January 11, 2023

Sunbeam Generators Private Limited: Ratings downgraded to [ICRA]BBB/[ICRA]A3+; Outlook revised to Stable from Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Cash Credit	7.00	7.00	[ICRA]BBB; downgraded from [ICRA]BBB+; outlook revised to Stable from Negative
Bank Guarantee	1.50	1.50	[ICRA]A3+; downgraded from [ICRA]A2
Untied Limits	1.50	1.50	[ICRA]BBB/[ICRA]A3+; downgraded from [ICRA]BBB+/[ICRA]A2; outlook revised to Stable from Negative
Total	**10.00**	**10.00**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings downgrade for Sunbeam Generators Private Limited's (SGPL) factors in a significant decline in the operating profit margin since FY2021 owing to a combination of factors including demand headwinds in the diesel generator business following the pandemic, significant input cost pressure which could not be entirely passed on to the customers through commensurate price hikes, and foray into the new businesses of infrastructure equipment where margins have remained subdued during the initial period of scale-up when the operating leverage remains high. Aided by a reduction in metal prices, an increase in the market share and new product offerings in the infrastructure equipment segment, while the operating margins have started to inch-up from the low of 0.4% in FY2022 (as against 2.9% in FY2020) to 0.9% in H1 FY2023, the pace of margin recovery has been slower than what ICRA had anticipated earlier. Consequently, the company's return on capital employed slipped into low single digits (~3-4%) since FY2021 and is expected to remain much lower than the cost of capital in FY2023 as well. Going forward, the company's ability to shore up its operating profit margins to the pre-Covid levels through adequate product price revisions and reduce the operating leverage by quickly increasing the scale of operations/market share of the transit mixer business would remain crucial from the credit perspective.

The ratings also remain constrained by the company's moderate scale of operations, making it vulnerable to a period of sustained industry downturn. SGPL is also exposed to high product concentration risk as ~91% of its revenues was derived from diesel genset in H1 FY2023. Besides, the company has limited geographical presence in the generator business as it is concentrated in South India (primarily Tamil Nadu [TN], Andhra Pradesh [AP] and Telangana). The ratings are also constrained by SGPL's high supplier concentration risk, with the company essentially involved in manufacturing and distributing Kirloskar Oil Engine Limited's (KOEL) branded diesel genset (where primary components such as engines and alternators are supplied by KOEL). As the geographical territories of operations are defined by KOEL, it limits new market expansion opportunities for SGPL. Given the limited value addition involved in assembling of diesel gensets amid the intense competition prevalent in this cyclical industry, SGPL's profitability indicators remain low. Further, demand from diesel generator [DG] sets remains vulnerable to the changing regulatory norms for tighter emission levels and a consequent increasing demand for alternative cleaner power back-up solutions. Besides, proposed implementation of new CPCB-4 norms (Central Pollution Control Board) is expected to lead to material price hikes for the new products complying with more stringent emission norms, which not only poses risk to medium term demand growth due to the higher cost implications for buyers, but also carries the potential for disruption in demand patterns during the transition period. However, with diversification of its product base in the infrastructure equipment industry, the product concentration risk is expected to reduce in the near term.

The ratings, however, favourably factor in the established track record of SGPL's management in the DG industry. The ratings also consider the company's established position as one of the leading original equipment manufacturers (OEM) for KOEL gensets for over 20 years in the 2.4-1,500 kVA segment of gensets. The ratings further take comfort from its healthy market share of diesel generators in TN, AP and Telangana. ICRA notes that the generator industry is facing headwinds from the steadily improving power situation in India. However, the increasing trend of adoption of gensets in urban high-rise residential complexes is likely to support a modest growth in demand over the near-to-medium term. The ratings also favourably factor in the steady revenue growth from the infrastructure equipment segment, especially transit mixers. ICRA notes that the company generated revenue of Rs. 44.5 crore from the sale of transit concrete mixers in FY2022, which is significantly higher than Rs. 14.6 crore generated from this segment in FY2021. This was largely aided by SGPL's tie-up with Ashok Leyland for manufacturing and mounting transit mixers on the vehicle chassis. Moreover, the company has been able to widen its tap SGPL's management expertise in driving various growth opportunities, which include initiatives to explore new opportunities in the infrastructure equipment segment. The ratings continue to reflect SGPL's modest financial profile, characterised by a low capital structure and comfortable coverage metrics.

The Stable outlook on the long-term rating reflects the gradually improving demand environment in the diesel generator segment, increasing market share in the infrastructure equipment segment, and plans to foray into other high-growth segments, which are expected to shore-up the revenues and profit margins, and in turn the business return indicators, going forward.

