Emson Gears Limited

February 03, 2025

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	118.40 (Enhanced from 100.40)	CARE BBB; Stable	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

While arriving at the rating of Emson Gears Limited (EGL), CARE Ratings Limited (CARE Ratings) has taken a combined view of EGL and Osho Forge Limited (OFL, rated 'CARE BBB; Stable'), as both companies (together referred to as 'Group') have common promoters, common management, and operational linkages.

Reaffirmation of rating assigned to bank facilities of EGL considers the improvement observed in profitability in FY24 (refers to April 01 to March 31) and the current financial year albeit moderation in scale of operations in FY24 and average financial risk profile of the group. The rating further derives comfort from the experienced promoters with long track record of operations, business synergies due to operational linkages within the group, well-established clientele, stable demand outlook from automobiles despite competitive auto-component industry, and cyclical end-user automobile industry. However, the rating remains constrained due to elongated operating cycle, margins susceptible to raw material price volatility, and inherent cyclicality of the auto component industry.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Improvement in group's total operating income (TOI) above ₹700 crore with profit before interest, lease, depreciation, and tax (PBILDT) margin at 9.00% on a sustained basis.
- Improvement in the operating cycle of the group below 60 days on a sustained basis.
- Improvement in group's capital structure as marked by overall gearing below 0.75x on a sustained basis.

Negative factors

- Decline in group's scale of operations with TOI falling below ₹400 crore with PBILDT below 7.00% on a sustained basis.
- Deterioration in group's capital structure as marked by overall gearing above 1.25x on a sustained basis.

Analytical approach: Combined

The combined financials of EGL and OFL have been considered, as both the companies are in the same line of business, have same promoters and group synergies, and are controlled by a common management team. The income derived from intra-group sales amounting to ₹135.14 (₹122.88 crore in FY23) accounted for ~24% of the total gross operating income in FY24.

Outlook: Stable

The 'Stable' outlook reflects CARE Ratings' expectation that the company is likely to maintain its operating and financial risk profiles over the near-to-medium term.

Detailed description of key rating drivers:

Key strengths

Improvement in profitability albeit moderation in scale of operations in FY24

The group's TOI witnessed moderation of ~9% in FY24 and stood at ₹425.93 crore led by moderation in sales realisations for pinions, crown wheels and gears majorly considering correction in commodity prices observed in the last fiscal year. However, the group was able to improve the operating profitability margins with PBILDT margin of 8.36%, against 7.93% in the last fiscal year; moderation in raw material prices and exercising control over operational and administrative expenses have helped the group in improving the operating profit margins.

The group has achieved TOI of ₹310.18 crore in 9MFY25 (refers to April 01 to December 31).

CARE Ratings expects operational performance of the group to improve over the medium term led by ongoing capex for increase in the installed capacity.

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

Average financial risk profile
Overall gearing and total debt to gross cash accruals (TD/GCA) of the group stood moderate at 1.08x and 6.76x, respectively, as on March 31, 2024. The interest coverage ratio remained moderate at 2.53x in FY24. Owing to higher working capital requirements and additional term loan availed for procurement of machineries, debt coverage indicators of the group are expected to remain moderate over short-to-medium term.
Interest coverage ratio of the group stands at 2.85x in H1FY25.
The group's ability to maintain its average financial risk profile while managing its working capital requirements would remain a key monitorable from credit perspective.

Business synergies due to operational linkages within the group
EGL procures raw material (forged components and semi-finished components) largely from its group company, OFL. EGL then provides value addition to the product (through machining) and subsequently sells the product to the client. Given the significant operational linkages within the group, the operational risk considering dependence on outside suppliers for raw materials remains low. OFL offers a credit period of 100- 120 days to EGL. Additionally, starting from FY24, EGL has also begun supplying materials to OFL under similar credit terms.

