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This rating methodology updates and supersedes ICRA's earlier methodology document on this sector, published in November 2022. While this revised version incorporates a few modifications, ICRA's overall approach to rating entities in the construction vehicles sector remains materially similar.

This rating methodology document explains ICRA's approach to analysing business and financial risk of entities engaged in the manufacture of construction vehicles. The objective is to help issuers, investors, and other interested market participants understand ICRA's approach to analysing the quantitative and qualitative risk characteristics of these entities that can influence the rating outcomes. This methodology does not include an exhaustive treatment of all factors that are reflected in the ratings but would enable the reader to understand the rating considerations that are usually the most important.

Overview

The Indian construction vehicle sector can broadly be divided into following sub-segments:

- Earth-moving equipment such as backhoes, wheeled loaders, excavators, diggers, dumpers and dozers. Earthmoving equipment deployed in mining are of larger tonnage and horsepower than those used in construction, and they also include some specialised equipment and implements such as underground mining equipment, articulated dump trucks, walking dragline and other tracked machines. Currently, this segment accounts for ~70% of the industry volumes.
- Material-handling equipment such as pick-and-carry (PNC) cranes and aerial cranes
- Road-building equipment such as soil compacters, motor graders, rollers and pavers.
- Concreting equipment such as concrete/transit mixers, batching plants and boom pumps.
- Material processing equipment – consisting of crushers and screeners

Rating Methodology

For analytical convenience, the key rating factors are grouped under the following broad heads – Industry Risk Assessment, Business Risk Assessment, and Financial Risk Assessment.

Industry Risk Assessment

- Demand drivers and Cyclicalities
- Competitive landscape
- Regulatory/ policy risks

Business Risk Assessment

- Scale of operations
- Market position
- Product portfolio
- Technology and product development capabilities

Financial Risk Assessment

- Profitability
- Leverage & coverage
- Working capital
- Liquidity and adequacy of cash flows

Other Elements of Credit Risk Assessment

Management Quality Assessment

Assessment of Environmental, Social and Governance (ESG) Risks

Industry Risk Assessment

Demand Drivers and Cyclicalities

Construction and mining equipment are critical components for capacity enhancement and gross fixed capital formation in any economy. The construction vehicle industry exhibits significant cyclicalities, often with sharp peaks and deep troughs. When construction, and mining/quarrying activity picks up, the sales surge, lead times stretch out and manufacturers can struggle to fulfil orders. Conversely, when activity slows, sales can fall away sharply, and contractors and rental companies find their fleets are more than adequate for the work they have on their books. ICRA evaluates the financial risks arising from such deep cycles, OEMs' risk mitigation practices, financial resilience and the past track record in tiding over such periods.

While the overall construction vehicle industry's fortunes are closely linked to the key drivers of the economy, such as investment in the infrastructure and construction space and industrial development, demand for each of the five sub-segments is linked to a different industry. Infrastructure investments in road building and construction activity drive the demand for earthmoving equipment, road construction equipment and material-handling equipment, while real estate and railways drive demand for concreting equipment. On the other hand, commodity cycles and the Government's mining policies determine the demand for mining (material processing) equipment. Demand for construction vehicles is heavily dependent on both - large Central Government projects and state-level investment plans – along with the budgetary funding availability. Projects announced and implemented in the state and the resultant equipment required is critical in estimating the future demand. This apart, private investment in infrastructure and capacity enhancement also has a significant impact on construction vehicle demand.

Competitive landscape

Competitive intensity in any industry is driven by multiple factors, including - industry fragmentation, entry barriers, nature of product or service (commoditised or differentiated), customer switching costs, and excess production capacity. Regulatory actions could also alter the level of competitive intensity in an industry. The Indian construction vehicle industry has over 200 players, with the presence of a few large global and local players. Competition has increased over the past decade with the entry of new OEMs into the market, while existing players have ventured into new segments to address the portfolio gaps and expanded their sales and service network, which has led to multiple players vying for a share in multiple sub-segments of the market. Nonetheless, certain OEMs continue to command strong market share in certain products.

Among the various segments of the construction vehicle industry, backhoes and excavators in the earthmoving segment account for a major share in terms of volumes (~70%) as well as value. While product diversity in the Indian market is adequate, given its relative nascency, demand currently leans largely towards general-purpose equipment as opposed to usage-specific or specialised equipment. While smaller capacity equipment is manufactured locally, the larger-sized or technologically complex/advanced equipment continues to be imported (or has higher share of imported components). The intense competition in the industry has also led to limited pricing power with the OEMs. While they do engage in periodic price hikes to pass on the impact of increased compliance costs or input costs, the ability to pass on these costs remains a function of the market scenario. Given the intense competition in the industry and limited switching cost for the customers, the OEMs must invest regularly in research and development (R&D) and new product development to differentiate and remain competitive in the market, as well as to meet the evolving regulations.

