February 16, 2021

Veljan Denison Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Cash Credit	32.00	32.00	[ICRA]BBB+ (Stable); Reaffirmed
Bank Guarantee	7.00	7.00	[ICRA]BBB+ (Stable); Reaffirmed
LC	6.00	6.00	[ICRA] A2; Reaffirmed
Term Loan	12.00	0.00	-
Unallocated	-	12.00	[ICRA]BBB+ (Stable); Reaffirmed
Total	**57.00**	**57.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation positively factors in the established track record of Veljan Denison limited (VDL) as a manufacturer of vane-based hydraulic pumps, valves and power pack systems, and a healthy financial risk profile with zero debt levels as on September 30, 2020, and an interest coverage of 15.43 times in 6M FY2021. The operating profit margins remain healthy at above 25% in the past five years given its presence in the niche hydraulic pumps manufacturing. However, the operating profit margins declined to 15.78% in 6M FY2021 owing to a decline in revenues. VDL's revenues declined to Rs. 27.10 crore in 6M FY2021 from Rs. 82.79 crore in FY2020 as sales were impacted owing to the Covid-19 pandemic. The ratings also note VDL's diversified customer base comprising both domestic and overseas customers.

The ratings are, however, constrained by the company's high customer concentration risk with the top five customers accounting for 70% of the revenues in FY2020, and high working capital intensity owing to high debtor and inventory days. The company receives payments from its distributors in around 3-4 months, from OEMs in 2-3 months, from direct exports in 5-6 months and from exports through distributors in around 12-15 months. Despite this, the liquidity position is comfortable with liquid cash balance of Rs. 30.03 crore as on September 30, 2020 and nil utilisation of working capital limits. ICRA also notes that VDL's revenues have remained in the range of Rs. 80-100 crore in the past five years owing to intense competition from cheaper imports and demand linked to capital expenditure across the industries. The ratings are also constrained by the project execution risk with the company undertaking construction of solenoid coil unit in Vizag and casting manufacturing unit in Pashamylaram at an estimated cost of Rs. 35 crore over the medium term.

The Stable outlook on the [ICRA]BBB+ rating reflects ICRA's opinion that VDL's presence in the niche hydraulic pumps manufacturing and a geographically diversified customer base comprising dealers (domestic and export) and OEMs would support the company's revenue and profit margins over the near term.

Key rating drivers and their description

Credit strengths

Long track record in the manufacturing of hydraulic pumps and valves – VDL has more than five decades of experience in the manufacturing of vane-based hydraulic pumps, valves and power pack systems. The company's customer base is geographically diversified as VDL exports its products to countries like the US, Australia and the Middle East and to OEMs like Escorts Construction Equipment Limited, Action Construction Equipment Limited etc in the domestic market.

Comfortable financial risk profile – The financial risk profile remains healthy with zero debt levels as on September 30, 2020, and an interest coverage of 15.43 times in 6M FY2021. Despite the addition of debt for the envisaged capex over the medium term, the debt coverage metrics are expected to remain comfortable.

Healthy operating profit margins – The operating profit margins remain healthy at above 25% levels in the past five years given the presence of VDL in the niche hydraulic pumps manufacturing segment. Although the operating profit margins fell to 15.78% in 6M FY2021 owing to a decline in revenues, the margins are expected to increase to more than 18% levels in FY2021 with an increase in revenues in H2 FY2021. VDL's revenues declined to Rs. 27.10 crore in 6M FY2021 from Rs. 82.79 crore in FY2020 owing to an adverse impact of the pandemic on its operations.

Credit challenges

High working capital intensity – The working capital intensity has remained high at 91% in FY2020 owing to high debtor and inventory days. The company receives payments from its distributors in around 3-4 months, from OEMs in 2-3 months, from direct exports in 5-6 months and from exports through distributors in around 12-15 months. Despite this, the liquidity position is comfortable with liquid cash balance of Rs. 30.03 crore as on September 30, 2020 and nil utilisation of working capital limits. The company keeps inventory of major raw materials like castings and vanes owing to long lead time in procurement.

