

July 30, 2021 *Revised*

GMM Pfaudler Limited: [ICRA]AA-(Stable)/[ICRA]A1+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term Loan	155.00	[ICRA]AA-(Stable); assigned
Long-term– Fund Based Working Capital	55.00	[ICRA]AA-(Stable); assigned
Short-term – Non-fund Based Limits	90.00	[ICRA]A1+; assigned
Short-term- Interchangeable Limits**	(55.00)	[ICRA]A1+; assigned
Total	300.00	

**100% Interchangeable with fund-based limits

*Instrument details are provided in Annexure-1

Rationale

The assigned ratings take into account the leadership position of GMM Pfaudler Limited (GMMPL) in engineering equipment and systems, including glass lined equipment (GLE) globally with strong in-house technical capabilities. GMMPL, along with its subsidiary, Mavag AG, recently acquired 54% in the global business of Pfaudler Inc. (its parent) for a total consideration of \$27.4 million, which was funded by debt of \$11 million and the rest from internal accruals. This acquisition is likely to benefit GMMPL in strengthening its presence in overseas markets by allowing access to new geographies, while supporting its revenue growth and providing cost synergies in the medium term. While GMMPL has been catering to reputed customers in domestic pharmaceutical and chemical sectors, the acquisition will allow it to cater to reputed overseas customers as well as provide cross-selling opportunities. The company plans to leverage its low-cost manufacturing facilities in India to acquire greater market share in mature markets and tap new markets such as South-East Asia and Eastern Europe. GMMPL also acquired the facilities of De Dietrich Process Systems India Private Limited in FY2021 and HDO Technologies Limited in FY2022, which enhances its manufacturing capacities in India. Further, some of the international facilities were recently modernised, which is expected to improve their efficiencies, going forward. The ratings also favourably consider the healthy revenue growth reported by the company in the past, which is likely to continue post-acquisition. While the profit margins of the India business remain robust, various cost rationalisation and modernisation measures at international facilities are expected to result in healthy margins on a consolidated basis. ICRA also notes the favourable demand prospects on account of healthy growth and capex expected in the pharma and speciality chemicals space, both in India and overseas.

Moreover, with these acquisitions, while the company has added new capacities, capabilities and markets, the debt levels have also witnessed an increase, resulting in moderation in debt protection metrics at a consolidated level. The total debt on a consolidated basis has increased to Rs. 1,095.2 crore (including ~Rs. 350 crore in Pfaudler, a pension liability of ~Rs. 463 crore and lease liabilities of Rs. 141 crore, along with other debt) as on March 31, 2021 from Rs. 50.0 crore as on March 31, 2020. This has resulted in moderation in debt coverage metrics as reflected by elevated gross debt/OPBDITA of ~3.8 times (adjusting for full year of Pfaudler's OPBDITA) in FY2021, while the same is expected to witness improvement.

In addition, the rating takes into account the company's moderately high working capital intensity due to high inventory level and vulnerability of profitability to volatility in steel prices, given the long production cycle. Furthermore, GMMPL's operations remain exposed to new capital investment cycles in key end-user segments, with the company deriving more than 80% of its revenues from the pharma and chemical sectors.

The Stable outlook on the long-term rating reflects ICRA's opinion that post-acquisition of the Pfaudler Group, GMMPL will benefit from its leadership position in the global anti-corrosive technologies market and synergies and will maintain a stable credit profile in the medium term.

Key rating drivers and their description

Credit strengths

Global leadership position in glass lined equipment business with strong in-house technical capabilities – GMMPL (standalone) derives ~60% of its domestic revenues from the GLE segment. It has been the market leader with more than 50% market share in the segment, with over five decades of experience and strong in-house technical capabilities. To cater to the growing demand, the management has been undertaking regular capex in recent years, along with domestic acquisitions. This has resulted in an increase in its installed manufacturing capacity from 1,290 equivalent units (EUs) in FY2017 to 2,700 EUs in March 2021. Furthermore, with the acquisition of Pfaudler, the company has acquired manufacturing facilities across Americas, China and Europe, thereby strengthening its foothold in the global market with around 40% market share in glass-lined equipment.

Reputed customer base from pharma and chemical industries – The company's clientele includes leading players in pharmaceuticals and chemical sectors, such as Sun Pharmaceuticals Industries Limited, Cipla Limited, BASF Group and GlaxoSmithKline PLC, among others. Furthermore, the customer base is quite diversified with the top five customers driving ~40% of the revenues in the Indian entity and the top 10 customers accounting for ~20% of the revenues in the Pfaudler Group.

