October 20, 2023

Somic ZF Components Private Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Short-term – Fund-based/ Non-fund based – Working capital facilities	31.75	31.75	[ICRA]A1; reaffirmed
Long-term/ Short-term – Fund-based/ Non-fund based - Working capital facilities	5.00	5.00	[ICRA]A(Stable)/[ICRA]A1; reaffirmed
Total	**36.75**	**36.75**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation factors in the expected continuation of Somic ZF Components Private Limited's (Somic ZF) healthy operating performance, aided by its stable operational profile and its strong parentage. The continued access to technical assistance from its promoters—Somic Ishikawa Inc., Japan (Somic) and ZF Friedrichshafen AG, Germany (ZF)—and the strong relationships of the promoters with global auto original equipment manufacturers (OEMs) continue to support Somic ZF's business prospects. Established in 1995, Somic ZF has a proven operational track record in the auto ancillary industry with established relationships with its customers (Maruti Suzuki India Limited, or MSIL, and JTEKT India Limited, or JTEKT, among others). Further, the ratings continue to favourably factor in the company's strong financial profile, characterised by no debt on its books (apart from lease liabilities) and strong cash and liquid investments (~Rs. 50.7 crore as of March 31, 2023).

The underlying demand for the passenger vehicle (PV) industry has remained strong in recent years, with preference for personal mobility aiding volumes since the relaxation in lockdowns. Even as the industry prospects were significantly impacted by the shortage of semiconductor chips in FY2022 and H1 FY2023, the industry volumes grew at a healthy pace in FY2023. Somic ZF, aided by the healthy demand in the PV industry, recorded a healthy growth in earnings in FY2023 (revenue growth of ~34%).

The company, benefitting from its cost efficiency measures, was able to report improved operating profits with OPBDITA margin of 8.6% in FY2023 over 7.8% in FY2022. An expectation of stable demand from the key end-user industry is likely to help Somic ZF record revenue and earnings growth over the medium term and help maintain a strong financial risk profile. The ratings remain constrained by Somic ZF's high segment and client concentration risks with the company deriving most of its revenues from the PV segment and 67.4% of its revenues in FY2023 emanating from two of its customers—MSIL and JTEKT. Nevertheless, the risk is partially mitigated by Somic ZF's long established relationships along with a healthy share of business with them. The ratings also factor in the vulnerability of earnings to competition from larger players and the inherent cyclicity of demand in the Indian automotive industry.

The Stable outlook on the long-term rating reflects ICRA's expectation that Somic ZF will continue to benefit from its strong parentage in terms of technical and financial support and would continue to earn steady business from its customers, given its healthy relationships with them. Aided by steady supplies, the company is expected to maintain a comfortable financial risk profile.

Key rating drivers and their description

Credit strengths

Strong technical and operational support from parent entities – Somic ZF enjoys access to design and technology transfer support from its parent entities, Somic and ZF (both have a strong presence in the global automotive industry), which has helped it secure new businessse from the subsidiaries of global OEMs operating in India. In addition, the parent entities have aided the company's financial flexibility, reflected in the guarantees provided by them to obtain foreign currency loans.

Healthy financial risk profile and strong liquidity profile – Somic ZF's financial risk profile remains strong, characterised by a strong capital structure (no external debt on its books as of March 31, 2023, apart from lease liabilities) and healthy coverage indicators. The healthy cash reserves of ~Rs. 50.7 crore as on March 31, 2023, provide additional comfort. The liquidity profile is also supported by financial flexibility in the form of unutilised working capital limits from banks.

Credit challenges

High segment and client concentration risks – The PV segment generated most of the company's revenues in FY2023 (more than 95%), thereby leading to high segment concentration risk. In line with the joint venture (JV) agreement between Somic and ZF, the company's business prospects are largely restricted to the PV segment, with supplies to the commercial vehicle (CV) segment limited to small CVs (less than 2 tonnes). Somic ZF's PV segment remains largely dependent on two customers, MSIL and JTEKT (together drove ~67.4% of revenues in FY2023). The client and segment concentration risks are, however, partially mitigated by the company's strong share of business in various product categories and its strong relationships with its customers. Additionally, the company has a demonstrated track record of securing incremental business from its clients over the years. While Somic ZF's focus on diversifying its customer profile is likely to help moderate client concentration levels to an extent over the medium to long-term, the revenue contribution of MSIL and JTEKT is likely to remain at significant levels.

