Talbros Engineering Limited

September 15, 2021

Ratings

Facilities/Instruments	Amount (Rs. crore)	Ratings	Rating Action
Long Term Bank Facilities	1.63 (Reduced from 5.59)	CARE BBB+; Positive (Triple B Plus; Outlook: Positive)	Reaffirmed; Outlook revised from Negative
Long Term / Short Term Bank Facilities	62.80	CARE BBB+; Positive / CARE A2 (Triple B Plus; Outlook: Positive/ A Two)	Reaffirmed; Outlook revised from Negative
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 ratings assigned to the bank facilities of Talbros Engineering Limited (TEL) continue to derive strength from the experienced promoters along with their long track record of operations, and reputed customer-base by virtue of their strong association and long-standing relationship with Original Equipment Manufacturers (OEMs) including Mahindra and Mahindra Limited among others. The rating also favorably factors in TEL's market position in axle shafts for the utility vehicles segment, growing traction from the export market, improvement in the profitability margins and comfortable financial risk profile characterized by low overall gearing and healthy debt coverage indicators.

However, the ratings continue to remain constrained by modest scale of operations, customer concentration risk, susceptibility of margins to volatility in raw material prices and dependence on the fortunes and cyclical nature of the auto industry.

<u>Rating Sensitivities</u>

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

- Sustained improvement in the top-line along with sustenance of profitability with growing business from exports.
- Ability to maintain the overall gearing at current levels after factoring in the planned debt-funded capex in a phased manner.

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

- Decline in the Total Operating Income below Rs.165 crores with low profitability on a sustained basis.
- High reliance on debt to fund large capex and increase in working capital borrowings leading to moderation in overall gearing of more than 1.20x.

<u>Outlook: Positive</u>

The revision in the outlook of Talbros Engineering Limited from 'negative' to 'positive' reflects the faster than envisaged recovery in operational performance backed by buoyant demand in the automotive industry. Furthermore, the rating outlook revision to positive reflects CARE's expectation of improved scale and profitability of the company in the near to medium term. The outlook may be revised to Stable in case of lower than envisaged improvement in sales and profitability, going forward.

Detailed description of the key rating drivers

Key Rating Strengths

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.14.63 crore as on March 30, 2021 (Rs.11.97 crore as on March 31, 2020).

Reputed customer base with established relationship albeit concentrated

TEL has an established relationship with leading auto manufacturers and the company is the TIER-1 vendor to these OEMs dealing with them from the past 15 years. Its top revenue contributors are well established players who enjoy a strong market position in the industry. The company derives major share of its revenue from Mahindra and Mahindra Limited, which contributed ~38% to the total gross sales in FY21 *(refers to the period from April 01 2020 to March 31 2021)* (PY:44% of its total gross sales) with top-5 customers contributing around 83% to its top-line during FY21 (PY: 82%), thereby exposing the company to customer concentration risk. However, the same is mitigated to an extent as the company is the sole supplier of rear axle shafts to most of its customers for their specific models.

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 49% to the total gross sales during FY21; PY: 55%) followed by Commercial Vehicle segment (contributed 19% to the total gross sales during FY21; PY: 19%) and tractors segment (contributed 7% to the total gross sales during FY21; PY: 5%) 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 FY21 (PY: 21%), thereby also leading to geographical diversification.

Improved operational performance
The profitability margins of the company stood comfortable. The PBILDT margin improved by 254 bps and stood at 11.79% during FY21 (PY: 9.24%) driven by change in the sales composition towards high margin export business. Further, the PAT margin also improved and stood at 4.45% during FY21 as against 1.80% during FY20 due to the reduction in finance cost.

Q1FY22 (refers to the period from April 01, 2021 to June 30, 2021) Performance: The company reported total operating income of Rs.67.54 crore during Q1FY22 as against Rs.16 crore during Q1FY21. The improvement is backed by the fact that Q1FY21 was an exceptional period due to the nation-wide lockdown. The PBILDT margin remained almost stable at 12.20% during Q1FY22 (Q1FY21: 12.75%). Further, in comparison to the Q1FY20 top-line of Rs.61.14 crore, the company recorded around 10% growth in Q1FY22.

Comfortable Financial Risk Profile
The overall gearing of TEL stood comfortable at 0.71x as on March 31,2021 (PY: 0.79x). The same improved marginally due to the repayment of long-term debt vis-à-vis 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. With improvement in profitability, the debt coverage indicators also stood comfortable. The interest coverage ratio and total debt to GCA stood at 4.82x and 3.30x as on March 31,2021 respectively (PY: 2.79x and 4.60x respectively).

