June 30, 2023

Ramco Systems Limited: Long-term rating downgraded, Short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based/CC	35.00	35.00	[ICRA]A- (Negative); downgraded from [ICRA]A (Negative)
Short-term, Fund-based	137.50	137.50	[ICRA]A2+; reaffirmed
Short-term, Non-fund Based	30.50	30.50	[ICRA]A2+; reaffirmed
Unallocated	11.50	11.50	[ICRA]A- (Negative)/[ICRA]A2+; long term rating downgraded from [ICRA]A (Negative) and short-term rating reaffirmed
Total	**214.50**	**214.50**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in the ratings considers moderation in Ramco Systems Limited's (RSL) credit profile owing to longer-than-anticipated delay in recovery in revenues and earnings. ICRA notes that, despite pick-up in orderbook in the last two quarters, revenue and margins are expected to remain subdued in the next two quarters considering the higher lead time between order-booking and execution, and higher Research & Development (R&D) spend. The revenue declined because of slower recovery in its key markets which resulted in lower order-booking and statistical drop in revenues resulting from the change in business model. While the revenues declined, the company's costs have increased significantly with resumption of travel and increased employee expenses; moreover, RSL had provided for bad debts in FY2023 owing to implementation related issues. The drop in revenues led to operating losses and stretched the coverage metrics in FY2023. ICRA expects the extent of loses to reduce in FY2024 with stabilisation of employee costs and improved revenues; however, provisions for bad debts will continue to impact RSL's margins. ICRA also takes note of the fund infusion through preferential equity issue and warrants to the tune of Rs. 130.0 crore which has assuaged cashflow concerns. The proceeds of the same were utilized towards repayment of debt, R&D spend and for working capital purposes.

The rating draws comfort from RSL's extensive track record, its established presence in the enterprise resource planning (ERP) business, and its long-term association with clientele of leading global companies across diversified verticals. ICRA also notes the financial flexibility arising from being part of the Ramco Group. The company has expanded its presence across geographies and diversified into other segments, leading to an improvement in order size in last few years. Although the credit metrics weakened on the back of subdued profitability, the capitalisation metrics are relatively comfortable.

ICRA notes of RSL's high R&D requirements that necessitate continuous investments, which are capitalised and result in high amortisation expenses. The ratings remain constrained by competition from much larger players in the segment, working capital intensive operations, susceptibility to exchange rate volatility, risk of employee attrition and vulnerability to changes in policies of domestic and foreign governments for the IT industry at large.

The Negative outlook reflects ICRA's belief that RSL's revenues will remain subdued over the next two quarters, impacting its profitability. Moreover, higher R&D expenditure and continued write-offs are expected delay improvement in earnings.

Key rating drivers and their description

Credit strengths

Extensive track record of nearly three decades and established presence in the ERP segment - Incorporated in 1997, RSL offers customised global payroll, logistics, SRP and EAM for various industries and has developed considerable expertise in catering to the aviation sector which includes Heli and MRO segment; it has forayed into US defense sector as well.

Diversified customer base of reputed companies – The company has an established clientele of reputed companies including Fortune 200 and Fortune 100 group from diverse sectors. RSL enjoys very high customer diversification with repeat orders from large clients, including industry majors even as the company continues to add a healthy number of new customers every year. The company added 46 new clients in FY2023, with 10% of the overall revenues accruing from its new customers. ICRA expects the company to consistently add new clients, on the back of long-standing track record of operations and niche product offerings in the aviation segment.

Financial flexibility as part of the Ramco Group – The Ramco Group of companies has diversified interests in cement, cotton, synthetic yarn, building products, software solutions, clean energy and biotechnology, among other sectors. RSL derives financial flexibility by being a part of the Ramco Group. ICRA also notes the fund infusion through preferential equity issue and warrants to the tune of Rs. 130.0 crore, which has assuaged cashflow concerns. The promoter also has an option of infusing Rs. 30.0 crore through share warrants anytime in the next 18 months.

Comfortable capital structure albeit moderation seen in the recent past – RSL's debt profile consists of only working capital debt and the company uses the same intermittently. The working capital debt outstanding as on March 31, 2023 stood at Rs. 38.0 crore. The company also had a fund raise to the tune of Rs. 130.0 crore in Q4 FY2023 which shored up the net-worth base against losses. Accordingly, the capital structure remained healthy marked by gearing of 0.2 times and TOL/TNW of 0.7x as on March 31, 2023 (most of the debt comprises lease liabilities). While ICRA expects the working capital debt levels to increase marginally in the near term on account of subdued margins, the debt metrics are expected to remain comfortable, going forward.

