is expected to inhibit its ability to achieve any further improvement in its capital structure. Since the company's capex plans are moderate, any further debt requirements will be linked to its working capital management. Any significant elongation of the working capital cycle (i.e. build-up in inventory or receivables) will result in higher funding requirements and consequently higher debt levels.

Acuite believes that the profitability from operations and management of working capital will be key moniterables.

Weaknesses

- **Continuing pressures on operating and financial parameters**

BPL continues to experience business pressures marked by declining trend in operating income which stood at Rs.2174.15 crore in FY2018 as compared to operating income of Rs.2192.69 crore in FY2017 and Rs.4764.22 crore in FY2016. Further, BPL has recorded turnover of ~Rs.705 crore till December 2018 (Provisional) which is significantly lower than Acuité's expectations. The decline in turnover in FY2018 is on account of limited order flow from MIL, which is the primary buyer of BPL and is facing stiff competition from the Chinese and Korean players. Further, there is limited visibility of turnover in the medium term as BPL is yet to perform in the non-mobile segment.

The Interest coverage ratio (ICR) stood 2.32 times in FY2018 as compared to 3.42 times in FY2017 mainly on account of deterioration in EBITDA and stable interest cost. The decline in operating margins during FY18 vis-à-vis FY17 along with decline in turnover has resulted in net cash accruals of Rs. 39.58 crore for FY2018 as compared to Rs. 72.55 crore in FY2017. Further, Debt/EBITDA is likely to decline to more than 2 times in FY2019 as compared to 0.73 times as on March 31, 2018 as against 0.63 times as on March 31, 2017.

Acuité believes that the business pressures are likely to continue till BPL is able to demonstrate a significant and sustainable improvement in its revenue growth and margins.

- **Highly competitive mobile handset industry**

BPL is operating in the mobile handset and electronics segment in India, which is characterised by presence of well-established big players such as Xiaomi, Samsung, Apple, Lenovo, and BBK Electronics among others. The advents of other brands such as Oppo, Vivo and OnePlus have proved to be intensely competitive in terms of features and pricing. The ability of these companies to continuously churn out newer models with a strong value proposition for the consumer has helped them to gain a significant share in the mobile market.

Further, apart from mobile handsets, MIL has also gradually ventured into the consumer electronics segments causing a shift in focus of BPL on manufacture other electronics items such as Air-conditioners, Refrigerators and Washing Machines also form a small part in the product offerings of BPL. During 9M FY2019 (Provisional), approximately 35 per cent of BPL's operating income was generated from the sale of LED televisions and other consumer electronic items which are characterized by longer product lifecycles and value for money proposition. This could result in profitability margin pressures over the near to medium term which may percolate down to vendors like BPL. On the flip side, policy initiatives by the Government of India such as increase in import duties for Completely Built-up Units (CBUs) and tax incentives for manufacturing entities are expected to support domestic players like BPL.

- **Customer concentration risk**

  BPL is the domestic manufacturing arm of MIL producing mobiles, tablets, LED TVs and other accessories for MIL and its subsidiary YU Televentures Private Limited. With turnover from MIL forming 96 percent of the total turnover of BPL, the operations of BPL are largely dependent on the growth of operations of MIL. The concentration risk is aggravated due to continual decline in market share in the mobile phones industry. MIL's market share stood at 9 percent as on Q3 FY2018. This is on account of stiff competition from the Chinese players who are offering value propositions to its customers, thus increasing their market share in the mobile handset segment. Going forward, BPL expects inflow of orders from customers other than MIL, which constituted ~4 percent of BPL's total turnover in FY2018. Acuité believes that the ability of BPL to diversify its client base will be a factor of key rating sensitivity.

Liquidity Position:

BPL has adequate liquidity marked by moderate net cash accruals to its maturing debt obligations. BPL generated cash accruals of Rs.39.58 to 144.70 crore during the last three years through 2017-18, while its maturing debt obligations were in the range of Rs. 5.22 to 15.91 crore over the same period. The cash accruals of BPL are estimated to decline to Rs.11.99-29.33 crore during 2019-21 while its repayment obligation are estimated to be around Rs. 5.09 to 11.00 crore. BPL has efficient working capital management as marked by gross current asset (GCA) days of 53 in FY 2018. This has led to lower reliance on working capital borrowings, the cash credit limit in BPL remains utilized at ~35 percent during the last 3 months period ended February 2019. BPL maintained unencumbered cash and bank balances of Rs.23.85 crore as on March 31, 2018. The current ratio of BPL stood moderate at 1.49 times as on March 31, 2018.

