Apollo Micro Systems Limited

May 01, 2018

Summary of rated instruments

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Fund based-Term Loan	7.40	[ICRA]BBB (Stable) Assigned
Fund based- Working Capital Facilities	84.50	[ICRA]BBB (Stable) Assigned
Non-fund based-Working Capital Facilities –BG	17.50	[ICRA]BBB (Stable) Assigned
Unallocated	0.60	[ICRA]BBB (Stable) Assigned
Non-fund based-Working Capital Facilities –LC	32.00	[ICRA]A3+ Assigned
Total	**142.00**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has assigned long-term rating of [ICRA]BBB (pronounced ICRA triple B) to the Rs. 7.40-crore term loans, Rs. 84.50 crore long-term fund based limits, Rs. 0.60-crore unallocated limits, and Rs. 17.50-crore long-term non-fund based limits of Apollo Micro Systems Limited (AMSL). The outlook on the long-term rating is 'Stable'. ICRA has also assigned short-term rating of [ICRA]A3+ (pronounced A three plus) to the Rs. 32.00-crore[1] non-fund based facilities of AMSL[2].

Rationale

The ratings factor in established presence of the company in electronic system design manufacturing (ESDM) segment with significant experience of the promoters and the management in the industry. The ratings consider AMSL's strong research and development (R&D) team, which works in collaboration with Defence Research and Development Organisation (DRDO) for new products development, and significant revenue growth during the period FY2013-17 at compounded annual growth rate (CAGR) of over 50% driven by healthy order inflow on the back of strong R&D investments. The ratings also factor in the eased liquidity position and strengthened capital structure with equity infusion of Rs. 181.8-crore in FY2018, post IPO in January 2018.

The ratings, however, are constrained by the long gestation periods in defence segment, and working capital intensive nature of operations owing to long production cycle given that the process is inspected at every stage of production, and stretched receivables as the payments are received after supplied systems are tested by its clients. AMSL's liquidity was stretched till December 2017 with complete utilisation of working capital limits owing to higher inventory and receivables, which has also limited the revenue growth in FY2018 to an extent. The ratings are also constrained by the modest order book of Rs. 147.3 crore as on March 14, 2018, which is 0.7 times FY2017 revenues limiting its revenue visibility to near term, high revenue concentration in defence sector, and intense competition in the defence ESDM industry.

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

Outlook: Stable

ICRA believes that the company will continue to benefit from the company's established presence in the industry, experienced management, and strong R&D team. The outlook may be revised to 'Positive' if substantial growth in revenue, and improved working-capital management, strengthens the financial risk profile. The outlook may be revised to 'Negative' if cash accrual is lower than expected, or stretch in the working capital cycle, weakens liquidity.

Key rating drivers

Credit strengths

Established presence in the ESDM segment – AMSL is an established player in the electronic system design manufacturing segment with significant experience of the promoters in the industry and experienced management team.

Strong R&D team with focus on developing new products – AMSL has a strong research and development team of 74 personnel, including 56 engineers, focussed on developing new products. The company works with DRDO for research on strategic defence missions developing commercially off-the shelf solutions, which are proprietary products of AMSL. AMSL's focus on R&D is reflected in the increasing spends on R&D over the years.

Healthy revenue growth for the period FY2013-17: AMSL witnessed significant revenue growth at CAGR of 54.2% for the period FY2013-17 supported by healthy order inflow on the back of strong R&D invested over the previous years. Despite the growth, scale of operations remained moderate with revenues of Rs. 211.3-crore in FY2017. Moreover, current year's revenue growth has been modest at y-o-y growth of 2% in FY2018 owing to lower order inflow and liquidity constraints till December 2017.

Eased liquidity position subsequent to IPO in January 2018: AMSL came out with initial public offering (IPO) in January 2018 and raised Rs. 156.0-crore in Q4 FY2018 to meet the working capital requirements, which has eased the liquidity position that was constrained till December 2017. The company has also raised Rs. 25.8-crore equity in Q3 FY2018.

