J.G.I Distribution Private Limited: [ICRANP] A4+ reaffirmed

December 28, 2020

Summary of rated instruments:

Instrument*	Current rated amount (NPR Million)	Rating Action
Short-term; fund-based limits	5,000.00	[ICRANP]A4+; reaffirmed

* Instrument details are provided in Annexure-1.

Rating action

ICRA Nepal has reaffirmed the short-term rating of [ICRANP]A4+ (pronounced ICRA NP A four plus) to the NPR 5,000 million fund-based limits of J.G. I Distribution Private Limited (JGIPL).

Rationale

The reaffirmation continues to factor in JGIPL's established position in the alcoholic beverage distribution business of Nepal, supported by the Group's four-decades long track record, strong position in the Nepalese Liquor industry, and the experience of its promoter group. The rating also reflects the company's diversified product portfolio with footprints in both the distillery and the brewery segments. The rating also derives comfort from the established sales channel (four warehouses and over 230 distributors) and the moderately diversified customer profile of JGIPL.

The rating, however, remains constrained by the moderate financial profile of JGIPL, characterised by a decline in the operating income, moderate profitability profile, modest gearing, stretched coverage indicators and weak liquidity position. The interest coverage ratio and the net profitability margin continued to remain under pressure in FY2020. The interest coverage retained at 1.1x and the net profit margin reported slight improvement to 0.3% in FY2020 (0.2% in FY2019) amid reduced operating incomes, despite on lower debt levels and declining interest rate scenario in the Nepalese banking industry. Further, the liquidity position of the company remains weak due to high volume of supplier's advances (~93% of total debts as of Jul-2020) despite moderate debtor and inventory days (33 and 39 days respectively in FY2020). Rating concerns also arise due to significant regulatory risks associated with the liquor industry.

Key rating drivers

Credit strengths

Group's established track record in Nepalese liquor industry and experienced management – The Group was founded by Mr. Vijay Kumar Shah (JGIPL's managing director and group chairman) back in 1973 as Jawalakhel Distillery starting its first commercial production with Ruslan Vodka. At present, there are altogether eight companies under the umbrella of JGI Group viz; four distilleries, one brewery one research unit (Technology and Research Center), JGI Pvt Ltd. and JGI Distribution Pvt. Ltd. The Group currently has a strong market share in the distillery-based products in Nepal. Decades long experience of the company's MD and adequately experienced senior management team also remains a positive for the company.

Established brands and diversified product range – JGIPL is the sole distributor of all the products of JGI Group. The company has a strong presence in the Vodka and the 40UP brown sprit segment (mainly Golden Oak), which are widely consumed distillery-based products in Nepal. The sales composition is ~59% 40UP brown spirits (Golden Oak, Black Oak, Royal Treasure, Himalayan Brandy, and others), ~34% white spirits (Vodka, Jin and Aaila) and ~7% in beer. However, the revenue is driven by its three major products – Golden Oak, Ruslan Vodka and Blue Diamond Gin. During FY2020, these three products accounted for approximately 89% of the company's revenue, higher than around 87% in FY2019.

Established sales channel - The company has an established supply chain comprising over 230 dealers across the country and four warehouses. The sales remain fairly diversified across its customers, with the top-20 customers accounting for ~54% of its sales in FY2020.

Credit challenges

Reduction in sales, driven by brown spirit segment – Company's revenue shrunk by ~15% in FY2020 in line with the industry, primarily due to the impact of Covid during its major sales season (April-June). However, the company had reported growth of ~15% in terms of the number of cases and ~21% in terms of amount during the first eight months of FY2020 (pre-Covid era) over the same period in FY2019. Product mix in FY2020 remained dominated by the brown spirit segment (~59%), primarily accounted for by a single product Golden Oak (at ~52%). The white spirit segment in total comprised ~34% share in line with FY2019's mix with Ruslan Vodka accounted for ~19% share and Blue Diamond Gin accounted for ~15% of the total sales for FY2020. The third segment – beer also reported a contraction of ~15% in FY2020 mainly due to the Covid-19 induced lockdown in the peak sales season. The Group has stopped production of Foster for now as AB InBev has sold its brand Foster to a Japanese company Asahi Breweries and the production licence from Asahi Breweries has not been received so far. However, the Group has production rights for another widely consumed beer across the world - Budweiser - and plans to produce the same from Feb-March of FY2021. Introduction of Budweiser and the import of Corona beer from India (which was previously being imported from Mexico) are expected to improve the performance of its beer segment in the near future.

Moderate financial profile with leveraged capital structure – The financial profile of JGI remains moderate and is characterised by leveraged capitalisation profile, despite a substantial equity injection in FY2019. JGI's gearing ratio stood at ~2.7 times as of mid-July 2020 (improved compared to 4.3 times as of mid-July 2019), with TD/OBPDITA[1] of 5.0 times and TOL/TNW[2] of 4.6 times. High gearing, in turn, results from the exceptional advance to suppliers in addition to the high working capital intensity, which is financed through external borrowings.

