GNA Axles Limited

August 04, 2020

Ratings

Facilities	**Amount (Rs. crore)**	**Ratings[1]**	**Ratings Action**
Long term Bank Facilities	244.00 (reduced from Rs. 270.00 crore)	CARE A+; Negative (Single A Plus; Outlook: Negative)	Reaffirmed; Outlook revised from Stable to Negative
Short term Bank Facilities	5.50 (reduced from Rs. 15.50 crore)	CARE A1 (A One)	Reaffirmed
Total Facilities	**249.50 (Rupees Two hundred Forty Nine crore and Fifty lakh only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of GNA Axles Limited (GAL) continue to derive strength from the long track record of operations with highly experienced promoter group and long & established business relationship with reputed clientele. The ratings further derive strength from comfortable profitability margins and overall solvency position.

The ratings are, however, constrained by the elongated operating cycle, exposure to client concentration risk and vulnerability of margins to raw material prices & foreign exchange volatility and the cyclical nature of the automobile industry.

Rating Sensitivities

Positive Factors

- Sustained improvement in scale of operations to more than Rs. 1200 cr.
- Sustained improvement in PBILDT margins to over 15% in the projected years

Negative Factors

- Continuation of negative growth in sales volume
- PBILDT margin remaining around 10% on a sustained basis
- Any major debt funded capex resulting in deterioration of capital structure to above 1x

Outlook: Negative

The revision in the outlook to ‘Negative’ from ‘Stable’ takes into account susceptibility of operations of GAL to the current slowdown in the auto industry, especially in the light of Covid-19 pandemic, and resulting likely moderation in the financial performance of the company during FY21. The outlook may be revised back to ‘Stable’ if the company is able to significantly improve its scale of operations and profitability margins.

Detailed description of the key rating drivers

Key Rating Strengths

Long track record of operations with an experienced management team: GAL is promoted by Mr Rachhpall Singh (Executive Chairman) and Mr Gursaran Singh (Managing Director) who have nearly five decades of industry experience. Other family members of the promoter group are also involved in the day-to-day business activities of the company. The directors are assisted by a team of professionals who are highly experienced in their respective domains.

Long and established business relationship with clients: The group has been in the auto component industry since 1946. GAL markets its products through a common marketing network at the group level providing a whole range of products including axles, gears and shafts under one roof. The company has been long associated with its clients. The association with some of the domestic clients has been since the commencement of company operations. Furthermore, over the years, the company has increased its focus on exports with clients in USA, Europe, Asia Pacific, Mexico, Brazil, etc. Exports contributed ~65% of the total operating income in FY20, compared to ~54 % in FY19. The company has been supplying to some of the export clients since 2000. Long and established relationships with clients provide revenue stability to the company. Apart from supplying directly to the Original Equipment Manufacturers (OEMs), the company also provides components to the tier-1 suppliers.