Credit challenges

Operating losses in the past few quarters owing to higher fixed costs and moderation in top line – Ramco Systems Limited (RSL) witnessed sustained moderation in revenues over the last two fiscal years. The company's operating revenues moderated by ~15% in FY2022 and ~7% in FY2023. The revenue declined because of slower recovery in its key markets which resulted in lower order-booking and statistical drop in revenues resulting from the change in business model. Both its Enterprise and Resource Planning (ERP) and Human Resource Planning (HRP) products require in-person meetings and demos in the Asia region to convince clients on the potential long-term benefits. Drop in scale of operations coupled with increase in employee costs as an effort to address attrition resulted in operating losses in FY2023. The employee costs as a percentage of revenues increased from 44.1% in FY2021 to 69.4% in FY2023. The margins were further exacerbated by bad debt write offs on account of implementation related issues. The OPBDITA margins stood at 0.1% and -27.5% in FY2022 and FY2023 respectively. However, the losses are expected to come down as RSL has taken cost optimisation efforts with respect to employee costs, offshoring of services as Covid has subsided and moderate improvement in revenues.

High competitive intensity – RSL faces intense competition from large established players such as SAP SE, Oracle Corporation., Netsuite Inc., among others, which limits its pricing flexibility and puts pressure on its margins.

Exposure to forex risk – RSL's profit margins are susceptible to volatility in forex rates and have been impacted by forex gain/(loss) arising from the same in the past. Some of the losses are mark to market provisions, which might be reversed subsequently. The company usually tries to mitigate the risk to an extent by timing the receivables from its subsidiaries and also by repaying the outstanding packing credit (foreign currency) debt using exports proceeds in foreign currency.

High working capital intensity resulting from high receivables and unbilled revenues - The company's operations are working capital intensive in nature on account of high debtor days of over 100. The company also has considerable unbilled revenues. However, the management's conscious decision to move to subscription model across divisions has reduced the quantum of unbilled revenues in the current year. Any large bad debt write-off (compared to normalised levels) remains a sensitivity factor.

High R&D spend – RSL incurs significant capex every year mainly towards R&D, which is capitalised. This R&D expenditure, if debt-funded, would put some pressure on the capital structure.

Vulnerable to industry risks such as employee attrition and adverse changes in Government policies - The company is also exposed to broader IT industry risks such as global demand slowdown, high employee attrition and adverse changes in foreign and domestic Government policies, etc.

Environment and Social Risks

Environmental considerations: The exposure to environmental risks remains low for the IT industry. For industry participants, the primary environmental impact arises from their use of electricity to power its systems and use of water resources. RSL has been undertaking initiatives, which are expected to have environmental benefits and improve sustainability of the organisation. Some of them include the reduction of carbon footprint by replacement of old generators, air conditioners, lifts & conventional lights with the latest energy efficient equipment; replacement of conventional lights across all the floors with smart and efficient LEDs; and replacement of old sanitary fittings with the latest water conserving sanitary fittings and sensor taps.

Social considerations: The exposure to social risks is moderate for the IT sector. Given that a sizeable part of the revenue generation is from outside India/international clients and as employees are deployed across multiple geographies, RSL remains exposed to various social risks, such as changes in immigration laws and cyber security issues. This situation could result in increased employee and administration costs and reputational damage to the company. RSL enhances its cyber security through adoption of sets of frameworks covering endpoint detection and response (EDR), data level protection (DLP), privileged access management (PAM), zero trust network (ZTN), data encryption at rest and in transit. The data and processes are monitored through security information and event management systems (SIEM) with security governance structure in place. All these supplement the company's existing information security management system (ISMS) and SOC2 Type II controls. RSL's systems are regularly audited every year by reputed third-party agencies to ensure information security for the services offered through SaaS. RSL has defined its data privacy and protection policies that are aligned with the data protection regulations of different countries to ensure data security. The profitability of industry participants including RSL remains vulnerable to increase in wage costs. The company has instituted various employee stock option plans (ESOPs) to increase employee commitment and engagement. As part of its business continuity plan, RSL's product development environment is backed up in two different geographies to mitigate seismic and political risks.

Liquidity position: Adequate

RSL's liquidity is adequate with ~Rs. 60 to 70 crore buffer in the form of unutilised working capital (after factoring in the drawing power), cash and bank balances and liquid investments of Rs.77.8 crore as on March 31, 2023. RSL had prepaid the term loans in FY2024 and does not have any term debt repayment obligation. RSL's capex spend (predominantly R&D) has been higher to the tune of Rs. 117.5 crore in FY2023 and Rs.87.6 crore in FY2022. As a part of the recent fund raise, the promoter also has an option of infusing Rs. 30.0 crore through share warrants anytime in the next 18 months. In addition to this, the company has healthy financial flexibility as part of the Ramco Group.

Rating sensitivities

Positive factors – A rating upgrade is unlikely, given the negative outlook on the long-term rating. ICRA could revise the outlook to Stable from Negative if there is sustained improvement in its revenues, coupled with strong recovery in operating margins, on the back of healthy order flows.

