# RACL Geartech Limited

September 23, 2022

**Ratings**

| Facilities/Instruments | Amount (₹ crore) | Rating[1] | Rating Action |
|---|---|---|---|
| Long Term Bank Facilities | 206.59<br>(Enhanced from 131.53) | CARE A-; Stable<br>(Single A Minus; Outlook: Stable) | Reaffirmed |
| Short Term Bank Facilities | 5.00 | CARE A2<br>(A Two) | Reaffirmed |
| **Total Bank Facilities** | **211.59<br>(₹ Two Hundred Eleven Crore and Fifty-Nine Lakhs Only)** | | |

Details of instruments/facilities in Annexure-1

**Detailed Rationale & Key Rating Drivers**

The ratings assigned to the bank facilities of RACL Geartech Limited continue to derive strength from experienced promoters along with their long track record of operations, established player in the transmission gears and shafts for automotive applications along with the reputed customer base, and geographically diversified revenue mix. Further, ratings also take comfort from comfortable operational performance with growing scale of operations and healthy profitability. However, the ratings are constrained by the ongoing project undertaken for the purpose of creating capacities for new products in lieu of the nomination letters received from customers, raw material price volatility risk along with the presence of foreign exchange fluctuation risk, high working capital intensive nature of operations along with cyclical nature of the automotive industry. The ratings also take cognizance of growing energy crisis in Europe which may adversely impact the operational performance of the manufacturing sector and development in this regard in ensuing quarters shall be a key credit monitorable.

**Rating Sensitivities**

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

- Sustained improvement in the scale of operations beyond Rs.350 crores while maintaining the profitability margins and continued relationship with its key customers.
- Improvement in the capital structure leading to overall gearing of below 0.75x

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

- Decline in scale of operations below Rs.225 crore
- Higher than envisaged capex leading to deterioration in the capital structure with continuing overall gearing of more than 1.2x.

**Detailed description of the key rating drivers**

**Key Rating Strengths**

**Experienced promoters**

RGL has more than three and a half decades of presence in the automobile component industry. Mr. Gursharan Singh, CMD of the company, joined the company as a plant head and has been associated with the company since its inception. He is a mechanical engineer with Post-Graduate Diploma in Export Management. He is ably supported by a team of professionals who have been with the company for more than two decades.

**Established player in transmission gears and shafts for automotive and industrial applications**

RGL is engaged in the business of manufacturing of transmission gears and shafts for automotive and industrial applications since 1980s. The company has renowned Original Equipment Manufacturers (OEMs) in the auto as well as industrial segment as its long-standing customers. It has an established relationship with some of the leading global original equipment manufacturers (OEMs) which cater to the premium segment. RGL's business risk profile has improved over the years by adding new customers by increasing its product portfolio and entering into new segment of automobile industry. The addition in customer base was supported by supply of quality products while adhering to international standards laid down by international quality assessment team.

**Reputed customer base**

Though, RGL has moderate concentration risk with top five customers contributing ~67% revenue in FY22 (PY: 78%), however, comfort is drawn from the fact that the company is a preferred vendor for many of its premium segment export customers with whom it has long-term relationships. Also, the management as a part of its strategy ensures that sales does not exceed 20% to

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

any single customer. The largest contributor during FY22 was 17% of the sales and thereby reduces dependence on few customers.

**Geographical and segment-wise diversification**

The export sales of the company accounted for 73% of its total gross sales during FY22 (PY: 76% of total gross sales). Of the total sales in FY22, nearly 57% of the sales were in Europe, 39% in India and Asia Pacific region and remaining from USA and Mexico. RGL earns relatively higher margins in export as the company is exporting its products to OEMs catering to premium segment. In terms of end-user segmentation, 2-wheelers contributed 49% of revenue in FY22 as against 45% in FY21 followed by tractors which contributed ~19% to the total gross sales during FY22 (PY: ~19%). Diversified product offering provides a competitive edge to the company /and makes it more sustainable in the long run.

**Comfortable operational performance**

The total operating income of the company reported y-o-y growth of ~33% and stood at Rs.274.82 crore during FY22 (PY: Rs.207.07 crore) on the back of healthy volume growth and additional capacities created on account of addition of certain new customers in the previous years.