Well-established clientele, despite high customer concentration risk
The group has established relationship with original equipment manufacturers (OEMs) such as Mahindra & Mahindra (M&M; rated 'CARE AAA; Stable/ CARE A1+'), International Tractors Limited, and SML Isuzu Limited among others. The reputed client base ensures timely payments and lends comfort to the revenue realisation. The group has been associated with these customers for over 16 years and receives regular orders from them. The OEMs have a rigorous supplier selection process, involving prototype development, product testing, and review of operating facilities, besides other benchmarking processes. The supplier selection process can range from two to three years, and it is only after a rigorous and lengthy process that a supplier is selected for regular supply by OEMs. However, EGL faces customer concentration risk with M&M accounting for ~43% of its total revenue in FY24 (~53% in FY23) and the balance is fragmented across various players. The revenue stream of OFL is concentrated with ~42% of the income being derived from its group concern EGL in FY24 (~47% in FY23). Apart from that, ~23% of OFL's total revenue in FY24 was derived from M&M (~24% in FY23) while the balance income was fragmented across various players. However, the group has an established relationship with its customers and gets regular orders from them, the income depends on the business operations of its clientele and their future growth plans.

Experienced promoters with long track record of operations
The group was promoted by Ashok Dhall and Gautam Dhall. The promoters/directors have rich experience of around four decades in the industry. Both the promoters are involved in the overall business operations of the group and are ably supported by a team of professionals who are highly experienced in their respective domains. To fund the group's business requirement in the past, regular funds have been infused by the promoters and related parties which stood at ₹31.95 crore as on March 31, 2024.

Stable demand outlook from automobiles despite competitive auto-component industry and cyclical end-user automobile industry
The Indian auto component industry is a crucial component of the OEM value chain, driving consistent demand for industry participants. The organised segment consists of original equipment manufacturers (OEMs) that specialise in the production of high-value, precision-engineered components, while the unorganised segment primarily focuses on lower-cost products for aftermarket applications, resulting in intense competition. The group's product portfolio is exclusively aligned with the automotive sector, making its growth directly dependent on the domestic automotive industry's performance, which is inherently cyclical and influenced by macroeconomic conditions. A significant challenge faced by indigenous component manufacturers is the limited adoption of advanced technologies and relatively low R&D investment, which places them at a competitive disadvantage compared to organised players. Mid-sized organised entities such as Osho Forge and Emson Gears have demonstrated a higher level of technological integration and R&D focus, providing them with a competitive edge over unorganised competitors.

Key weaknesses

Elongated operating cycle
The group has huge product portfolio with over 480 SKUs leading to high level of inventory holding in form of WIP and finished goods. As on March 31, 2024, the inventory holding stood at 110 days. (Previous Year [PY]:89 days). On the customer side, the group has a well-established and reputed customer base to which it extends a credit period of up to 120 days leading to average collection days stood at 60 days, as on March 31, 2024 (PY: 51 days). On the raw material procurement side, the group is offered payment terms ranging from 80 days to 150 days by its suppliers leading to average creditors days of 71 days as on March 31,

2024 (PY: 57 days). The group's operations are thus working capital intensive resulting in elongated operating cycle of 100 days in FY24 (PY: 84 days).

Margins susceptible to raw material price volatility and foreign exchange risk
The group's operations are raw material intensive in nature with the raw material cost constituting ~58% of the income in FY23-24 period. With global steel prices highly volatile in nature and susceptible to speculative trading, the margins of group are exposed to raw material fluctuation risk. Given large variety of products being manufactured for different types of customers, which necessitates large inventory holding, the margins are exposed to adverse movement in the raw material prices. The raw materials are completely procured from domestic markets. With initial cash outlay for procurement in domestic currency and some part of sales realisation on in foreign currency, the group is exposed to the fluctuation in exchange rates as group does not undertake foreign exchange hedging.

Presence in competitive auto-component industry and cyclical automobile industry
The Indian auto component industry is a critical part of the OEM value chain. An organised segment of this industry includes OEMs who are engaged in manufacturing high-value precision instruments, while the unorganised segment comprises low-valued products catering to after-market services, resulting in high competition. However, one of the main challenges faced by the indigenous component manufacturers is the low-level of technology adaptation and R&D intensity which gives an edge to organised players.