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

Comfortable profitability margins and solvency position: In FY20, the scale of operations of GAL declined marginally by ~3% on a year-on-year (y-o-y) basis on account of lower quantity sold in the domestic market, owing to slowdown in demand, coupled with lower sales realization per unit sold in both the domestic and export market. The PBILDT margin also moderated in FY20 to 13.82% (from 15.55% in FY19), though continued to remain at a comfortable level due to various modernization & up-gradation projects undertaken by the company in the past which has led to improved efficiencies and also due to favorable foreign exchange fluctuations during the year. The moderation in PBILDT margins in FY20 was mainly on account of higher freight expenses incurred during the year coupled with increase in other operational expenses incurred during the year (including employee costs, power costs, etc). The PAT margins also declined to 5.75% from 7% in FY19 due to lower PBILDT margins and increase in depreciation and interest costs during the year due to the debt funded capex undertaken by the company in the past. The capital structure of the company remained comfortable, though slightly deteriorated on account of increased term loans availed by the company for the on-going capacity enhancement capex being undertaken by the company. The debt coverage indicators marked by total debt to GCA ratio and interest coverage ratio stood comfortable at 2.11x, as on March 31, 2020 and 9.25x in FY20, respectively (PY: 1.67x and 17.95x, respectively). The deterioration in debt coverage indicators was mainly on account of lower profitability during the year and increase in term loans availed by the company (for the capex) and subsequent increase in interest expenses during the year.
In Q1FY21 (UA), the total income of the company declined significantly by ~68% on a y-o-y basis to Rs. 81.67 cr. from Rs. 258.18 cr. in Q1FY20 because of spread of Covid-19 pandemic which led to closure of manufacturing facilities due to imposition of lockdown by government. This resulted in production loss in the month of April-20 (operations started from May 05, 2020) and weak demand from the OEMs due to the slowdown in the auto industry in both the domestic and key export markets. This was further augmented by lower sales realization per unit sold in both the domestic and exports market during the period. The PBILDT margins of the company declined to 7.33% in Q1FY21 from 16% in Q1FY20 on account of lower absorption of fixed expenses (employee costs, power expenses etc.) with decline in scale of operations. The interest coverage ratio stood at 2.15x in Q1FY21, declining significantly from 11.61x in Q1FY20.
The company was undertaking two capex projects including setting-up of a new unit for manufacturing of axle shafts for LCVs, Small Pick-ups and SUVs and for enhancing its existing manufacturing facilities at a total cost of Rs. 170 cr. funded through term loan of Rs. 150 cr. and remaining through internal accruals. Both the projects have been completed, within the time & cost estimates. Post capex, the manufacturing capacities of the company have increased to ~6 million pieces per annum from the pre-capex capacities of ~4 mn pieces per annum.

Reputed clientele; albeit, customer concentration risk: GAL has a long history of supplying auto parts to reputed OEMs who enjoy strong market position. Furthermore, for its export clients, GAL supplies auto parts for their plants located in various geographies including USA, Brazil, Australia, Mexico, Italy, Spain, etc., thereby mitigating the risk arising from slowdown in one particular geographical location. However, the revenue stream of GAL remains concentrated with top-5 and top-10 clients accounting for about 72% and around 84%, respectively, of the total income in FY20 (PY: 66% and 80%, respectively). Any significant deterioration in the performance of these clients is expected to have an impact on the financial profile of GAL.

Key Rating Weaknesses
Susceptibility of margins to volatility in raw material prices, foreign exchange risk and cyclical nature of the industry: The operations of the company are raw material intensive in nature with the raw material cost constituting around 57% of the income in FY20. Furthermore, GAL derives a substantial portion of its income from exports while the raw material procurement is done completely from the domestic market, thereby exposing the company to risks associated with adverse fluctuations in the foreign currency. However, the forex risk is mitigated to some extent as a part of the working capital limit is availed in foreign currency thereby providing hedge against adverse currency movements. GNA's products find applications in the automobile sector (commercial vehicles, tractors and off-highway vehicles) which is cyclical in nature. The demand for this industry is susceptible to changes in the economic climate. A fall in the level of economic activity can dissuade the customers, thereby impacting the sales of the automotive industry as the automobile manufacturers may limit the production levels.
The automobiles sector was already grappling with soft consumer demand in FY20. Additionally, the strict enforcement of Government rules to adopt new emission standards, led to OEMs hiking their product prices and further deferred consumers' purchases. With outbreak of Covid-19 pandemic, economic activities across the country remain disrupted since March 2020 due to lockdown. The pandemic caused disruptions in supply chains and brought manufacturing activity to a halt for nearly 30 days. Due to the multiple lockdowns, various OEMs, ancillaries and dealers located in containment zones, witnessed near nil activity in April and few days of May 2020. The overall economic uncertainty with macro-economic headwinds and constrained financing environment may translate into weak consumer sentiment and result in contraction in demand for OEMs.

Elongated operating cycle: The operating cycle of the company elongated further to 120 days, as on March 31, 2020 (PY: 99 days) on account of elongated average collection days. This was mainly due to lockdown imposed in India and abroad which led to some of the payments which were due from its customers getting delayed in the month of March-2020.

