March 13, 2023

Sany Heavy Industry India Private Limited: Ratings downgraded to [ICRA]BBB+(Negative)/[ICRA]A2

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Unallocated Limits	100.00	100.00	[ICRA]BBB+ (Negative); downgraded from [ICRA]A- (Negative)
Short-term Unallocated Limits	100.00	100.00	[ICRA]A2; downgraded from [ICRA]A2+
Total	**200.00**	**200.00**	

**Instrument details are provided in Annexure-I*

Rationale

The downgrade in the ratings of Sany Heavy Industry India Private Limited's (SHIL) reflects the sustained pressure on its credit profile and coverage metrics in the backdrop of slower-than-anticipated recovery in its profitability margins on account of elevated input costs (raw material and freight) and aggressive strategy adopted to gain market share. In addition, the company has not been able to improve its working capital cycle leading to higher-than-expected leverage and weaker coverage metrics in 9M FY2023. Given its aggressive scale up plans as witnessed over the past few years, ICRA expects that SHIL will remain reliant on incremental working capital borrowings and/or extended parent support over the medium term, which could continue to constrain its credit metrics and liquidity position.

ICRA notes that SHIL's scale of operations improved significantly in FY2022 and 9M FY2023, supported by the improvement in its market share in the hoisting equipment and mining segments. However, the company's adjusted[1] operating profitability margins remained moderate, at around 2-4% in FY2022 and 9M FY2023 and are estimated to remain ~4-5% in FY2023-FY2024 (compared with ~8-10% in FY2017-FY2019). Moreover, sizeable exposure to customers with weak credit profiles exposes SHIL to the risk of bad debt write-offs, which could further impact its profitability. This apart, SHIL's operations have remained working capital-intensive in nature, owing to high inventory levels and elongated receivables, with the company having entered deferred payment sale contracts with some of its customers. This has resulted in a significant increase in its working capital requirements. Consequently, the leverage metrics, TOL[2]/TNW, deteriorated to 10.8 times as on December 31, 2022 from 4.4 times as on March 31, 2021. Nonetheless, the parent group, i.e., the China-based Sany Heavy Industry Co. Ltd. (SANY), has extended the credit period for select products, which supports its liquidity to a large extent. SHIL has capex plans of Rs. 500-600 crore over the medium term, which is expected to be funded by financial support from SANY. Infusion of long-term funds or meaningful reduction in current assets remains important from the credit perspective, considering SHIL's aggressive growth plans and consequent impact on its working capital requirement. The company is exposed to increased re-financing risk, given the short-term maturity of its debt.

ICRA, however, notes that SHIL benefits from the operational, technological and managerial support from its parent company, SANY, one of the largest mining and construction equipment manufacturers globally. SANY, and its Group companies, supplies around 70% of its raw material requirements. Over the years, SHIL has a track record of receiving support in the form of extended credit period from the SANY Group entities, which has supported the working capital cycle to a large extent. The company also benefits from the Group's strong financial flexibility by raising funds at attractive rates, as a few of its lenders

[1] *Operating profits including interest income on deferred sales.*

[2] *Adjusted TOL/TNW i.e. Total outside liabilities less group company creditors stand at 2.3 times as on December 31, 2022 from 1.3 times as on March 31, 2021 and 0.4 times as on March 31, 2020*

(foreign banks) are associated with the parent entity. Senior personnel of the SANY Group, including the Group's president on SHIL's board, indicates its strategic importance for the parent entity. The ratings derive comfort from its diversified product mix and the improving market share of its key products, which has supported revenue growth over the years, despite significant volatility in the end-user industry.

ICRA notes that there was an Income Tax search and seizure operation on the company in November 2021. Any significant liability due to the same, along with any major write-off from debtors, remains a key monitorable.

The Negative outlook on the long-term rating reflects ICRA's opinion that SHIL's credit profile will remain under pressure owing to the moderate profitability levels and its stretched working capital cycle.

Key rating drivers and their description

Credit strengths

Part of global major SANY Group – SHIL is a wholly-owned subsidiary of the China-based Sany Heavy Industry Co. Ltd., which is a global major in the construction equipment industry. SHIL benefits from the extensive product portfolio, its global presence and the Group's technological knowledge. SANY and its Group companies supply around 70% of SHIL's raw material requirements. It benefits from the financial support in the form of extended credit period by the Group companies. SHIL also benefits from the Group's strong financial flexibility, by raising funds at attractive rates, as few of its lenders (foreign banks) are also associated with the parent entity. The involvement of senior personnel from the SANY Group, including the Group's president on SHIL's board, indicates its strategic importance for the parent Group.

Improving market share in hoisting equipment segment, excavators, and mining dumpers – Hoisting equipment (cranes and piling rigs) has become the company's key product segment, accounting for ~45% of the overall revenues in 9M FY2023. In addition, it has seen healthy demand for excavators (accounting for ~35% of the overall revenue) and mining equipment (constituting ~15% of the overall revenue), which has helped to improve its revenues to Rs. 3,009 crore in FY2022 and Rs. 3,148 crore in 9M FY2023 (compared with Rs. 2,053 crore in FY2021). SHIL is focused on increasing exports sales (tele handlers gaining traction in the US market) and rental-asset portfolio, which along with addition of higher margin products in the product portfolio, will support its revenue growth and operating margins, going forward.

