

September 06, 2024^(Revised)

SML Isuzu Limited: Ratings upgraded; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	75.50	53.04	[ICRA]AA- (Stable); Upgraded from [ICRA]A+ (Stable)
Long-term Fund-based – Cash Credit	85.00	210.00	[ICRA]AA- (Stable); Upgraded from [ICRA]A+ (Stable)
Short-term – Fund based working capital	377.00	380.00	[ICRA]A1+; Upgraded from [ICRA]A1
Total	537.50	643.04	

*Instrument details are provided in Annexure-I

Rationale

The ratings upgrade for the bank facilities of SML Isuzu Limited (SML) factors in the healthy improvement in the entity's scale of operations, aided by steady demand in the commercial vehicle industry, especially the bus segment. The company's return and credit metrics improved materially in FY2024, benefitting from operating leverage benefits on account of an improved scale of operations and various cost efficiency measures. Expectation of continuation of steady demand in the bus segment is likely to help the company continue to record healthy cash accruals, leading to an improvement in its credit profile, going forward.

SML reported a healthy growth in bus sales in FY2024 (~14% YoY growth in bus sales volume) and recorded revenues of ~Rs. 2,196 crore in FY2024 (~21% YoY growth), aided by both volume and realisation growth. Aided by improved scale of operations, the company's operating profit margin improved to 8.1% in FY2024 (from 4.4% in FY2023). The company's performance in Q1 FY2025 also remained strong, with the company recording a revenue growth of ~18% on a YoY basis and an operating margin of ~11%. ICRA notes that the working capital debt for the company increased to ~Rs. 350 crore as of March 31, 2024, with SML building up inventory of finished goods during the school bus season. The working capital debt has come down to ~Rs. 180 crore as of June 30, 2024, aided by healthy sales volume in Q1 FY2025. Going forward, the company has no major capex requirement apart from the regulatory and regular maintenance capex, which is expected to be funded from the mix of external funding and internal cash accruals.

The ratings continue to factor in favourably the established presence of SML in the school and executive bus segment in India, and its strong parentage with its largest shareholder, Sumitomo Corporation, lending it both managerial as well as strategic support, besides supporting its creditworthiness among financiers. SML has historically maintained a strong market position in the school and executive bus segment in India, supported by its strong brand and expanding sales channel. In the passenger carrier segment, SML is present in the 5-12 tonnes sub-segment, with ~22.8% market share in its addressable segment in FY2024. Given the significance of the bus segment to its overall business, both in terms of revenue and profitability, the company has been focusing on upgrading its product portfolio to compete more effectively in the staff sub-segment and has launched front overhang (FOH) diesel buses in the recent past.

The company's business profile continues to be constrained by its limited presence in the goods carrier segment (trucks). SML's product portfolio is restricted to light commercial vehicles (LCVs) and intermediate commercial vehicles (ICVs) in the range of 3.5-12.0 tonnes, which account for only 7-9% of the total CV sales in India. Nevertheless, with focused efforts, the company has been able to improve its market share over the last three years in this category, aided by acceptability of its new cabin and increased focus of marketing team and dealers on truck sales.

ICRA notes that SML's revenue growth prospects over the medium-to-long-term remain exposed to the gradual shift towards electric vehicles (EVs). Although penetration of electric buses (e-buses) is primarily limited to the state road transport undertakings (SRTU) at present, the e-bus market in India is likely to witness a healthy traction over the medium term. Accordingly, SML's ability to adapt to the transition towards EVs will remain important to support its business prospects, and it may need to invest materially to enhance its product profile.

The Stable outlook factors in the expectation of sustained healthy performance of SML, going forward, aided by steady demand in the commercial vehicle (CV) industry, especially in the bus segment, wherein SML has a strong presence.

