ICRA

February 20, 2017

Sona Koyo Steering Systems Limited

Instrument	Rated Amount	Rating Action
Term Loans	Rs. 244.99 crore (revised from INR 276.70 crore)	Upgraded to [ICRA]AA-(Positive) from [ICRA]A+(Stable)
Long-Term Fund based Limits	Rs. 81.35 crore	Upgraded to [ICRA]AA-(Positive) from [ICRA]A+(Stable)
Long-Term Unallocated Limits	Rs. 74.95 crore (revised from INR 43.24 crore)	Upgraded to [ICRA]AA-(Positive) from [ICRA]A+(Stable)
Short-Term Fund Based Limits	Rs. 52.50 crore	Reaffirmed at [ICRA]A1+
Short-Term Non-Fund Based Limits	Rs. 55.00 crore	Reaffirmed at [ICRA]A1+
Commercial Paper	Rs. 15.00 crore	Reaffirmed at [ICRA]A1+
Total	**Rs. 523.79 crore**	

Rating Action

ICRA has upgraded the long term ratings of the bank facilities of Sona Koyo Steering Systems Limited (SKSSL / "the company") from [ICRA]A+ (pronounced ICRA A Plus) to [ICRA]AA- (pronounced ICRA Double A Minus). The outlook on the long-term rating has been revised to 'Positive'. ICRA has also reaffirmed the short term rating of [ICRA]A1+ (Pronounced ICRA A One Plus). Total rated amount of bank facilities is INR 508.79 crore. ICRA has also reaffirmed the short term ratings of SKSSL's INR 15.00 crore Commercial Paper at [ICRA]A1+ (Pronounced ICRA A One Plus).

Rationale

The rating upgrade takes into consideration expectation of stronger business and financial linkage of SKSSL with JTEKT Corporation (SKSSL's key shareholder and technology supplier) following the recent development wherein latter has decided to buy-out the entire 25.12% stake of Sona group (held through Sona Autocomp Holdings in the company. Being part of Toyota Motor Corporation and among the leading manufacturers of steering systems and bearings, globally, JTEKT's increased ownership (45.22%[1]) in SKSSL is likely to benefit the latter through stronger management focus besides opening-up new business opportunities. Further, the change in ownership would also result in stronger synergies between SKSSL and JTEKT Sona Automotive India Limited (JSAI), which is a 51:49 JV between SKSSL and JTEKT and engaged in manufacturing of high-margin Column-based Electric Power Steering (C-EPS) system in India.

The ratings continue to factor in SKSSL's leading position in the steering system segment in India with strong presence in the Manual Steering Gear, Hydraulic Power Steering and Electric Power Steering (C-EPS) for Passenger Vehicle OEMs. SKSSL is among the leading suppliers of steering systems to some of the leading PV OEMs including Maruti Suzuki India Limited (MSIL), Mahindra & Mahindra (M&M), Toyota Kirloskar Motors India Limited (TKML) and Honda Cars India Limited (HCIL) with healthy share of business in their key models. By virtue of technology agreement with JTEKT Corporation, the company has access to the technological advancement in the steering system space, which along with its strong expertise in manufacturing and backward integration supports its business profile. Over the years,

[1] Before open offer; The buyout has triggered a mandatory open offer to purchase up to an additional 26% stake in line with SEBI regulations

the company has backward integrated its operations (especially for manufacturing aluminum die-casting based components) and also achieved fairly high level of localization of sub-components.

While on a standalone-level, SKSSL's product portfolio primarily comprises of manual steering gears, C-EPS (for MSIL's Alto) and HPS, on a consolidated-level, the company's product portfolio widens to include C-EPS (through JSAI) and Steering Column (through SFAL). In addition to steering systems, SKSSL generates 14% of its sales from manufacturing of driveline products including axle, propeller shafts and case differentials. Apart from catering to PV OEMs in India, the company also manufactures Electronic Power Assist Module (EPAM) for Off-Highway vehicles and caters primarily to John Deere for its global market requirements.

In line with recovery in PV demand, SKSSL has witnessed healthy growth in operating income during H1 FY 2017 aided by presence in some of the successful models of its key customers. MSIL continues to be the largest customer and has accordingly contributed to company's revenue growth during the year besides scale-up in business with TKML.