Modest scale of operations – The scale of operations is modest with revenues less than Rs. 100 crore in the past five years and has remained in the range of Rs. 80-100 crore in the past five years owing to intense competition from cheaper imports and demand linked to capital expenditure across the industries.

Moderate project execution risk – The company is exposed to the project execution risk as it is undertaking construction of solenoid coil unit in Vizag and casting manufacturing unit in Pashamylaram at an estimated cost of Rs. 35 crore over the medium term. This is expected to be funded through a new term loan of Rs. 20-25 crore and the rest through internal accruals.

High customer concentration risk – The customer concentration risk remains high with the top five customers accounting for 70% of the revenues in FY2020. Around 53.46% of the revenue came from VHL in FY2020.

Liquidity position: Strong

VDL's liquidity position is strong with a liquid cash surplus of Rs. 30.03 crore as of September 30, 2020 and a cushion in the working capital limits. The average fund-based limit utilisation stood low at 7.55% in the past nine months ending December 2020. The cash accruals are expected to be at ~Rs. 8-9 crore in FY2021 and are sufficient for the capex of ~Rs. 2.00 crore and debt repayment of Rs. 0.34 crore in FY2021. Overall, ICRA expects VDL to be able to meet its near-term commitments through internal accruals as well as cash and yet be left with sufficient cash surpluses.

Rating sensitivities

Positive Factors – The ratings could be upgraded if the scale of operations and profitability margins improve along with a reduction in debtor days on a sustained basis. Specific credit metrics that could lead to an upgrade of VDL's rating include RoCE of more than 16.00% on a sustained basis.

Negative Factors – The ratings could be downgraded if there is a significant decline in revenues or margins or any deterioration in the working capital cycle, adversely impacting the liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology]()
Parent/Group Support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Incorporated in 1973, Veljan Denison Limited (VDL) is a listed company on BSE that manufactures hydraulic vane pumps, motors, valves and power pack systems. The company has its manufacturing unit in Patancheru, Hyderabad. The company was promoted by Mr. V C Janardan Rao, a qualified engineer with specialisation in fluid power. The company indigenously manufactures precision engineering components and has its own research and development (R&D) wing.

Key financial indicators

Veljan Denison Limited	FY2019	FY2020	6MFY2021*
Operating Income (Rs. crore)	87.51	82.79	27.10
PAT (Rs. crore)	16.33	13.44	1.45
OPBDIT/OI (%)	29.81%	26.06%	15.78%
RoCE (%)	15.98%	12.42%	3.43%
Total Outside Liabilities/Tangible Net Worth (times)	0.30	0.19	0.13
Total Debt/OPBDIT (times)	0.74	0.29	0.00
Interest Coverage (times)	19.54	27.39	15.43
DSCR (times)	7.43	8.57	9.23

**provisional; Source: Veljan Denison Limited*

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress); DSCR: (PBIT + Mat Credit Entitlements - Fair Value Gains through P&L - Non-cash Extraordinary Gain/Loss)/(Interest + Repayments made during the Year)

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in	Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
					16-Feb-2021	17-Dec-2019	24-Dec-2018	21-Nov-2017
1	Cash Credit	Long Term	32.00	-	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
2	Bank Guarantee	Long Term	7.00	-	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
3	LC	Short Term	6.00	-	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2
4	Term Loan	Long Term	0.00	-	-	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
5	Unallocated	Long Term	12.00	-	[ICRA]BBB+ (Stable)	-	-	-

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	-	10.18%	-	32.00	[ICRA]BBB+ (Stable)
NA	Bank Guarantee	-	-	-	7.00	[ICRA]BBB+ (Stable)
NA	LC	-	-	-	6.00	[ICRA]A2
NA	Unallocated	-	-	-	12.00	[ICRA]BBB+ (Stable)

Source: *Veljan Denison Limited*

Annexure-2: List of entities considered for consolidated analysis – Not Applicable

ANALYST CONTACTS

K. Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Srinivasan R
+91 44 4596 4315
r.srinivasan@icraindia.com

Vinay Kumar G
+91 40 4067 6533
vinay.g@icraindia.com

Tejal Shree
+91 40 40676523
tejal.shree@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches