Voltamp Transformers Limited

July 07, 2020

Ratings

Bank Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term bank facilities	10.00	CARE AA; Stable [Double A; Outlook: Stable]	Reaffirmed
Long-term/Short-term bank facilities	282.50	CARE AA; Stable / CARE A1+ [Double A; Outlook: Stable / A One Plus]	Reaffirmed
Total Facilities	**292.50 (Rupees two hundred ninety two crore and fifty lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale and Key Rating Drivers

The ratings assigned to the bank facilities of Voltamp Transformers Ltd (VTL) continue to be underpinned by its established track record of operations in transformer business with reputed and diversified clientele, experienced management with a conservative policy on use of debt along with its comfortable capital structure and healthy debt coverage indicators. The ratings further derive strength from improvement in its operating profitability (PBILDT) margin and cash flow from operations during FY20 (refers to the period from April 01 to March 31) which has led to further improvement in its already strong liquidity.

The long term rating, however, continues to remain constrained on account of VTL's moderate scale of operations along with moderation in its revenue visibility, high reliance on non-fund based working capital limits and susceptibility of its profitability to volatile raw material prices and competitive pressure. The ratings also take into cognizance the expected moderation in VTL's total operating income (TOI) and profitability during H1FY21 owing to unprecedented disruptions caused by the spread of Covid-19 pandemic; however, it may be noted that, the company has not availed the moratorium granted by the lenders as a COVID relief measure (as permitted by the Reserve Bank of India; RBI) for its debt obligations due to its strong credit profile and ample liquidity.

Rating Sensitivities

Positive Factors

- *Increase in total operating income (TOI) by over 50% from FY20 levels on a sustained basis; along with diversification in its product profile*
- *Improvement in its PBILDT margin and overall return on capital employed (ROCE) to above 20% on a sustained basis along with sustenance of its comfortable capital structure and healthy liquidity*

Negative Factors

- *Sustained decline in total operating income (TOI) at a compounded annual rate of 30% or above in next two years ended FY22*
- *Significant depletion in liquidity with its unencumbered liquid investments falling below Rs.300 crore or significant elongation in its gross working capital cycle with sustained negative cash flow from operations*
- *Deterioration in its overall gearing to 0.50x or above on a sustained basis*

Detailed description of the key rating drivers

Key Rating Strengths

Experienced management with long track record of operations in transformer industry

Late Mr. Lalit Kumar Patel, principal promoter of VTL, was a technocrat having over four decades of experience in the transformer industry. Company is currently being managed by the second generation of the promoter family, along with a team of professionals.

Mr Kunjal L. Patel, Vice Chairman of VTL, is the son of Late Mr. Lalit Kumar Patel and holds a bachelor's degree in Electrical Engineering. He has over two decades of vast experience in production & marketing of transformers and looks after the overall operations of the company including purchase & planning, manufacturing, quality control and design

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

aspects. Mr. Kanubhai S. Patel, Chairman & Managing director of the company, is a Chartered Accountant by profession. He looks after the general management, new business sourcing and overall strategy building for VTL.

During past few years, when the transformer industry witnessed a challenging phase with subdued order inflow and aggressive bidding by industry players which adversely impacted their profitability and resulted in elongation of receivables, VTL was able to successfully navigate through this phase on account of its selective order bidding and focus on cash flows, instead of aggressive debt-funded growth.

Diversified and reputed clientele

VTL has a diversified clientele with more than 1,000 customers across various end-use industries such as power, oil refineries, textile, chemical, real estate, automobile, infrastructure and steel spread across the country. Over the years, VTL has established long standing relationship with reputed players in these industries which have facilitated it in securing repeat orders from its clients. Furthermore, over 95% of VTL's sales in last three years have been to private players having good credit profile, thereby resulting in very limited exposure to State Government power sector undertakings wherein inherently the receivables are elongated. Client concentration also remained low as VTL's top 10 customers comprised only around 26% of its total sales during FY20, similar to FY19 level.

VTL's focus on private players with good credit profile along with significantly diversified clientele has held it in good stead over the years by way of relatively steady profitability and healthy generation of cash flows through timely realisation of receivables. Company's focus on collections has resulted in significant reduction in its outstanding debtors from around Rs.150 crore as on March 31, 2020 to around Rs.40 crore as on May 31, 2020.

Steady scale of operations and improved profitability during FY20

VTL's focus on cash flows with selective order bidding has resulted in a steady growth in its scale of operations over the years with stable profitability and build-up of significant unencumbered liquid investments which has been maintained in the company.

