Talbros Engineering Limited

August 02, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating	Remarks
Long-Term Bank Facilities	11.72 (reduced from 19.61)	**CARE A-; Negative (Single A Minus; Outlook: Negative)**	Reaffirmed and Outlook revised from Stable to Negative
Long/Short Term Bank Facilities	57.80	**CARE A-; Negative/ CARE A2+ (Single A Minus; Outlook: Negative/ A Two Plus)**	Reaffirmed and Outlook revised from Stable to Negative
Total	**69.52 (Rupees Sixty Nine Crore and Fifty Two Lakhs only)**		

**Details of facilities in Annexure-1*

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Talbros Engineering Limited (TEL) continue to derive strength from the experience of the promoters in the auto ancillary industry, long track record of operations and the reputed client base with longstanding relationships. The ratings continues to draw comfort from its consistent growth in total income and operating profits, moderate coverage indicators, and regular infusion of funds by promoters in form of unsecured loans and completion of majority capex for increasing the capacity. However, the ratings are constrained by relatively leveraged capital structure, Increased inventory levels on account of downward spiral in automobile sales, customer and product concentration risk, susceptibility to volatility in raw material prices and dependence on the fortunes of the cyclical auto industry.

Going forward the ability of the company to profitability increase scale of operations, manage its working capital efficiently, any further capex and its funding pattern would be key rating sensitivities.

Outlook: Negative

The outlook for the rating has been revised to negative on account of increase in inventory levels at the end of FY19, profitability margins on account of overall slowdown in the auto sector. Going forward, the outlook may be revised to 'Stable' if inventory levels reduce to more sustainable levels and the overall operating cycle gets normalized.

Detailed description of the key rating drivers

Key Rating Strengths

Long track record of operations with experienced promoters

TEL has a long track-record of operations dating back to 1980 and was earlier part of the erstwhile Talbros Group. The Talbros Group was founded in 1930s by Talwar family and has been into manufacturing of automotive components since 1957. The BNT Talbros Group is original equipment (OE) suppliers to many vehicle manufacturers in India, including passenger vehicles, commercial vehicles, trucks, buses, light-utility vehicles etc. The key managerial personnel of TEL - Mr. Rajesh Talwar, President and Mr. Tarun Talwar, Chief Operating Officer have a vast experience in the automotive and engineering industry and are actively involved in the day-today operations of the company.

Reputed client base with established relationship albeit concentration risk

TEL has an established relationship with leading auto manufacturers. Its top revenue contributors are well established players who enjoy strong position in the industry. TEL is the sole supplier of rear axle shafts for various models to most of its clients. The top 3 customers of the company (Mahindra & Mahindra Ltd., Spicer India Ltd., Automotive Axles Ltd.) contributed 69% of the total sales in FY19 as against 68% in FY18, with Mahindra & Mahindra Ltd. contributing to ~40% of its total sales. TEL's total sales are further diversified with ~80% (PY: 79%) sales derived from domestic market and the balance 20% (PY: 21%) sales from exports. The company export to countries like North America, South America, Brazil and Canada. About 90% of all axle shafts manufactured by TEL are used by Original Equipment Manufacturers (OEMs) or Tier 1 suppliers. With respect to the new capex undertaken by the company at the IMT, Faridabad plant, which is fully automated, the company has been able to achieve process efficiency and thus improve its operational performance.

Financial Risk Profile

In FY19, the total operating income of TEL witnessed y-o-y 32% growth to Rs.269.25 crore as against Rs.203.97 crore in FY18. The growth in total operating income is on account of expansion done in order to meet new orders from existing and new customers and increased utilization levels. The PBILDT margins declined during FY19 to 8.89% in FY19 (PY: 10.17%) and PAT margin stood at 2.66% in FY19 (PY: 4.38%). The decrease in profit margins is primarily due to increase in raw material costs

(steel).
In FY19, the total debt increased to Rs.80.36 crore as on 31-Mar-19 as against Rs.51.97 crore as on 31-Mar-18. The increase in debt is on account of funding of expansion activities. Majority of debt comprises of working capital limits which is inherent in auto component industry. As on 31-Mar-19, the overall gearing moderated to 1.23x (PY: 0.88x) and total debt/ GCA stood high at 5.46x (FY18: 3.60x). However, the company maintained its cash accruals at Rs.14.73 cr (FY18: Rs.14.43 cr). Interest coverage ratios declined during FY19 to 3.51x (FY18: 6.10x).