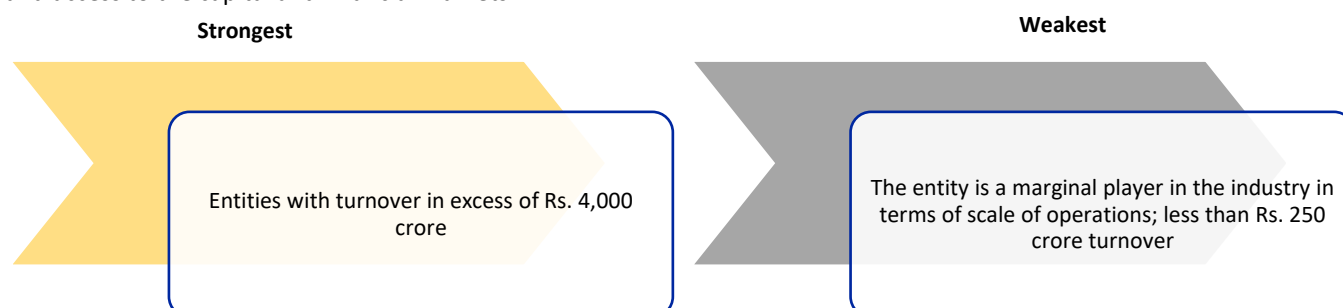
Regulatory/ Policy Risks

The construction vehicle industry, over the years, has been witnessing regulatory changes in terms of tightening of emission norms and safety features. While an OEMs' ability to meet the tightening standards in terms of equipment specifications is largely dependent on its technological and product development capabilities, the timelines for implementing these also remain critical. Furthermore, these changes typically result in product price increases, and accordingly, have the potential to impact demand, at least on a temporary basis (as was seen in the case of the revision in emission norms in 2021). Accordingly, regulatory and policy risks are looked at by ICRA as a part of the construction vehicle industry's risk assessment. Overall, while there have been regulatory changes, largely these have not been detrimental to the industry, given that information about the impending changes is known to the industry participants in advance, providing sufficient time to adapt.

Business Risk Assessment

Scale of operations

An entity's scale, reflected in its revenue base, is one of the key drivers of business strength and operating flexibility. A large scale of operation generally reflects greater market penetration, improved bargaining power and higher purchasing/operating efficiencies, while enhancing the business attractiveness for various stakeholders, including employees, customers and investors. Effectively, a large scale enables better cost absorption and greater ability to offer competitive pricing to buyers. A healthy scale of operations is an indicator of the staying power, flexibility in the market for deploying timely pricing strategies and access to the capital and financial markets.



Market Position

In addition to the scale of operations, a construction vehicle OEM's market position - as determined by its share within the specific sub-segments - is also an important determinant of its business strength and operating flexibility. A strong market position leads to revenue stability and pricing flexibility. An analysis of the competitive landscape, movement in market share and threat of imports, helps ICRA understand the level of price and product competition.

A company's market share can determine its ability to influence business trends and pricing within the industry. Accordingly, an assessment is made of the trend in the OEMs' scale and positioning within the industry. As the market share of an OEM can vary over a period, various qualitative aspects are also considered like the shift in consumer preferences, competitive intensity, new product introduction cycle and pricing strategy, while evaluating the trend in market share.

The Indian construction vehicle market is dominated by a few large OEMs for each product category. The past decade has witnessed the entry of several new players, mostly joint ventures and subsidiaries of global majors. Import threats from the established overseas manufacturers increased in the past decade, as large overseas manufacturers targeted product gaps in high potential markets like India. The ability to establish and sustain market share, in an evolving competitive landscape, requires a strong product and deep pockets to fund market penetrative strategies, given the strong incumbents. Apart from market share and brand strength of construction vehicle OEMs, the dealership and service network as well as financing tie-up with lenders also have a bearing on the market position.

Strongest

Market leader with greater than 50% market share (in addressable product segments).
Product market is largely organised

Weakest

Market is fragmented with the unorganised segment accounting for >50% of the market. Within the organised space, the market share of the rated entity is less than 10% (in the addressable product segments)

Dealer and Service Network

Given the vast geography and customer dispersion, an extensive dealership and service network across the country is important to ensure a strong market presence across various regions. Also, the local service network with ready availability of spare parts is critical for a high uptime and hence predictable cash flows for the equipment operators. A high base of installed equipment in turn leads to sizeable spare parts and service demand within a region.