Although SKSSL is positioned as the leading player in steering system space, it faces stiff competition from Rane group, which has presence in the segment through entities such as Rane Madras (for manual steering gears) and Rane NSK (for C-EPS). Further, as part of their strategy to mitigate vendor concentration, OEMs tend to mitigate the risk by appointing more than one supplier. SKSSL's key customer - MSIL has also been following this strategy, which may limit growth prospects for SKSSL going forward. The ratings also continue to factor SKSSL's high concentration on the domestic Passenger Vehicle industry and dependence on select OEMs. Although the risk is partially mitigated by strong market share of OEMs, especially MSIL and SKSSL's high share of business. There is limited scope for margin improvement as majority of revenues come from labour intensive manual steering gears. Most of the C-EPS business at consolidated level is done through JSAI.

Following the recent development, ICRA will continue to monitor developments related to JTEKT's open offer and subsequent change in company's business strategies over the medium-term.

Key Rating Drivers
Credit Strengths:

- Leading manufacturers of steering systems in India with strong share of business with top PV OEMs
- Dominant position in the domestic passenger car steering systems industry; market leader in the manual steering gear segment with approximately 48% share in the PV segment.
- Technical collaboration and ownership by JTEKT, Japan (a Toyota Group company), a prominent global steering system manufacturer
- Increased acceptance of C-EPS (over competing technology P-EPS) by domestic passenger vehicle manufacturers to drive improvement in market position in the near term
- Synergistic product offering of SKSSL and SKSSL's 49% JV - JTEKT Sona Automotive (JSAI) has helped secure new models' business from existing clients
- Ability to develop high tech and high margin offerings, like the zero backlash intermediate shaft for select OEMs, which augurs well for business prospects
- R&D team's patented product Electronic Power Assist Module (EPAM – used in off-highway vehicles) has improved sales to John Deere and has witnessed interest from new OEMs in America
- Significant backward integration investments and localization measures have reduced the raw material costs

Credit Challenges:
- Increasing competition in passenger car industry and increasing presence of other global competitors limits margin improvement
- High revenue concentration with its top customer MSIL (~50% of total sales)
- Technology-intensive nature of products leads to recurrent research and development Capex
- Although raw material costs are negotiated with OEMs as per commodity index, conversion costs are not covered which could impact profitability in the light of increasing labour costs and fuel costs
- Limited scope for margin improvement as high margin CEPS business is carried through JSAI

Rating Sensitivities:
- Higher than projected debt funded capital expenditure and overheads related to setting-up a new manufacturing unit
- Inability of the company to secure share of business in new model launches by its key customers

Description of key ratings drivers highlighted above:
SKSSL enjoys strong relationship with major PV OEMs and has established a strong reputation in the steering systems business. On a consolidated level SKSSL is able to cater to the EPS demand of all major OEMs and have approximately 45-50% market share in the PV segment. The sales in H1 FY2017 have increased 3.4% against H1 FY2016, with significant growth coming from TKML driven by new business for *Innova* and *Fortuner* models. In addition, the company's E-PAM business is also expected to contribute in the near-term. On a consolidated level there was a dip in sales in both FY2016 and H1 FY2017 because of a decline in sales of JSAI, which in turn was a result of weak Honda car sales.

Sales from MSIL declined in H1 FY2017 because of fewer CEPS sales as there was a significant decline in *Alto* volumes (SKSSL's EPS supplies to MSIL is limited to *Alto*). The EBITDA margin of SKSSL was adversely impacted by a 1% rise in employee costs, which was slightly offset by lower raw material costs.

The standalone debt profile improved in FY2016 and H1 FY2017 due to repayment of maturing long-term borrowing aided by healthy cash flow generation and modest capital expenditure. On a consolidated level, the credit metrics look better since JSAI has minimal debt and surplus cash balances.

Analytical Approach
"For arriving at the rating, ICRA has considered consolidated view of SKSSL (along with its group companies Sona Fuji Kiko Automotive Limited (SFAL; rated [ICRA]A/Positive) and JTEKT Sona Automotive India (JSAI; not rated), since all the companies operate in the same line of business."