Revenue growth prospects in global markets remain limited; exposed to cyclicity in domestic market – Over the years, Somic ZF's export revenues have remained muted, with the domestic market generating most of its revenues. The company is a JV between global automotive component suppliers with a presence in various geographies through different JVs, which limits the interest of the parents in providing it with export business. Since its revenues are derived entirely from the automotive segment, Somic ZF's revenues and earnings are vulnerable to the Indian auto industry cycles, as seen in the past. While the management is focussed on expanding Somic ZF's revenues from export markets, a material diversification is only likely to happen over the medium to long-term.

Liquidity position: Strong

Somic ZFs liquidity profile remains strong, characterised by expectations of healthy fund flow from operations, healthy cash and liquid investments (~Rs. 50.7 crore as on March 31, 2023) and buffer in working capital facilities of Rs.20-25 crore. The company has no repayment obligations and moderate capex plans of ~Rs. 20-25 crore in FY2024. The same are expected to be funded through internal accruals and retained cash flows of about ~Rs.30-40 crore in FY2024.

Rating sensitivities

Positive factors – A material diversification of its clientele would be seen as a credit positive for the company. Also, a rating upgrade might be triggered if it can record a material improvement in revenue and profitability on a sustained basis, leading to an improvement in its return indicators, while maintaining a healthy liquidity profile.

Negative factors – A negative rating action could be triggered if there is any significant impact on cash accruals or deterioration in working capital cycle, leading to weakening of the company's financial and/or liquidity profile. Specific credit metrics that could trigger a downgrade would be Total debt/OPBDITA greater than 1.8 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology – Auto Component Suppliers
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Incorporated in 1995 as Sona Somic Components Limited, Somic ZF manufactures ball joints for steering systems as well as suspension arms and stabiliser links primarily for PVs. Its shares are currently held in the ratio of 50:50 by the Somic Group and the ZF Group. The company's customer base includes reputed entities like MSIL, JTEKT, Tata Motors Ltd., and Hyundai Motors India Limited, among others. It has three manufacturing facilities, one each at Gurugram (Haryana), Chennai (Tamil Nadu) and Gujarat.

About promoters:

Somic: Established in 1916, Somic designs and manufactures ball joint units and dampers for steering and suspension systems. It has seven manufacturing facilities in Japan and eight foreign affiliations in USA, France, China, India, Thailand and Indonesia. Its key customers include Toyota Motor Corporation, Suzuki Motor Corporation, Isuzu Motors Limited, Honda Motor Company Limited and JTEKT Corporation, among others.

ZF: The ZF Group is a German car parts maker with headquarters at Friedrichshafen, Germany. It is primarily known for its design, research and development (R&D), and manufacturing activities in the automotive industry. It is a worldwide supplier of driveline and chassis technology for cars and CVs. The Group reported €43.8 billion (14% YoY growth) in sales during CY2022.

Key financial indicators (audited)

	FY2022	FY2023
Operating income	464.2	622.0
PAT	16.0	25.0
OPBDIT/OI	7.8%	8.6%
PAT/OI	3.4%	4.0%
Total outside liabilities/Tangible net worth (times)	0.5	0.5
Total debt/OPBDIT (times)	0.1	0.1
Interest coverage (times)	49.9	69.2

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

Source: Company financials, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2023 (Rs. crore)	Date & rating in FY2024	FY2023	FY2022	FY2021
					Oct 20, 2023	Aug 18, 2022	Jun 28, 2021	-
1	**Fund-based/Non-fund Based – Working capital**	Short term	31.75	NA	**[ICRA]A1**	[ICRA]A1	[ICRA]A1	-
2	**Fund-based/Non-fund Based – Working capital**	Long term / Short term	5.00	NA	**[ICRA]A(Stable)/ [ICRA]A1**	[ICRA]A(Stable)/ [ICRA]A1	[ICRA]A(Stable)/ [ICRA]A1	-
3	**Term loans**	-	--	--	-	-	[ICRA]A(Stable)	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Short-term – Fund-based/Non-fund Based – Working capital	Simple
Long-term/short-term – Fund-based/Non-fund Based – Working capital	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 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	Fund based/ Non-fund based – Working capital	NA	NA	NA	31.75	[ICRA]A1
NA	Fund based/ Non-fund based – Working capital	NA	NA	NA	5.00	[ICRA]A(Stable)/[ICRA]A1

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis – Not applicable

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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.

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