August 09, 2023

Delux Bearings Private Limited: Rating upgraded to [ICRA]BBB (Stable)

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating	NA	NA	[ICRA]BBB (Stable); upgraded from [ICRA]BBB- (Stable)
Total	**NA**	**NA**	

**Instrument details are provided in Annexure-I*

Rationale

The rating upgrade of Delux Bearings Private Limited (DBPL) factors in the expected sustenance of the healthy scale up in revenue witnessed in FY2023. DBPL reported 18% YoY growth in its revenue in FY2023, supported by increases in sales volumes on the back of stable demand. The rating upgrade also factors in the expected operational and financial synergies from DBPL's integration with the Fersa Group, a leading global player in the bearings industry. While ownership was transferred in January 2023, more clarity has emerged now on the integration benefits of access to technology for new products, newer geographies as potential markets, clientele and supply chain for sourcing. These are expected to support DBPL's revenue growth and also aid the improvement in margins over the medium term. The rating continues to factor in DBPL's established operational track record and its promoter's extensive experience of more than two decades in the bearing manufacturing business. Over the years, DBPL has been able to develop a wide customer base of reputed Original Equipment Manufacturers (OEMs) and tier-I/II automotive suppliers, with whom it enjoys established relationships that have resulted in repeat order inflow. Also, DBPL's revenue stream continues to be diverse across both domestic and export markets.

The rating, however, remains constrained by DBPL's moderate scale of operations, resulting in limited economies of scale; and highly competitive and fragmented nature of the industry, which limits the pricing flexibility of industry participants. These factors, coupled with partial outsourcing of manufacturing activity and vulnerability to volatility in raw material prices, have led to moderate profit margins. Moreover, the margins remain susceptible to adverse movements in foreign exchange rate, given the sizeable revenue contribution from exports. However, the risk is mitigated to an extent since the company hedges its forex exposure selectively. ICRA also notes the considerable capex plans over FY2024-FY2026 towards augmenting its manufacturing capacities and product mix, which is expected to result in some increase in its debt levels. Despite the same, the debt protection metrics are expected to remain comfortable with the expected scale up of operations and improved internal accrual generation. Nonetheless, timely commissioning and scaling up of revenues from the same will be key monitorables. ICRA also notes the demerger of DBPL and its subsidiary, Iridescent Enterprise Private Limited, in FY2023 and the subsequent transfer of some liquid investments and immovable properties to the latter, in line with the earlier understanding. Also, as indicated by DBPL's management, ICRA understands that DBPL will not be extending any funding support to this entity in the future.

The Stable outlook on the rating reflects ICRA's opinion that DBPL's credit profile will be supported by scaling up of internal accruals, while maintaining comfortable coverage metrics, despite debt-funded capex over the near to medium term.

Key rating drivers and their description

Credit strengths

Extensive experience of promoters in the bearing business – Incorporated in 2000, DBPL is engaged in manufacturing and selling a wide variety of bearings, primarily for the automotive industry. Its established operational track record, coupled with extensive experience of the promoters in the industry, has enabled the company to scale up its operations. DBPL is currently managed by Mr. Rohan Rathod (Chairman & Managing Director), supported by a qualified and experienced management team. Also, Mr. Carlos Miguel Oehling and Mr. Pedro Pablo Andreu have joined as directors post the majority stake acquisition by the Fersa Group.

Financial and operational synergies emanating from strong parentage – The Fersa Group, a Spanish company engaged in design, production and distribution of high-quality bearings for the global automotive and industrial markets, acquired majority stake in DBPL in January 2023. DBPL's business profile is expected to strengthen from this integration. With the required technical expertise from the Group, the company is expected to produce other products (like taper roller bearings, or TRBs, and syncro rings), thus reducing its reliance on clutch release bearings and bringing about product diversification. Additionally, DBPL is expected to benefit from various other integration synergies. In addition to the technological support needed for new product additions, DBPL will also benefit from the established sourcing chain of the Fersa Group, which will aid in margin improvement. Moreover, better brand visibility and access to newer geographies are expected to support top-line growth.

Well entrenched distribution network and established relationships with customers, including reputed companies – DBPL primarily caters to the commercial vehicle (CV) segment (driving ~70% of total revenues), followed by bearing sales for passenger vehicles (PVs), three-wheelers (3Ws), off-highway vehicles and tractors. This exposes the company to the cyclicality inherent in the CV industry, although mitigated to some extent by its widening product portfolio and increasing revenue share from other segments. Moreover, over the years, the company has developed a wide and diversified customer base of reputed international and domestic customers. Further, it enjoys established relationships with its key customers, resulting in repeat orders. Also, DBPL's recent integration with the Fersa Group is expected to further widen its clientele.

Diversified revenue stream across both domestic and export markets – DBPL has a diversified geographical presence in both the domestic and export markets, thus insulating it to an extent from the moderation in demand from any one market. In FY2023, exports accounted for ~30% of its revenue, while aftermarket sales (~41%) and sales to auto OEMs/tier-I companies (~30%) accounted for the remaining portion. Going forward, post association with the Fersa Group, DBPL's share of exports (those that are margin accretive) is expected to increase. Moreover, its aftermarket sales continue to be supported by an established brand and well-entrenched distribution network across the country.