Key Rating Weaknesses
Low bargaining power with customers and susceptibility of margins to volatility in raw material prices
There exists limited bargaining power with the customers. Since the major customers are auto companies/OEMs, the company does have a mechanism wherein any revision in the raw material prices is reset by the OEMs on monthly basis and the change in the raw material prices are accommodated subsequently. The major raw material (Steel) cost accounts for 55%-60% of total operating income, furthermore, global prices for Steel are volatile which exposes TEL to price risk.
Due to its expansion project, the company has been procuring more raw materials in order to produce more units. Over the years, the cost of raw material has also increased.
Major capital expenditure completed during FY19, albeit debt funded
TEL has installed new machineries at their Faridabad plants in order to meet increased automotive components demand. The company undertook expansion work at a total cost of ~Rs.28 crore. The total capex includes ~Rs.12 crore and ~Rs.16 crore as project cost at Sector-4 and IMT respectively. The total capex for the above projects and other maintenance capex incurred in FY19 were primarily funded through a total debt of Rs.21 crore loan from financial institutions and the balance through internal accruals. As a result, the overall gearing reached to 1.23x in FY19 as against 0.88x in FY18. TEL's majority of the capex is complete which has led to increase in installed capacity to 21 lakhs units in FY19 (PY: 18 lakhs). The capacity utilization stood at 91.80% in FY19.

Liquidity: In FY19, the current ratio stood at 1.06 as against 1.23 in FY18. The operating cycle increased to 86 days in FY19 from 79 days in FY18. In FY19, average inventory days were 66 days (PY: 57 days) with the average collection days being 59 days (PY: 53 days). Since majority of the capex is over, the liquidity is expected to improve from FY20 onwards.

Industry scenario:
There was an increase in auto sales in FY19 over FY18, by ~6.5%. Commercial vehicles recorded the highest growth of ~16% in FY19. Sales in exports also improved and registered a growth by ~14.5%. However, the auto industry is witnessing a slowdown in growth from the last quarter of FY19. Domestic economic activity slowed down through the year and weakened notably in the second half of FY19. In Q1 FY20, automobile sales witnessed the sharpest decline of 10.5% y-o-y in the last 5 years on back of price hikes in passenger vehicles and two wheeler segments due to new safety norms starting April 1, 2019, higher insurance costs, higher ownership costs, liquidity crisis in the NBFC sector, increased load carrying capacity for M&HCVs that led to high inventories at retail (dealers) level causing slow movement in wholesale movement of vehicles.
Going forward, CARE expects demand to continue to remain muted during Q2 FY20 and pick up only by Q3 FY20 and continue in Q4 FY20 with various planned product launches, festival demand and pre-buying of automobiles before the implementation of BS-VI norms on April 1, 2020. Also, with higher MSPs announced for FY20, farm income is expected to be marginally higher and encourage rural spending.

Analytical approach: Standalone

Applicable Criteria
CARE's Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
CARE's criteria for Short Term Instruments
Rating Methodology-Manufacturing Companies
Rating Methodology – Auto Ancillary Companies
CARE's methodology for financial ratios (Non-Financial sector)

About the Company
Talbros Engineering Ltd (TEL), originally a part of Talbros Automotive Components Ltd. was separated into another company in 1996. TEL is engaged in the manufacturing of automotive rear axle shafts and other splined shafts and forgings used in commercial vehicles, utility vehicles and tractors. TEL has total five manufacturing plants with total manufacturing capacity of 21 lakhs axle shafts per annum as on March 31, 2019. The company manufactures and sells 90% of its products to domestic Original Equipment Manufacturers (OEMs) and Tier-1 suppliers of auto components.

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

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	203.97	269.25
PBILDT	20.74	23.94
PAT	8.96	7.20
Overall gearing (times)	0.88	1.23
Interest coverage (times)	6.10	3.51

A: Audited

Status of non-cooperation with previous CRA: ICRA suspended the rating in September, 2016 on non-availability of the information.

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-Term Loan	-	-	Apr 2022	11.72	CARE A-; Negative
Fund-based - LT/ ST-Cash Credit	-	-	-	57.80	CARE A-; Negative / 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 (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.	Fund-based - LT-Term Loan	LT	11.72	CARE A-; Negative	-	1)CARE A-; Stable (04-Jan-19)	1)CARE A-; Stable (09-Feb-18)	1)CARE BBB+ (29-Nov-16)
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	57.80	CARE A-; Negative / CARE A2+	-	1)CARE A-; Stable / CARE A2+ (04-Jan-19)	1)CARE A-; Stable / CARE A2+ (09-Feb-18)	1)CARE BBB+ / CARE A2 (29-Nov-16)

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

Name of the Instrument	Detailed explanation
Financial covenants	
As per sanction letter of the bank, 'all unsecured loans/ deposits from promoters and related parties as on 31 March, 2019 to the extent of Rs. 12 crore shall stay subordinated to bank loans and to remain invested in business during the tenure of our facilities'.	Unsecured loans from promoters as on 31-March-2019 stood at Rs.8.46 crore and has been treated as quasi-equity and considered in the net worth of the company as per CARE's policy.
Non financial covenants - None	

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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