Key Rating Weaknesses
Modest scale of operations however albeit growing
Though, the scale of operations of the company remained modest however, the same reported y-o-y growth by ~10% to Rs.239.21 crore during FY21. The same was due to the better realizations with increase in the proportion of sales from the export market (contributed ~25% to the sales during FY21 as against ~21% in the previous year) and increased share of business with one of the key customers.

Low bargaining power with customers and susceptibility of margins to volatility in raw material prices
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 the given threshold limit in the raw material prices, is reset by the OEMs on monthly basis. The major raw material (Steel) cost accounts for around 53% of total cost of sales in FY21 (PY: 54%), furthermore, global prices for Steel are volatile which exposes TEL to price risk.

Industry Prospects
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 many 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.
As per CARE research, considering the normal and optimistic scenario for the industry, the Passenger Vehicle segment (comprising of Passenger Cars, Utility Vehicles and Vans) is expected to grow in the range of ~12-17% in FY22. Over the ten years between FY11 and FY21, the UV segment have witnessed good growth of 12.9% CAGR. UV, as a share of PV, has increased from 12.6% in FY11 to 39.1% in FY21. This growth in UV is driven by increased customer preference for UV styled vehicles and a shift from compact cars to compact UVs.
The demand-supply imbalance has been created in the industry due to the supply-side disruptions caused by the shortage of semiconductors, which find application in the automotive industry. Chips are used in some of the models of SUVs/UVs, where TEL is expected to incur marginal loss of domestic OEM sales. However, the loss of domestic sales is expected to be compensated with the increasing export sales. Exports increased by ~44% to Rs.9.2 cr. in Aug,2021 from Rs.6.4 cr. in FY20.

Liquidity: Adequate
The company has adequate liquidity as characterized by sufficient cushion in expected gross cash accruals of Rs.23.20 crore vis-à-vis repayment obligations of Rs.6.24 crore during FY22 and modest cash and bank balance of Rs.3.74 crores as on March 31, 2021. Going forward, the company has planned to avail capex of Rs.40 crore in FY22 and FY23 for capacity enhancements primarily to cater to growing export demand, out of which Rs.8 crore would be routine in nature and for the same, 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, 2021 and has above unity current ratio.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch'
CARE's Policy on Default Recognition
Rating Methodology-Manufacturing Companies
Criteria for Short-term Instruments
CARE's methodology for auto ancillary companies
CARE's methodology for financial ratios (Non-Financial Sector)
Liquidity analysis-Non-financial sector entities

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 21 lakhs axle shafts per annum as on March 31, 2021. 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 (Rs. crore)	FY20 (A)	FY21 (A)
Total operating income	217.35	239.21
PBILDT	20.09	28.20
PAT	4.02	10.65
Overall gearing (times)	0.79	0.71
Interest coverage (times)	2.79	4.82

A: Audited

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: *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	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	April,2022	1.63	CARE BBB+; Positive
Fund-based - LT/ ST-Cash Credit	-	-	-	62.80	CARE BBB+; Positive / CARE A2

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Fund-based - LT-Term Loan	LT	1.63	CARE BBB+; Positive	-	1)CARE BBB+; Negative (08-Oct-20)	1)CARE BBB+; Stable (11-Dec-19) 2)CARE A-; Negative (02-Aug-19)	1)CARE A-; Stable (04-Jan-19)
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	62.80	CARE BBB+; Positive / CARE A2	-	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)	1)CARE A-; Stable / CARE A2+ (04-Jan-19)

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

Name of the Instrument	Detailed explanation
A. Financial covenants	
I. Fund-based Limits	• Debt service coverage ratio: Company shall at all times maintain debt service coverage ratio of 1.2x • Adjusted Leverage Ratio: Company shall ensure that leverage ratio shall, at all times, not exceed the maximum leverage ratio of 2.5x. • Debt/EBITDA should less than equal to 3.5x as per ABS of FY21.
B. Non-financial covenants	
I. Cash Credit	• Statement of stock and book debts, on a monthly basis, to be submitted latest by the 25th of subsequent month. *Note: The utilization in WCDL/CC will be determined by Drawing Power on the basis of monthly stock statements submitted. The computation drawing power would be as follows:* *75% on (Book Debts less than 120 days Plus Stock minus Creditors)*

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

Sr. No.	Name of the 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

Click here to view Bank Lender Details

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

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About CARE Ratings:

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