Liquidity: Adequate - GAL's liquidity position has remained adequate as reflected by current ratio of 1.85x, as on March 31, 2020 (PY: 1.66x). The quick ratio of the company stood at 1.31x, as on March 31, 2020 (PY: 1.13x). The company had free cash & bank balance of Rs.21.1 crore as on March 31, 2020 (PY: Rs. 0.36 crore). The average utilization of cash credit limit remained at ~10% on an average, while the PCFC limit remained fully utilized in the last 12 months ended June- 2020. The operating cycle of the company stood elongated at 120 days, as on March 31, 2020. The company has a total debt repayment obligation of Rs.31.16 cr. in FY21, which is proposed to be met through the internal accruals. The company has already paid around Rs. 10.28 cr. till June 30, 2020, out of the total debt repayment obligation due for the year. The firm has not availed the moratorium offered by RBI in light of Covid-19 pandemic, for payment of its debt obligations.

Analytical approach: Standalone.

Applicable Criteria
Criteria on assigning Outlook and credit watch to Credit Ratings
Financial ratios – Non-Financial Sector
CARE's policy on default recognition
Liquidity Analysis of Non-Financial Sector Entities
CARE's methodology for manufacturing companies
Criteria for Short Term Instruments
CARE's methodology for Auto Ancillary Companies

About the Company
GNA Axles Limited (GAL) is a Jalandhar based company, incorporated in the year 1993. GAL is the flagship company of the GNA group, set-up in the year 1946 for manufacturing of auto components for commercial vehicles, tractors and off-highway equipments. The company is engaged in the business of manufacturing and supplying axle shafts and spindles (ranging from 2 kg to 150 kg) to OEMs and Tier-1 suppliers. GAL has its manufacturing facilities located in Hoshiarpur, Punjab with an installed capacity of ~6 million pieces per annum, as on March 31, 2020. Apart from catering to the domestic clients, GAL also exports its products to USA, Brazil, Sweden, Mexico, Italy, Spain, etc.

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	935.20	910.29
PBILDT	145.44	125.77
PAT	65.49	52.32
Overall gearing (times)	0.42	0.43
Interest coverage (times)	17.95	9.25

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	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	40.00	CARE A+; Negative
Non-fund-based - ST-Bank Guarantees	-	-	-	0.50	CARE A1
Term Loan-Long Term	-	-	May-2025	124.00	CARE A+; Negative
Fund-based - LT-Packing Credit in Foregin Currency	-	-	-	80.00	CARE A+; Negative
Non-fund-based - ST-Letter of credit	-	-	-	5.00	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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Cash Credit	LT	40.00	CARE A+; Negative	-	1)CARE A+; Stable (05-Jul-19)	1)CARE A; Positive (03-Jan-19) 2)CARE A; Positive (26-Jul-18)	1)CARE A; Stable (12-Jun-17) 2)CARE A; Stable (13-Apr-17)
2.	Non-fund-based - ST-Bank Guarantees	ST	0.50	CARE A1	-	1)CARE A1 (05-Jul-19)	1)CARE A1 (03-Jan-19) 2)CARE A1 (26-Jul-18)	1)CARE A1 (12-Jun-17) 2)CARE A1 (13-Apr-17)
3.	Term Loan-Long Term	LT	124.00	CARE A+; Negative	-	1)CARE A+; Stable (05-Jul-19)	1)CARE A; Positive (03-Jan-19) 2)CARE A; Positive (26-Jul-18)	1)CARE A; Stable (12-Jun-17) 2)CARE A; Stable (13-Apr-17)
4.	Fund-based - LT-Packing Credit in Foregin Currency	LT	80.00	CARE A+; Negative	-	1)CARE A+; Stable (05-Jul-19)	1)CARE A; Positive (03-Jan-19) 2)CARE A; Positive (26-Jul-18)	1)CARE A; Stable (12-Jun-17) 2)CARE A; Stable (13-Apr-17)
5.	Non-fund-based - ST-Letter of credit	ST	5.00	CARE A1	-	1)CARE A1 (05-Jul-19)	1)CARE A1 (03-Jan-19) 2)CARE A1 (26-Jul-18)	1)CARE A1 (12-Jun-17) 2)CARE A1 (13-Apr-17)

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

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Fund-based - LT-Packing Credit in Foregin Currency	Simple
3.	Non-fund-based - ST-Bank Guarantees	Simple
4.	Non-fund-based - ST-Letter of credit	Simple
5.	Term Loan-Long Term	Simple

***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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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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