Acquisition of Pfaudler Group to provide entry into new markets and benefits of economies of scale, cross-selling opportunities and cost synergies – GMMPL (standalone) was deriving less than 10% of its total revenues from export sales, thereby restricting its global presence and revenue growth. The acquisition of the Pfaudler Group will provide GMMPL an opportunity to cater to overseas customers and explore new markets. The company will also benefit from the addition of new products in its portfolio and from cross-selling opportunities. The company plans to leverage its low-cost manufacturing facilities in India to acquire greater market share in mature economies and tap newer markets such as South & East Europe as well as South East Asia. ICRA expects moderation in the profit margin at a consolidated level in the medium term, following a relatively lower profit margin in overseas operations.

Earlier healthy growth in scale of operations likely to continue after acquisition, along with strong margin profile in the Indian business – At a consolidated level (GMM and its Switzerland based subsidiary- Mavag AG), the company grew at a 19% CAGR during FY2016–FY2020 driven by regular order inflows from chemical and pharmaceutical industries. The company (GMM and Mavag) reported healthy growth of 28% and the operating income stood at Rs.757 crore in FY2021. With two months of revenues from Pfaudler, the operating income at a consolidated level stood at Rs. 1,001 crore for FY2021. ICRA expects the growth trajectory to continue, post-acquisition, following the large capex plans by pharma and chemical industries as part of the China+1 strategy adopted by manufacturers across the globe. While the standalone operating profit margin improved to 24% in FY2021 from 19% in FY2020, the consolidated margin stood at 14% due to low margin in subsidiaries as well as one-time transaction related expenses (non-cash). The company's ability to increase its market share through low cost sourcing and benefiting from economies of scale, will remain critical for margin improvement in the Pfaudler Group.

Credit challenges

Significant increase in debt levels and moderation on debt protection metrics following Pfaudler acquisition – While GMMPL remained debt-free in the past, its debt level increased significantly as on March 31, 2021. At a consolidated level, the debt level increased from Rs. 50 crore as on March 31, 2020 to Rs. 1,095 crore as on March 31, 2021, due to a term loan of Rs. 91 crore (for acquiring Pfaudler and a Hyderabad unit) and working capital limits of Rs. 14.8 crore in the Indian entity, a term loan of ~Rs. 37 crore in Mavag and ~Rs. 350 crore in Pfaudler. The increase in debt was also attributable to pension liabilities of ~Rs. 463 crore and lease liabilities of ~Rs. 141 crore as on March 31, 2021. The debt coverage metrics, as reflected

by gross debt/OPBDITA, stood at ~3.8 times (adjusting for full year of Pfaudler’s OPBDITA) in FY2021. Furthermore, the debt increased in FY2022 due to ~Rs. 60 crore of term loan availed for acquiring a unit from HDO Technologies Limited in Gujarat. ICRA notes that the pension liability is a long-term plan extending around 25 years with an average annual pay-out of around \$2.5 million.

Operations exposed to new capital investment cycles in key end-user segments – GMMPL (standalone) derives ~60% of its revenues from the GLE segment, which mainly caters to pharmaceutical and chemical sectors. While the other segments (heavy engineering and proprietary products) in India are expected to grow and the contribution of systems and service segments from Pfaudler group will increase substantially following the acquisition, pharma and chemical will continue to dominate the revenue profile, going forward as well. Thus, the company’s operations will remain exposed to capex cycles in key end-user segments. The risk is partly mitigated by the replacement demand derived from these segments for the glass-lined equipment and geographic diversification with the acquisition of Pfaudler Group.

Vulnerability of profitability to volatility in steel prices amid a long production cycle – Carbon steel and stainless steel are the major raw materials for the company. GMMPL’s inventory days have remained high during the period under review on account of its long production cycle and high raw material inventory. Given high inventory level, the profit margin remains vulnerable to steel price movements. Nevertheless, GMMPL has been able to pass on any significant movement in steel prices to its customers. Furthermore, heavy engineering projects are covered under a price-variation clause, which provides some comfort.

Liquidity position: Adequate

The company’s liquidity is adequate considering the free cash of ~Rs. 30 crore in India and unutilised bank lines of ~Rs. 60 crore as on March 31, 2021. While the consolidated cash and bank balance stood at ~Rs. 290 crore as on March 31, 2021, the ease of fungibility and repatriation of the same to different locations remains uncertain. Further, while the company has sizeable pension obligations, ICRA draws comfort from the close ended nature of the fund and long tenure of the same. The consolidated debt repayments, including pension liabilities, are around Rs. 80 crore for FY2022, which along with the planned capex is expected to be comfortably met by the accruals.

Rating sensitivities

Positive factors – Consistent growth in operating income and profitability and DSCR of 3.25 times on a sustained basis can lead to a rating upgrade

Negative factors – Any large debt funded capex or acquisition adversely impacting the capitalisation and coverage indicators might lead to rating downgrade. DSCR below 2.5 times on a sustainable basis will also be a rating trigger

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of GMM Pfaudler Limited. As on March 31, 2021, the company had 16 subsidiaries, which are all enlisted in Annexure-2.

