Lokesh Machines Limited

October 13, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	75.67 (Enhanced from 62.61)	CARE BB+; Negative (Double B Plus; Outlook: Negative)	Reaffirmed and outlook revised from stable
Long Term / Short Term Bank Facilities	6.25	CARE BB+; Negative / CARE A4 (Double B Plus ; Outlook: Negative/ A Four)	Reaffirmed and outlook revised from stable
Short Term Bank Facilities	13.25	CARE A4 (A Four)	Reaffirmed
Total Facilities	95.17 (Rs. Ninety-Five Crore and Seventeen Lakhs Only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Lokesh Machines Limited (LML) continue to remain constrained by stretched liquidity position, elongated operating cycle resulting in extensive utilization of working capital limits, revenues (to a large extent) being dependent on the auto sector which has muted growth prospects. The ratings are further tempered by, net losses reported by LML during FY20 (FY refers to the time period between April 01 to March 31) and Q1FY21 along with significant y-o-y decline in the total operating income (TOI). Nevertheless, the ratings remain underpinned by, experienced promoters with established track record in the machine tool industry, long standing relationships with marquee OEM players, moderate order book position and comfortable capital structure albeit moderate debt coverage indicators.

Outlook: Negative

Negative outlook is on account of declining scale of operations, elongating operating cycle and losses being reported q-o-q, which if continues, may have an adverse impact on the overall financial risk profile of the company, going forward. The outlook may be revised to "stable" if the company is able to demonstrate consistent improvement in its operational and financial performance in the coming quarters.

Rating Sensitivities

Positive factors:

- ✓ Increase in the contribution of SPM resulting in TOI increasing to more than Rs 170 crore while improvement in PBILDT margin to 15% or above in future.
- ✓ Ability of the company to improve its operating cycle to less than 180 days, on a sustained basis.

Negative factors:

- × Decline in the TOI to less than Rs 100 crore or continued net losses.
- × Any further elongation in the operating cycle from the present level.

Detailed description of the key rating drivers

Key Rating Weakness

Decline in operating income accompanied by net loss during FY20 and Q1FY21

Owing to the subdued demand from the automobile industry and lockdown imposed during the last ten days in the month of March (which usually happens to be a major revenue generating month for LML) TOI of the company declined by 34% y-o-y during FY20 as finished products (GPM) amounting to Rs 25 crore could not be shipped. Consequently, the company also reported net losses during Q4FY20 and FY20. The company resumed operations at reduced capacities from May, 2020 which resulted in subdued performance during Q1FY21 as well. LML booked a net loss on a revenue of ~Rs 16 crore in Q1FY21 which is about half of the revenue it achieved during the corresponding quarter of last year.

Elongated Operating Cycle

The operating cycle for the company remained elongated and further stretched from 202 days as on March 31, 2019 to 292 days as on March 31, 2020 on account of the increased inventory holding period of the company. The average collection period

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

in FY20 also elongated to 82 days from 54 days because of lower TOI as against similar receivable levels like previous year. Resultantly, the utilisation of working capital bank limits remained high. Also, the company availed additional COVID relief loan amounting to Rs 4.45 crore in order to meet its short term cash flow mismatches.

Significant reliance on auto sector coupled with prospects in Aerospace Segment
The fortunes of LML are highly dependent on the performance of the automobile industry which currently is in a bad shape. Although, percentage contribution from non-auto customers have been increasing Y-o-Y as LML is focused towards diversifying the revenue channels but the revenue concentration from Auto segment continues to remain high at more than 50%. However, the company has prospects to tap the aerospace sector where precision job work has high demand where LML specializes.

Key Rating Strengths
Experienced Promoters
LML is promoted by Mr M. Lokeswara Rao, who has four decades of experience in Machines Tools industry. He worked for eleven years in HMT before starting LML. The company also derives strength and managerial capabilities from experience of other promoters i.e. Mr. Kishore Babu, Mr. M. Srikrishna and Mr. M. Srinivas who also have rich experience in the Machine Tools design and manufacturing segment. Mr. B. Kishore Babu is the Co-promoter of Lokesh Machines Limited. He is an Engineering graduate and has worked in the various departments' right from shop floor, designs, planning, production, assembly, Purchase and application engineering and has also been trained in various countries. The promoters have also been infusing funds to repay some of company's debt obligations. The company is also supported by four other directors from diversified fields like finance, power and designing

Satisfactory capital structure albeit moderate coverage indicators
Despite increase in the total term debt and erosion in the net worth, the capital structure of the company continues to remain comfortable with a below unity overall gearing ratio at 0.57 (PY: 0.54) as on March 31, 2020. However, the coverage indicators of the company remained at moderate level with an interest coverage ratio of 1.06x in FY20 and long term debt equity ratio of 0.16x as on March 31, 2020

Long standing relationships with reputed clientele
With more than two decades of operations in machine tools industry LML has been successful in establishing itself as one of prominent CNC manufacturers in India. Further, the company has been successful in obtaining repeat orders for its machinery division from major OEM manufacturers like Mahindra and Mahindra, International Tractors Limited, Kirloskar Oil Engines Limited and VE Commercial Vehicles Ltd
With a separate plant at Pune which caters specifically to the demand of Mahindra and Mahindra Ltd, LML has customer with strong credit profile which ensure timely collections. This division under takes cylinder manufacturing and other job works to Mahindra and Mahindra Ltd.