Key rating drivers and their description

Credit strengths

Strong parentage, with large shareholding by Sumitomo Corporation – Sumitomo Corporation (rated Baa1 by Moody's) is the largest shareholder of the company (~43.96% stake), lending both managerial as well as strategic support to the company, besides supporting its creditworthiness among financiers. This has enabled SML to raise funds from banks/ financial institutions at competitive rates. Besides, Sumitomo Corporation has provided corporate guarantee for credit facilities from Japanese banks, which reflects the promoter's willingness to support the company. The promoters have active representation in the company's board and senior management, including the managing director.

Strong market position in the school bus and executive coach segment in India – SML has a strong presence in the school bus and executive coach segment in India with a market share of ~17% in the 5-12 tonnes bus segment in FY2024. The company's strong presence in this segment is supported by its strong brand and expanding sales channel. Historically, school bus sales accounted for 75-80% of the company's total bus sales. SML reported a steady growth in bus sales in FY2024, with the company having an overall market share of 9% in the domestic bus segment.

Product launches aimed at plugging gaps in portfolio; expanding sales network to support growth over medium-to-long-term – The company has taken several initiatives to improve its product portfolio, such as launching of its Global Series Trucks (with new improved cabins) and FOH buses. Moreover, in the special application vehicle segment, the company manufactures a vehicle for the cold chain market, demand of which is expected to increase. SML has also improved its international presence over the last two years and its vehicles are well accepted in neighbouring countries like Nepal, Bangladesh and Sri Lanka. Further, the company is focusing on improving its exports to African and West Asian markets. These efforts to plug portfolio gaps and expand its sales network are likely to support its business growth and help maintain its market position over the medium term.

Credit challenges

Exposed to cyclicity in the CV industry; although higher share of buses partially mitigates the risk – SML is exposed to cyclicity in the CV industry, which leads to volatility in its cash flows and profit margins. However, this is partially mitigated by the higher share of buses in its portfolio, which enjoys comparatively steadier demand. ICRA expects the bus segment to continue to help SML mitigate the impact of cyclicity in the CV segment to an extent over the medium term.

Low market share in the CV industry because of limited product range in goods carriers and intense competition in buses from several large players – SML is a niche player in the domestic CV industry with a market share of 1.4% in FY2024 and 1.9% in Q1 FY2025 because of limited product range compared to large CV OEMs. The key reason for the low market share is SML's absence in some of the key segments within the Light Commercial Vehicles (LCV) and Medium and Heavy Commercial Vehicles (M&HCV) goods segments (which account for ~80% of industry sales). At present, the company has limited capabilities to compete with incumbents in the goods carrier segments, especially in the heavy commercial vehicles (HCV) category (i.e., vehicles above 12 tonnes). Its product offerings in the goods carrier segment are limited to the niche 3.5–12 tonnes category, with no presence in high volume segments such as small commercial vehicles (SCVs) and MHCV trucks. Nevertheless, with

focused efforts, the company has been able to improve its market share in the LCV truck segment. Its market share in the 3.5-12 tonnes goods carrier segment improved to 5.0% in FY2024 from 4.3% in FY2020, aided by acceptability of its new cabin, and increased focus of marketing team and dealers on truck sales.

The competition in the bus segment is steadily increasing with various feature-packed new model introduced by market players. Like the goods carrier segment, the bus segment is also dominated by Tata Motors Limited (TML), which is the only full range player having presence across the spectrum of passenger carriers. As a result, SML Isuzu is likely to intense competition in the bus segment, going forward. Given the importance of the bus segment to its overall business, the company upgraded its product portfolio to compete more effectively in the segment and launched FOH diesel buses in FY2021. These FOH buses have a new powertrain and higher horsepower and can be used as both school buses and tourist and city buses. Despite intense competition, the management remains confident that the company would be able to maintain its strong market position in the addressable segment.

