Rating Rationale

Ethnic Tobacco (India) Ltd [ETIL]

27 Sep 2018

Brickwork Ratings reaffirms 'BBB/ A3+' for the bank loan facilities of Rs 188.50 Crs of Ethnic Tobacco (India) Ltd (ETIL or the 'Company')

Particulars:

Facilities#	Amount (Rs Crs) Previous	Amount (Rs Crs) Present	Tenure	Ratings[1] Previous	Ratings[1] Present
Fund based: CC/OCC/PCFC/FUBD/ FDBP/PSFC Standby Line of Credit Term loans	53.00 12.00 12.56	53.00 12.00 -	Long term	BWR BBB [Pronounced BWR Triple B] (Outlook: Stable)	BWR BBB [Pronounced as BWR Triple B] (Outlook: Stable) Reaffirmed
Fund based : EPC/PCL/PC **Non Fund based limits**: CEL (Forward Contract)	117.00 6.50	117.00 6.50	Short term	BWR A3+ [Pronounced BWR A Three Plus]	BWR A3+ [Pronounced as BWR A Three Plus] Reaffirmed
Total	**201.06**	**188.50**	**Rupees One Hundred and Eighty Eight Crores and Fifty Lakhs Only**		

#Annexure I shows details of bank loan facilities
[1]*For definitions of the rating symbol please visit our website* www.brickworkratings.com

Ratings Reaffirmed

Rationale/Description of Key Rating Drivers/Rating sensitivities:

BWR has essentially relied upon the audited financials upto FY17, FY18 Provisionals, publicly available information and information/ clarifications provided by the Company's management.

The reaffirmation of ratings takes into consideration the established track record of the Guntur based Ethnic Group in the tobacco processing industry, experienced management, reputed & diversified clientele and Group's average financial risk profile marked by its modest net worth, moderate gearing and debt protection metrics. The ratings, however, continue to remain constrained by the susceptibility of the profitability margins to volatility in tobacco prices, stretched operating cycle of the business owing to higher inventory levels, significant intra-Group transactions, highly regulated nature of the tobacco industry and intense industry competition.

Going forward, the ability of the company to increase the scale of operations, improve profitability, reduce intra-group transactions and manage its working capital efficiently would remain the key rating sensitivities.

Rating Outlook: Stable

BWR believes **Ethnic Tobacco (India) Ltd [ETIL]'s** business risk profile will be maintained over the medium term. The 'Stable' outlook indicates a low likelihood of rating change over the medium term. The rating outlook may be revised to 'Positive' in case the revenues and profit show sustained improvement. The rating outlook may be revised to 'Negative' if the revenues go down and profit margins show lower than expected figures.

Key rating drivers

Established track record of operations & experienced management - Ethnic Tobacco (India) Ltd (ETIL) is the flagship Company of the Guntur based Ethnic Group, which is engaged in the manufacturing & trading of tobacco. The Group is established for around 13 years now. The management has extensive experience in tobacco processing industry.

Reputed & diversified clientele and modest order book - The Company mainly sells to diversified and reputed international companies in the US, Europe, Egypt, Middle East and India. The Company has an export order book in hand of ~ Rs 208 Crs for execution during next few months. The Company exports to UAE, Netherlands, Italy, Greece, USA and various other European countries. The Company generally has running and repetitive domestic orders of ~Rs 100 Crs- Rs 125 Crs at any given point in time.

Average financial risk profile- The Company has an average financial risk profile marked by its modest net worth (FY17 Audited: Rs 133.55 Crs), moderate gearing (FY17 Audited: 1.50 times) and debt protection metrics [FY17 Audited: ISCR- 2.39 times; DSCR: 1.02 times]. The Company's profitability margins, capital structure and coverage metrics were adequate during FY17 & FY18.

Competitive advantage from presence of the group across the tobacco value chain–The promoters, through four group entities –Ethnic Tobacco (India) Ltd [ETIL], Ethnic Agros Ltd (EAL), Ethnic Spices Pvt Ltd (ESPL) and Indtob International Pvt Ltd (ITIPL), have presence across the tobacco value chain. ETIL is the flagship Company of the Group, where the manufacturing of tobacco takes place. While tobacco is manufactured mostly in ETIL, the trading of tobacco takes place in EAL, ESPL and ITIPL, for facilitating purchase of tobacco from Tobacco Board Auction Platforms, which is further sold to ETIL. The integrated presence provides operational and cost advantages.