JGI purchases and holds its major stock during the April-May of each year with expectations of a probable increase in the applicable duty to distillery product through a budget (budget is announced towards end of May). This results in relatively high inventory days towards the end of the year (mid-July).

Stretched liquidity profile – The company's liquidity position is stretched, given its moderate profitability, increase in debtors' days and sizeable advances to suppliers, primarily a deposit to one of its group units. Considering the advances, the working capital loan utilisation has come well below the drawing power, however, disregarding the advances to suppliers, the company has exceeded its drawing power as of mid-July 2020 as utilisation generally remains high towards the year-end.

Moderate profitability profile with stretched coverage indicator – The company's profitability continued to remain under pressure with marginal improvement in FY2020 with PAT/OI[3] of 0.3% with moderate operating margin OPBDITA/OI (3.6%) mainly on account of reduced interest expenses. Lower debt during the declining interest rate scenario reduced the finance cost of the company by ~19% during FY2020, while sales in the same period decreased by ~15%. With the lower overall profitability profile, cash generation and coverage ratio remained weak (NCA/TD of ~2% and an interest cover of 1.1 times) in FY2020.

1 TD-total debt, OPBDITA-Operating profit before depreciation interest tax and amortization, NCA-net cash accruals

2 TOL-total outside liabilities

3 PAT- profit after tax, OI- operating income

Regulatory risk – The Government's high import tariff on finished liquors provides duty protection and high entry barriers to the domestic spirits industry. Nevertheless, this also exposes JGIPL to import tariff-related regulation changes. Reduction or removal of import-duty/ tariff could have a significant impact on the company's revenue profile, profit margin and debt coverage indicators. Also, liquor remains one of the highest taxed commodities in Nepal with the excise tariff increasing steadily on a year-on-year basis. Continued increase in tariff and competitive pressure could diminish JGIPL's ability to pass on the incremental cost to the consumers, which could reduce the profit margins. Furthermore, any restriction by the regulatory agency in promotion, sales and distribution of liquor could also have an impact on JGIPL.

Analytical approach: For arriving at the ratings, ICRA Nepal has applied its rating methodology as indicated below.

Links to applicable criteria:
Corporate Credit Rating Methodology

About the company

Incorporated in August 2016, J.G.I. Distribution Private Limited (JGIPL) is the sole distributor of alcoholic beverages produced by four distilleries (Vijay, Asian, Himalayan, Rolling River) and Raj Brewery, all under Jawalakhel Group of Industries in Nepal. It is also the distributor of certain varieties of imported wines & beers.

The company is solely promoted by Mr. Bijay K. Shah. JGIPL belongs to the Jawalakhel Group of Industries, which has over four decades of operations in the production of alcoholic beverages in Nepal. JGIPL has its presence across the country through four warehouses and over 230 dealers.

Key financial indicators

	FY2017 (Audited)	FY2018 (Audited)	FY2019 (Audited)	FY2020 (Provisional)
Operating income-OI (NPR million)	11,455.6	15,265.8	13,312.0	11,277.4
OPBDITA/OI (%)	2.3%	2.5%	3.6%	3.6%
Total debt/Tangible net-worth-TNW (times)	6.2	7.5	4.3	2.7
Total outside liabilities/ TNW (times)	6.4	8.3	5.6	4.6
Total debt/OPBDITA (times)	7.8	7.4	6.5	5.0
Interest coverage (times)	1.8	1.4	1.1	1.1
NWC /OI (%)	19%	21%	29%	24%
Current ratio (times)	1.15	1.12	1.17	1.21

Source: Company data

Annexure-1: Instrument Details

Instrument	Last rated limit (Amount in NPR Million)	Current rated Limit (Amount in NPR Million)	Rating
Short-term; fund based (Cash credit/ Overdraft)	450.00	1,350.00	[ICRANP] A4+ (reaffirmed)
Short-term; fund based (Working Capital)	3,950.00	3,650.00	
Grand total (A+B)	**4,400.00**	**5,000.00**	

Analyst Contacts:

Mr. Kishor Prasad Bimali, (Tel No. +977-1-4419910/20)
kishor@icranepal.com

Ms. Kushum Bhattarai, (Tel No. +977-1-4419910/20)
kushum@icranepal.com

Relationship Contacts:

Ms. Barsha Shrestha, (Tel No. +977-1-4419910/20)
barsha@icranepal.com

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For more information, visit www.icranepal.com

ICRA Nepal Limited,
Sunrise Bizz Park, 6th Floor, Dillibazar, Kathmandu, Nepal.
Phone: +977 1 4419910/20
Email: info@icranepal.com
Web: www.icranepal.com

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