November 30, 2022

Supertron Electronics Private Limited: Long-term rating upgraded to [ICRA]A+; Short-term rating reaffirmed; Outlook revised to Stable; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term fund-based Cash Credit	145.00	165.00	[ICRA]A+ (Stable); Upgraded from [ICRA]A; Outlook revised to Stable from Positive
Long term fund based – Term Loan (GECL)	40.00	40.00	[ICRA]A+ (Stable); Upgraded from [ICRA]A; Outlook revised to Stable from Positive
Long-term Fund-based – Channel financing	175.00	175.00	[ICRA]A+ (Stable); Upgraded from [ICRA]A; Outlook revised to Stable from Positive
Short-term Non- Fund-based – Letter of Credit	-	209.00	[ICRA]A1; reaffirmed
Short-term Non- Fund-based – Bank Guarantee	-	73.00	[ICRA]A1; reaffirmed
Short-term Non- Fund-based – Bank Guarantee (Interchangeable)	-	(35.00)	[ICRA]A1; reaffirmed
Short-term Non- Fund-based – Forward Contract (Forex)	-	4.00	[ICRA]A1; reaffirmed
Long Term/Short Term – Unallocated	30.00	-	-
Short term – non-fund based	216.00	-	-
Total	**606.00**	**666.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating action factors in the healthy performance of Supertron Electronics Private Limited (SEPL) in FY2022 and ICRA's expectations that the company's financial performance is likely to remain comfortable, notwithstanding a likely slowdown in the growth trajectory in FY2023. Strong demand for IT hardware products, primarily driven by Covid-19 induced restrictions/lockdown had resulted in a healthy increase in SEPL's turnover, profits and cash accruals. The company's total indebtedness, as measured by Total Outside Liability to Tangible Net worth (TOL/TNW), remained at 3.37 times in FY2022 compared to 3.40 times in FY2021 and 4.36 times in FY2020. The interest coverage (OPBDITA/ Interest cost) of the company improved to 7.01 times in FY2022 from 3.99 times in FY2021 and 1.77 times in FY2020. While removal of restrictions is likely to impact the growth rate and lead to some elongation in the working capital cycle of the company, ICRA expects the company to maintain healthy credit metrics, going forward.

The ratings continue to consider the established track record of the company in the IT product distribution business. It has a strong distribution network, supported by a wide base of intermediary partners comprising over 10,000 dealers in more than 900 cities and towns, enabling SEPL to have a diversified geographical presence. The company has been increasing the number of tie-ups with leading IT hardware and product vendors, which along with the addition of new geographies supported the consistent revenue growth in the last few years.

The ratings, however, also factor in the intensely competitive nature of the IT hardware distribution business, which limits the scope of further margin expansion. SEPL has a relatively concentrated vendor base, with product sales of the top five vendors cumulatively contributing ~83% to the top line in FY2022. Nonetheless, ICRA notes that the strong market position of such vendors mitigates the concentration risk to an extent. As a sizeable portion of the contracts with the top vendors are exclusive in nature, the vendors are also dependent on SEPL to increase their own market share in the country, reducing the risk further. SEPL is also dependent on imports for a significant share of its overall procurement and is thus exposed to forex risks as well. However, SEPL has been able to mitigate such risks to an extent owing to partial hedging through forward covers as well as price protection and discounts offered by the vendors, which also protect the company from the risks of inventory obsolescence.

The Stable outlook on [ICRA]A+ rating reflects ICRA's opinion that the capital structure and debt coverage indicators of the company would continue to remain healthy, notwithstanding a slowdown in the growth trajectory.

Key rating drivers and their description

Credit strengths

Established player in the IT hardware distribution industry, exclusive tie-ups with leading product manufacturers – SEPL is an established player in the IT hardware distribution business having tie-ups with leading hardware vendors like Dell, Acer, Seagate, Lenovo, and Samsung, among others. SEPL's product offerings include desktops, laptops, monitors, hard drives, flash drives, printers, servers, and tablets, besides other IT hardware products. A sizeable share of the company's top line is contributed by the sale of products through exclusive distributorship tie-ups, ensuring a relatively secure revenue stream. Going forward, the share of revenues from the exclusive tie-ups is expected to increase further from the current levels.

