CEAT Limited

January 06, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term Bank Facilities	1,000 (reduced from Rs.1,070 crore)	**CARE AA; Stable (Double A; Outlook: Stable)**	**Reaffirmed**
Short term Bank Facilities	1,150 (reduced from Rs.1,300 crore)	**CARE A1+ (A One Plus)**	**Reaffirmed**
Total	**2,150 (Rs. Two thousand one hundred and fifty crore only)**		
Commercial Paper	350 **(Rs. Three hundred Fifty crore only)**	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities and short term instruments of CEAT Limited (CEAT; CIN No: L25100MH1958PLC011041) continues to factor in the established market position of CEAT as brand and experience of the promoters in domestic tyre industry. CEAT owing to wide and robust distribution network continues to generate large part of its Total Operating Income (TOI) from replacement market.

Post reporting robust sales volume backed growth in its TOI for FY19, CEAT reported moderation in TOI during H1FY20. The pronounced slowdown in demand for commercial vehicles that started from H2FY19 and continued in H1FY20 impacting the income growth for most of the tyre manufacturers during H1FY20. CARE believes, the weakness in tyre demand particularly from OEMs is expected to continue till H1FY21. In case of CEAT, demand volatility is mitigated to certain extent owing to large contribution of income from replacement & exports market.

The leverage and debt coverage indicators of CEAT that have remained comfortable in past are expected to witness some moderation going forward. The envisaged moderation is on account of large capex (greenfield and brownfield) being implemented for expanding product portfolio and elevating the capacities. CARE believes, despite the envisaged moderation, the debt coverage would still remain adequate as the expanded capacities and improved product mix would translate into expansion in its operating profit margins going forward. Timely completion of envisaged capex and subsequent ramping up would be key rating monitorable.

The ratings, however, continue to be tempered by volatility in operating margins to fluctuation in raw material prices, exposure to cyclicality prevalent in the automobile industry and high competition prevalent in the domestic tyre industry and change in government policy.

Ability of the company to complete the ongoing projects in a timely manner and stabilization of the ongoing projects would be a key rating sensitivity. Further, any large debt-funded capital expenditure more than what is envisaged and ability of the company to contain volatility in margins would be the key rating monitorables.

Rating Sensitivities

Positive Factors

- Total Debt to GCA below 1.88x on sustained basis
- Improvement in PBILDT margin over 13% on sustained basis
- Improvement in ROCE above 16% on a sustained basis
- Improvement in PBILDT interest cover over 8.5x on sustained basis

Negative Factors

- Deterioration in PBILDT margin below 11% on sustained basis
- Deterioration in Total Debt to Cash Flow from Operations (reported) above 3.0x on sustained basis
- Total debt/PBILDT above 2.60 times on a sustained basis
- Interest cover (PBILDT / Gross Interest) declining below 5.0x on sustained basis.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters and proficient management:

CEAT Limited belongs to the RPG Group. RPG group is a diversified conglomerate having business interests across diverse businesses like automotive tyres, infrastructure, information & technology, pharmaceuticals, plantations and power

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

ancillaries. The group is headed by Mr Harsh Vardhan Goenka while CEAT's day to day operations are headed by Mr Anant Vardhan Goenka - Managing Director.

Established brand with diversified product portfolio and distribution network:

CEAT is one of the leading tyre companies in the country and caters to the various user segments which include Trucks and Buses (T&B), Light Commercial Vehicles, Tractors, Two wheelers (2W) & Three wheelers (3W), Passenger Vehicles and off-road tyres. CEAT has a widespread distribution network spread across the country with more than 3,400 dealers, more than 270 distributors and more than 300 exclusive CEAT Shoppes & CEAT Tyre service hub servicing over 30,000 sub-dealers. CEAT derives close to 60% of its revenue from the replacement market which mitigates the business risk to a large extent.

Volume backed growth in FY19; albeit realization remained muted:

On a consolidated basis, CEAT reported about 12% YoY increase in revenue in FY19 largely due to increase in sales volumes coupled with marginal increase in average sales realizations. The performance of the auto industry was robust during first half of FY19 and thereafter it started deteriorating on account of a confluence of factors like revised axle load norms, liquidity issues and general economic slowdown. These factors continued to impact the demand for automobiles especially Commercial vehicle segment in H1FY20 as well. Nevertheless, CEAT reported marginal increase in top-line in H1FY20 on the back of stable performance in the replacement market and increase in export sales in H1FY20.

Capital structure continues to remain comfortable despite marginal deterioration:

CEAT including its 100% subsidiary CEAT Specialty Tyres Ltd (CSTL) is undertaking capex to the tune of ~Rs.3700 crore from FY18-FY23 towards increase in capacities across PV radial, T&B radial and 2 wheelers. Large capex under implementation which is partially debt funded would lead to moderation in the capital structure and debt coverage indicators in the medium term. Nevertheless, comfort can be derived from the fact that CEAT is earning healthy cash profits which can also be utilized to fund the capex to a large extent. As on March 31, 2019, overall gearing stood at 0.59x and the same is expected to deteriorate marginally going forward. Further, the repayments of majority of term loans availed for capex have a moratorium up to FY22-FY23. Any further large debt-funded capital expenditure other than envisaged would be a key rating sensitivity.

Key Rating Weaknesses

Deterioration in operating margin in FY19 and Exposure to volatility in raw material prices:

In FY19, the operating margin of CEAT has contracted to 9.34% from 10.11% in FY18 due to persistent rise in material cost and other operating overheads. However, in H1FY20, the margin has improved to 10.22% on the back of benign raw material prices.

The key raw material used in manufacturing of tyre are natural rubber, Carbon Black, fabric and other chemicals. Natural rubber prices comprises about 30-40% of total cost structure of tyre. Natural rubber prices were lower in FY19 in comparison to FY18. However, the prices of carbon black have increased by about 17% in FY19 as compared to the previous year. Further, crude oil prices which impact the price of other chemicals used in tyre manufacturing also remained volatile during FY19; average crude oil prices for FY19 were higher by 17% and showcased high level of volatility.

Exposure to cyclicality in the automobile industry:

The performance of tyre manufacturers is dependent on the performance of the automobile industry, which is cyclical in nature. Nevertheless, auto ancillaries which have a significant exposure to replacement market are insulated to an extent as the demand for the auto components in the replacement market is an indirect function of the growth posted by Original Equipment Manufacturers (OEMs). Further, diversified product portfolio and presence in the export markets mitigates this risk to an extent.

High level of competition from Domestic and International Players:

Historically the tyre industry has witnessed intense competition between the Indian players and the Chinese tyre manufacturers. The level of competition by international player is significantly higher in the Trucks and Buses segment which is price sensitive. However measures taken by the government like imposition of anti-dumping duty (implemented in September 2017) and anti-subsidy countervailing duty (implemented in July 2019) on tyre imports from China have helped Indian tyre manufacturers.

Liquidity: Strong

The liquidity profile of CEAT is strong as evinced by the fact that it is expected to earn Gross Cash Accruals of about Rs.501 crore in FY20. As against that CEAT has repayment obligations of about Rs.188 crore (principal and interest) in FY20. As on September 30, 2019, CEAT had cash and cash equivalents of Rs.97.83 crore. As on October 31, 2019, CEAT had unutilized fund based working capital limit of Rs.336.64 crore.

Analytical approach:
CARE has taken a consolidated approach in analyzing the financials of CEAT Limited. The list of companies which have been consolidated is presented in **Annexure 4**. CARE has taken consolidated approach owing to high degree of financial, managerial and business linkages between the entities.

