ICRA

February 16, 2017

Tejas Networks Limited

Instrument	Amount	Rating Action
	Rs crore	February 2017
Long Term/Short Term - Fund Based	339.75 (enhanced from 202.73)	Long-term rating upgraded to [ICRA]A(Stable) from [ICRA]BBB+(Positive); short-term rating upgraded to [ICRA]A1 from [ICRA]A2+
Long Term/Short Term - Non Fund Based	156.20 (enhanced from 129.50)	
Long Term/Short Term - Unallocated	63.91 (reduced from 187.59)	
Term loan	NIL (reduced from $6 mn)	-
Total	**559.86**	

Rating Action

ICRA has upgraded the long-term rating for Rs 339.75 crore fund based limits (enhanced from Rs 202.73 crore), Rs 156.20 crore non-fund based limits (enhanced from Rs 129.50 crore) and Rs 63.91 crore unallocated limits (reduced from Rs 187.59 crore) of Tejas Networks Limited ('TNL' / 'the company') to [ICRA]A (pronounced as ICRA A) from [ICRA]BBB+ (pronounced as ICRA triple B plus). The outlook on the long-term rating has been revised from 'Positive' to 'Stable'. ICRA has also upgraded the short-term rating for the bank facilities of the company from [ICRA]A2+ (pronounced ICRA A two plus) to [ICRA]A1 (pronounced as ICRA A one).

Rationale:

The upgrade in long-term rating takes into account the sustained growth in revenues of TNL over the last two years aided by healthy demand from domestic and export customers as well as the improvement in capital structure and liquidity on account of recent equity fund raising and improvement in working capital cycle. TNL's revenue visibility going forward is supported by strong order book, expected growth in optical fibre network deployment by domestic telecom operators and tie-ups with foreign original equipment manufacturers (OEMs). The equity funds raised and improved cash collections during H1FY2017 have been used for the working capital debt reduction, leading to sustainable improvement in debt protection metrics. The rating action also takes into account the proposed initial public offering (IPO) of shares of TNL expected to materialize in the near term. The rating continues to draw comfort from the technically competent management, strong product profile and reasonably diversified customer base of the company.

The ratings, however, are constrained by the stiff competition faced by TNL from global players like Nokia, ZTE, Huawei, etc, who have more diversified product offerings. TNL needs to continuously invest in research and development (R&D) to stay competitive in a technologically intensive industry; in the past such R&D costs have constrained free cash flows, leading to high dependence on debt to fund the working capital requirements. Notwithstanding the current order book and buoyant near-term demand profile, TNL's long-term revenue prospects will be linked to the capital expenditure cycles of its customer base; past volatility in order inflows and revenues have adversely impacted the financial profile of the company in certain years. ICRA also notes that TNL is exposed to foreign exchange risks due to the high import component in its purchases, though the risk is offset to some extent by the increasing export sales.

Going forward, TNL's ability to maintain the healthy revenue growth and reduced working capital cycle would be the key rating sensitivities.

Key rating drivers

Credit Strengths

- Sustained growth in revenue for the past two years driven by improved order flows both in the domestic as well as export market
- Reduction in debt levels aided by recent equity capital infusion and improvement in working capital cycle
- Positive outlook for demand prospects of company's products in the near-to-medium term
- Technically qualified management, diversified product profile and ability to generate repeat orders from clients

Credit Weakness

- Stiff competition faced from globally reputed players such as Huawei, ZTE, Nokia etc
- Need for continued investments in R&D to stay competitive constrains free cash flows
- TNL is exposed to foreign exchange risks due to the high import component in its purchases; however, this is mitigated to some extent by the growing export sales

Description of key rating drivers highlighted above:

The rating upgrade factors in the strong revenue growth reported by the company in H1FY2017 vis-à-vis H1FY2016, driven by increased contribution from export segment as well as robust performance in the domestic market. The export business has contributed 47% of the total topline of the company in H1FY2017 (as compared to only 28% in FY16), which establishes the global acceptability of TNL's products. This performance in FY2017 maintains the growth trajectory that was set in FY2016, when the company reported a 62% year on year growth in revenues. The outlook for TNL's products, which are primarily used in cellular backhaul of optical fibre network, looks favourable due to increased fiberization of backhaul for telecom towers, significant potential for penetration of fiber optic networks in tier-2 and tier-3 cities of India, and increased spend by private telecom operators towards augmenting their 3G/4G networks. TNL has been able to repeat orders from its customer base, reflecting the high product quality and price competitiveness.

TNL had raised Rs 64.9 crore of fresh equity capital during H1FY2017, which has been primarily used to reduce the working capital borrowing level of the company. Moreover, there has been significant reduction in the working capital cycle of the company over FY2016 and H1FY2017, aided by faster collection of receivables and change in inventory management policy. TNL now follows a turnkey model for manufacturing, wherein the raw materials and components are procured by the electronic manufacturing services vendors, rather than being carried on the books of TNL as done earlier. As a result of these developments, the total debt level has reduced significantly between March 2016 (Rs 247.5 crore) and September 2016 (Rs 95.8 crore), leading to improvement in capital structure and liquidity profile of TNL. The rating continues to draw comfort from the technically competent management, strong product profile and diversified customer base of the company.

TNL however faces high competition from global players in the optical networking equipment market such as Huawei, ZTE and Nokia; these larger competitors have more diversified product and service offerings catering to the broader telecom equipment and networking industry. Nonetheless, TNL has been able to maintain its market share in its addressable market in the domestic industry, aided by strong product profile. TNL needs to continuously invest in research and development (R&D) to stay competitive in a technologically intensive industry; in the past such R&D costs have constrained free cash flows, leading to high dependence on debt to fund the working capital requirements.

Analytical approach:

Links to applicable Criteria

Corporate Credit Ratings: A Note on Methodology

About the Company:

Tejas Networks Limited was incorporated in 2000 is primarily into the design and manufacturing of optical transmission products which find application in cellular backhaul, high-speed broadband and backbone network. Over the years, the company has received funding from various investors such as Cascade Capital Mauritus, Mayfield XII Mauritus, Sandstone Private Investments Mauritius; Samena Capital Dubai etc. In FY2016, TNL reported a profit after tax (PAT) of Rs 28.5 crore on an operating income of Rs 627.5 crore; in FY2015, the company reported a net loss of Rs 17.5 crore on an operating income of Rs 386.8 crore (based on consolidated financials).

Status of non-cooperation with previous CRA: Not Applicable.

Any other information: Not Applicable**.**

Rating History for last three years:
Table: Rating History

Sl No.	Name of Instrument	Current Rating			Chronology of Rating History for the past 3 years		
		Type	**Rated amount (Rs. Crore)**	**Month - year & rating**	**Month - year& Rating in FY2017**	**Month - year& Rating in FY2016**	**Month - year& Rating in FY2015**
				Feb 17	**Jul-16**	**Mar-15**	**Feb-14**
1	Fund based	Long term/Short term	339.75	[ICRA]A (Stable)/A1	[ICRA]BBB+ (Positive)/A2+	[ICRA]BBB+ (Stable)/A2+	[ICRA]BBB (Stable)/A2
2	Unallocated		63.91				
3	Non-fund based		156.2				
4	Term Loan	Long Term	NIL	-	[ICRA]BBB+ (Positive)	-	-

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

Details of Instruments

Name of the instrument	Date of issuance	Maturity Date	Size of the issue (Rs. Cr)	Current Rating and Outlook
Fund based limits	-	-	339.75	[ICRA]A(Stable)/A1
Non-fund based limits	-	-	156.20	
Unallocated	-	-	63.91	

Source: Tejas Networks Limited

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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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