Links to applicable Criteria
Corporate Credit Rating –A Note on Methodology
Auto Components Suppliers Methodology

About the Company
Incorporated in 1984, Sona Koyo Steering Systems Limited (SSKL) product portfolio includes two distinct product lines viz. steering systems and driveline products. Steering systems include both manual as well as power steering systems, which comprise -steering gears and columns. The Driveline product portfolio includes case differentials, axle components, rear axle assemblies and propeller shafts. SKSSL supplies these products to various passenger vehicle OEMs including Maruti Suzuki India Limited (MSIL), Mahindra & Mahindra (M&M), Tata Motors Limited (TML), Toyota Kirloskar Motor Private Limited (TKML), etc. The company has manufacturing facilities located in Gurgaon, Dharuhera, Chennai and Sanand. A new land has been acquired in Jalisana, Gujarat, which will be developed later to cater to Maruti Suzuki's new plant in Gujarat.

SKSSL benefits from its strong relationships with most passenger car and UV manufacturers in India and maintains dominant position for steering system supplies to MSIL, HMIL, Nissan, Toyota and M&M amongst other OEMs.

The company has been successfully able to secure the business for various new model launches by global OEMs leading to customer diversification. MSIL remains the largest customer of SKSSL (Standalone) accounting for almost 50% of the total revenues in FY16.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Table: Rating History

S.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 FY2016	Month- year & Rating in FY2015	Month- year & Rating in FY2014
				Feb 2017	Feb 2016	Feb 2015	Feb 2014
1	Term Loans	Long Term	244.99	[ICRA]AA- (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)
2	Long-Term Fund based Limits	Long Term	81.35	[ICRA]AA- (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)
3	Long-Term Unallocated Limits	Long Term	74.95	[ICRA]AA- (Positive)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)
4	Short-Term Fund Based Limits	Short Term	52.50	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A1
5	Short-Term Non-Fund Based Limits	Short Term	55.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A1
6	Commercial Paper	Short Term	15.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A1

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 Instrument

Name of the instrument	Size of the issue (Rs. Cr)	Interest Rate	Maturity Date	Current Rating and Outlook
Term Loan 1	5.00		FY2018	[ICRA]AA-/Positive
Term Loan 2	0.20		FY2020	[ICRA]AA-/Positive
Term Loan 3	1.98		FY2021	[ICRA]AA-/Positive
Term Loan 4	1.57	10.28%	FY2017	[ICRA]AA-/Positive
Term Loan 5	13.50	10.65%	FY2019	[ICRA]AA-/Positive
Term Loan 6	5.63		FY2018	[ICRA]AA-/Positive
Term Loan 7	34.00		FY2020	[ICRA]AA-/Positive
Term Loan 8	33.00		FY2020	[ICRA]AA-/Positive
Term Loan 9	36.00		FY2022	[ICRA]AA-/Positive
Term Loan 10	39.09		FY2021	[ICRA]AA-/Positive
Term Loan 11	5.02		FY2019	[ICRA]AA-/Positive
Term Loan 12	30.00	10.50%	FY2023	[ICRA]AA-/Positive
Term Loan 13	40.00	10.10%	FY2023	[ICRA]AA-/Positive
Unallocated	74.95			[ICRA]AA-/Positive
LT Fund Based Facility 1	20.00			[ICRA]AA-/Positive
LT Fund Based Facility 2	0.85			[ICRA]AA-/Positive
LT Fund Based Facility 3	10.00			[ICRA]AA-/Positive
LT Fund Based Facility 4	27.50			[ICRA]AA-/Positive
LT Fund Based Facility 5	8.00			[ICRA]AA-/Positive
LT Fund Based Facility 6	10.00			[ICRA]AA-/Positive
LT Fund Based Facility 7	5.00			[ICRA]AA-/Positive

ST Fund Based Facility 1	12.50			[ICRA]A1+
ST Fund Based Facility 2	10.00			[ICRA]A1+
ST Fund Based Facility 3	30.00			[ICRA]A1+
ST Non Fund Based Facility 1	20.00			[ICRA]A1+
ST Non Fund Based Facility 2	15.00			[ICRA]A1+
ST Non Fund Based Facility 3	10.00			[ICRA]A1+
ST Non Fund Based Facility 4	10.00			[ICRA]A1+
Commercial Papers	15			[ICRA]A1+

Source: Sona Koyo Steering Systems 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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