May 20, 2024

ZF Steering Gear (India) Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term, Fund-based – Cash Credit	30.0	30.0	[ICRA]A+(Stable); reaffirmed
Long-term / Short-term Non-fund Based Facilities	20.0	20.0	[ICRA]A+(Stable)/[ICRA]A1+; reaffirmed
Total	**50.0**	**50.0**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation for ZF Steering Gear (India) Limited (ZFI) continues to factor in its strong credit profile, backed by its net debt free position, minimal utilization of working capital lines and strong liquidity in the form of free cash and liquid investments (~Rs. 157.7 crore as on September 30, 2023). The ratings also continue to factor in ZFI's dominant position in the domestic power steering segment and established relationships with key Original Equipment Manufacturers (OEMs) in the domestic commercial vehicle (CV) and tractor sectors. ICRA also notes the formation of two subsidiaries by ZFI – DriveSys Systems Private Limited (DriveSys) and NexSteer Systems Private Limited (NexSteer), along with formation of a joint venture – Metacast Auto Private Limited (Metacast), as a part of its backward integration drive – the move is expected to support profitability through in-house manufacturing of machined castings. DriveSys started commercial production from March 2024.

ICRA also notes the entire stake sale by the foreign joint venture (JV) partner, Robert Bosch Automotive Steering GmbH (RBAS, a major global steering system manufacturer, which held 25.79% stake in ZFI as of December 31, 2022) to the Indian promoters, in March 2023.

While ZFI has reported a healthy financial risk profile over the years, characterized by comfortable capitalization and strong liquidity metrics, ICRA notes that on a consolidated basis, the company has overall capex plans of more than Rs. 150.0 crore over the near to medium term, primarily for backward integration. Out of this planned capex, the company had incurred capex of over Rs. 75.0 crore as of March 31, 2024. Given that these investments are likely to be partially debt-funded, there would be some moderation in credit metrics from earlier levels. However, ICRA expects the capitalization and coverage indicators to remain comfortable over the medium term, aided by its steady earnings profile and with scheduled repayment of term loans. The company's liquidity position is also expected to remain strong over the medium term, supported by its healthy operational profile and cash accruals; nevertheless, developments on the patent infringement litigation by ZF Germany, and payouts for penalties/settlements if any for the same remain a monitorable.

The ratings continue to remain constrained by the company's modest scale of operations compared to industry peers, susceptibility to the inherent cyclicality in the domestic CV and tractor industries, and the constant need to upgrade and develop new technology-driven products. The company's ability to keep pace with the same, especially in view of the exit of the foreign JV partner, remains to be seen.

The Stable outlook on the long-term rating factors in ICRA's expectation that ZFI would continue to benefit from its strong business position with various OEMs, helping it to record stable cash flows and maintain a strong credit profile.

Key rating drivers and their description

Credit strengths

Strong position in domestic steering systems industry for M&HCVs and tractors; established relationships with leading OEMs – The Indian steering gear market is primarily dominated by three major players—viz., JTEKT India Limited (erstwhile Sona Koyo Steering Systems Limited; rated [ICRA]AA/Stable/A1+), ZF Rane Automotive India Private Limited (Rane Group; rated [ICRA]AA-/Stable/A1+) and ZFI. While JTEKT is primarily present in the passenger vehicle (PV) segment, ZFI and Rane Group are mainly present in the CV and tractor segments. Overall, the domestic Medium and Heavy Commercial Vehicles (M&HCV) and tractor steering systems market is primarily duopolistic, with ZFI and the Rane Group jointly commanding virtually all of the total market share in CV segment.

Comfortable capitalisation and strong liquidity position – ZFI is net debt free (as of September 30, 2023), resulting in comfortable coverage indicators with Total Debt/ OPBDITA of 0.9 times and DSCR of 49.9 times in H1 FY2024. ICRA expects the coverage indicators to remain comfortable in the medium term. Its liquidity position remains strong supported by free cash and liquid investments to the tune of ~Rs. 158 crore as on September 30, 2023, and unutilized working capital limits of ~Rs. 44 crore as of February 29, 2024. Although the company has some debt-funded capex plans lined up over the near term pertaining to backward integration initiatives, ICRA believes that the same is not expected to materially impact the credit metrics adversely. Besides, these backward integration initiatives are expected to support ZFI's profitability, going forward, through in-house sourcing of machined castings.

Credit challenges

Susceptible to inherent cyclicality in domestic CV and tractor segments; negligible presence in PVs – ZFI is a tier-I supplier, with most of its revenues coming from the CV segment and with minimal presence in the PV segment, which is dominated by JTEKT. Akin to other players, the company is exposed to the cyclical nature of the industry in which it operates. Nevertheless, its established market position and strong relationships with its clientele enables the company to mitigate such challenges to an extent. Further, steering systems, as critical automobile components, are subject to changes in design and need technology investments to transition between emission norms or change in fuel to prevent obsolescence.

Litigation with respect to patent infringement and exit of foreign JV partner and associated business implications – On November 13, 2022, ZFI intimated the stock exchanges regarding a communication received from ZF Germany in relation to an alleged infringement of the trademark "ZF" and/or "ZF India", for which it has demanded Rs. 100 crore from ZFI in damages. While the company is of the opinion that it has not committed any act of infringement, ICRA would continue to monitor developments in this regard as the same can have an impact on the company's liquidity profile. ICRA also takes note of the commercial suits filed against ZF Friedrichshafen AG (ZF AG) and others by ZFI in June 2023, including (i) Suit for permanent injunction under the Trade Marks Act for damages and other reliefs against ZF AG and others, and ZFI along with other reliefs claimed damages of Rs. 200 crore from them, and (ii) Suit for passing off, seeking permanent injunction and damages under the Trade Marks Act and other applicable laws against ZF AG and others, and ZFI along with other reliefs claimed damages of Rs. 200 crore from them.