Product Portfolio

The strength of a product portfolio is important for an OEM to sustain a competitive market position and enable it to cater to a diverse customer profile. A diversified product portfolio enhances an OEMs' ability to counter any demand variation in a specific product category or end-user industries. An OEM with a meaningful presence across different product segments tends to have a lower exposure to the cyclical trends. Apart from portfolio diversity, it is imperative for an OEM to continuously refresh its product profile to address the evolving needs of customers and keep up with the latest regulatory developments.

Strongest

Highly diversified, with no single product segment accounting for more than 30% of revenues

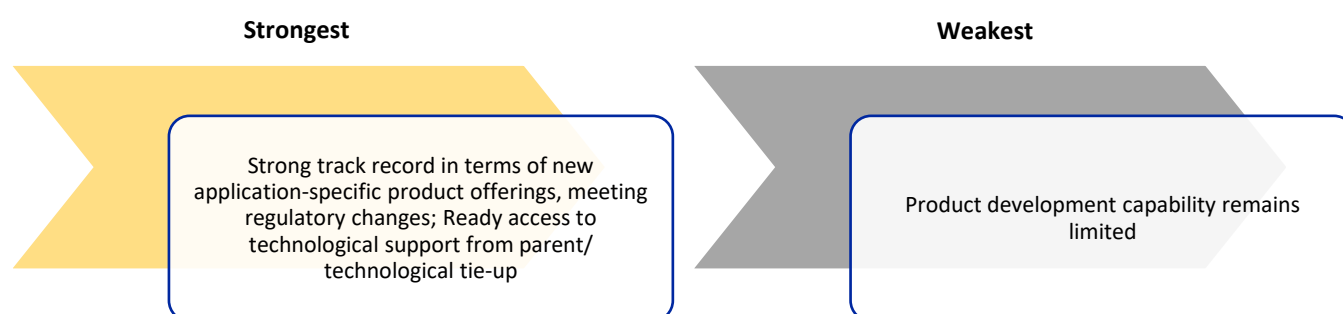
Weakest

Presence in a single product segment

Technology and Product Development Capabilities

Traditionally, the Indian construction vehicle industry has witnessed a relatively lower focus on developing advanced equipment with the view to maintaining lower initial cost for customers. Accordingly, the product portfolio of domestic OEMs, in certain product segments, lags compared to their global counterparts. However, factors such as better turnaround time, complex mining and infrastructure projects, evolving regulatory requirements, usage of equipment in municipal/city works, increasing requirements to complement/ substitute manpower with equipment has led to a shift in construction vehicle demand in favour of both higher tonnage as well as compact equipment. The OEMs have also introduced compact equipment models of excavators, wheel loaders etc. that are customised to suit certain application segments. Evolving regulatory requirements (i.e., emission norms and safety regulations) and increasing foray of international OEMs has prompted players to invest in developing new and advanced platforms. As a result, while evaluating the competitive position of an OEM on a forward-looking basis, due importance is given to an OEMs' future product development strategy, technology tie-ups and R&D efforts.

The evolving regulatory requirements regarding emission norms and safety regulations also necessitate constant upgradation and adaptation of vehicles in a cost-efficient manner. In this respect, ICRA tries to evaluate an OEM's technology tie-ups (including parent support) for product design and engineering, and its in-house R&D capabilities, as reflected in new product launches and launches of complex equipment. These investments also serve as indicators of the OEM's focus on improving its product development capabilities, and its ability to develop new products. The OEMs focus on emerging trends such as electrification through product launches, technology tie-ups, investment and localisation remain important to ensure future readiness.



Financial Risk Assessment

ICRA analyses the long period past financial performance trends and estimates the future financial performance to assess the financial risk exposure of an entity, i.e., to evaluate the sustainability and adequacy of cash flows against its debt servicing obligations. The financial metrics provide a useful reference not only to evaluate the performance trends of an entity over a given time horizon, but also to enable a comparison with its peers. The financial risk assessment is not done in isolation but in conjunction with the business and the industry risks that the entity is exposed to. An entity with low exposure to business and industry risks would generally have stable cash flows and thus higher tolerance to operate with a relatively moderate financial risk profile. In contrast, entities that are exposed to high business and industry risks need to maintain a stronger financial risk profile to have adequate cushion to manage cash flow volatility. The various financial metrics assessed by ICRA could be divided into five categories viz., Profitability, Leverage, Coverage, Liquidity and Cash Flows¹. Given the uncertainty around how the various credit drivers could evolve in the future, ICRA also carries out a sensitivity analysis to assess the impact of the key variables on the financial profile of the entity to evaluate its ability to withstand stress events.

