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Mumbai

CRISIL Equities assigns IPO grade 3/5 to VRL Logistics Limited

CRISIL Equities has assigned a CRISIL IPO grade of "3/5" (pronounced "three on five") to the proposed initial public offer (IPO) of VRL Logistics Limited (VRL). This grade indicates that the fundamentals of the IPO are average relative to other listed equity securities in India. However, this grade is not an opinion on whether the issue price is appropriate in relation to the issue fundamentals. The grade is not a recommendation to buy, sell or hold the graded instrument, or a comment on the graded instrument's future market price or its suitability for a particular investor.

The assigned grade reflects VRL's position as one of the leading players in the domestic freight transportation business and the robust outlook for the logistics sector. CRISIL Research expects the industry to grow at 11% CAGR to Rs 4.6 tn in 2013-14. A strong network of 859 self-owned and franchise branches, 44 transshipment hubs and a fleet of 2,573 trucks enables VRL to offer logistics solutions to a diversified base of customers across India and also focus on the high-margin less than truck load (LTL) business. The company primarily caters to small and mid-sized companies, which reduces the business concentration risk. During the six months period ended September 30, 2010, no single customer contributed more than 2% of revenues and the 10 largest customers accounted for only 5.08% of revenues. VRL has also established a strong presence in passenger transportation services in Karnataka, Maharashtra and Goa, and plans to enter other high-growth metropolitan and Tier 2 cities in western, central and northern India. The grade is further supported by a strong second line of management.

The grade is moderated by VRL's historically aggressive debt-funded expansion program which resulted in high gearing and strained its financials. We have taken into account the inherent cyclicality of the transportation industry, where VRL operates an asset-heavy business model; this makes it difficult for the company to adjust its capacity to recession-led reduced freight availability. Further, the company's management information system has scope for improvement.

About the company and the issue

Established in 1976, VRL is a transportation and logistics service provider based in Hubli, Karnataka. It is the largest private sector owner of commercial vehicles with a fleet of 2,573 trucks and 256 buses. VRL operates goods transportation services across 534 cities in 20 states and six union territories, supported by a strong network 436 self-owned branches and 423 exclusive franchise offices. It has established 44 transshipment hubs which offer flexibility to transport a broad range of goods and services to multiple destinations. VRL launched passenger transportation services in 1996 and currently offers these services in 93 cities of Karnataka, Maharashtra and Goa, along 188 routes.

VRL's revenues increased at a CAGR of 14.1% between FY08 and FY10 to Rs 7.1 bn on the back of huge expansion in fleet size and stable contribution from the wind power business. EBITDA margins declined from 19.8% in FY08 to 16.7% in FY09 as the company did not pass on the incremental cost to the customers following the economic downturn. However, EBITDA margin rebounded in FY10 to 19.4% close on the heels of economic revival, which supported freight availability and freight rates. The increased operating cash flow helped the company reduce its borrowings resulting in lower interest cost. VRL's profit increased at a CAGR of 96% between FY08 and FY10 to Rs 288.7 mn.

VRL will utilise the IPO proceeds to a) buy vehicles for the passenger and goods transportation business (Rs 1.4 bn), b) prepay certain loans availed by the company (Rs 1.1 bn) and c) for general corporate purpose.

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CRISIL IPO (Initial Public Offering) Grading is an opinion on the fundamentals of the graded issue that reflects CRISIL's independence and expertise. This opinion is expressed as a relative assessment in relation to other listed equity securities in India. The assessment is based on a grading exercise carried out by industry specialists from CRISIL Research. A CRISIL IPO Grade 5/5 indicates strong fundamentals and a CRISIL IPO Grade 1/5 indicates poor fundamentals. CRISIL IPO Grading reflects its assessment of the graded company's equity fundamentals as distinct from an assessment of debt fundamentals. A CRISIL IPO Grade should not be construed to mean a comment on the price of the graded security nor is it a recommendation to invest or not to invest in the graded security.

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