Prolonged slowdown in CV demand weakened credit metrics – SML's sales were significantly impacted in FY2021-FY2022 by the macro-economic challenges brought about by the pandemic, especially the lacklustre demand for buses, given the aversion to public transport and curtailed capex by corporates and educational institutes. Given the low scale of operations in FY2021 and FY2022, the company reported operating losses, which resulted in a significant erosion in the net worth, besides increased dependence on working capital borrowings (~Rs. 234 crore as on March 31, 2022 compared to ~Rs. 160 crore as on March 31, 2021). Accordingly, the company's return and credit indicators remained weak in FY2021 and FY2022. The company's credit profile has improved over the past two fiscals, aided by improved profitability and limited capex outgo. Even as the company had a higher-than-expected working capital intensity in FY2024, leading to an increase in the short-term debt of the company, the same was primarily due to the inventory build-up of school buses for supplying in the peak season. The company reported better-than-expected credit metrics in FY2024, aided by a healthy operating performance. Going forward, the company's debt levels are expected to remain at similar levels, with capex likely to remain limited to regulatory capex requirements and maintenance/upgradation capex. Strong financial flexibility of SML for being majorly owned by Sumitomo Corporation (rated Baa1 by Moody's) continues to provide comfort.

Environment and Social Risks

Environmental considerations: Automotive manufacturers remain exposed to climate transition risks emanating from a likelihood of tightening emission control requirements, with the Government focused on reducing the adverse impact of automobile emissions. Accordingly, an OEM's prospects remain linked to its ability to meet tightening emission requirements. The companies in the sector may need to invest materially to develop products to meet regulatory thresholds or expected transition to alternative fuel vehicles, which may have a moderating impact on their return and credit metrics. The exposure to litigation/penalties arising from issues related to waste and water management for the OEM remains relatively low.

Social considerations: Automotive OEMs have a healthy dependence on human capital and retaining human capital, maintaining healthy employee relations as well as supplier ecosystem remain essential for disruption free operations. Another social risk that automotive OEMs face 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 company's reputation and create a more long-lasting adverse impact on demand. Entities like SML also remain exposed to any major shift in consumer preferences/demographics, which are a key demand driver and, accordingly, may need to make material investments to realign their product portfolio.

Liquidity position: Adequate

SML's liquidity is **adequate**, supported by expected net cash accruals of Rs. 140-160 crore per annum and an average buffer of Rs. 313.8 crore in the fund-based working capital limits over the sanctioned limits of Rs. 630.0 crore in the 13-month period ending in June 2024. In relation to these sources of cash, SML has capex requirements of Rs. 50-70 crore in FY2025 and debt repayments of ~Rs. 25 crore in FY2025.

Rating sensitivities

Positive factors – The company's ability to strengthen its business profile by gaining market share in the commercial vehicle industry, aided by new product launches, would be favourably considered for an improvement in the rating. A sustained increase in its profitability and credit metrics could also lead to a rating upgrade.

Negative factors – Pressure on the ratings could arise in case of a weakening in the financial risk profile due to a large debt-funded capex or slowdown in demand. Additionally, pressure on the ratings could arise if SML cedes material market share in its addressable segments. The ratings could also be downgraded in case of material deterioration in the credit profile of its parent company, Sumitomo Corporation, or weakening of financial and operational linkages with the parent company. Specific credit metric that could lead to ratings downgrade includes an interest coverage of less than 5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Commercial Vehicles
Parent/Group support	Parent Company: Sumitomo Corporation, Japan ICRA expects the parent entity, Sumitomo Corporation (a 43.96% stake) to be willing to extend financial support to SML out of its need to protect its reputation from the consequences of a group entity's distress. The Managing Director and three other board members of SML are representatives of Sumitomo Corporation.
Consolidation/Standalone	The ratings for SML Isuzu Limited are based on its standalone financials.

About the company

Incorporated in 1983, SML Isuzu Limited (formerly Swaraj Mazda Limited) is a commercial vehicle OEM with a healthy market position in the school bus segment. It operates in the light commercial vehicle (LCV) and medium commercial vehicle (MCV) segments of the automobile industry and has a product portfolio comprising buses, trucks (including tippers) and specific application vehicles. The company has a manufacturing facility at Nawanshahar, Punjab, with a production capacity of 24,000 units per annum.