Applicable Criteria
[Criteria on assigning 'outlook' and 'credit watch']
[CARE's Policy on Default Recognition]
[Short Term Instruments]
[Financial ratios – Non-Financial Sector]
[Rating Methodology: Consolidation and Factoring Linkages in Ratings]
[Rating Methodology - Manufacturing Companies]
[Rating Methodology - Auto Ancillary Companies]

About the Company
Established in 1958, CEAT Limited (CEAT) is flagship entity under RPG Group (Rama Prasad Goenka Group). RPG group is a conglomerate having more than 15 companies catering to diverse businesses spanning across automotive tyres, infrastructure, information & technology, pharmaceuticals, plantations and power ancillaries. RPG group acquired the company in 1982. CEAT is engaged in the manufacturing of tyres, tubes and flaps and it is one of the leading tyre manufacturer in domestic market. Products manufactured find application in heavy-duty trucks and buses, light commercial vehicles, earthmovers, forklifts, tractors, trailers, cars, motorcycles and scooters as well as auto-rickshaws. It caters to demand from both OEM (Original Equipment Manufacturer) and replacement market. Large part of its income is contributed from replacement market.
In India, CEAT operates with five manufacturing units located at Mumbai, Nagpur, Nasik, Ambernath (Maharashtra; operationalized in FY18), Halol (Gujarat). CEAT is also in the process of setting up plant at Chennai. Furthermore, CEAT has outsourced the production facilities of tyres to several third party conversion agencies located at Maharashtra, Hyderabad (Telangana) and Calicut (Kerala). CEAT operates with an aggregate capacity of 817 Tonnes Per Day (TPD).

Covenants of rated instrument / facility: Not available.

Brief Financials (Rs. crore) CEAT (Consolidated)	FY18 (A)	FY19 (A)	H1FY20 (UA)
Total operating income	6,236.56	6,984.51	3,459.85
PBILDT	630.36	652.18	353.70
PAT	233.29	251.08	125.84
Overall gearing (times)	0.34	0.59	0.64
Interest coverage (times)	6.08	7.02	4.89

A: Audited
Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

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

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Term Loan-Long Term	-	-	-	December 2028	500.00	CARE AA; Stable
Fund-based - LT-Cash Credit	-	-	-	-	500.00	CARE AA; Stable
Non-fund-based - ST-BG/LC	-	-	-	-	1150.00	CARE A1+
Commercial Paper	-	-	-	February 2020	350.00	CARE A1+

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Term Loan-Long Term	LT	500.00	CARE AA; Stable	-	1)CARE AA; Stable (08-Jan-19)	1)CARE AA; Stable (08-Jan-18)	1)CARE AA (14-Oct-16)
2.	Fund-based - LT-Cash Credit	LT	500.00	CARE AA; Stable	-	1)CARE AA; Stable (08-Jan-19)	1)CARE AA; Stable (08-Jan-18)	1)CARE AA (14-Oct-16)
3.	Non-fund-based - ST-BG/LC	ST	1150.00	CARE A1+	-	1)CARE A1+ (08-Jan-19)	1)CARE A1+ (08-Jan-18)	1)CARE A1+ (14-Oct-16)
4.	Commercial Paper	ST	350.00	CARE A1+	-	1)CARE A1+ (08-Jan-19)	1)CARE A1+ (08-Jan-18) 2)CARE A1+ (18-Jul-17)	1)CARE A1+ (14-Oct-16)
5.	Debentures-Non Convertible Debentures	LT	-	-	-	1)Withdrawn (08-Jan-19)	1)CARE AA; Stable (08-Jan-18)	1)CARE AA (14-Oct-16)

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not available

Annexure-4: List of subsidiaries which are consolidated

Name of the subsidiary	Percentage of holding
Associated CEAT Holdings Company (Private) Limited	100.0%
CEAT AKKhan Limited	70.0%
CEAT Specialty Tyres Limited (CSTL)	100.0%
Rado Tyres Limited (RTL)	58.6%
CEAT Specialty Tyres Inc. (Subsidiary of CSTL)	CSTL holding is 100%
CEAT Specialty Tyres B.V (Subsidiary of CSTL)	CSTL holding is 100%

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

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About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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