March 27, 2023

Neon Motors Private Limited: [ICRA]BB+(Stable)/[ICRA]A4+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based – Term loans	5.00	[ICRA]BB+(Stable) assigned;
Long-term fund-based – Cash credit	87.00	[ICRA]BB+(Stable) assigned;
Short term – Non-fund based	6.50	[ICRA]A4+ assigned;
Long-term/short-term – Unallocated	0.06	[ICRA]BB+(Stable)/ [ICRA]A4+ assigned;
Total	**98.56**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings for Neon Motors Private Limited (NMPL) factor in its established presence as an authorised dealer for passenger vehicles (PV) and commercial vehicles (CV) for Mahindra and Mahindra Limited (M&M) and PV dealer for Hyundai Motors India Limited (HMIL) in 12 districts across Andhra Pradesh (AP) and Telangana. The ratings are further supported by the improving market share of M&M in the automobile sector, with healthy demand for its new launches and the established market position of HMIL in the PV segment. Healthy demand for PVs, especially in the utility vehicle (UV) segment, a key focus segment for M&M, would augur well for the company's growth in the medium term. The company has a healthy network with 33 showrooms/sales depots, 20 workshops/service centres, and two stockyards across AP And Telangana. After being impacted by the Covid-19 pandemic in FY2021, the company's revenues witnessed a strong growth of over 120% in FY2022 and 99% in 9M FY2023, on the back of the addition of new showrooms, easing supply constraints, and healthy demand. It will launch three new showrooms in H2 FY2023, which is expected to result in a healthy growth of 40-50% for the company in FY2024.

The ratings are, however, constrained by the company's modest capital structure owing to high working capital borrowings, thin margins inherent to the dealership business, and low net-worth position. The ratings are further constrained by the intense competition in the PV and CV markets in India and the limited bargaining power of dealers, with pricing policies decided by principal OEMs. Any supply constraints emanating from semiconductor chip shortages would be a key monitorable; however, ICRA notes that semiconductor availability has been improving on a sequential basis.

The Stable outlook on NMPL's rating reflects ICRA's opinion that the company's established position as a dealer of HMIL and M&M and healthy demand will support ramping up the revenues and earnings.

Key rating drivers and their description

Credit strengths

Authorised dealer of M&M and HMIL – NMPL is an authorised dealer of Mahindra (PV and CV) in Telangana and AP and HMIL PV in Telangana. The promoters have been operating in the dealership business for more than 10 years, which has helped NMPL in developing its brand in the served regions.

Good network with presence in 12 districts of AP and Telangana – NMPL has 33 showrooms/sales points, 20 service workshops, and two stockyards spread across 12 districts of Telangana and AP. The company is further opening two new showrooms and workshops in FY2023, which will support the revenue growth, going forward.

Favourable demand for passenger vehicles – The demand for passenger vehicles improved in FY2022 and FY2023 with increased preference of owning personal car for travel given the spread of Covid-19. In addition, the sport utility vehicle (SUV) segment has seen a significant increase in preference, which has aided the substantial revenue growth for NMPL as M&M's flagship models are primarily in the said segment only. The demand for PV has remained healthy, however, the supply from OEMs has remained constrained in FY2023 given the semiconductor chip shortages. In 10M FY2023, M&M's share in the domestic market has improved from FY2022 and commands a healthy share of about 35% in light commercial vehicles (LCV), which will support the revenues in the near term.

Credit challenges

Modest financial risk profile – The financial profile of NMPL is modest, characterised by a gearing of 4.9 times as on March 31, 2022, given the high working capital debt owing to inventory held, and thin margins inherent in the dealership business, impacting the company's net worth. Thin profitability led to modest debt protection indicators reflected in the TD/OPBITDA of 6.2 times for FY2022. However, coverage indicators have been comfortable as indicated by interest coverage of 2.8 times in FY2022. Moreover, the scale of operations is expected to improve significantly, which will support the capital structure and net-worth position of the company, despite a likely increase in debt in the near term.