Outlook: Negative

Acuité believes that BPL's credit profile will be impacted by significant moderation in operating income and profitability margins over near to medium term. The rating may be downgraded in case this continued moderation in its operating performance thereby impacting its liquidity and debt protection matrices. Conversely, the outlook may be revised to 'Stable' if BPL is able to display higher than expected performance in terms of scale of operations and improvement in margins and is able to diversify its client base while maintaining working capital cycle and liquidity profile.

About the Rated Entity - Key Financials

	Unit	FY18 (Actual)	FY17 (Actual)	FY16 (Actual)
Operating Income	Rs. Cr.	2,174.15	2,192.69	4,764.22
EBITDA	Rs. Cr.	79.30	119.06	171.77
PAT	Rs. Cr.	29.88	64.69	140.01
EBITDA Margin	(%)	3.65	5.43	3.61
PAT Margin	(%)	1.37	2.95	2.94
ROCE	(%)	22.18	39.18	81.29
Total Debt/Tangible Net Worth	Times	0.18	0.25	0.21
PBDIT/Interest	Times	2.32	3.42	5.38
Total Debt/PBDIT	Times	0.73	0.63	0.31
Gross Current Assets (Days)	Days	53	74	57

Status of non-cooperation with previous CRA (if applicable)

Not applicable

Any other information

None

Applicable Criteria

- Default Recognition - https://www.acuite.in/criteria-default.htm
- Manufacturing Entities - https://www.acuite.in/view-rating-criteria-4.htm
- Financial Ratios And Adjustments -https://www.acuite.in/view-rating-criteria-20.htm

Note on complexity levels of the rated instrument
https://www.acuite.in/criteria-complexity-levels.htm

Rating History (Upto last three years)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
09-Mar-2018	Cash Credit	Long Term	5.00^	ACUITE A-/Stable (Assigned)
	E-VFS	Long Term	200.00	ACUITE A-/Stable (Assigned)
	Cash Credit	Long Term	5.00	ACUITE A-/Stable (Assigned)
	Letter of Credit	Short Term	125.00*	ACUITE A2+ (Assigned)
	Letter of Credit	Short Term	125.00	ACUITE A2+ (Assigned)
	Letter of Credit	Short Term	75.00**	ACUITE A2+ (Assigned)
	Inland Letter of Credit /Foreign Letter of Credit	Short Term	180.00***	ACUITE A2+ (Assigned)
	Inland Letter of Credit /Foreign Letter of Credit	Short Term	45.00	ACUITE A2+ (Assigned)
	Letter of Credit	Short Term	90.00	ACUITE A2+ (Assigned)

^One way interchangeability towards Non-Fund Based Limits
**Sub-Limit of Rs.20.00 cr. in the form of Cash Credit/WCDL*
*** Sub-Limit of Rs.5.00 cr. in the form of Cash Credit Limit*
**** Sub-Limit of Rs.35.00 cr. in the form of Cash Credit Limit*

***Annexure – Details of instruments rated**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Cash Credit	Not Applicable	Not Applicable	Not Applicable	5.00^	ACUITE BBB/ Negative (Downgraded from ACUITE A-/Stable)
Cash Credit	Not Applicable	Not Applicable	Not Applicable	35.00*	ACUITE BBB/ Negative (Downgraded from ACUITE A-/Stable)
Proposed	Not Applicable	Not Applicable	Not Applicable	205.00	ACUITE BBB/ Negative (Downgraded from ACUITE A-/Stable)
Letter of Credit	Not Applicable	Not Applicable	Not Applicable	175.00**	ACUITE A3+ (Downgraded from ACUITE A2+)
Letter of Credit	Not Applicable	Not Applicable	Not Applicable	75.00	ACUITE A3+ (Downgraded from ACUITE A2+)
Inland Letter of Credit /Foreign Letter of Credit	Not Applicable	Not Applicable	Not Applicable	145.00	ACUITE A3+ (Downgraded from ACUITE A2+)
Inland Letter of Credit /Foreign Letter of Credit	Not Applicable	Not Applicable	Not Applicable	90.00	ACUITE A3+ (Downgraded from ACUITE A2+)
Proposed Bank Facility	Not Applicable	Not Applicable	Not Applicable	120.00	ACUITE A3+ (Downgraded from ACUITE A2+)

^One way interchangeability with Non-Fund Based Limits
**Sublimit of Non-Fund Based Limits.*
***Sub-Limit of Rs. 20.00 cr in the form of Cash Credit/WCDL*

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About Acuité Ratings & Research:

Acuité Ratings & Research Limited (Erstwhile SMERA Ratings Limited) is a full-service Credit Rating Agency registered with the Securities and Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI), for Bank Loan Ratings under BASEL-II norms in the year 2012. Since then, it has assigned more than 6,000 credit ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Mumbai.