Key rating drivers and their description

Credit strengths

Extensive operating track record in genset manufacturing – Established in 1996, SGPL has a long operating history in the genset business. The management's rich experience, for over two decades, in the genset manufacturing business has helped SGPL in expanding its geographical reach within its regions of operations in TN, AP and Telangana.

Revenue visibility through established relationship with KOEL and Ashok Leyland; revenues have witnessed an uptrend in FY2023 – SGPL is one of the leading OEMs for KOEL for the 2.4-1500 kVA genset segment. Its established relationship with KOEL, spanning over 20 years, has been positively reflected in SGPL's prominent presence in the diesel genset market in TN, AP and Telangana (a ~21.59%[1] market share in FY2022). Additionally, the ratings derive comfort from the inflow of steady orders for transit mixers. Ashok Leyland contributed ~10% to its total revenue vide the contract for manufacturing and mounting of concrete mixers on their chassis. The revenue growth witnessed in H1 FY2023 is expected to sustain over the near term due to established relationship with KOEL and Ashok Leyland. Moreover, the company has been able to tap SGPL's management expertise in driving various growth opportunities, which include initiatives to explore new product additions (like boom pumps, batching plants, concrete pump) in the infrastructure equipment segment.

Modest financial risk profile characterised by low gearing and comfortable debt coverage indicators – The company has external borrowing comprising entirely cash credit borrowing facilities of Rs.3.05 crore outstanding as on March 31, 2022. The utilisation levels of fund-based limits remained low during the 12-month period ended in November 2022. This resulted in low debt levels and a comfortable capital structure with a gearing and Total Outside Liabilities/Tangible Net Worth of 0.1 times and 0.9 times, respectively as on March 31, 2022. Despite lower operating margin in FY2022 vis-à-vis FY2021, low external debt levels led to a modest interest coverage of 3.0 times in FY2022, which improved to 8.4 times in H1 FY2023 following the improvement in profit margins.

[1] Source: SGPL

Credit challenges

Slower than expected pick-up in profit margins – SGPL witnessed a significant decline in the operating profit margin since FY2021 on account of a combination of factors including demand headwinds in the diesel generator business following the pandemic, significant input cost pressures which could not be entirely passed on to the customers through commensurate price hikes, and foray into the new businesses of infrastructure equipments where margins have remained subdued during the initial period of scale-up when the operating leverage remains high. Aided by a reduction in metal prices and an increase in market share and new product offerings in the infrastructure equipment segment, while the operating margins have started to inch-up from the low of 0.4% in FY2022 (as against 2.9% in FY2020) to 0.9% in H1 FY2023, the pace of margin recovery has been slower than what ICRA had anticipated earlier. Going forward, the company's ability to shore up its operating profit margins to pre-covid levels through adequate product price revisions and reducing operating leverage by quickly increasing the scale of operations/market share of the transit mixer business, would remain crucial from the credit perspective.

Modest scale of operation, exposure to high geographical and product concentration risks – The company's scale of operations is moderate and is characterised by high product and geographical concentration. Moderate scale of operations makes the company vulnerable to a period of sustained industry downturn. SGPL also faces high product concentration risk with a predominant share of its revenue (82% in FY2022 and 91% in H1 FY2023) coming from genset sales. However, it has been diversifying its product profile and is manufacturing various infrastructure equipment at present. It generates a substantial revenue from the infrastructure segment through sale of concrete mixers, which contributed 15% to its revenue in FY2022 and 7% in H1 FY2023. Further, the company's genset sales are restricted to TN, AP and Telangana, resulting in geographical presence in the diesel genset segment being restricted to South India. Also, it faces direct competition from Genlite Engineering Pvt. Ltd. (another KOEL's OEM), which has geographical presence in SGPL's addressable markets.

Operations exposed to inherent cyclicality prevalent in diesel genset industry as well as changes in regulations – The company's revenue growth in the genset segment remains exposed to the inherent cyclicality associated with the capex undertaken by the industrial/retail sector. After a decline in FY2021 following the pandemic, SGPL's top line improved in FY2022 and H1 FY2023 owing to revival in demand from the key end-user industries post normalisation of the Covid-19 related disruptions. Further, its efforts to diversify its product profile in the industrial segment is expected to reduce earnings volatility to an extent. That said, demand from diesel generator [DG] sets remains vulnerable to the changing regulatory norms for tighter emission levels and a consequent increasing demand for alternative cleaner power back-up solutions. Besides, proposed implementation of new CPCB-4 norms (Central Pollution Control Board) is expected to lead to material price hikes for the new products complying with more stringent emission norms, which not only poses risk to medium term demand growth due to the higher cost implications for buyers, but also carries the potential for disruption in demand patterns during the transition period.