¹ For more details, readers may refer to the documents titled, "Rating Approach—Financial Ratio Analysis", available on ICRA's website

Profitability

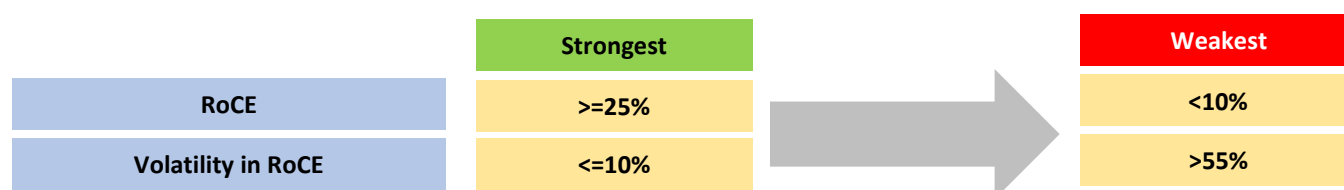
Profitability metrics are a measure of an entity's efficiency and return on investments. It is imperative for most businesses to invest regularly in physical assets, product development, marketing, and human capital to sustain or improve their positions. Entities that have superior profitability can do so through internally generated resources with low dependence on external financing. Moreover, such entities can generate sufficient surplus for not only meeting debt servicing obligations but also to reward equity investors. This in turn improves their ability to attract fresh capital for future business requirements. Moreover, entities with higher profitability have better resilience to economic downturns and are more likely to generate adequate internal resources for re-investment and debt servicing.

Profitability is a measure of the earnings generated by an entity in a given time period in relation to the resources deployed and is measured by profit margins and the return on capital employed (RoCE). The construction vehicle industry witnesses significant variations in profitability through industry cycles. Commodity price volatility and the ability to successfully pass on or absorb fluctuations can have a material impact on an OEM's profitability. A price undercutting strategy by any player to gain market share could lead to a discount war, which would have a more detrimental impact on high-cost manufacturers. Procurement strategies and optimal supply chains allow for better asset efficiencies and retention of profit margins. Owing to the high operating leverage, profitability is also contingent on asset sweating.

Validity of Business Risk through

Profitability Metrics

[Indicative Metrics²]



Leverage & Coverage

Financial leverage is a measure of an entity's dependence on borrowed funds. Lower the dependence on borrowings, the lower (better) the leverage. Most construction vehicle OEMs in India have low leverage, and their debt profile largely consists of short-term working capital debt. When an entity borrows, it is obliged to pay both interest as well as principal to the lenders as per a defined schedule. This increases the fixed cost burden on the borrowing entity and in the limiting case, increases the default risk. While high leverage may mean high risk from a credit perspective, it is an often-adopted course by shareholder-oriented managements, given that high leverage, in good times, leads to high returns on equity capital. An entity's financial leverage could thus be a function of its management's financial policy and risk tolerance, besides being a point-in-time reflection of an entity's business and financial choices. An entity with lower leverage is better equipped to withstand volatility in cash flow generation in situations of economic downturn, competitive challenges, unexpected costs, changing consumer preferences, or regulatory changes.

Ratio	Computation
Indebtedness Ratio	(Total Outside Liabilities) / (Tangible Net Worth) (Total Outside Liabilities) / (Market Capitalisation)
Debt to Profit Ratio	(Total Debt) / (Operating Profit)

Total Outside Liabilities = Total Debt + All Long-Term and Short-Term External Liabilities such as Deferred Tax Liability, Creditors and Other Liabilities

² The indicative financial metrics mentioned here and elsewhere in the document are intended to provide a broad overview to the readers regarding what ICRA generally considers as 'relatively strong' or 'relatively weak' metrics. It is, however, possible that an entity has relatively weaker metrics on one or more financial parameters, but its credit risk is assessed to be low because of other mitigating factors, including (but not limited to) stronger metrics on other financial parameters, a healthy business risk profile, strong financial flexibility or a strong promoter group that is willing to extend distress support to it.