About the company

Incorporated in 1962 as Gujarat Machinery Manufacturers Private Limited, the company was renamed as GMM Pfaudler Limited in 1999, with Pfaudler Inc. acquiring 51% stake in it. As on March 31, 2021, the promoter and promoter group held 54.95% stake in the company, of which Pfaudler Inc. (ultimately held by Deutsche Beteiligungs AG) held around 32.7%.

GMMPL directly acquired 34.45% stake in Pfaudler Group and 19.6% through its wholly-owned subsidiary, GMM Mavag AG, for a total consideration of ~Rs. 206 crore in February 2021. Post-acquisition, GMMPL enjoys ~40% of the market share in the global GLE market, while it continues to enjoy over 50% market share in the domestic market. The company also derives revenue from manufacturing proprietary products (mixing, filtration and drying equipment) and execution of heavy engineering projects in the domestic market. In its overseas operations, a significant revenues share is contributed by service and system segments. Currently, GMMPL owns thirteen manufacturing facilities across Americas, Europe and Asia.

Key financial indicators (audited)

GMMPL Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	591.1	1,001.1
PAT (Rs. crore)	71.1	63.4
OPBDIT/OI (%)	18.98%	13.85%
PAT/OI (%)	12.03%	6.33%
Total Outside Liabilities/Tangible Net Worth (times)	0.6	3.5
Total Debt/OPBDIT (times)	0.4	7.9
Interest Coverage (times)	32.1	13.6

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Total debt includes pension liabilities and lease liabilities

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)			Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2021 (Rs. crore)	Date & Rating in	Date & Rating in	Date & Rating in	Date & Rating in
					July 30, 2021	FY2021	in FY2020	in FY2021
1	Term Loans	Long-term	155.00	91.00	[ICRA]AA-(Stable)	-	-	-
2	Fund Based Limits	Long-term	55.00	-	[ICRA]AA-(Stable)	-	-	-
3	Non-fund Based Limits	Short-term	90.00	-	[ICRA]A1+			
4	Interchangeable Limits*	Short-term	(55.00)	-	[ICRA]A1+			

*Interchangeable with fund-based working capital limits

Instrument	Complexity Indicator
Long-term Fund-based – Term Loan	Simple
Long-term– Fund Based Working Capital	Simple
Short-term – Non-fund Based Limits	Very Simple
Short-term- Interchangeable Limits	Very simple

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 analyzing 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, is available on ICRA's 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 Loan-I	April 2021	6.4%	Apr 2025	65.00	[ICRA]AA-(Stable)
NA	Term Loan-II	January 2021	~2%	Jan 2025	44.00	[ICRA]AA-(Stable)
NA	Term Loan-III	June 2020	7.2%	May 2025	46.00	[ICRA]AA-(Stable)
NA	Fund-based Working Capital Limits	-	-	-	55.00	[ICRA]AA-(Stable)
NA	Non-fund Based Limits	-	-	-	90.00	[ICRA]A1+
NA	Non-fund based Interchangeable Limits	-	-	-	(55.00)	[ICRA]A1+

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	GMMPL Ownership	Consolidation Approach
GMM Pfaudler Limited	100% (rated entity)	Full Consolidation
Mavag AG	100%	Full Consolidation
GMM International S.a.r.l	54%	Full Consolidation
Pfaudler GmbH	54%	Full Consolidation
Pfaudler Normag Systems GmbH	54%	Full Consolidation
Pfaudler Interseal GmbH	54%	Full Consolidation
Pfaudler France S.a.r.l	54%	Full Consolidation
Pfaudler S.r.l	54%	Full Consolidation
Pfaudler Limited	54%	Full Consolidation
Pfaudler Services Benelux B.V.	54%	Full Consolidation
Pfaudler Private Limited	54%	Full Consolidation
Pfaudler Ltda	54%	Full Consolidation
Pfaduler S A de C.V.	54%	Full Consolidation
Pfaudler (Chang Zhou) Process Equip. Co. Ltd	54%	Full Consolidation
GMM Pfaudler US Inc	54%	Full Consolidation
Edlon Inc	54%	Full Consolidation
Glaesteel Parts and Services Inc.	54%	Full Consolidation

Corrigendum

Document dated July 30, 2021 has been corrected with revisions as detailed below:

1. *In the second paragraph of the body of the rationale (page no. 1) and in the first point of the credit challenge (page no. 3) the revision is made*
2. *The revision pertains to total debt and its break up as on March 31, 2021 and March 31, 2020. Accordingly, the Total Outside Liabilities/Tangible Net Worth (times) and Total Debt/OPBDIT (times) has been recalculated and updated (page no. 4).*

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