Moderate order-book position albeit strategic alliances with key global players
As of August, 2020 the company has an outstanding order book of Rs 81.14 crore which includes orders for GPM (General Purpose Machines), SPM (Special Purpose Machines) and job works. The existing order-book provides short term revenue visibility to the company. Further, LML has a strategic alliance with Tongtoi Machine & Tool Company Ltd. Taiwan (One of the leading machine tool manufacturing companies) to manufacture Hi-Speed Vertical Machining center model EZ5 for the Indian Market thereby providing assured revenue along-with better collection turnaround.

Industry Outlook
In March 2020, auto industry sales (including PVs, CVs and two & three wheelers) registered a y-o-y double-digit decline of about 41.6% in overall sales vis-à-vis a decline of about 11.6% registered during the corresponding period previous year. The sales decline during the period was largely on account of weak demand for commercial vehicles that recorded a sharp decline of over 86% followed by about 50% decline in passenger vehicles segment**.** Price hikes of about 10-15% in passenger vehicles and two wheeler segments due to new safety norms starting April 1, 2019, higher insurance costs and unsold inventories at retail (dealers) level causing slow movement in wholesale movement led to the overall decline of automobile sales during the month.
After a gloomy 1st quarter in on-going fiscal, the 2nd quarter began on a good note as July 2020 witnessed positive growth (M-o-M) in production, domestic sales and exports of automobiles. Passenger vehicles, tractors and 2&3 wheelers segments have shown good momentum during the month on a sequential basis, which gives us hope for recovery in the forthcoming future

Liquidity: Stretched
The liquidity position of the company is stretched with extensively utilized bank limits, modest cash balance and tightly matched accruals to repayment obligations. The average working capital utilization was high at 96.65% for the past twelve

months ended June, 2020. The company had availed additional line of credit (COVID loans of Rs 4.45 crore) for meeting some of its fixed cost during the lockdown period. Also, the company has availed moratorium for servicing its debt obligations for a period six months (March, 2020 to August, 2020).

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
Rating Methodology -Auto Ancillary Companies
Rating Methodology -Manufacturing Companies
Financial ratios –Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Criteria for Short Term Instruments
CARE's Policy on Default Recognition

About the Company
Lokesh Machines Ltd (LML) incorporated in December 1983 is promoted by Mr. M Lokeswara Rao and the company has started commercial operations from 1986. The company's operations can be segregated into two divisions namely Machines and Components division. The company initially started the operations by doing job works for Hindustan Machine Tools Limited (HMT) later on moved to manufacturing of machines. Under machinery division, LML manufactures Special Purpose Machines (SPM) and General Purpose Machines (GPM). Under component division, the company manufactures automobile components viz., cylinder heads, and cylinder blocks and also executes job work for automobile manufacturers like Mahindra & Mahindra (M&M) and Ashok Leyland etc. The company is listed on BSE and NSE.

Brief Financials (Rs. crore)	FY19(A)	FY20 (A)
Total operating income	191.18	126.22
PBILDT	32.00	12.47
PAT	6.77	-4.68
Overall gearing (times)	0.54	0.57
Interest coverage (times)	2.48	1.06

A: Audited
Status of non-cooperation with previous CRA: NA

Any other information: NA

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	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	March, 2035	11.22	CARE BB+; Negative
Fund-based - LT-Cash Credit	-	-	-	64.45	CARE BB+; Negative
Non-fund-based - ST-Letter of credit	-	-	-	10.00	CARE A4
Non-fund-based - ST-ILC/FLC	-	-	-	3.25	CARE A4
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	6.25	CARE BB+; Negative / CARE A4

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-Term Loan	LT	11.22	CARE BB+; Negative	-	1)CARE BB+; Stable (28-Aug-19)	1)CARE BB; Stable (14-Jan-19)	1)CARE B-; Stable (03-Jan-18)
2.	Fund-based - LT-Cash Credit	LT	64.45	CARE BB+; Negative	-	1)CARE BB+; Stable (28-Aug-19)	1)CARE BB; Stable (14-Jan-19)	1)CARE B-; Stable (03-Jan-18)
3.	Non-fund-based - ST-Letter of credit	ST	10.00	CARE A4	-	1)CARE A4 (28-Aug-19)	1)CARE A4 (14-Jan-19)	1)CARE A4 (03-Jan-18)
4.	Non-fund-based - ST-ILC/FLC	ST	3.25	CARE A4	-	1)CARE A4 (28-Aug-19)	-	-
5.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	6.25	CARE BB+; Negative / CARE A4	-	1)CARE BB+; Stable / CARE A4 (28-Aug-19)	-	-

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 the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Fund-based - LT-Term Loan	Simple
3.	Non-fund-based - LT/ ST-Bank Guarantees	Simple
4.	Non-fund-based - ST-ILC/FLC	Simple
5.	Non-fund-based - ST-Letter of credit	Simple

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

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