Diversified geographical presence – SEPL has been able to establish a pan-India footprint through a wide network of channel partners and branch offices. The southern region continued to remain the largest revenue contributor in FY2022 as well, contributing ~35% to the company's top line, followed by the northern and western regions with revenue share of ~30% and ~25%, respectively.

Demonstrated ability to grow business, backed by favourable demand outlook for IT hardware products – SEPL's top line has witnessed a CAGR of ~15% between FY2017 and FY2022 to reach ~Rs. 5,589 crore on the back of its wide distribution network, new business acquisitions via new vendor tie-ups and increased business from its existing suppliers. Further, SEPL reported a year-on-year OI growth of ~23% in FY2022, primarily driven by the sustained demand for IT hardware products (laptops, desktops, notebooks etc.) consequent to the rising work from home (WFH) and e-learning practices amid the pandemic. The demand for IT hardware products continue to remain adequate in the current fiscal as well with SEPL achieving a revenue of ~Rs. 2,685 crore in H1 FY2023 against ~Rs. 2,750 crore over the same period previous year. The demand is expected to remain favourable for SEPL in the near term and ICRA believes that the company would continue to grow profitably in the current fiscal as well, though the growth rate would remain muted. The working capital cycle is also likely to improve further, going forward.

Improvement in financial risk profile, characterised by healthy return metrics and debt coverage metrics – SEPL's overall profit at an absolute level improved in FY2022, led by growing volumes and economies of scale. The ROCE of the company also improved and stood at a comfortable level of 25.4% in FY2022 (23.5% in FY2021). The interest cost remained flat, resulting in an improvement in the debt coverage metrics, as reflected by an interest coverage of 7.01 times (3.99 times in FY2021) and Total Debt/OPBDITA of 2.66 times (2.95 times in FY2021) as on March 31, 2022. The company's ability to sustain its margins while growing volumes without any material elongation in the working capital cycle would remain key monitorables, going forward.

Wide distribution network with low customer concentration risk – The company has an established customer base of over 10,000 dealers in more than 900 cities and towns. The customer concentration has been low with the top ten customers accounting for 20% of total sales in FY2022, down from 24% in FY2021. As growth prospects are higher in tier-II and tier-III cities, SEPL has an extensive reach in these areas through a strong distributor network and is planning to increase its presence in these markets further.

Credit challenges

Relatively concentrated vendor base – Sales of products from Dell, Lenovo, Acer, Seagate, and Samsung, SEPL's largest suppliers, account for the major portion of the company's revenues. Products of these five vendors accounted for almost 83% of SEPL's revenue in FY2022 and FY2021, among which Dell alone contributed to a significant portion (39% of the top line in FY2022). This exposes the company to vendor concentration risk. However, most of these suppliers have given exclusive distribution rights to SEPL, so they are also dependent on SEPL to increase their own market share in India, which mitigates the risk to some extent. Also, addition of new vendors is increasing its diversity. Some of the recent tie-ups with companies like Harman, Barco, Kaspersky, Silicon Power, Cybernetix, Pelco etc. have shown encouraging results, which are likely to further diversify SEPL's vendor base.

Low operating margin, working capital intensity increases in current year – Inherent to the nature of the distribution business, SEPL's profit margins continued to remain low. However, the operating margin increased considerably to ~2.8% in FY2022 as lower amount of discount was passed on as demand was high. The operating margin stood at ~2.0% in FY2021. The net margin followed suite and increased to ~1.8% in FY2022 from ~1.1% in FY2021. Going forward, the margins are expected to remain range bound given the nature of the business in which the company operates. The company has high stocking requirements and has to extend credit to its dealers. A large part of the working capital requirements is funded by credit period offered by OEMs. The working capital requirements were on the lower side in FY2021 and FY2022 owing to strong demand and limited supplies, which brought down both inventory holding days as well as debtors. However, in the current year, the same has increased, which would impact its liquidity to some extent.

Exposure to forex risks – The company remains exposed to adverse movement in forex rates as a significant portion of goods is imported and no export sales take place. Such risks are, however, mitigated by the partial hedging policy followed by the company as well as the price protection offered by SEPL's vendors. ICRA also notes that the proportion of import has reduced over the last few years due to discontinuation of the mobility business, which was wholly imported.