Credit challenges

Muted profitability margins and return indicators; vulnerability to fluctuations in input prices and forex rates – SHIL's profitability remains vulnerable to fluctuations in input prices and forex rates, amid intense competition. The company's operating margins and adjusted operating margins reduced to -0.7% and 1.8%, respectively, in FY2022, and despite YoY improvement, these are expected to remain at around 4-5% in FY2023-FY2024 (~8-10% in FY2017-FY2019) due to elevated input prices, high imported content and the competitive pricing strategy adopted. Further, being a net importer, it has sizeable unhedged foreign currency exposure. This leads to exposure to the adverse movements in forex rates (as seen in FY2022). Consequently, its return indicators were moderate, as reflected in RoCE of -13.8% in FY2022 (13.6% in FY2021).

Elongated receivables leading to high reliance on short-term borrowings and support from parent – SHIL's operations remain working capital-intensive due to the high inventory requirements and stretched receivables, which coupled with the company entering deferred payment sales, led to a significant increase in receivables (Rs. 2,874 crore as on January 31, 2023 Vs Rs. 2,363 crore in March 2022 and Rs. 1,675 crore in March 2021). The working capital has been largely funded by the extended credit period from the parent entity, along with the working capital borrowings, which increased to ~Rs. 500 crore (as on December 31, 2022, viz. nil as on March 31, 2020) over the last two years. As a result, the debt coverage indicators have been under pressure. The interest coverage is expected to remain below 5.0 times and Adj. TOL/TNW above 2.0 times in the near term. Given the short-term nature of the borrowings along with the deferred payment sales, SHIL remains exposed to re-financing risk and thus, support from the parent and group entities remains critical.

Competitive industry and inherent cyclicality in end-user industry – The industry is intensely competitive across the product segments, limiting its overall pricing power. Further, the mining and construction equipment industry is cyclical in nature with performance dependent on investments in the end-user industry such as infrastructure, mining, and construction. The cyclical nature of the industry leaves SHIL's operating performance vulnerable to demand swings that reflect economic cycles.

Liquidity position: Adequate

SHIL's liquidity position is expected to remain adequate, supported by undrawn working capital lines ~Rs. 300 crore as on December 31, 2022) and free cash and bank balances of Rs. 70 crore (as on December 31, 2022). Its working capital cycle is largely supported by the extended credit period from its Group entities. Any revision in the SANY Group's policy towards the extended credit period to SHIL, adversely impacting the liquidity position, remains a key monitorable. The company has marginal debt repayment obligations.

Rating sensitivities

Positive factors – The outlook can be revised to Stable if there is a significant improvement in profitability and working capital cycle.

Negative factors – Negative pressure on SHIL's ratings could arise in case of its inability to improve the profit margins and working capital cycle, or if it undertakes any large debt-funded capex, which impacts its liquidity position and capital structure.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Construction Equipment
Parent/Group support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financial statements of the rated entity.

About the company

SHIL, incorporated in 2002, was initially set up as a marketing company for the SANY Group's products in India. The Group invested in a manufacturing facility in 2006 and the plant became operational in 2009. The company manufactures and/or assembles excavators, hoisting equipment, mining equipment and concrete equipment such as truck cranes, concrete mixers and batching plants and motor graders in India. It also trades some of the products of its parent company in India. SHIL is present in the export markets (South East Asia and the SAARC nations) and has a subsidiary in Bangladesh, though, at present, its revenue profile is dominated by the domestic market.

Key financial indicators (audited)

	FY2021	FY2022	9M FY2023*
Operating income (Rs. crore)	2053.7	3009.9	3148.5
PAT (Rs. crore)	51.6	(127.2)	53.8
OPBDIT/OI (%)	4.0%	(0.7%)	1.1%
PAT/OI (%)	2.5%	(4.2%)	1.7%
Total outside liabilities/Tangible net worth (times)	4.4	10.6	10.8
Total debt/OPBDIT (times)	4.0	(19.0)	11.9
Interest coverage (times)	6.3	(0.7)	1.0

Source: ICRA Research; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Provisional*

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 on Dec 31, 2023 (Rs. crore)	Date & Rating on	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020	
					Mar 13, 2023	Mar 2, 2022	Mar 16, 2021	Nov 27,2019	Apr 29, 2019
1	**Unallocated Limits**	Long-term	100.0	NA	[ICRA]BBB+ (Negative)	[ICRA]A- (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Positive)
2	**Unallocated Limits**	Short-term	100.0	NA	[ICRA]A2	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Unallocated Limits	Not Applicable
Short-term – Unallocated Limits	Not Applicable

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 / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	**Long-term Unallocated Limits**	NA	NA	NA	100.0	[ICRA]BBB+ (Negative)
-	**Short-term Unallocated Limits**	NA	NA	NA	100.0	[ICRA]A2

Source: Company

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

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About ICRA Limited:

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