Shareholder's Funds or Tangible Net Worth = Net Worth - Revaluation Reserves + Minority Interest + Equity component of hybrid instruments as assessed by ICRA based on the instruments' contractual terms

Assessment of Leverage

[Indicative Metrics]

	Strongest		Weakest
Indebtedness Ratio	$\leq 0.9x$		$> 3.0x$
Debt to Profit Ratio	$\leq 0.5x$		$> 5.0x$

Entities with higher profitability and lower leverage will generally have better coverage ratios and thereby healthier financial risk profiles. The debt coverage indicators that are examined include Interest Coverage Ratio, ratio of Net Cash Accruals to Total Debt and Debt Service Coverage Ratio (DSCR). Further, the profile of debt in terms of maturity and average cost is also analysed. High leverage also exposes an entity to interest rate risks.

Ratio	Computation
Interest Coverage Ratio	(Operating Profit) / (Interest expense)
Debt Service Coverage Ratio (DSCR)	(Net Profit After Tax + Interest + Depreciation) / (Gross Interest + Repayment + Dividend on Preference Shares)

Assessment of Coverage

[Indicative Metrics]

	Strongest		Weakest
Interest Coverage	$\geq 18.0x$		$< 2.0x$
DSCR	$\geq 4.0x$		$< 1.1x$

Working capital analysis

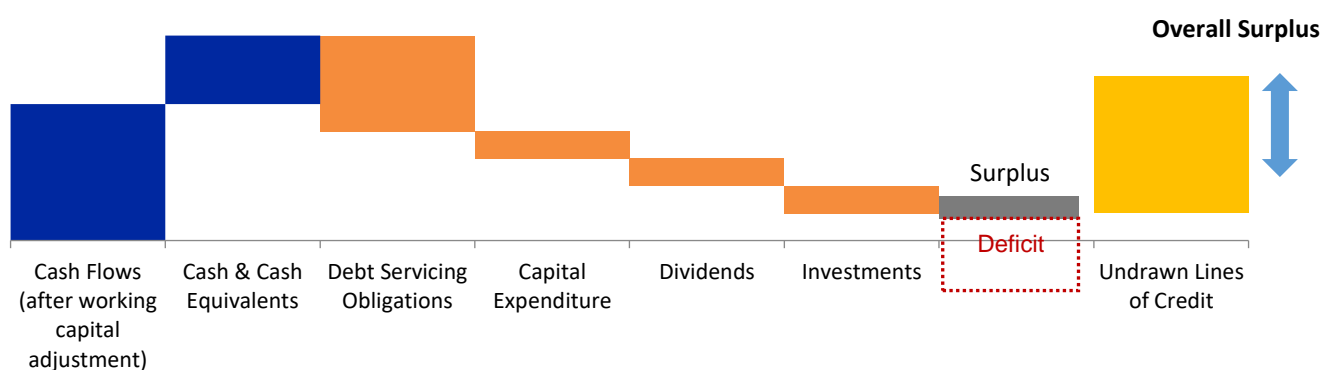
ICRA's evaluation of the financial position of a construction vehicle OEM also involves a detailed assessment of its working capital management, with the emphasis being more on its cash flow generation. A high inventory level increases the holding cost and working capital requirements while inadequate inventory might lead to a market share loss. At the same time, an inventory build-up can also result from one-time events to support scheduled product launch by the OEMs in the immediate future or for effective supply-chain management. While extended credit periods from vendors is an indication of bargaining power of the rated entity and a substitute for working capital borrowing, stretched creditor days, over and above the contractual creditor terms, could be an indication of liquidity strain. ICRA compares the working capital intensity of the entity to be rated with its peer group to gauge its ability to negotiate credit terms with customers and suppliers. This also serves as a proxy of its business strength.

Liquidity and adequacy of cash flows

Liquidity is the measure of an entity's ability to meet its short-term cash obligations from various internal or external resources. Internal resources include cash flows from operations (adjusting for working capital changes), unencumbered cash and cash equivalents on balance sheet and potential cash inflows from the monetisation of physical and financial assets. External resources include undrawn lines of credit or planned equity capital. The short-term obligations include both the committed as well as the contingent claims on an entity's cash, including the debt-servicing obligations, working capital requirements, capital expenditure and other investment outlays, dividend and share buyback-related outflows, besides the sudden demand arising from crystallisation of discrete events such as litigation penalty. Higher the cushion available between the resources available

(especially internal resources) and the obligations, the better the liquidity profile of an entity. Liquidity is generally assessed in conjunction with the vulnerability of an entity to timely refinancing/ renewal of short-term sources of funding. Depending upon the circumstances, an entity that has a relatively modest liquidity profile, but a strong refinancing ability may not be viewed too unfavourably. ICRA also notes that the liquidity available with an entity may be for a temporary period and hence an entity's overall policy towards maintaining adequate liquidity (given the trade-off between returns and liquidity) is accorded due importance in the analytical approach³.