Govt. regulation on tobacco industry- Tobacco is a controlled industry due to the associated health hazards- hence there are restrictions in the domestic market for procurement and sale of tobacco. Given the health hazards associated with the products, any changes in regulations on procurement policies by the foreign countries and duties laid down by the World Health Organization (WHO) can impact revenues for the company.

Stagnant demand outlook for tobacco industry- With increasing health awareness and various initiated programmes curbing the consumption of tobacco, the demand growth for tobacco products is expected to remain subdued in the medium term.

Agro-climatic risk- Availability of raw tobacco is susceptible to climate-related risks and Government (tobacco board) policy on production. This gives rise to volatility in supply and consequently, raw tobacco prices.

Stretched operating cycle of the business owing to higher inventory levels- The Company's operating cycle was stretched at 221 days in FY18 owing to high inventory holding days, due to the nature of tobacco processing business. There is seasonality of sales in Tobacco industry. The peak season of sales starts from March and ends in September. Hence, the Company is required to stock high inventories during the peak season, which results in higher inventories at the end of the financial year.

Analytical approach

For arriving at its ratings, BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

About the Company

Established in 2005 at Guntur, Andhra Pradesh, Ethnic Tobacco (India) Ltd is engaged in the processing and sale of tobacco leaves in the domestic and international markets. The company is a "Trading House" and is an export house recognized by Govt. of India. The Company deals in all kinds of Tobacco products such as FCV (Flue-Cured Virginia) [contributed 66% to total revenues in FY18], Non FCV (34%) and all grades of Tobacco varieties. The Company also deals in Quality wise Flavor Quality, Filler Quality, Virginia types and Sun Cured, Air cured, Burley Tobaccos with different types of chemical characteristics. The company is ISO 9001: 2008 certified by Aqa International, USA. The Tobacco Threshing Unit at Guntur, A.P. (spread at around 34 acres area- Factory & godown) operates at 81% of capacity. The Company purchases various types of Tobacco (FCV and Non FCV) from Andhra Pradesh and Karnataka auction platforms which are operated by Tobacco Board, Govt of India and other local dealers who purchase from farmers. The processed tobacco is then sold mostly to domestic Customers such as ITC, VST (Vazir Sultan Tobacco), Godfrey Phillips India Ltd etc and exports are made to International cigarette manufacturers in USA, Greece, Dubai, Singapore, Egypt, Brazil, China etc. Domestic sales contributed 77% to total revenues in FY18 followed by exports (23%). The manufacturing of tobacco contributed ~78% to total revenues in FY18 followed by Trading (22%).

A.P. based Ethnic Group comprises four main operating entities- Ethnic Tobacco (India) Ltd; Ethnic Spices Pvt Ltd [set up in 2006 to trade in spices ; however, it currently trades only in raw tobacco; rated BWR BBB- (Stable)], Ethnic Agros Ltd [set up in 2006, trades in raw tobacco; rated BWR BBB- (Stable)], IndTob International Pvt Ltd [set up in 2010, trades in raw tobacco; rated BWR BBB- (Stable)]. The Group has a significant presence in A.P. & other Southern states. At Consolidated Group level, on a provisional basis, Net sales was around Rs 644 Crs for FY18 (after netting off the intra-Group sales made to Ethnic Tobacco (India) Ltd by the other three Group entities).

Mr. T Murali Mohan is the Managing Director. Mr T. Venkata Rao, Chairman, Mrs T. Venkataramana, Mr. M G Nagarjuna Reddy and Mr. P. Prakasa Rao are the other directors.

Financial Performance

Total operating income was almost stagnant at Rs 478.92 Crs in FY17 compared to Rs 477.41 Crs in FY16. PAT was also almost flat at Rs 6.76 Crs in FY17 as against Rs 6.62 Crs in FY16 mainly due to higher sales and reduced interest & finance charges. The company's sales has been almost stagnant, mainly due to stagnation of demand in the traditional markets. Tangible net worth was Rs 133.55 Crs as on March 31 2017. Total debt was Rs 200.28 Crs as on March 31 2017 and Total debt/ Tangible net worth stood at 1.50 times as on March 31 2017. ISCR and DSCR were adequate at 2.39 times and 1.02 times respectively for FY17. Current ratio at 1.20 times was also adequate for FY17. On a provisional basis, the Company has reported total operating income and PAT of Rs 479.22 Crs and Rs 6.98 Crs respectively for FY18. Further, on a provisional basis, the Company has achieved net sales of ~ Rs 265 Crs till date in FY19. The key financial indicators are summarized in Annexure II.

