Talbros Engineering Limited

August 04, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	4.43 (Enhanced from 1.63)	CARE A-; Stable (Single A Minus; Outlook: Stable)	Revised from CARE BBB+; Positive (Triple B Plus; Outlook: Positive)
Long Term / Short Term Bank Facilities	60.00 (Reduced from 62.80)	CARE A-; Stable / CARE A2+ (Single A Minus; Outlook: Stable/ A Two Plus)	Revised from CARE BBB+; Positive / CARE A2 (Triple B Plus ; Outlook: Positive / A Two)
Total Bank Facilities	**64.43 (Rs. Sixty-Four Crore and Forty-Three Lakhs Only)**		

Details of instruments/facilities in Annexure-1.

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Talbros Engineering Limited (TEL) factors in continued improved performance during FY22 (refers to period April 01 to March 31) marked by higher than envisaged total operating income and profitability margins on the back of growing demand from exports, commercial vehicles and utility vehicles along with improvement in financial risk profile characterized by low overall gearing and healthy debt coverage indicators. The ratings also continue to derive strength from the experienced promoters along with their long track record of operations, diversified segment base and reputed customer-base by virtue of their long-standing relationship with Original Equipment Manufacturers (OEMs). However, the ratings continue to remain constrained by modest scale of operations, susceptibility of margins to volatility in raw material prices along with exposure to foreign fluctuation risk, working capital intensive operations, dependence on the fortunes and cyclical nature of the auto industry.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- Sustained improvement in the scale of operations with beyond Rs 600 crore along with improvement in PBILDT margin above 15% and increase in share of business on sustained basis
- Sustained improvement in return on capital employed (ROCE) beyond 21%

Negative factors – Factors that could lead to negative rating action/downgrade:

- Decline in total operating income below Rs 300 crore
- Decline in PBILDT margin below 11%
- Any un-envisaged debt-funded capital expenditure deteriorating its capital structure at above 0.50x

Detailed description of the key rating drivers

Key rating strengths

Improved operational performance albeit modest scale of operations:

The improvement in the operational performance of the company during FY22 is reflected by increase in volume from 15.64 lakh units to 19.56 lakh units of axle shafts along with improvement in per unit realisation rate from Rs. 1,476 to Rs. 1,714 in FY22 backed by recovery in the auto industry except tractors, demand of which, remained low throughout the year. Further, increase in other operating revenue from Rs 8.27 crore to Rs 17.08 crore, majorly consisted of scrap sales and duty drawback also contributed towards improved operational performance. Even though, the company had modest scale of operations whereby its total operating income stood at Rs.352.24 crore during FY22 (PY: Rs 239.14 crore), however the same is mitigated by the company's continued focus on exports and long association with its customers. The PBILDT margin of TEL also improved by 134 bps from 11.76% in FY21 to 13.11% in FY22 on account of reduction in expenses of power and fuel, employee costs and manufacturing expenses like processing charges and repairs and maintenance of P&M, building etc as company is constantly moving towards automation, lean manufacturing techniques and higher efficiency by continuously adding up robotic technologies thereby helping in reduction of factory lead time, efficient use of material along with replacement of old machines with Vertical Machining Centre (VMC) and Computer Numerical Control (CNC)which has reduced dependence on highly skilled labour.

Long track record of operations with experienced and resourceful promoters

TEL has a long track-record of operations dating back to 1980 and was earlier part of the erstwhile Talbros Group. The Talbros Group was founded in 1930s by Talwar family and has been into manufacturing of automotive components since 1957. The key managerial personnel of TEL - Mr. Rajesh Talwar, President and Mr. Tarun Talwar, Chief Operating Officer have a vast experience in the automotive and engineering industry and are actively involved in the day-today operations of the company. The promoters have supported the company with infusion of unsecured loans which stood at Rs.20.52 crore as on

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

March 31, 2022 (Rs.14.63 crore as on March 31, 2021).

Reputed client base with long standing relationship
TEL has a long and established relationship with reputed OEMs and Tier-1 suppliers. Its top revenue contributors are well established players who enjoy strong market position in the industry like Mahindra & Mahindra, Ashok Leyland, Spicer India limited etc and is the sole supplier of rear axle shafts to most of its customers for their specific models. The company is also focussing on exports which contributed ~25% of the gross sales in FY22.

Diversified Segment base
The company caters to the axle requirements of varied segments, thereby insulating it from the volatility in any one segment. The company derives major share of its revenue from the Utility Vehicles segment contributed 47% to the total gross sales during FY22 (PY: 47%) followed by Commercial Vehicle segment contributed 20% to the total gross sales during FY22 (PY: 18%) and tractors segment contributed 4% to the total gross sales during FY22 (PY: 6%) in the domestic market. Further, the company also has presence into the exports (primarily replacement market) which contributed around 25% to the total gross sales during FY22 (PY: 25%), thereby also leading to geographical diversification.

Comfortable financial risk profile
The overall gearing of TEL stood comfortable at 0.69x as on March 31,2022 (PY: 0.71x). The same improved marginally due to the repayment of short-term debt taken in FY21 along with the increase in the net-worth base due to the accretion of profits and infusion of funds by the promoters in the form of subordinated debt which is partially offset by term loan taken for purchase of land and capacity expansion from 21 lakh unit to 24 lakh unit. With improvement in profitability, the debt coverage indicators also improved and stood comfortable. The interest coverage ratio and total debt to GCA stood at 5.46x and 2.56x as on March 31,2022 respectively (PY: 4.81x and 3.30x respectively).