Liquidity snapshot over any defined period



Other Elements of Credit Risk Assessment

Parentage/ group support

Considering that most of the large construction vehicle manufacturers in India are subsidiaries or joint ventures of global majors, the global parents' commitment to the Indian market and to the Indian entity being rated are also important parameters while assessing credit profile of Indian subsidiaries/JVs. Parent support in the form of access to beneficial credit terms and capital infusion has supported several of these manufacturers during cyclical downturns. Consequently, the parents' financial strength, its strategy and commitment to the Indian operations are of importance. In case of joint ventures between global OEMs and Indian entities, the relative strengths brought by the partners to the JV, their commitment and willingness to support the Indian operations are key monitorables. Development of substitutes to a JV, either through a wholly owned subsidiary or an alternative manufacturing location in nearby geographies, could affect the Indian entity's prospects. In case of a joint venture, commitment from the multiple partners and a common strategy are important for the long-term financial health of these JVs.

Financing Availability

With most construction vehicle purchases in India relying on external funding, the financing environment plays an important role in supporting its demand. In India, the construction vehicle financing market is well established, represented both by banks as well as non-banking finance companies (NBFCs). The availability of credit from the financial institutions, hence, plays a key role in supporting construction vehicle sales and demand. Additionally, some OEMs also have captive finance companies, although these captive NBFCs account for only a limited share of the overall construction vehicle financing market. A well-managed captive finance arm can be utilised strategically by an OEM – at times by advancing loans to a category of borrowers that may have a relatively weak credit profile. In addition, they may help the OEM in penetrating into certain markets or a product segment where the OEM has a marginal presence. However, any build-up of non-performing assets in their portfolio can impact the cash flows of construction vehicle OEMs as they may have to infuse additional equity into the financing entity.

³ For more details on how ICRA assesses liquidity, readers may refer to the document titled, "Liquidity Analysis of Entities in the Non-Financial Sector" published on ICRA's website

to comply with the regulatory norms and loss-funding requirements. Accordingly, for manufacturers with captive finance companies, ICRA tries to assess the capital requirements for the captive finance business⁴.

Debt Servicing Track Record

A history of past delays or defaults in meeting interest and principal repayment obligations reduces the comfort level with respect to the company's future debt servicing capability and willingness. Nevertheless, the reasons behind past defaults are also analysed, which could also be due to adverse demand situations in the relevant industry. A company's ability to honour its debt obligations during the period of cyclical stress is also factored in.

Event Risk

ICRA recognises the possibility of events such as unrelated diversification, mergers and acquisitions, business restructuring, asset sales and spin-offs, litigations, equity infusion and refinancing, which could have a material impact on the credit profile of an entity. Incorporating the impact of such discrete events in the credit rating, from the beginning, is often difficult. Depending on whether and when such events occur, the rating opinion could be substantially different. ICRA applies its analytical judgment in such cases, based on the rated entity's track record, the credibility of the management and the experience of having seen similar situations play out in other entities. However, given the nature of such events, it is possible that the rating may undergo a material change later, upon the occurrence of the event.

Foreign currency-related risks

Given the lack of local sources for several key inputs like undercarriage parts and special steel, import content in the Indian construction vehicle industry is high in select categories, exposing entities to forex volatility. Imports and forex impact the costing and pricing strategy and raw material inventory requirements. Since several of the Indian construction vehicle manufacturers are subsidiaries/ joint ventures of global OEMs, the bulk of the critical technology components come from the parent, in return for which the manufacturer also pays a royalty or technical-knowhow fees. ICRA takes into consideration the hedging policy of the entity towards mitigating such foreign currency risks and the impact of adverse movement in foreign exchange rates on its cost structure.

Tenure mismatches, and risks relating to interest rates and refinancing

Large dependence on short-term borrowings to fund long-term investments can expose an entity to significant re-financing risks, especially during periods of tight liquidity. Financial flexibility, and the existence of adequate buffers of liquid assets/ bank lines to meet short-term obligations is viewed positively. Similarly, the extent to which an entity could be impacted by movements in interest rates is also evaluated.

Contingent liabilities/off-balance sheet exposures

ICRA evaluates the likelihood of devolvement of contingent liabilities/ off-balance sheet exposures and the financial implications of the same.