Status of non-cooperation with other CRA:, CRISIL Ratings, vide its rating rationale dated March 19 2018, has migrated its rating on the bank facilities of Ethnic Tobacco (India) Ltd [ETIL] to the ' Issuer Not Cooperating' category. CRISIL has also simultaneously withdrawn its ratings on certain other bank loan facilities of the company.

Any other information: Not applicable.

Rating History for the last three years:

Sl. No.	Facility	Current Rating (2018)			Rating History		
		Tenure	Amount (Rs Crs)	Rating	28-June-2017^	28-Mar-2016^^	2015
1.	Fund based	Long term	65.00	BWR BBB (Stable) Reaffirmed	BWR BBB (Stable) Reaffirmed	BWR BBB (Stable) Assigned	-
2.	Fund based Non Fund based	Short term	117.00 6.50	BWR A3+ Reaffirmed	BWR A3+ Reaffirmed	BWR A3+ Assigned	-
	Total		**188.50**	**Rupees One Hundred and Eighty Eight Crores and Fifty Lakhs Only**			

^Amount rated: Rs 201.06 Crs; ^^Amount rated: Rs 226.48 Crs

Hyperlink/Reference to applicable Rating Criteria

- **General Criteria**
- **Approach to Financial Ratios**
- **Manufacturing Companies**
- **Short Term Debt**
- **Trading Entities**

Analytical Contacts	Media

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Ethnic Tobacco (India) Ltd (ETIL)

Annexure I: Details of the Bank Loan facilities rated

Existing Facilities- Consortium of five banks, State Bank of India being the Lead Bank		
Bank	**Facility**	**Existing (Rs in cr)**
Fund Based:		
State Bank of India	Export Packing Credit Cash Credit Standby Line of Credit	65.00 18.00 12.00
Lakshmi Vilas Bank	OCC/PCL/PCFC/FUBD/FDBP/PSFC	20.00
Syndicate Bank	EPC/PCL	30.00
Indian Bank	OCC	15.00
Canara Bank	PC	22.00
Fund Based Total		**182.00**
Non- Fund Based:		
State Bank of India	CEL (Forward Contract)	6.50
Total (FB+NFB)		**188.50**

Annexure II
Key Financial Parameters

Particulars	31/Mar/2016	31/Mar/2017
Result Type	**Audited**	**Audited**
Total Operating Income (Rs Crs)	477.41	478.92
EBITDA (Rs Crs)	34.94	32.89
PAT (Rs Crs)	6.62	6.76
Tangible Net Worth (Rs Crs)	123.80	133.55
Total Debt/TNW (Times)	1.35	1.50
Current ratio (Times)	1.26	1.20

Note on complexity levels of the rated instrument:
BWR complexity levels are meant for educating investors. The BWR complexity levels are available at www.brickworkratings.com/download/ComplexityLevels.pdf Investors queries can be sent to info@brickworkratings.com.

About Brickwork Ratings
Brickwork Ratings (BWR), a SEBI registered Credit Rating Agency, accredited by RBI and empaneled by NSIC, offers Bank Loan, NCD, Commercial Paper, MSME ratings and grading services. NABARD has empaneled Brickwork for MFI and NGO grading. BWR is accredited by IREDA & the Ministry of New and Renewable Energy (MNRE), Government of India. Brickwork Ratings has Canara Bank, a leading public sector bank, as its promoter and strategic partner.
BWR has its corporate office in Bengaluru and a country-wide presence with its offices in Ahmedabad, Chandigarh, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi along with representatives in 150+ locations. BWR has rated debt instruments/bonds/bank loans, securitized paper of over ₹ 13,22,500 Cr. In addition, BWR has rated over 7000 MSMEs. Also, Fixed Deposits and Commercial Papers etc. worth over ₹62,000 Cr have been rated.

BWR has rated over 30 PSUs/Public Sector banks, as well as many major private players. BWR has a major presence in ULB rating of nearly 102 cities