Auto dealership business characterised by high competition, thin margins and weak bargaining position – The dealership business is characterised by thin margins and low bargaining power of the dealer, as margins on vehicles are determined by the principal. The inherently low-value addition and intense competition in the auto dealership business have resulted in low operating margins for the company. The OPM moderated in FY2022 to 2.1% from 2.9% in FY2021 owing to higher overheads for establishing the new showrooms and workshops. NMPL launched three new showrooms and workshops in FY2022.

Although the company is an authorised dealer of M&M and HMIL, its sales and profitability remain susceptible to intense competition from other dealers of M&M and HMIL as well as other OEMs in the regions. The dealers have to pass on additional benefits to customers to increase sales owing to intense competition, which impacts their profitability to an extent.

Liquidity position: Adequate

NMPL's liquidity is adequate, with a buffer of Rs. 10.1 crore in working capital limits as on December 31, 2022, against repayment obligations of about Rs.1-1.5 crore over the next twelve months. While the company's retained cash flows are expected to be negative given the strong growth expected in revenues, the liquidity will be supported by Rs. 25.0 crore of enhancement in the working capital limits, disbursed in February 2023, and another Rs. 20.0 crore expected to be sanctioned in March 2023.

Rating sensitivities

Positive factors – NMPL's ratings could be upgraded, if there is any sustained improvement in the scale of operations. Substantial growth in earnings leading to improvement in coverage metrics and the net worth position of the company could lead to a rating upgrade.

Negative factors – The ratings could witness a downward revision, if any decline in the revenue/profitability of the company leads to a deterioration in debt protection metrics. Further, stretched working capital cycle impacting the liquidity position of the company can trigger a rating downgrade. A specific credit metric for downgrade is if DSCR is less than 1.3 times, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology – Automobile Dealerships
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of NMPL

About the company

Neon Motors Private Limited (NMPL) was set up in 2012 as an automobile dealer for Mahindra and Mahindra Limited (M&M)'s commercial vehicle (CV) segment in Vishakhapatnam, Andhra Pradesh and later expanded to include passenger vehicles (PV) as well. The company further expanded in Hyderabad (Telangana) and added a dealership of Hyundai Motors India Limited's (HMIL) passenger vehicles in 2021. As on January 31, 2023, the company had 33 showrooms/sales depots, 20 workshops/service centres, and two stockyards spread across 12 districts in Andhra Pradesh and Telangana.

Key financial indicators (audited)

	FY2021	FY2022
Operating income	143.6	316.5
PAT	2.0	1.3
OPBDIT/OI	2.9%	2.1%
PAT/OI	1.4%	0.4%
Total outside liabilities/Tangible net worth (times)	3.2	7.3
Total debt/OPBDIT (times)	2.9	6.2
Interest coverage (times)	5.4	2.8

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amounts in Rs. crore
Source: Company data, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2022 (Rs. crore)	Date & rating in FY2023	FY2022	FY2021	FY2020
					Mar 27, 2023	-	-	-
1	**Fund based – Term loans**	Long-term	5.00	2.50	**[ICRA]BB+(Stable)**	-	-	-
2	**Fun based – Cash credit**	Long-term	87.00	-	**[ICRA]BB+(Stable)**	-	-	-
3	**Non fund based/BG**	Short-term	6.50	-	**[ICRA]A4+**	-	-	-
4	**Unallocated limits**	Long-term/ short-term	0.06	-	**[ICRA]BB+(Stable)/ [ICRA]A4+**	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term - fund-based – Term Loans	Simple
Long term – fund based – Cash credit	Simple
Short term – Non fund based – Bank guarantee	Very simple
Long term / Short term – unallocated limits	Not applicable

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Term Loan-I**	FY2022	NA	FY2028	2.50	[ICRA]BB+(Stable)
NA	**Term Loan-II**	FY2023	NA	FY2029	2.50	[ICRA]BB+(Stable)
NA	**Cash credit**	NA	NA	NA	87.00	[ICRA]BB+(Stable)
NA	**Bank guarantee**	NA	NA	NA	6.50	[ICRA]A4+
NA	**Unallocated limits**	NA	NA	NA	0.06	[ICRA]BB+(Stable)/[ICRA]A4+

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis: Not applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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