The PBILDT margin are comfortable and usually remain range bound between 20 to 22% backed by their significant presence in export markets and also sales to some of the premium customers. The PBILDT margin stood at 22.13% in FY22 (PY: 26.18%) whereby FY21 was an aberration owing to sale of some high margin prototypes to new customer. Moreover, in last two quarters of FY22, as geo-political situation started deteriorating globally from January, 2022, there was sudden increase in input costs and volatility in the market, thereby impacting margins.

**Current year performance:** During Q1FY23, the company reported total operating income of Rs.80.82 crore, whereby it recorded y-o-y growth of ~41% and q-o-q growth of ~11%. The PBILDT margin stood at 21.85% during Q1FY23 as against 21.33% in Q4FY22 and 23.12% in Q1FY22.

**Key Rating Weaknesses**

**Moderate Capital structure**

The capital structure of the company moderated, whereby the overall gearing stood at 1.26x as on March 31, 2022 (PY: 1.02x) owing to addition in term debt with capital expenditure undertaken and also higher utilization of working capital limits in line with growing scale of operations. The debt coverage indicators also moderated with interest coverage ratio and total debt to GCA of 4.91x and 4.02x respectively in FY22 (PY: 6.42x and 4.02x respectively).

**Foreign Exchange fluctuation and raw material price risk**

The company derives its revenue majorly through exports which is approx. 73% (PY: 78%). Though the profitability margins are exposed to volatility in foreign exchange however the same are mitigated with the availment of export credit in foreign exchange. Further, the company discounts the invoices with banks at an early stage to minimize the forex fluctuation risk. Further, the company's main raw material include steel and forgings and the increase/decrease in their prices also exposes the company to raw material price risk, however, the same is mitigated as there is pass through to the customers.

**Working capital intensive nature of operations**

Being in auto ancillary industry, the operations of the company are working capital intensive in nature. The company has to maintain inventory of around 3.5 months with large product range (more than 500 products under regular production). Also, to cater the demand of major customers, company stocks inventory at its warehouses near customers' factory for uninterrupted flow of products with minimum transit time (The company has the warehouses in Austria for the same purpose). Credit period of close to 2 months is allowed to domestic customers, contributing 27% of total operating income, while collection from overseas customers, which contributes 76% of total operating income, usually happens in 3-4 months. Furthermore, the company gets credit period of up to 1.5 months from the suppliers which it has been reducing to avail cash discounts. Overall, this leads to a working capital cycle of around 5 months, which further leads to high reliance on the fund-based facilities to meet the working capital requirements. The average working capital utilization remained 79% during trailing 10-month period ended July, 2022.

**Project Risk**

The company has projected capital expenditure of Rs.60 crore for FY23 for the purpose of creating capacities for existing products alongside new customers and modernization/upgradation of existing plant and machinery. RGL manufactures very high-quality precision components, whereby all the investments are made by the company on the basis of tentative supply schedules of the customers both domestic as well as export. The schedules are received in the form of nomination letters for components which are for the entire life of the vehicle. No investment is made by the company unless the company gets a nomination letter from the customer which normally takes 1 to 2 years-time for supply so that company can arrange machines and develop tooling for the components and most of the critical machines are imported having delivery period up to 12 months.

The company received nomination letter from new customer for supply of certain new component parts for which the capex was undertaken, wherein Rs.30 crore of the capex has already been incurred up to the latest date. Further, the said capex is less than 50% of the tangible net worth base. The same is to be funded by a combination of term debt and internal accruals, whereby Rs.45 crore of term loan has been sanctioned by the bank.

**Industry prospects**
The automobile industry is highly cyclical in nature and automotive component suppliers' sales are directly linked to sales of auto OEMs. Furthermore, the auto-ancillary industry is highly 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.
The ongoing Russia-Ukraine war has triggered increasing input prices along with energy crisis in Europe. Manufacturers in Europe are laying-off workers and shutting down the production lines with Russia's abrupt cut-off of gas to Europe. However, the company supplies parts for the customers in premium segment, which is insulated to some extent. The company has projected healthy growth in top-line owing to the confirmed orders from customers along with nomination letters received from some of the reputed export customers for newer component parts.