Dependence on KOEL's brand and key diesel genset component – The company mainly depends on KOEL for purchasing the large share of its key components such as engines and alternators, which exposes SGPL to supplier concentration risks. Further, the products are sold under KOEL's brand. However, the risk is partly mitigated because of SGPL's established relationships with KOEL and co-branding privileges enjoyed by the entity. Moreover, SGPL's established distributor profile in the region supports the long-term sustainability of its relationship with KOEL.

Low profitability due to low entry barriers and stiff competition – The genset manufacturing industry is characterised by stiff competition with low entry barriers. SGPL competes with other OEMs of KOEL as well as other genset brands in its region of operations. The primary components of diesel gensets such as engines and controllers are manufactured by KOEL and the company's value addition to the final product remains relatively lower. Intense competition and high supplier concentration resulted in restricted pricing flexibility and hence its profitability is low, as reflected by its operating profit margin of 0.4% and return on capital employed (RoCE) of 3.1% in FY2022.

Liquidity position: Adequate

SGPL does not have any external term loan as on date. Moreover, the company has moderate average working capital utilisation level of 3% during the 12-month period ended in November 2022. As of end-November 2022, the company's cash credit limits of Rs. 7 crore remained entirely undrawn, leaving a comfortable liquidity headroom. In addition, it had unencumbered cash and liquid investment of Rs. 12.1 crore as on September 30, 2022 (Rs. 9.96 crore as on March 31, 2022). Therefore, the company's liquidity has been assessed as adequate.

Rating sensitivities

Positive factors – ICRA could upgrade SGPL's ratings if the company is able to significantly improve its profitability while scaling up its operations.

Negative factors – Pressure on the company's ratings could arise if the company is unable to demonstrate an improvement in profit margins going forward. Further, the rating could also come under pressure if there is any adverse change in the business relationship with KOEL/ Ashok Leyland, or if sizeable capex/investments weaken its liquidity position. Specific credit metric that could also lead to ratings downgrade include Total Debt/ OPBITDA of more than 2.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone financial statement of the issuer

About the company

Incorporated in 1996, SGPL is involved in the assembly and distribution of canopied diesel generator sets and is one of the leading generator OEMs for KOEL. The company offers genset in the wide range of 2.4-1,500 kVA rating. SGPL also has presence in the infrastructure equipment sector through transit mixers (own branded). The company has wind electric generators installed in the Coimbatore region (capacity of 1.75 MW). SGPL manufactures sheet metal parts and is equipped with an in-depth sheet metal conversion expertise, complemented by the next-generation machinery infrastructure. SGPL's manufacturing unit is in Puducherry. The manufacturing set-up includes a steel processing centre, equipped with a combination of semi and fully automatic CNC machines. It has an in-house fabrication shop that produces highly precise fabricated components.

Key financial indicators

SGPL	FY2021 (Audited)	FY2022 (Provisional)	H1 FY2023 (Provisional)
Operating income	183.0	286.4	150.2
PAT	0.9	1.1	0.4
OPBDIT/OI	0.9%	0.4%	0.9%
PAT/OI	0.5%	0.4%	0.3%
Total outside liabilities/Tangible net worth (times)	0.9	0.9	-
Total debt/OPBDIT (times)	2.6	3.0	-
Interest coverage (times)	3.5	3.0	8.4

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Jan 11, 2023	Mar 10, 2022	Dec 10, 2020	Sep 25, 2019
1	**Cash Credit**	Long Term	7.00	3.05	[ICRA]BBB (Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
2	**Bank Guarantee**	Short Term	1.50	-	[ICRA]A3+	[ICRA]A2	[ICRA]A2	[ICRA]A2
3	**Untied Limits**	Long Term / Short Term	1.50	-	[ICRA]BBB (Stable) / [ICRA]A3+	[ICRA]BBB+ (Negative) / [ICRA]A2	[ICRA]BBB+ (Stable) / [ICRA]A2	[ICRA]BBB+ (Stable) / [ICRA]A2

Complexity level of the rated instruments

Instrument	Complexity Indicator
Cash Credit	Simple
Bank Guarantee	Very Simple
Untied Limits	NA

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 analysing 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 are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Cash Credit**	NA	NA	NA	7.00	[ICRA]BBB (Stable)
NA	**Bank Guarantee**	NA	NA	NA	1.50	[ICRA]A3+
NA	**Untied Limits**	NA	NA	NA	1.50	[ICRA]BBB (Stable) / [ICRA]A3+

Source: Company

Annexure II: List of entities considered for consolidated analysis: Not Applicable

ANALYST CONTACTS

Jayanta Roy
+91 33-71501100
jayanta@icraindia.com

Priyesh Ruparelia
+91 22-61693328
priyesh.ruparelia@icraindia.com

Ritabrata Ghosh
+91 33-71501107
ritabrata.ghosh@icraindia.com

Brinda Goradia
+91 22-6169 3341
brinda.goradia@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.