Credit challenges

Long gestation periods in defence segments – The research and development cycle of defence products and solutions is long, which could stretch over several years. Moreover, AMSL offers solutions which form part of larger delivery system made by other system integrators with ultimate usage by Ministry of Defence (MoD), which elongates the cycle further. Successful research and development of systems (for MoD) by AMSL is critical for revenue growth.

Working-capital intensive nature of operations – AMSL's working capital intensity has been high at over 50% over the past five years owing to higher inventory and debtor days. AMSL's production cycle is very long given scrutiny and inspection involved in every stage of production, starting from raw material procurement to delivery of the systems. Moreover, the systems need to tested by its customers after delivery, only after which they release the payments. This results in high debtor days. The company meets a part of its working-capital requirements by stretching payments to creditors; however, the same are backed by LCs.

High sector concentration and modest order book – AMSL derives majority of revenues from defence sector and are dependent on the Government of India (GoI) and PSUs for their projects, which are subjected to GoI's policies and priorities. AMSL has an order book of Rs. 147.3 crore as on March 14, 2018, which is 0.7 times FY2017 revenues limiting its revenue visibility to the near term. However, the company receives small orders regularly throughout the year, and the order inflow is expected to be regular and healthy going forward.

Intense competition in defence ESDM segment – AMSL faces competition from Defence PSUs, global firms, and other players in the local market. The company's ability to improve technological know-how and offer superior services at competitive rates to its customers is critical given the high competition.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

Corporate Credit Rating Methodology

About the company:

Apollo Micro Systems Limited, started as a proprietary concern in 1985 and incorporated in March 1997 by Mr. Karunakar Reddy as a private limited company, is engaged in electronic system design and manufacturing (ESDM) providing electric and electronic hardware and software solutions for mission critical applications to defence, aerospace, navy, and home land security. AMSL converted to public limited company and came out with an IPO in January 2018. The company's manufacturing unit is located in Hyderabad with its lab area confirming with electrostatic discharge requirements with ESD safe furniture and controlled environment. AMSL is ISO 9001:2015 and CEMILAC certified.

In FY2017, according to restated financials (as per IND-AS), the company reported a net profit of Rs. 18.6-crore on an operating income of Rs. 211.3-crore compared to a net profit of Rs. 10.0-crore on an operating income of Rs. 159.0-crore in the previous year.

Key financial indicators (audited)

	FY 2016	FY 2017
Operating Income (Rs. crore)	159.0	211.3
PAT (Rs. crore)	10.0	18.6
OPBDIT/ OI (%)	15.9%	19.2%
RoCE (%)	22.8%	30.1%
Total Debt/ TNW (times)	1.6	1.4
Total Debt/ OPBDIT (times)	2.8	2.2
Interest coverage (times)	3.1	3.6
NWC/ OI (%)	53.6%	54.5%

Source: AMSL, restated financials, and ICRA research.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

S. No.	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years @		
		Type	Amount Rated (Rs. Crore)	Amount Outstanding	Date & Rating	Date & Rating in FY18	Date & Rating in FY17	Date & Rating in FY16
					May 2018	-		- -
1	Term Loans	Long-term	7.40	7.40	**[ICRA]BBB (Stable)**			- -
2	Fund-based	Long-term	84.50	NA	**[ICRA]BBB (Stable)**			
3	Non fund-based	Long-term	17.50		**[ICRA]BBB (Stable)**			
4	Unallocated	Short-term	0.60	NA	**[ICRA]BBB (Stable)**			
5	Non-Fund-based	Short-term	32.00	NA	**[ICRA]A3+**			

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	Term Loans	June - 2013	NA	September 2019	7.40	[ICRA]BBB (Stable)
NA	Fund-based	NA	NA	NA	84.50	[ICRA]BBB (Stable)
NA	Non fund-based	NA	NA	NA	17.50	[ICRA]BBB (Stable)
NA	Unallocated	NA	NA	NA	0.60	[ICRA]BBB (Stable)
NA	Non-Fund-based	NA	NA	NA	32.00	[ICRA]A3+

Source: AMSL.

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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.

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