Company's TOI, post registering a 28% y-o-y growth in FY19, grew marginally by around 4% in FY20 to Rs.878.65 crore. Growth in TOI was restricted mainly due to dip in income during Q4FY20 owing to discontinuation of operations from March 23, 2020 due to a nationwide lockdown announced by the Central Government as a measure to check the spread of Covid-19 pandemic. This resulted in an overall y-o-y dip of ~7% in the sales volume during FY20, though sales realisation improved ~11% during the year due to VTL's diversified product mix and better pricing power.

PBILDT margin of the company improved during FY20 by over 150 bps to 14.64% during FY20 aided by reduction in raw material prices, while PAT margin also remained healthy at over 10% during the year. While VTL's operating ROCE remained healthy at over 29% during FY20, its total ROCE was restricted to below 16% due to moderate return of around 6-8% p.a. registered on its sizeable investment portfolio which formed a good part of the company's overall capital employed. Gross cash accruals (GCA) of the company also remained healthy at over Rs.90 crore, in FY20, similar to FY19 level.

Comfortable capital structure and healthy debt coverage indicators

VTL's capital structure continued to remain comfortable marked by a strong net worth base of Rs.747.22 crore as on March 31, 2020 against no outstanding fund-based debt (except for interest free mobilization advances) and a market capitalisation of around Rs.1,150 crore as on June 26, 2020. Its overall gearing was very comfortable at 0.04x as on March 31, 2020 (P.Y.: 0.04x).

Its debt coverage indicators, viz. PBILDT interest coverage, Total Debt/GCA and Total Debt/PBILDT, also continued to remain highly comfortable on the back of its low debt profile, healthy cash flows and steady profitability.

Liquidity: Strong

Liquidity of VTL continues to remain strong marked by nil term debt repayment obligations, nil utilization of fund based working capital limits along with presence of healthy and growing unencumbered liquid investments which stood at ~Rs.535 crore as on May 31, 2020 (having increased from Rs.453.92 crore as on March 31, 2020). Almost 69% of its liquidity was invested in mutual funds as on March 31, 2020. Company mainly utilises non-fund based limits in the form of bank guarantees in its normal course of business, the average utilisation of which (including long-term performance guarantees) remained moderate at ~70% during the twelve months ended May 2020.

Further, with a comfortable capital structure, VTL has sufficient gearing headroom to raise additional debt for its capex/working capital needs. Also, its entirely unutilized fund based working capital bank lines are more than adequate to meet its incremental working capital needs over the next one year. VTL's liquidity is further underpinned by its healthy current ratio of over 5x as on March 31, 2020. Its focus on collections have resulted in controlled receivable days, however negligible credit period availed by the company from its suppliers owing to its strong liquidity and requirement to maintain adequate inventory level for uninterrupted production results in an elongated working capital cycle of around 120 days.

Despite the uncertainty emanating from the spread of a black swan event like the Covid-19 pandemic, the company has made payment of full salaries to all its employees, including to contract workers, and has also made its vendor payments and statutory dues on time. Furthermore, it has also not sought/availed any moratorium on any of its debt from its lenders; the option for which was available as per RBI's package announced as a Covid-19 relief measure.

Key Rating Weaknesses

Moderate scale of operations along with moderate revenue visibility and expected fall in its TOI and profitability during H1FY21 owing to Covid-19 pandemic

Despite its long track record of operations, VTL's scale of operations has remained moderate marked by a TOI of Rs.878.65 crore during FY20. Further, the order book of VTL stood at Rs.471.05 crore as on June 08, 2020 translating into 0.54x of its FY20 TOI, thus only providing a moderate revenue visibility. However, the stance of VTL's management of generally being selective in bidding for orders over the years has also resulted in steady cash flow backed growth for the company.

Manufacturing operations of the company, post discontinuation from last week of March 2020 due to imposition of nationwide lockdown to control the spread of Covid-19 pandemic, gradually commenced from April 22, 2020 and the company has also received new orders of over Rs.80 crore in Q1FY21. However, with non-commencement of full scale operations at the end of its vendors and customers, VTL's operations are currently at sub-optimal levels and consequently its TOI and profitability are expected to contract during FY21; and especially during H1FY21. Nevertheless, its healthy liquidity and long track record of operations in the industry is expected to help in tiding over the adverse impact of Covid-19. However, VTL's scale of operations is expected to remain at a moderate level for the foreseeable future compared to the size of the transformer industry and the larger capital goods industry.

