Centum Electronics Limited (Revised)

November 8, 2022

Ratings

Facilities	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	196.70	CARE BBB; Stable (Triple B; Outlook: Stable)	Reaffirmed
Long-term/short-term bank facilities	159.00	CARE BBB; Stable/CARE A3+ (Triple B; Outlook: Stable/ A Three Plus)	Reaffirmed
Total bank facilities	**355.70 (₹ Three hundred fifty-five crore and seventy lakh only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

The ratings assigned to the bank facilities of Centum Electronics Limited (CEL) continue to derive strength from the business vintage of close to three decades; the experienced promoters; the established association with a reputed clientele base, from which CEL has been receiving repeat orders; the above-average financial risk profile, marked by consistent debt reduction and consequent improvement in the capital structure. While the company's profitability was impacted during Q1FY23, it is likely to improve gradually, considering that the billing for the Strategic Electronic Business Unit (SEBU) commences during the second half of the financial year. The ratings also take note of the comfortable order book size of CEL, which augurs well for its growth in the near to medium term.

These ratings strengths are partially offset by the working capital-intensive operations and its exposure to the French subsidiary, Centum T&S (CTS; erstwhile Centum Adetel Group), which has been incurring losses. CEL's management has guided that the operations of CTS are self-sustainable, and therefore, it does not require any financial support from CEL. However, any financial assistance from CEL to CTS, leading to the weakening of CEL's liquidity, will weigh negatively on its credit profile.

Rating sensitivities

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

- Increase in the scale of operations beyond ₹500 crore while maintaining ROCE >12%.
- Total debt (TD)/gross cash accruals (GCA) <3x.

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

- Unforeseen financial support to CTS, adversely impacting the debt protection metrics of CEL.
- Significant decline in the scale of operations and overall gearing >1.5x.

Detailed description of the key rating drivers

Key rating strengths

Experienced promoters and established track record: Apparao V Mallavarapu Rao, Chairman and Managing Director (CMD), has more than three decades of experience in managing the electronics business. CEL is engaged in the business of designing and manufacturing high-end electronics modules, systems and subsystems, since 1994. He has ventured into and successfully managed joint ventures (JVs) with several multinational companies. The CMD is supported by Nikhil Mallavarapu, Executive Director, and Dr Swarnalatha Mallavarapu, Non-Executive Director. The company has a high level of corporate governance with six independent directors and the support of the managerial team with a vast experience in the field of electronics system designing and manufacturing.

Diversified product and revenue mix across different geographies and industries: The company's offerings range from customised product design and development, manufacturing services, and turnkey solutions for mission-critical applications in the defence, aerospace, space, industrial, medical and communications industries. The company broadly operates under two business segments, namely, SEBU and the Electronics Manufacturing Solutions Business Unit (EMS).
CTS (a subsidiary of CEL) has an engineering division in France, with electronic system designing capabilities in the industrial sector. The acquisition of CTS by CEL was primarily to take advantage of CTS' designing capabilities in the industrial sector, as

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

CEL's designing is largely limited to the defence and aerospace industries. While the synergy is yet to take place, however, under a steady state, CEL will become a one-stop solution to all the companies across sectors for their electronic manufacturing and design needs.

Established association with a reputed clientele base: CEL has delivered mission-critical electronics on almost all satellite programmes of the Indian Space Research Organisation (ISRO), including the ambitious Chandrayaan and Mangalyaan projects, and also delivered 300-500 components for almost every Indian space mission.

The clientele base consists of reputed defence segment and aerospace research organisations such as the Space Application Centre, ISRO, Defence Research and Development Organisation (DRDO), ABB, Thales, Rafale, etc.

Above-average financial profile, marked by satisfactory coverage indicators: CEL's revenue has declined during FY21 and further in FY22. The SEBU division was impacted by the COVID-19 lockdown. Post-lifting of the lockdown, the industry faced a severe shortage of semiconductors and containers, increasing the lead time. Also, the orders forecasted from the EMS division were delayed by the clients due to uncertainties in the business environment.

