November 22, 2019

Tejas Networks Limited: Ratings reaffirmed; outlook revised to Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based	244.50	242.00	[ICRA]A / [ICRA]A1; reaffirmed; outlook revised from Positive to Stable
Non-fund based	149.50	199.50	
Unallocated	165.86	118.36	
Total	**559.86**	**559.86**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in the rating outlook takes in to account the decline in Tejas Networks Limited (TNL)'s revenue and profitability during H1FY2020 on account of reduction in new orders from the government sector. The outlook on revenues from the government sector is muted for the second half of FY2020 as well; consequently, TNL is expected to report a y-o-y decline in its turnover in FY2020. Due to the high fixed cost base of TNL, the profit margins are expected to reduce in FY2020. In addition, TNL continues to face delays in realization of receivables from certain government sector customers, which has put pressure on the cash flows. Nonetheless, ICRA notes that TNL is working towards sustained change in revenue mix from its customer segments through increased focus on India Private and International segments, which are expected to provide more stable business going forward.

The ratings continue to be constrained by the stiff competition faced by TNL from global players such as Nokia, Ciena, and Huawei, among others, who have a more diversified product offering and the advantage of economies of scale. TNL needs to continuously invest in research and development (R&D) to stay competitive in a technologically intensive industry. TNL's long-term revenue prospects will be linked to the capital expenditure cycles of its customer base.

The ratings, however, continue to draw comfort from TNL's strong track record in the industry, coupled with its long-term relationship with some large clients, which has helped it to maintain a healthy market share in the optical networking space in India. TNL's financial risk profile is marked by strong capital structure and debt protection metrics and robust liquidity position with nil debt and cash and liquid investments of around Rs 290 crore as on September 30, 2019, notwithstanding the decline in free cash flows due to increase in the receivables position. The ratings continue to draw comfort from the established market share of TNL in the domestic optical transmission products market and the reasonably diversified product profile, which has received global recognition in the recent past.

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that TNL will continue to benefit from its extensive track record in the industry, along with its strong capital structure and liquidity profile. Ability to generate improved revenue and profitability through sustained growth in business from India Private and International segments whilst improving its overall collection cycle period, will continue to remain key rating sensitivities.

Key rating drivers and their description

Credit strengths

Technically qualified management and established relationship with customers – TNL has a technically qualified management team and a fairly diversified product offering, as evidenced by its strong intellectual property portfolio and healthy market share in the optical networking space in India. Also, its long-term relationship with some large clients enables it to generate repeat business, thus supporting the revenue profile. The company also has long term relationship with some large clients which would enable it to generate repeat business whilst taking advantage of the expected growth in optical fibre network deployment.

Robust liquidity profile – Notwithstanding the weakening revenue and profitability in H1FY2020 as compared to FY2019, the company's liquidity profile remained robust, as reflected by around Rs. 290 crore of cash and liquid investments, as on September 30, 2019. The strong liquidity provides the company the ability to compete with global peers who are much larger, besides, providing flexibility to expand its market presence.

Strong capital structure and gearing- Despite its high working capital intensity, TNL had nil bank debt as on September 30, 2019 as against a networth of Rs 1316 crore. This results in the company maintaining healthy coverage indicators.

Credit challenges

Decline in revenue and profitability - The company's revenue and profitability declined in H1FY2020 vis-à-vis previous year due to steep fall in orders from its government sector customers. Revenues declined by 44% and net profit by 98% during H1FY2020 on a y-o-y basis. During H1FY2019, government sector customers accounted for 62% of the total turnover. The outlook on revenues from the government sector continues to be muted for second half of FY2020, as a result of which the company is likely to see a y-o-y decline in revenues for the full year. Due to the high fixed cost base of TNL, the profit margins are expected to reduce in FY2020. ICRA notes that TNL is working towards such sustained change in revenue mix in terms offrom its customer segments through increased focus on India Private and International segments, would which are expected to provide more stable business going forward.

High working capital intensity – TNL's financial profile has historically been characterised by high inventory holding as well as high collection days.. In addition, the company's working capital cycle has been impacted by delay in realization of receivables from certain government sector customers for orders executed in FY2019. This has resulted in decline in free cash flows over FY2019 and H1FY2020.