Environmental and Social Risks

Environmental considerations – ZFI is not directly exposed to climate transition risks from the likelihood of tightening emission control requirements (as its products are used by different categories of OEMs), but its automotive manufacturing customers remain highly exposed to the same. Accordingly, ZFI's prospects are linked to the ability of its customers to meet tightening emission requirements. The company may need to invest materially to develop products to cater to electric vehicles, even though a transition towards the same in the segments catered to is likely to be only gradual. The company has been taking steps to reduce its carbon footprint by relying more on renewable sources. In this respect, the company has investments in windmills, which meet 25-30% of the company's total power requirement. ZFI's exposure to litigation/ penalties from issues related to waste and water management remains relatively lower as one of its units (at Pithampur) is a zero-discharge plant.

Social considerations – ZFI, like most automotive component suppliers, has strong dependence on human capital such as retaining talents, and maintaining healthy relationship with employees and suppliers (essential for disruption-free operations for the entity). ZFI has been taking initiatives to impart training, technical knowledge upgradation and quality betterment for its employees for improving their capacities and capabilities. Another social risk that ZFI faces pertains to product safety and quality, wherein instances of product recalls and high warranty costs may not only lead to a financial implication but could also harm the reputation and create a more long-lasting adverse impact. In this regard, ZFI's strong track record of catering to leading automotive manufacturers underscores its ability to mitigate these risks to an extent.

Liquidity position: Strong

The company has a strong liquidity profile, characterised by the expectation of healthy cash flow from operations of Rs. 30-50 crore, and free cash and liquid investments of Rs. 157.7 crore as of September 30, 2023. In addition, the company has a buffer of Rs. 44 crore from unutilised working capital lines as on February 29, 2024. Against these sources of liquidity, the company is likely to have moderate debt repayment obligations, as the capital expenditure (capex) outlay remains sizeable over the near to medium term, at ~Rs. 150 crore planned for backward integration and expected to be funded through a mix of internal accruals and external borrowings.

Rating sensitivities

Positive factors – The ratings can be upgraded with significant improvement in scale and return indicators (RoCE) on a sustained basis, while maintaining its current level of capitalisation and liquidity position.

Negative factors – There could be downward pressure on ratings if ZFI's operating performance deteriorates, leading to a sustained decline in operating profitability, and / or if its liquidity profile weakens over the medium term.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology - Auto Components
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the consolidated financials of ZFI. The company has two subsidiaries, details of which are enlisted in Annexure-2.

About the company

ZF Steering Gear (India) Limited was founded by the Munot family and ZF Lenkystene GmbH. Later, Robert Bosch Automotive Steering GmbH acquired ZF Lenkystene GmbH and renamed it as Robert Bosch Automotive Steering GmbH. The company manufactures, assembles and deals in steering gears, with presence across mechanical steering gears as well as hydraulic power steering gears. ZFI's manufacturing plants are located at Shirur district in Maharashtra and Pithampur district in Madhya Pradesh. The company's steering gears are supplied to various state transport undertakings as well as to heavy vehicles such as dumpers and haulage trucks. With this, M&HCV segment dominates the revenue pie for the company, with moderate revenue contribution from the tractors segment. As on March 31, 2024, the promoter group (Munot family) held 67.17% stake in the company.

Key financial indicators

ZFI - Consolidated	FY2022 Audited	FY2023 Audited	9M FY2024 Unaudited
Operating Income (Rs. crore)	318.2	457.1	353.7
PAT (Rs. crore)	18.3	24.5	35.4
OPBDIT/OI (%)	14.5%	13.8%	11.8%
PAT/OI (%)	5.7%	5.4%	10.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.2	0.2	-
Total Debt/OPBDIT (times)	0.7	0.7	-
Interest Coverage (times)	148.7	87.7	88.8

PAT: Profit after Tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

Source: ZFI, ICRA Research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2025) Type	Amount rated (Rs. crore)	Amount outstanding as on Mar 31, 2024 (Rs. crore)	Chronology of rating history for the past 3 years: Date & rating in FY2025	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022
					May 20, 2024	-	Mar 21, 2023	Nov 29, 2022	Mar 28, 2022
1	**Long-term Fund-based**	Long-term	30.00	-	**[ICRA]A+ (Stable)**	-	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**
2	**Long-term / Short-term Non-fund Based**	Long-term/ Short-term	20.00	-	**[ICRA]A+ (Stable) / [ICRA]A1+**	-	**[ICRA]A+ (Stable) / [ICRA]A1+**	**[ICRA]A+ (Stable) / [ICRA]A1+**	**[ICRA]A+ (Stable) / [ICRA]A1+**

Source: Company

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based	Simple
Long-term / Short-term Non-fund Based	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 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-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	**Long-term Fund-based**	NA	NA	NA	30.00	**[ICRA]A+(Stable)**
NA	**Long-term / Short-term Non-fund Based**	NA	NA	NA	20.00	**[ICRA]A+(Stable)/ [ICRA]A1+**

Source: Company

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

Annexure-2: List of entities considered for consolidated analysis

Company Name	ZFI Ownership	Consolidation Approach
DriveSys Systems Pvt Ltd	100.00%	Full Consolidation
NexSteer Systems Pvt Ltd	100.00%	Full Consolidation

Source: ZFI Annual Report FY2023

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About ICRA Limited:

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