Liquidity position: Adequate

The company's liquidity position remains adequate. SEPL's working capital requirement increased substantially in FY2021 and FY2022 to support the significant top line growth, leading to negative cash flow from operations in both these years. The same is likely to improve in FY2023 given the likely muted top line growth. Nevertheless, likely increase in the inventory and receivables are likely to have some bearing on the liquidity. Nonetheless, availability of adequate working capital limits from banks and low debt repayment obligations are likely to support the overall liquidity position of the company.

Rating sensitivities

Positive factors – ICRA may upgrade SEPL's ratings if it maintains healthy credit metrics along with an improvement in the liquidity position. The specific trigger for ratings upgrade would be an interest cover of 7.5 times on a sustained basis.

Negative factors – Pressure on SEPL's ratings may arise if an elongation in the working capital cycle adversely impacts the liquidity position of the company. Any reduction in the absolute profit, leading to an interest cover below 5 times on a sustained basis, could lead to ratings downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Established in 1993, Supertron Electronics Private Limited (SEPL) is in the business of IT products distribution and marketing of various IT hardware products, including desktops, laptops, monitors, external hard drives, flash drives, printers and servers, among others. A sizeable portion of SEPL's business comes from the sale of a range of products from Dell, Samsung, Acer, Seagate and Lenovo.

In FY2022, the company reported a net profit of Rs. 103.4 crore on an operating income of Rs. 5,588.6 crore compared to a net profit of Rs. 52.0 crore on an operating income of Rs. 4,558.9 crore in the previous year.

Key financial indicators (audited)

SEPL Standalone	FY2021	FY2022
Operating income	4558.9	5588.6
PAT	52.0	103.4
OPBDIT/OI	2.0%	2.8%
PAT/OI	1.1%	1.8%
Total outside liabilities/Tangible net worth (times)	3.40	3.37
Total debt/OPBDIT (times)	2.95	2.66
Interest coverage (times)	3.99	7.01

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Nov 30, 2022	Dec 20, 2021	Sep 11, 2020	Jul 22, 2019
1	Fund-based – Cash Credit	Long term	165.00	-	[ICRA]A+ (Stable)	[ICRA]A (Positive)	[ICRA]A-(Positive)	[ICRA]A- (Stable)
2	Fund based – Term Loan (GECL)	Long term	40.00	39.17	[ICRA]A+ (Stable)	[ICRA]A (Positive)	-	-
3	Fund-based – Channel financing	Long-term	175.00	-	[ICRA]A+ (Stable)	[ICRA]A (Positive)	[ICRA]A-(Positive)	[ICRA]A- (Stable)
4	Non- Fund-based – Letter of Credit	Short-term	209.00	-	[ICRA]A1	-	-	-
5	Non- Fund-based – Bank Guarantee	Short-term	73.00	-	[ICRA]A1	-	-	-
6	Non- Fund-based – Bank Guarantee (Interchangeable)	Short-term	(35.00)	-	[ICRA]A1	-	-	-
7	Non- Fund-based – Forward Contract (Forex)	Short-term	4.00	-	[ICRA]A1	-	-	-
8	Unallocated	Long Term/ Short Term	-	-	-	[ICRA]A (Positive) / [ICRA]A1	-	-
9	Non-fund based	Short term	-	-	-	[ICRA]A1	[ICRA]A2+	[ICRA]A2+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term fund-based – Cash Credit	Simple
Long term fund based – Term Loan (GECL)	Simple
Long-term Fund-based – Channel financing	Simple
Short-term Non- Fund-based – Letter of Credit	Very Simple
Short-term Non- Fund-based – Bank Guarantee	Very Simple
Short-term Non- Fund-based – Bank Guarantee (Interchangeable)	Very Simple

Short-term Non- Fund-based – Forward Contract (Forex)	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA’s website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Cash Credit**	NA	NA	NA	165.00	[ICRA]A+ (Stable)
NA	**Channel Financing**	NA	NA	NA	175.00	[ICRA]A+ (Stable)
NA	**Term Loan (GECL)**	FY2021	NA	FY2026	40.00	[ICRA]A+ (Stable)
NA	**Letter of Credit**	NA	NA	NA	209.00	[ICRA]A1
NA	**Bank Guarantee**	NA	NA	NA	73.00	[ICRA]A1
NA	**Bank Guarantee (Interchangeable)**	NA	NA	NA	(35.00)	[ICRA]A1
NA	**Derivative Limit**	NA	NA	NA	4.00	[ICRA]A1

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis: Not Applicable

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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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