Munitions India Limited

September 10, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	2,000.00 (Reduced from 3,000.00)	CARE AA+; Stable	Reaffirmed
Long-term / Short-term bank facilities	1,000.00	CARE AA+; Stable / CARE A1+	Assigned

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Ratings assigned to bank facilities of Munitions India Limited (MIL) derives strength from its strategic importance to the Government of India (GoI), established market position in defence sector and healthy order book. The rating is also underpinned by large manufacturing capacities with adequate pool of trained manpower, high entry barrier within the industry limiting competition, comfortable capital structure marked by strong net worth, support extended by government through infusion of funds towards capex requirements, and minimal reliance on working capital borrowings as the company is receiving 60% of orders executable in the fiscal year in the form of advance and remaining 40% on delivery for its existing orders. CARE Ratings Limited (CARE Ratings) also notes the company's foray in exports of ammunitions to diversify its revenue streams which contributed ~23% in FY24 and winning of tenders floated by Army, Navy and Airforce post corporatisation. As the company's current employees are on deemed deputation from Ministry of Defence, the pension, gratuity and other ancillary employee expenses are to be borne by government. However, deemed deputation is set to over by September 30, 2024, and new policy with respect to deemed deputation shall remain a key monitorable. These strengths are partially offset by high dependence on the defence sector, which contributes to the bulk of its revenues and its working capital-intensive operations due to high inventory and receivables. Furthermore, operating profit margins remain vulnerable to input cost fluctuations in its fixed price defence contracts despite this is mitigated to certain extent with the presence of price escalation clause and long-term contracts with suppliers for supply of raw material. The rating is also constrained considering teething challenges faced by new Defence Public Sector Undertakings (DPSU's) in converting to a company and qualified audit report; despite clean report from Comptroller and Auditor General (CAG). Going forward, to receive orders from defence, MIL has to continue participating in tenders and would face competition from private sector, and its ability to convert these tenders in orders remain to be seen.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Significantly and sustainably improving operating performance by 10% to 15% leading to higher cash accrual.
- Total debt to profit before interest, lease rentals, depreciation, and taxation (TD/PBILDT) improving to below 0.75x.
- Gross current asset days sustaining under 200 days.

Negative factors

- Diluting stake of GoI to below 51% in the company.
- Changing stance of GoI support to MIL reflecting in lower order inflows and revenues.
- Weakening of operating performance leading to significantly declining margin and constrained liquidity.
- Large debt-funded capex or sizeable working capital requirement weakening the capital structure beyond 0.5x.

Analytical approach: Standalone and factoring its 100% ownership by GoI for which it is a strategically important entity in the defence sector.

Outlook: Stable

The stable outlook reflects the rated entity likely to maintain its established position in defence sector and will continue to remain strategically important to GoI.

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

Detailed description of key rating drivers:

Key strengths

Highly strategic importance to GoI as a DPSU and a dominant supplier to Indian defence forces

MIL is wholly owned by GoI. Cabinet committee on security (CCS) in its meeting held on July 29, 2020, approved to convert Ordnance Factory Board (OFB), an attached office of Ministry of Defence (MoD), in over one 100% government-owned corporate entities registered under the Companies Act 2013. The cabinet meeting held on June 16, 2021, approved to convert 41 production units of OFB into seven DPSUs. MIL is one such seven DPSUs. Accordingly, 12 production units and three non-production units of erstwhile OFB, pertaining to production of ammunition and explosives were transferred to MIL on October 01, 2021. MIL took over ammunition and explosives from the erstwhile OFB.

Established client and product base

MIL, being in the defence sector, has established products in relation to defence and its customer primarily is the armed forces. MIL's product portfolio includes small, medium and large calibre ammunition, naval ammunition, mortar and aerial bombs, grenades, propellants, tank ammunition, multi barrel rocket, explosives, smoke, and pyrotechnics. The company sells its products to Army, Navy, Ministry of Home Affairs (MHA) and Air Force. The company also exports its products. These factories have been producing ammunitions and high explosives for over 150 years.

Accredited manufacturing units spread across India

MIL is engaged in production, testing, research and development, and marketing of comprehensive range of ammunition and explosives for Army, Navy, Air force and Para-Military forces. It has 12 manufacturing units, which are across India, and ~23000 workforces. MIL's units are certified with ISO-9001:2015 (for quality management system), ISO 14001:2015 (for environment management safety), ISO 145001:2018 (for occupational health and safety management system), ISO/IEC/17025 (for national accreditation board for testing and laboratories), and ISO 50001:2018 (for energy and management systems).

Robust order book providing adequate revenue visibility

The company's unexecuted order book as on August 31, 2024, stood at~ ₹24,000 crore which includes export orders worth ₹5500 crore. The order book stands at ~3.30x of the FY24 operating income, which provides adequate revenue visibility. To run these DPSU's indents placed up to September 30, 2021 on erstwhile OFB have been converted into deemed contracts, and every year, 60% amount of these contracts for supply of respective products pertaining to that year's target is being paid by the Ministry of Defence Services to DPSUs as advance per the terms and conditions stipulated in the deemed contract and these are interest free. Additionally, the government's focus on rolling out reforms to increase India's defence product manufacturing capability and gradually reduce imports will support the order inflow in the medium-to-long term. CARE Ratings anticipates that in the coming years these new DPSUs would explore and establish newer markets in the country and abroad and become self-sustainable.

Significant support from GoI

MIL being a DPSU and owned entirely by GoI has significant support and involvement from the government. The company has robust order book of ~₹18,500 crore from MoD to be executed by FY27. Further, the funding for the capex is being provided by the government. In FY24, government infused ~₹580 crore for capex. Going forward, in next two years, the company plans to incur capex of ~₹1500 crore which will be partly funded by GoI. Furthermore, upon corporatisation of the erstwhile OFB, OFB's employees have been transferred to the company on deemed deputation for an initial period of two years, which was later extended by one more year (till September 2024). Employees continue to be the employees of GoI and their gratuity and pension liability continue to be the obligation of the central government. However, CARE Ratings notes that deemed deputation is set to get over by September 2024 and the policy/decision taken by the government and its impact on MIL shall remain a key monitorable.

Professional management, functional and financial autonomy to improve profitability

With professional management, functional and financial autonomy and more accountability, restructuring will help in making these DPSUs more productive and profitable assets, enhance competitiveness and improving efficiency, and also aid in exploring newer markets, in the country and abroad. Newly created DPSUs have the potential to earn profit from their supplies to services, other government organisations (like MHA), civil trade and exports through participation in competitive bidding.

Rising exports mitigating the customer concentration risk to some extent

MIL bids for defence projects floated by the army, navy and air force. In FY24, Indian army remained as major customer, accounting for ~51% of the turnover. While army contributed the bulk of MIL's revenue, however considering increased exports, dependency on this has significantly come down from the previous year where the contribution from army stood at ~67%. In

FY24, ₹1697 crore (~23%) of the revenue is contributed by the export market which is a considerable improvement from earlier ~5%. The company continues to derive ~70% of its total revenue from MoD (Army, Navy, Airforce) and MHA. Due to the high concentration of government sector orders, revenue booking, and cash flows are vulnerable to delays in project execution or final payment clearance in some cases. Furthermore, it has significant exposure to MoD under GoI which relies on budgetary means to clear its dues.

Improving overall performance

The company's performance in FY24 has improved in terms of revenue and operating margins. The revenue has grown by ~56% to ₹7256 crore from ₹4652 crore reported in FY23. Along with revenue, PBILDT margins have also improved to 6.85% from (0.59%) reported in FY23. In FY24, the company has also exported arms and ammunitions, which contributed to improved revenue and profitability.

Comfortable financial risk profile

The company's capital structure is strong with no debt outstanding though there are capex LC's open of ₹945 crore. The company has fund-based facilities of ₹2000 crore which was not utilised. The company does not plan to avail term debt for its capex, as this will be funded by GoI and through internal accruals. CARE Ratings expects MIL's financial risk profile to remain comfortable going forward,

Key weaknesses

Working capital intensive business

The company operates in a working capital intensive industry. The company manufactures over 1500 types of products of different calibres. To manufacture these, vide variety of products company needs to, on an average, maintain raw material inventory of ~₹2500 crore- ₹3000 crore. Further, in FY24, finished and semi-finished goods amounted to ~₹1500 crore. Thus, ~₹4500 crore was invested in inventory. Before supply, finished goods are subject to successful inspection, which if delayed, , increases the inventory holding period for MIL. Furthermore, as on March 31, 2024, the company had receivables of ~₹1400 crore. MIL receives 60% advance from army, navy and air force against its supplies and the balance is received within two to three months from army and within one month from navy and air force, for the supplies made to MHA it receives 40% advance, whereas for export orders 15% money is received in advance. The balance 85% for export orders is received before the goods are dispatched.

Challenges faced by new DPSUs

Although the corporatisation is expected to improve efficiencies, transition is a critical and complex process, having many inherent challenges. MIL also faced initial challenges with respect to the implementation of business strategies, change of the tax regime, financial accounting, quality management systems, store procurement procedures and enhanced delegation of financial powers and to reduce bureaucratic administrative procedures.

Foreign exchange fluctuation risk

MIL remains exposed to forex risk, as the company is involved in the import of raw material and export of finished goods. By virtue of import and export, it has a natural hedge to some extent. ~40% of its forex risk is hedged through natural hedge; however, the balance ~60% forex exposure as of now remains unhedged. However, as expressed by the management, the company is in the process of implementing the hedging policy.

Qualified audit report

The company's statutory auditor has given adverse opinion for FY23 and qualified opinion for FY24. The qualified opinion for FY24 relates to issues regarding prior period adjustments, non-reconciliation of trade receivables, trade payables and balances with government authorities. Auditor has also pointed absence of proper reports of physical verification of assets in some of the units. This apart few other matters were emphasised by the auditor. Upon discussion with the management of the company, CARE Ratings notes that many of the observation points made by statutory auditor in FY23 and FY24, related to assets, liabilities, receivable and payables are due to legacy issues. Since records and assets of erstwhile ordnance factory board were created/accumulated over decades of operations, correcting such errors is taking time and as and when the discrepancy comes to notice it is being rectified. The company has already addressed many issues. Further, per the management, given the new incorporation of the company, its size, volume and geographical spread of units, systems and controls required by the statutory auditor is taking some time to get fully incorporated in the current system. However, CARE Ratings notes that the CAG Audit for FY23 reports no observations made by the statutory auditor. Further for FY24, CAG audit is under process CARE Ratings will continue to monitor the same and adverse opinion by CAG shall remain key rating monitorable.

Liquidity: Strong

The company's liquidity profile is healthy supported by cash and liquid investments of ~₹3500 crore as on March 31, 2024, against nil term debt repayments. The company plans to undertake capex of about ₹1500 crore over next two years part of which will be funded partly by GoI and partly through internal accruals. Further, the company also receives advance for the order it executes. The average working capital utilisation for the 12-month ending in August 2024, remained at ~35% for non-fund-based facility which further provides cushion to the company's liquidity.

Assumptions/Covenants: Not applicable

Environment, social, and governance (ESG) risks: Not applicable

Applicable criteria

Definition of Default
Factoring Linkages Government Support
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Manufacturing Companies
Financial Ratios – Non financial Sector

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Industrials	Capital goods	Aerospace and defense	Aerospace and defense

Incorporated in August 2021, MIL is a Central Public Sector Enterprise (CPSE) under MoD, Government of India. It is engaged in production, testing, research and development and marketing of comprehensive range of ammunition and explosives for Army, Navy, Air force and Para-Military forces. The company is based out of Pune and has 12 manufacturing units across the country.

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)
Total operating income	4,652.18	7,256.33
PBILDT	-27.40	497.41
PAT	73.35	560.07
Overall gearing (times)	0.06	0.11
Interest coverage (times)	NM	230.28

A: Audited; NM: Not Meaningful, Note: these are latest available financial results

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned and Rating Outlook
Fund-based - LT-Cash Credit		-	-	-	2000.00	CARE AA+; Stable
Non-fund-based - LT/ ST-BG/LC		-	-	-	1000.00	CARE AA+; Stable / CARE A1+

Annexure-2: Rating history for 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 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022
1	Fund-based - LT-Cash Credit	LT	2000.00	CARE AA+; Stable	-	1)CARE AA+; Stable (01-Aug-23)	-	-
2	Non-fund-based - LT/ ST-BG/LC	LT/ST	1000.00	CARE AA+; Stable / CARE A1+				

LT: Long term; ST: Short term; LT/ST: Long term/Short term

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

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT-Cash Credit	Simple
2	Non-fund-based - LT/ ST-BG/LC	Simple

Annexure-5: Lender details

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

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

Contact us

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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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