**Liquidity: Adequate**
Adequate liquidity characterized by sufficient cushion in estimated gross cash accruals vis-à-vis repayment obligations of Rs.29.51 crore and modest cash balance of Rs.0.73 crore as on March 31, 2022. Further, the company is planning to undertake capex of Rs.60 crore in FY23 for the purpose of upgradation/modernization of its existing unit and the same is expected to be funded by addition in term debt by Rs.45.20 crore while remaining from internal accruals. Its bank limits are utilized to the extent of 79% and it has sought enhancement in bank lines, supported by above unity current ratio, which stood at 1.15x as on March 31, 2022 (PY: 1.18x).
**Analytical approach:** Standalone approach

**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**
RGL (formerly Raunaq Automotive Components Limited) was incorporated in 1983 and is engaged in the business of manufacturing of transmission gears and shafts for automotive and industrial applications. The company was initially promoted by the Raunaq Group. However, due to financial difficulties the company was referred to Board for Industrial and Financial Reconstruction (BIFR) in 2001. Post-restructuring and with a new management team under leadership of Mr. Gursharan Singh (CMD), RGL came out of the BIFR purview in November 2007. The company has two manufacturing units in Uttar Pradesh at Gajraula and Noida.

| Brief Financials (Rs. crore) | 31-03-2021 (A) | 31-03-2022 (A) | Q1FY23 (UA) |
|---|---|---|---|
| Total operating income | 207.07 | 274.82 | 80.82 |
| PBILDT | 54.36 | 60.83 | 17.66 |
| PAT | 23.38 | 23.95 | 6.05 |
| Overall gearing (times) | 1.02 | 1.26 | NA |
| Interest coverage (times) | 6.42 | 4.91 | 3.42 |

A: Audited; UA: Unaudited

**Status of non-cooperation with previous CRA:** Not Applicable
**Any other information:** Not Applicable
**Disclosure of Interest of Independent/Non-Executive Directors of CARE Ratings Ltd.:** Not Applicable
**Disclosure of Interest of Managing Director & CEO:** Not Applicable
**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 | ISIN | Date of Issuance (DD-MM-YYYY) | Coupon Rate (%) | Maturity Date (DD-MM-YYYY) | Size of the Issue (₹ crore) | Rating Assigned along with Rating Outlook |
|---|---|---|---|---|---|---|
| Fund-based - LT-Term Loan | | - | - | 2027 | 115.09 | CARE A-; Stable |
| Fund-based - LT-Cash Credit | | - | - | - | 91.50 | CARE A-; Stable |
| Non-fund-based - ST-BG/LC | | - | - | - | 5.00 | 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 (₹ 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 | 115.09 | CARE A-; Stable | - | 1)CARE A-; Stable (27-Oct-21) | 1)CARE BBB+; Stable (03-Sep-20) | 1)CARE BBB; Positive (09-Aug-19) |
| 2 | Fund-based - LT-Cash Credit | LT | 91.50 | CARE A-; Stable | - | 1)CARE A-; Stable (27-Oct-21) | 1)CARE BBB+; Stable (03-Sep-20) | 1)CARE BBB; Positive (09-Aug-19) |
| 3 | Non-fund-based - ST-BG/LC | ST | 5.00 | CARE A2 | - | 1)CARE A2 (27-Oct-21) | 1)CARE A3+ (03-Sep-20) | 1)CARE A3 (09-Aug-19) |

*Long Term / Short Term

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

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

| Sr. No. | Name of Instrument | Complexity Level |
|---|---|---|
| 1 | Fund-based - LT-Cash Credit | Simple |
| 2 | Fund-based - LT-Term Loan | Simple |
| 3 | Non-fund-based - ST-BG/LC | Simple |

**Note on complexity levels of the rated instrument:** CARE Ratings Ltd. 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.

**Annexure 5: Bank Lender Details for this Company**

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

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**About CARE Ratings Limited:**

Established in 1993, CARE Ratings Ltd. is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India (SEBI), it has also been acknowledged as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). With an equitable position in the Indian capital market, CARE Ratings Limited provides a wide array of credit rating services that help corporates to raise capital and enable investors to make informed decisions backed by knowledge and assessment provided by the company.
With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.



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