Accounting quality

ICRA reviews the accounting policies, notes to accounts, auditors' comments and other disclosures that are parts of the Annual Report of a rated entity. Deviations, if any, from the accounting standards/ practices are assessed and the financial statements of the entity are adjusted to reflect the impact of such deviations

⁴ For more details on how ICRA assesses support extended by/to a rated entity, readers may refer to the documents titled, "Rating approach – Implicit Parent or group support", available on ICRA's website

Management Quality Assessment

In addition to the industry, business and financial risk analysis, all credit ratings incorporate an assessment of the quality of the rated entity's management and its financial policies. As a part of its process, ICRA undertakes discussions with the rated entity's management to understand its views on past performance as well as its plans and strategies, besides the outlook on the industry. Some of the points assessed are:

- » Experience of the promoter/ management in the industry
- » Commitment of the promoter/ management to the rated entity
- » Risk appetite of the promoter/ management and risk mitigation plans/ implementation of effective financial controls
- » Policies on leveraging, managing interest rate and currency risks
- » Management plans on new projects and expansions

Periodic interactions with the management help in ascertaining the shifts, if any, in their financial policies.

Assessment of Environmental, Social and Governance Risks

The assessment of the Environmental, Social and Governance (ESG) risks by ICRA involves a broad range of considerations that pertain to the sustainability of an entity, with focus on aspects that can have a material impact on its credit quality. While the Environmental (E) & Social (S) risks tend to be both sector-related as well as entity-specific and could be driven by external factors such as regulations or demographic changes, the Governance (G) risks are largely entity-driven. The impact of the E&S risks on an entity's credit profile tends to be asymmetric. If the ESG risks are material but unmitigated, these generally translate into pulling down the rating, but generally the ratings are not pushed up even when the ESG context is favourable.

Environmental and Social Risks

As this methodology highlights, while undertaking the credit assessment of entities, ICRA seeks to incorporate all the relevant credit considerations into its rating decisions while taking a forward-looking view on the risks and the mitigating elements. The relevant credit considerations include (sometimes overtly, sometimes covertly) the E&S factors that could affect the rated entity/transaction. While ICRA's analytical approach does not explicitly disaggregate these risks to assess their impact on the rating, these risks are often assessed broadly. Further, it is not always feasible to fully or precisely disaggregate the subcomponents of E&S risks in credit analysis as these considerations often tend to overlap.

That said, the materiality of the E&S risks and the time horizon over which they are expected to crystallise differs widely across sectors and entities. In some cases, while the E&S risks could be material but their effect on the credit profile may be muted because of the other fundamental strengths of the entity. In other cases, the adverse impact of the E&S risks is expected to play out in the distant future, and hence these considerations do not necessarily weigh on the rating today—with the expectation that when these risks manifest in the distant future, the rated entity by then would possibly adapt itself by realigning its business model.

While evaluating E&S risks, ICRA's objective is only to assess the direct and indirect risks that an entity faces and how it already is or is intending to mitigate the impact of such risks on its credit profile. As an example, ICRA only assesses whether an entity is exposed to physical climate risks, or carbon transition risks such as those arising from changes in regulations or other environmental and social risks; and seeks to understand the various mitigation and adaptation approaches that the entity is implementing to mollify these risks. construction vehicle entities are exposed to risks related to evolving regulations on emission norms and transition to cleaner equipment. With the increasing focus on carbon-neutrality, the pace of regulatory changes and shifts in consumer behaviour could have a material bearing on the business and financial position. Moreover, transition to cleaner power/energy may have a bearing on coal demand, which could have an impact on demand for certain categories of construction vehicles. Accordingly, entities in the construction vehicle industry have an exposure to carbon transition risks.

On the social dimension, the construction vehicle industry has a prominent dependence on human capital, in terms of direct and indirect employees, contractual labour, as well as operators/ drivers employed by the construction vehicle buyers. Being in the manufacturing business, maintaining healthy employee relations as well as safety of employees by the OEMs as well as the supplier ecosystem is essential for disruption-free operations. Further, while skilled operator/ driver shortage issues have emerged over the past few years, the OEMs are increasingly offering training and other such programmes to mitigate these challenges. Moreover, social risk arising out of restrictions in some mining areas and right of way issues in road construction entities could have an impact on equipment demand. Another social risk that the construction vehicle OEMs face pertains to product safety and quality.

Governance Practices

A sound corporate governance structure attempts to make clear the distinction of power and responsibilities between the board of directors and the management. The constitution of an entity's board, besides the entity's adherence to legal and statutory compliance requirements, are factored in during credit assessments. ICRA seeks to gain a qualitative understanding of an entity's commitment towards following transparent and credible practices by the way its financial statements are reported, their level of disclosures, consistency in communication and the openness about sharing information during the credit rating exercise. Besides, the corporate group structure (whether simple or complex), the rated entity's related-party transactions and instances of supporting group entities at the expense of debt holders are assessed.