High reliance on non-fund based working capital limits

VTL's operations are heavily reliant on non-fund based working capital limits since it has to extend bank guarantees (both performance and financial) to its customers; the average tenor of performance bank guarantees (PBGs) extended by it for transformers sold by it range from 3-6 years. However, there has not been any instance of invocation of such guarantee extended by the company over last many years. Furthermore, over the past few years, the transformer failure rates on its supplied products have been low. VTL's transformers have witnessed low defects / failures, as reflected from its low expenditure on repairs and hence restricted requirement of accumulation of funds in its provisions for warranties, the period for which usually ranges from 12 to 60 months.

The PBGs are normally extended by VTL for the defect liability period on the transformers supplied to its clients and occasionally also for release of retention money. Financial bank guarantees are required by it for availment of mobilization advances. However, large part of the guarantees issued by the company is in the nature of PBG.

Exposure to volatile raw material prices and competitive pressure

The prices of primary raw materials such as copper and cold rolled grain oriented (CRGO) steel required by VTL (which account for ~60% of total raw material cost) are highly volatile in nature as they are linked to prices in global market. This exposes VTL's profitability to raw material price fluctuation risks since majority of the company's orders are fixed price in nature. Also, with global manufacturing of CRGO steel concentrated amongst 15 major suppliers and lack of any meaningful domestic manufacturing capacity exposes the company to price volatility arising from forex fluctuation encountered by the importers of this material, from whom company procures it locally. Company does not have major imports or export income and has a reasonable hedging policy in place for its major raw materials (mainly copper).

Stable long-term demand outlook; albeit susceptibility to cyclical demand and challenging medium-term scenario due to Covid-19 pandemic

Government plans to add 93 GW of power generation capacity by 2022 would require a strong power evacuation infrastructure base in the country and this shall fuel the demand for Transmission & Distribution (T&D) equipment. Government's focus on rural electrification, reduction in T&D losses and its efforts to increase coal availability and green energy market is expected to result in stable demand for T&D players in near to medium term. Around 3 lac MVA transformation capacity is expected to be added in the 13th five-year plan (FYP), i.e. till FY22, out of which around 69% was added till 9MFY20, which resulted in double digit growth in the industry to over Rs.16,440 crore. While there was some de-growth in the production volumes for transformers in FY20 due to delays in order finalization and lack of availability of proper funding, overall, going forward, expected addition of balance transformation capacity is expected to augur well for the manufacturers of T&D equipment including transformers. However, company remains susceptible to cyclicality associated with capital goods industry which forms sizeable client base for the company, along with weak overall economic growth in the medium-term induced largely by the outbreak of Covid-19 pandemic.

Analytical Approach: Standalone

Applicable Criteria:
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
CARE's methodology for manufacturing companies
Financial ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector

About the Company
Promoted by Mr. Lalit Kumar Patel and his family in 1967, VTL is engaged in manufacturing of electrical transformers. Its product portfolio comprises oil-filled power and distribution transformers upto 160 mega volt ampere (MVA), 220 kilo volt (KV) class and dry type transformers upto 12.50 MVA, 33 KV class. The products find application in varied industries including power, oil refineries, real estate, infrastructure and steel.
VTL has a diversified clientele, including private players and select PSUs, with private players contributing to majority of its revenue. Company's production facilities are located at Makarpura and Savli in Vadodara, Gujarat with an aggregate installed capacity of 13,000 MVA as on March 31, 2020.
Promoters of VTL have initiated an amalgamation between VTL and Kunjal Investment Private Limited (KIPL); an investment arm of VTL's promoter family which holds 42.94% shareholding in VTL. Equity shares of VTL held by KIPL are proposed to be issued and allotted to the shareholders of KIPL. The promoters' shareholding in VTL is expected to remain same post amalgamation. None of the promoters' shares were pledged as on June 10, 2020.

Brief Financials (Rs. crore)	FY19 (A)	FY20#
Total operating income	845.70	878.65
PBILDT	111.04	128.59
PAT	84.84	89.38
Overall gearing (times)	0.04	0.04
Interest coverage (times)	188.97	177.34

A: Audited, # Abridged audited financial results published on Bombay Stock Exchange (BSE)

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
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	282.50	CARE AA; Stable / CARE A1+
Fund-based - LT-Cash Credit	-	-	-	10.00	CARE AA; Stable

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.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	282.50	CARE AA; Stable / CARE A1+	-	1)CARE AA; Stable / CARE A1+ (07-Oct-19)	1)CARE AA; Stable / CARE A1+ (05-Sep-18)	1)CARE AA; Stable / CARE A1+ (03-Oct-17)
2.	Fund-based - LT-Cash Credit	LT	10.00	CARE AA; Stable	-	1)CARE AA; Stable (07-Oct-19)	1)CARE AA; Stable (05-Sep-18)	1)CARE AA; Stable (03-Oct-17)

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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