Stiff competition faced from globally reputed players – The company is exposed to stiff competition from other global players such as Nokia, Huawei, and Ciena, among others, who have a long-standing presence and a more diversified product portfolio. TNL needs to continuously invest in R&D to stay competitive in a technologically intensive industry.

Liquidity position: Strong

Although there has been a high build-up of receivables over FY2019 and H1FY2020, the company's liquidity profile continues to remain strong, aided by unencumbered cash and liquid investments of Rs 290 crore as on September 30, 2019 and availability of sanctioned undrawn fund-based working capital limits from banks. As on September 30, 2019, the company had no long-term debt on its books from banks. Going forward, the recovery of the large overdue receivables can further strengthen the liquidity position. The company has ongoing R&D expenditure towards new product development which is expected to be funded out of the cash flow from operations.

Rating sensitivities

Positive triggers – ICRA could upgrade TNL's rating if it demonstrates an improvement in revenue and profitability through focus on increased revenue share from International and India Private segments. Specific credit metrics that could lead to upgrade TNL's rating would include improvement in the working capital intensity, i.e NWC/OI, less than 50% on a sustained basis.

Negative triggers – Negative pressure on TNL's rating could arise if continued volatility in order inflows adversely impacts the revenue profile and profitability, or a further stretch in the working capital cycle, weakens the liquidity profile.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology](#)
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on the consolidated financial profile of the rated entity.

About the company

Tejas Networks Limited was incorporated in the 2000. It designs and manufactures optical transmission products, which find application in cellular backhaul, high-speed broadband and backbone network for the transportation of data and voice over optical fiber. The company's products are also used in defense communication networks and by utility companies. The company successfully completed its IPO in June 2017 and is now a listed company.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	749.8	900.3
PAT (Rs. crore)	106.5	147.2
OPBDIT/OI (%)	20.4%	21.8%
RoCE (%)	11.8%	13.5%
Total Outside Liabilities/Tangible Net Worth (times)	0.0	0.0
Total Debt/OPBDIT (times)	0.0	0.0
Interest Coverage (times)	11.4	11.5
DSCR	3.9	11.7

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2020) Type	Amount Rated	Amount Outstanding	Current Rating 22-Nov-2019	Earlier Rating 24-May-2019	Rating History for the Past 3 Years FY2020 31-May-2018	FY2019 6-Sep-2017	FY2018 6-Aug-2017
1	Fund based	LT/ST	242.00	-	[ICRA]A (Stable)/A 1	[ICRA]A (Positive)/A 1	[ICRA]A (Positive)/A 1	[ICRA]A (Stable)/A 1	[ICRA]A (Stable)/A 1
2	Non-fund based	LT/ST	199.50	-	[ICRA]A (Stable)/A 1	[ICRA]A (Positive)/A 1	[ICRA]A (Positive)/A 1	[ICRA]A (Stable)/A 1	[ICRA]A (Stable)/A 1
3	Unallocated	LT/ST	118.36	-	[ICRA]A (Stable)/A 1	[[ICRA]A (Positive)/A 1	[ICRA]A (Positive)/A 1	[ICRA]A (Stable)/A 1	[ICRA]A (Stable)/A 1

Amount in Rs. crore

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	Fund based limits	-	-	-	242.00	[ICRA]A (Stable)/A1
NA	Non-fund based	-	-	-	199.50	[ICRA]A (Stable)/A1
NA	Unallocated	-	-	-	118.36	[ICRA]A (Stable)/A1

Source: Tejas Networks Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Tejas Communication Pte Limited	100.00%	Full Consolidation
Tejas Communications (Nigeria) Limited	100.00%	Full Consolidation
Tejas Israel Limited	NA*	Full Consolidation
vSave Energy Pvt Limited	NA**	Full Consolidation

*wholly owned subsidiary since acquisition on August 17, 2010 and liquidated with effect from November 25, 2018

**wholly owned subsidiary since incorporation on November 06, 2013 which has been dissolved and struck off with effect from July 28, 2018

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About ICRA Limited:

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