CEL's turnover declined by 18.7% to ₹348 crore in FY22, which further led to a decline in the profit before depreciation interest and taxes (PBDIT) margin. However, the collection period of the company has been improving, translating into higher cash flow from operations and a consequent reduction in debt levels. With a sizeable order book in hand, the company is likely to maintain growth and profitability in the near to medium term, despite the continuing challenges on the supply side. The company's debt coverage indicators and capital structure continue to remain satisfactory.

Key rating weaknesses

Working capital-intensive nature of operations: Amid the shortage of containers and semiconductors, the lead time and procurement costs have increased. The procurement orders are placed based on the client's acceptance to absorb the price difference and pay advances to reduce the lead time. CEL has been able to collect the advances for executing the orders and the reliance on the working capital (WC) limits has reduced in recent months.

The WC limits are not expected to increase and the company expects the semiconductor and container shortage to continue during FY23. Post ease of the above-mentioned constraints, CEL plans to undertake a capex of ₹25-30 crore in the SEBU division.

Investment in the loss-making subsidiary but no guarantee or commitment by CEL towards debt servicing: CEL took over Adetel in 2016, which was a stressed asset, and is currently named CTS. At the time of acquisition, Adetel had two divisions – an Energy division and an Engineering division. The Energy division was incurring losses, as finding a market was challenging, and it was sold off in FY20. CTS' operations were envisaged to be profitable subsequently but were impacted by the COVID-19 pandemic. Considering the high debt repayments in the near to medium term, CTS' operations must turn around as per the envisaged timelines.

CEL has the Put option liability to purchase an additional stake in CTS from its existing shareholders. CEL does not estimate any financial support required to be extended to CTS.

Liquidity: Adequate

The liquidity is adequate, with expected improvement in cash accruals, aided by a recovery in business and an improved order book position. The current ratio of the company stood at 1.19x as on March 31, 2022 (PY: 1.18x). The company had a cash and bank balance of ₹15.21 crore as on March 31, 2022. With improvement in the collection cycle and customer advances, the average WC utilisation has come down in recent months and the average utilisation was at 67% for the last 12 months ending August 31, 2022.

Analytical approach

Standalone, along with factoring in the support to CTS, a subsidiary of CEL.

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
Manufacturing companies

About the company

CEL was founded in 1994 in Bengaluru by Apparao V Mallavarapu (Rao), a first-generation entrepreneur. The company is into the design and manufacturing of electronic systems and manufactures high-end electronic modules, subsystems and systems used in the aerospace, defence, and industrial electronics sectors.

Brief Financials (₹ crore)	March 31, 2021 (A)	March 31, 2022 (A)	June 30, 2022 (UA)
TOI	428.00	348.01	99.41
PBILDT	65.94	42.60	7.34
PAT	23.98	11.77	(0.01)
Overall gearing (times)	0.58	0.39	NA
Interest coverage (times)	3.96	2.97	2.22

A: Audited; UA: Unaudited; NA: Not available.

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 the covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of the 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/ ST-CC/PC/Bill discounting	-	-	-	-	159.00	CARE BBB; Stable/CARE A3+
Non-fund-based - LT-Bank guarantee	-	-	-	-	196.70	CARE BBB; Stable

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/ ST-CC/PC/Bill discounting	LT/ST*	159.00	CARE BBB; Stable/ CARE A3+	1)CARE BBB; Stable/ CARE A3+ (01-Apr-22)	1)CARE BBB; Stable/ CARE A3+ (18-May-21)	-	-
2.	Non-fund-based - LT-Bank guarantee	LT	196.70	CARE BBB; Stable	1)CARE BBB; Stable (01-Apr-22)	1)CARE BBB; Stable (18-May-21)	-	-

*Long term/Short term.

Annexure-3: Detailed explanation of the covenants of the rated instruments/facilities

Working Capital Facilities	Detailed Explanation
A. Financial covenants	
I. Adjusted total net worth (TNW)	ATNW> = ₹217 crore
Ii. Total outside liabilities (TOL)/adjusted quasi TNW	TOL/adjusted quasi TNW <1
Iii. Interest cover	Interest cover >3x
B. Non-financial covenants	None

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

Sr. No.	Name of Instrument	Complexity Level
1.	Fund-based - LT/ ST-CC/PC/Bill discounting	Simple
2.	Non-fund-based - LT-Bank guarantee	Simple

Annexure-5: Bank lender details for this company

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

Note on the 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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