The company was set up as Swaraj Vehicles Limited for manufacturing LCVs and was promoted by Punjab Tractors Limited (PTL) in technical and financial collaboration with Mazda Motor Corporation, Japan, and Sumitomo Corporation, Japan. However, the technical collaboration agreement with Mazda expired in 2004 and Mazda exited by selling off its stake to Sumitomo Corporation. Around the same time, SML entered into a technical collaboration agreement with Isuzu Motors, Japan. Sumitomo Corporation and Isuzu Motors own 43.96% and 15.00% stake, respectively, in the company.

Sumitomo Corporation: Sumitomo Corporation, headquartered in Tokyo, is one of Japan's largest trading companies, and a core member of the Sumitomo Group. The firm's total assets as of March 31, 2024, amounted to ¥11 trillion. The company trades and invests in a wide range of sectors and classifies its businesses under six business segments: (1) metal products; (2) transportation and construction systems; (3) environment and infrastructure; (4) media and digital; (5) living related goods and services & real estate, and (6) mineral resources, energy, chemical and electronics. The Group has multiple investments in India in the automotive and other industrial segments.

Key financial indicators (audited)

SML Standalone	FY2023	FY2024	Q1 FY2025*
Operating income	1,819.9	2,195.9	746.1
PAT	19.8	107.9	46.4
OPBDIT/OI	4.4%	8.1%	10.9%
PAT/OI	1.1%	4.9%	6.2%
Total outside liabilities/Tangible net worth (times)	4.2	3.2	-
Total debt/OPBDIT (times)	3.3	2.4	-
Interest coverage (times)	3.2	5.9	8.9

Source: Company, ICRA Research; * Limited Audit; All ratios as per ICRA's calculations; Amount in Rs. crore

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

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Current (FY2025)				Chronology of rating history for the past 3 years							
				FY2025		FY2024		FY2023		FY2022	
Instrument	Type	Amount Rated (Rs Crore)	Sep 06, 2024	Date	Rating	Date	Rating	Date	Rating	Date	Rating
Long term Fund based – Term Loan	Long Term	53.04	[ICRA]AA-(Stable)	-	-	14-Aug-23	[ICRA]A+(Stable)	01-Aug-22	[ICRA]A+(Negative)	18-Aug-21	[ICRA]A+(Negative)
				-	-	-	-	18-Jul-22	[ICRA]A+(Negative)	-	-
Long term Fund based – Cash Credit	Long Term	210.00	[ICRA]AA-(Stable)	-	-	14-Aug-23	[ICRA]A+(Stable)	01-Aug-22	[ICRA]A+(Negative)	18-Aug-21	[ICRA]A+(Negative)
				-	-	-	-	18-Jul-22	[ICRA]A+(Negative)	-	-
Short -term – Fund-based working capital	Short Term	380.00	[ICRA]A1+	-	-	14-Aug-23	[ICRA]A1	01-Aug-22	[ICRA]A1	18-Aug-21	[ICRA]A1+
				-	-	-	-	18-Jul-22	[ICRA]A1	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term Loan	Simple
Long-term fund-based – Cash Credit	Simple
Short -term – 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	Term Loan-I	May 2022	NA	April 2025	3.65	[ICRA]AA-(Stable)
NA	Term Loan-II	October 2021	NA	March 2025	1.08	[ICRA]AA-(Stable)
NA	Term Loan-III	October 2022	NA	December 2025	6.75	[ICRA]AA-(Stable)
NA	Term Loan-IV	March 2023	NA	January 2028	41.56	[ICRA]AA-(Stable)
NA	Cash Credit	NA	NA	NA	210.00	[ICRA]AA-(Stable)
NA	Short-term Fund Based Limits	NA	NA	NA	380.00	[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

Corrigendum

Document dated September 06, 2024, has been corrected with revisions as detailed below:

Revisions: - Page 3 – ESG related comments has been added in the rationale

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