Key rating weaknesses
Working Capital intensive operations:
Being in the auto ancillary industry, the operations of the company are working capital intensive in nature. The company maintains inventory of around 2-3 months with large product range of axle shafts and spindles. The average debtor days usually remain in the range of 60 days as its OEMs have higher bargaining power. Further, the creditors period remains in the range of 2-2.5 months. The company's operating cycle, though improved, remained elongated at 73 days as on March 31, 2022 (PY: 77 days).

Cyclical nature of the automotive industry:
The automobile industry is cyclical in nature and automotive component suppliers sales are directly linked to sales of auto OEMs. Furthermore, the auto-ancillary industry is competitive with the presence of a large number of players in the organized as well as unorganized sector. While the organized segment majorly caters to the OEM segment, the unorganized segment mainly caters to the replacement market and to tier II and III suppliers.

Low bargaining power with customers and susceptibility of margins to volatility in raw material prices along with the presence of foreign fluctuation risk
Though, there exists limited bargaining power with the customers, since the major customers are auto companies/OEMs, however, the company does have a mechanism wherein any revision beyond 5% in the raw material prices, is reset by the OEMs on quarterly/half yearly basis. The major raw material (steel) cost accounts for around 55% of total cost of sales in FY22 (PY: 53%), furthermore, global prices for steel are volatile which exposes TEL to price risk. Further, the company is also engaged in exports of axles shafts which exposes it to forex risk, though, based on the management's insight and market information, the company enters into hedging to cover part of its foreign exchange risk. Due to the currency fluctuations company reported gain on foreign exchange transactions of Rs. 1.09 crore during FY22 (PY: Gain of Rs. 0.28 crore).

Industry Outlook:
The long-term growth outlook for the Indian auto industry is positive, driven by robust economic growth outlook, focussed government policies with vision for 2047, government focus on road and infrastructure development, increasing income levels, current low levels of vehicle penetration, rapid urbanisation, growing demand for farm mechanisation, emergence of newer technologies in the farming sector, increasing Government spend in rural sector, and continued focus of government on improving the state of agriculture in India. However, concerns regarding supply chain constraints due to the ongoing geopolitical tensions also persist. In addition, the second hike in repo rates by RBI, along with an increase in third party insurance rates from June 2022, might hurt the demand sentiments in the near term.

Liquidity: Adequate
The company has adequate liquidity as characterized by sufficient cushion in expected gross cash accruals of Rs.36.46 crore vis-à-vis repayment obligations of Rs.9.58 crore during FY23. Going forward, the company has planned to incur capex of Rs. 30 crore which will be spread over FY23 and FY24, out of which Rs 11 crore shall be routine in nature and remaining for setting up of an additional unit in Faridabad. The company proposes to use internal accruals for setting up of new unit, however, the debt has already been tied-up in the debt equity ratio of 67:33. The company has sufficient headroom to raise debt going forward with comfortable capital structure having an overall gearing below 1x. Its bank limits are utilized to the extent of 75% for the

past twelve months ending June 30, 2022 and has above unity current ratio with operational cash flows of Rs 16 crore during FY22 (PY: Rs.11.54 crore).

Analytical approach: Standalone

Applicable criteria
Policy on default recognition
Financial Ratios – Non-financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Auto Ancillary Companies
Manufacturing Companies

About the company
Talbros Engineering Ltd (TEL), originally a part of Talbros Automotive Components Ltd. was separated into another company in 1996. TEL is engaged in the manufacturing of automotive rear axle shafts and other splined shafts and forgings used in commercial vehicles, utility vehicles and tractors. TEL has total five manufacturing plants with total manufacturing capacity of 24 lakhs axle shafts per annum as on March 31, 2022. The company manufactures and sells 75% of its products to OEMs in the domestic market and remaining 25% are exported, primarily to the replacement market of North America.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	Q1FY23 (UA)
Total operating income	239.14	352.24	NA
PBILDT	28.13	46.16	NA
PAT	10.65	22.10	NA
Overall gearing (times)	0.71	0.69	NA
Interest coverage (times)	4.81	5.46	NA

A: Audited; UA: Unaudited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term Loan		-	-	Sept-26	4.43	CARE A-; Stable
Fund-based - LT/ ST-Cash Credit		-	-	-	60.00	CARE A-; Stable / CARE A2+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Term Loan	LT	4.43	CARE A-; Stable	-	1)CARE BBB+; Positive (15-Sep-21)	1)CARE BBB+; Negative (08-Oct-20)	1)CARE BBB+; Stable (11-Dec-19) 2)CARE A-; Negative (02-Aug-19)
2	Fund-based - LT/ ST-Cash Credit	LT/ST*	60.00	CARE A-; Stable / CARE A2+	-	1)CARE BBB+; Positive / CARE A2 (15-Sep-21)	1)CARE BBB+; Negative / CARE A2 (08-Oct-20)	1)CARE BBB+; Stable / CARE A2 (11-Dec-19) 2)CARE A-; Negative / CARE A2+ (02-Aug-19)

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities: Not Applicable

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based - LT-Term Loan	Simple
2	Fund-based - LT/ ST-Cash Credit	Simple

Annexure-5: Bank lender details for this company

To view the lender wise details of bank facilities please click here

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
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