Moderate leverage levels and comfortable debt protection metrics – The company's debt profile remains comfortable, supported by lower debt levels and steady internal accrual generation reflected in the total outside liabilities/ tangible net worth (TOL/TNW) ratio of 1.1 times as on March 31, 2023. Given DBPL's considerable capex plans over FY2024–FY2026 towards adding new machinery to augment its manufacturing capacities and product mix, its debt levels are expected to increase. Despite the same, the debt protection metrics are expected to remain comfortable with the expected scale up of operations and improved internal accrual generation.

Credit challenges

Moderate scale of operations leading to limited economies of scale – Despite posting healthy revenue growth in the past few years, the company's scale of operations continue to remain moderate with revenues of Rs. 213.2 crore (provisional) in FY2023, thus translating into limited economies of scale. Nonetheless, the company has been able to demonstrate steady scaling up in the past fiscals, which coupled with addition to the product mix and an increase in manufacturing capacities is expected to drive future revenue growth. Moreover, DBPL is also expected to benefit from the established presence and network of the Fersa Group.

High competitive intensity limits pricing flexibility – The company faces stiff competition from other unorganised and organised players, which limits its pricing flexibility and bargaining power with suppliers and customers, thereby constraining margins to some extent. However, the company benefits to an extent from its established brand, wide distribution network and diversified revenue stream

Moderate profit margins owing to partial outsourcing of manufacturing activity – The company outsources the production for a sizeable part of its sales and procures semi-processed components for the balance, limiting the value addition in its operations. Coupled with vulnerability to raw material price volatility, high competitive intensity and limited economies of scale result in moderate profit margins for DBPL. Nonetheless, increasing economies of scale, diversification of the product mix and expected synergies, with the Fersa Group acquiring majority stake, are expected to reduce its input costs and improve margins to some extent. Also, DBPL's margins remain susceptible to adverse movements in foreign exchange (forex) rates, given the sizeable revenue contribution from exports. However, the risk is mitigated to an extent as the company hedges its forex exposure selectively.

Liquidity position: Adequate

DBPL's liquidity remains **adequate**, supported by steady internal accrual generation and free cash and bank balances/liquid investments of ~Rs. 2.5 crore of June 30, 2023. Further, the company has sufficient cushion in the form of its undrawn working capital lines with an average working capital utilisation of 46% during the last 12 months ended March 2023. The company will be incurring considerable capex during FY2024–FY2026, which will be funded through a mix of debt and internal accruals. Moreover, it has debt repayment liability of around Rs. 4.0–10.0 crore p.a. over this period, which is expected to be comfortably met through its internal accrual generation.

Rating sensitivities

Positive factors – ICRA could upgrade DBPL's rating if it demonstrates healthy growth in its scale and profit margins, on a sustained basis, along with strengthening of its liquidity profile and maintaining its debt protection metrics.

Negative factors – Negative pressure on DBPL's rating could arise if there is considerable decline in revenues and internal accrual generation or higher than anticipated debt-funded capex or deterioration in working capital cycle that impacts the company's liquidity position and debt coverage metrics. Specific credit metrics that could lead to a rating downgrade include Total Debt/ OPBDITA of more than 2.7 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Suppliers
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of DBPL. As on March 31, 2023, the company had one subsidiary, which is enlisted in Annexure-II.

About the company

Incorporated in 2000, DBPL is involved in manufacturing and selling a wide variety of bearings, primarily for the automotive industry. It sells its bearings under the 'Delux' brand in the domestic market, and its manufacturing facilities are at Surendranagar and Rajkot in Gujarat. The company has been promoted by the Rathod family and it caters to exports, OEM and aftermarket demand for bearings and automotive parts. In January 2023, the Fersa Group, a Spanish company engaged in design, production and distribution of high-quality bearings for the global automotive and industrial markets, acquired majority stake in DBPL.

Key financial indicators

DBPL – consolidated	FY2021	FY2022	FY2023*
Operating income	127.3	173.8	213.2
PAT	9.0	12.3	9.5
OPBDIT/OI	9.5%	7.7%	7.0%
PAT/OI	7.1%	7.1%	4.5%
Total outside liabilities/Tangible net worth (times)	0.5	0.8	1.1
Total debt/OPBDIT (times)	0.4	2.0	2.2
Interest coverage (times)	16.9	12.9	6.4

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore, FY2023 numbers are ICRA estimates basis the consolidation done of provisional standalone financials for both the companies (DBPL and its subsidiary Dlxinfinity Driveline Private Limited)*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Aug 09, 2023	Aug 05, 2022	-	-
1	Issuer rating	Long term	-	-	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer Rating	Not Applicable

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	Issuer rating	-	-	-	-	[ICRA]BBB (Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	DBPL Ownership	Consolidation Approach
Dlxinfinity Driveline Private Limited*	100.0%	Full consolidation

*Source: Company data * DBPL has acquired this entity from the erstwhile shareholders and is a wholly owned subsidiary w.e.f September 8, 2021.*

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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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Branches