Liquidity: Adequate
Liquidity position of the group is characterised by an above unity current ratio since last five fiscal years. The repayment obligations of the group stood at ₹16.40 crore for FY25 against the expected GCA of ~₹22.92 crore. Operating cycle has remained higher at 100 days in FY24 considering working capital intensive operations. Although average working capital utilisation has remained high at ~90-95% for last 12 months ending September 2024. However, it has unencumbered cash and cash equivalents to the tune of ~₹12 crore as on March 31, 2024. The group would be incurring capex of ~₹40-45 crore in FY25 and FY26 for procurement & installation of machineries to increase the capacity that will be funded through long-term bank debt and infusion of unsecured loans by the promoters.

Assumptions/Covenants: Not applicable

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

Applicable criteria

Consolidation
Definition of Default
Factoring Linkages Parent Sub JV Group
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Manufacturing Companies
Financial Ratios – Non financial Sector
Auto Components & Equipments

About the company and industry

Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Consumer discretionary	Automobile and auto components	Auto components	Auto components & equipment

EGL belongs to the Emson Group of Punjab, founded in 1970 and has a group company OFL. EGL was incorporated as a partnership firm in 1970, by the name, 'M/s Emson Sales'. In April 1996, the firm was reconstituted as a closely held company to take-over the business carried out under the firm. EGL is engaged in manufacturing and selling automobile parts such as differential and transmission gears, crown wheels and pinions among others. OFL is a closely held company incorporated in June 1993. It is engaged in manufacturing automobile parts such as axles, bull gears and shafts. The company has both forging and machining facilities at its manufacturing plants. The manufacturing facilities of the group are in Ludhiana, Punjab, and parts manufactured are primarily sold to OEMs based in India catering to the tractor and commercial vehicle industry. The group is promoted by Ashok Dhall and Gautam Dhall (son of Ashok Dhall).

Combined financials of OFL and EGL:

Brief Financials (₹ crore)	March 31, 2023 (UA)	March 31, 2024 (UA)	9MFY25 (UA)
Total operating income	467.37	425.93	310.18
PBILDT	37.06	35.59	NA
PAT	10.24	8.55	NA
Overall gearing (times)	0.94	1.08	NA
Interest coverage (times)	2.50	2.53	NA

UA: Unaudited; NA: Not Available, Note: these are latest available financial results. Combined financials are unaudited. Standalone audited financials are available.

Basis of combination: The numbers have been combined through row-by-row addition of all line items of entities mentioned under Analytical approach after excluding intra-group transactions.

Standalone financials of EGL:

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)	9MFY25 (UA)
Total operating income	277.05	274.92	267.78
PBILDT	21.95	21.86	NA
PAT	5.16	5.03	NA
Overall gearing (times)	0.98	1.30	NA
Interest coverage (times)	2.65	2.71	NA

A: Audited UA: Unaudited NA: Not Available; 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	Coupon Rate (%)	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned and Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	-	64.75	CARE BBB; Stable
Fund-based - LT-Term Loan	-	-	-	August 01, 2032	53.65	CARE BBB; Stable

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	64.75	CARE BBB; Stable	1)CARE BBB; Stable (28-Nov-24)	1)CARE BBB; Stable (07-Nov-23)	1)CARE BBB-; Stable (04-Oct-22)	1)CARE BB+; Positive (03-Dec-21) 2)CARE BB+; Stable (05-Apr-21)
2	Fund-based - LT-Term Loan	LT	53.65	CARE BBB; Stable	1)CARE BBB; Stable (28-Nov-24)	1)CARE BBB; Stable (07-Nov-23)	1)CARE BBB-; Stable (04-Oct-22)	1)CARE BB+; Positive (03-Dec-21) 2)CARE BB+; Stable (05-Apr-21)

LT: Long 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	Fund-based - LT-Term Loan	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.

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About us:
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