Summing Up

ICRA's credit ratings are symbolic representations of its opinion on the relative credit risk associated with the rated entity. This opinion is arrived at following a detailed evaluation of the rated entity's industry, business and financial risks, its likely cash flows and the adequacy of such cash flows vis-à-vis the debt servicing obligations and other funding requirements. ICRA's rating approach also involves an assessment of the entity's management quality and governance practices. In addition to these considerations, an entity's credit rating may also be influenced by its ownership, the nature of linkages with its parent or group entities, degree of financial flexibility, the corporate legal structure, track record of operations and that of debt servicing, and vulnerability (if any) to discrete event risks.

ANNEXURE

Summary of rating factors and an example to illustrate the key building blocks of a credit rating

		Strong			Comfortable			Adequate			Moderate			Weak		
Industry Risk	Industry Position															
	Scale															
Business Risk	Market Share															
	Product Diversification															
	Technology & Product Development Capabilities															
Financial Risk	Profitability and Earnings Stability															
	Leverage															
	Coverage															
		Enhance					Support/ Neutral					Hinder				
Do these factors enhance or hinder the credit profile?	Diversification															
	Refinancing Dependence, Liquidity and Financial Flexibility															
	Currency Risk															
	Financial Policy															
	Management, Governance & Reporting															
		Very High				High				Moderate				Low		
Parent Support	Likelihood of Parent Support															
	Rating of Parent	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B/ C category	
	Final Rating	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B/ C category	

The above graphic is only for illustration purpose and does not represent a rating output from a formulaic model. The ratings assigned by ICRA are determined by Rating Committees based on both quantitative and qualitative considerations.

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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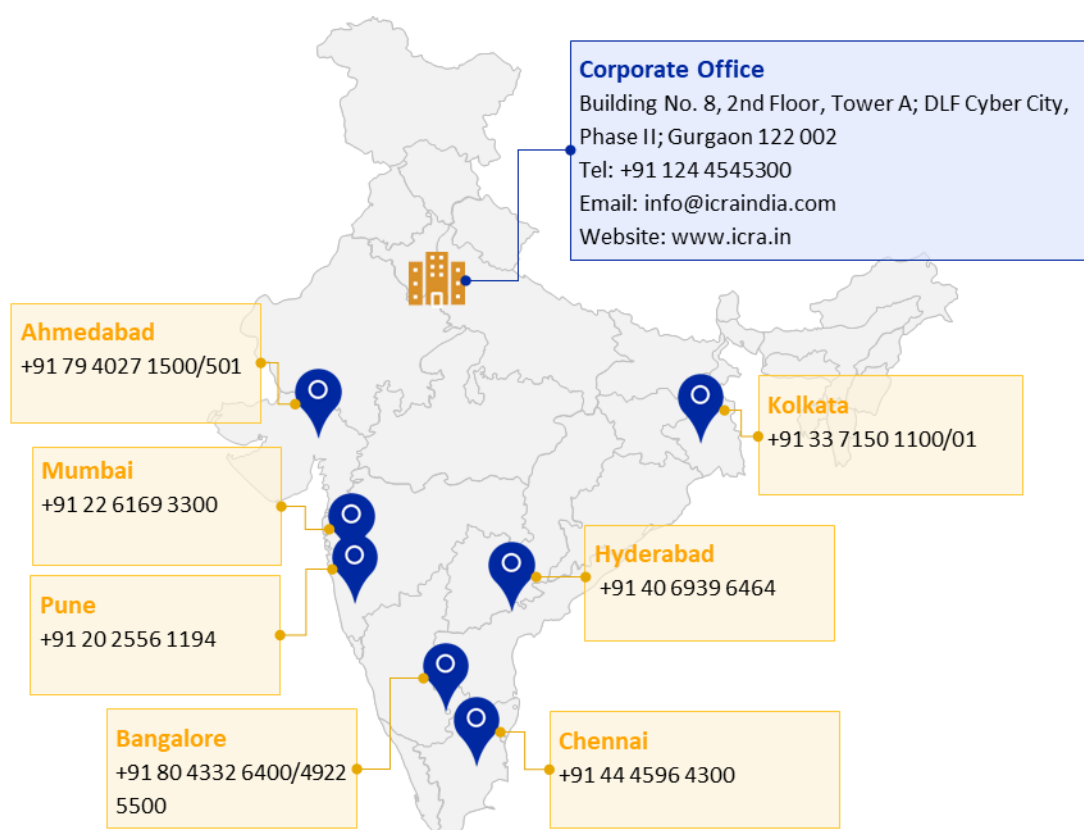


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