Negative factors – The rating could be downgraded if any material delay in rebound of revenues or margins stretches its liquidity profile. A stretch in working capital intensity due to delay in recovery or higher-than-expected debt funded capital expenditure could also be a negative rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for IT-Services
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Ramco Systems Limited. As on March 31, 2023, the company had 19 subsidiaries and an associate, which are all enlisted in Annexure-2.

About the company

RSL was initially set up as a division of Ramco Industries Limited in 1989, before being spun off into an independent entity in 1999. Headquartered in Chennai, RSL is a leading cloud-based technology company with global operations. It provides ERP, HCM and aviation maintenance and engineering (M&E) as well as maintenance repair and overhaul (MRO) software to customers across the globe. It is part of the reputed Ramco Group of companies, a business conglomerate with interests in cement, cotton, synthetic yarn, cement software solutions, clean energy and biotechnology, among others.

Key financial indicators (audited)

RSL Consolidated	FY2022	FY2023
Operating Income (Rs. crore)	531.1	492.2
PAT (Rs. crore)	(73.0)	-206.9
OPBDIT/OI (%)	0.1%	-27.5%
PAT/OI (%)	-13.8%	-42.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.5	0.7
Total Debt/OPBDITA (times)*	77.9	-0.8
Interest Coverage (times)	0.1	-13.6

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; * includes lease liability classified under IND AS 116; The calculation for FY2023 is based on information available in the abridged financials.*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

S.No	Instrument	Current Rating (FY2024)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2023 (Rs. crore)	Date & Rating	Date & Rating in FY2022		Date & Rating in FY2020		Date & Rating in FY2019
					Jun 30, 2023	March 17, 2022	April 29, 2021	Mar 23, 2020	Apr 08, 2019	April 06, 2018
1	Cash Credit	Long Term	35.0	-	[ICRA]A- (Negative)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Term loan	Long Term	-	-		-	[ICRA]A (Stable)	[ICRA]A- (Positive)		
3	EPC/PCFC/WCDL	Short Term	137.5	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
4	LC/Bank Guarantees	Short Term	30.5	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
5	Unallocated	Long Term/ Short term	11.5	-	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A (Negative)/ [ICRA]A2+	[ICRA]A (Stable)/ [ICRA]A2+	[ICRA]A- (Positive)/ [ICRA]A2+	[ICRA]A- (Positive)/ [ICRA]A2+	

Complexity level of the rated instrument

Instrument	Complexity Indicator
Cash Credit	Simple
EPC/PCFC/WCDL	Very Simple
LC/Bank Guarantees	Very Simple
Unallocated	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, is available on ICRA's website: Click Here

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	Cash Credit	NA	NA	NA	35.00	[ICRA]A-(Negative)
NA	EPC/PCFC/WCDL	NA	NA	NA	137.50	[ICRA]A2+
NA	LC/BG	NA	NA	NA	30.50	[ICRA]A2+
NA	Unallocated	NA	NA	NA	11.50	[ICRA]A-(Negative)/[ICRA]A2+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	RSL Ownership	Consolidation Approach
Ramco Systems Corporation, USA	98%	Full Consolidation
Ramco Systems Ltd, Switzerland	100%	Full Consolidation
Ramco Systems Sdn. Bhd, Malaysia	100%	Full Consolidation
Ramco Systems Pte. Ltd., Singapore	100%	Full Consolidation
RSL Enterprise Solutions (Pty) Ltd., South Africa	100%	Full Consolidation
Ramco Systems Canada Inc., Canada	98%	Full Consolidation
Ramco Systems FZ-LLC, Dubai	100%	Full Consolidation
RSL Software Co. Ltd., Sudan	100%	Full Consolidation
Ramco Systems Australia Pty Ltd., Australia	100%	Full Consolidation
Ramco Systems Inc., Philippines	100%	Full Consolidation
Ramco Systems (Shanghai) Co. Ltd., China	100%	Full Consolidation
Ramco System Vietnam Company Limited, Vietnam	100%	Full Consolidation
PT Ramco Systems Indonesia, Indonesia	100%	Full Consolidation
Ramco Systems Macau Limited, Macau	100%	Full Consolidation
CityWorks (Pty.) Ltd., South Africa	30%	Equity Method
Ramco Software Japan Limited, Japan	100%	Full Consolidation
Ramco Systems Defense and Security Incorporated, USA	98%	Full Consolidation
Ramco Middle East for Information Technology, Saudi Arabia	100%	Full Consolidation
Ramco System LLC, Qatar	100%	Full Consolidation

Source: *RSL financials FY2023;* ***Note:*** *ICRA has taken a consolidated view of the parent (RSL), its subsidiaries and associates while assigning the ratings.*

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