November 08, 2024

Paras Defence & Space Technologies Limited: Ratings reaffirmed; outlook revised to Stable from Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based – Cash credit	39.0	39.0	[ICRA]A- (Stable); reaffirmed and outlook revised to Stable from Negative
Long-term/ Short-term – Non-fund based – Bank guarantee & LC	157.75	157.75	[ICRA]A- (Stable)/[ICRA]A2+; reaffirmed and outlook revised to Stable from Negative
Long-term–Fund-based–Overdraft	5.00	5.00	[ICRA]A- (Stable); reaffirmed and outlook revised to Stable from Negative
Total	**201.75**	**201.75**	

**Instrument details are provided in Annexure-I*

Rationale

The revision in outlook of Paras Defence & Space Technologies Limited (PDSTL) to Stable from Negative reflects the improvement and the expected sustenance in its operating margins, working capital intensity and the consequent improvement in its liquidity position. The operating margins increased to 27.5% at a consolidated level in H1 FY2025 due to change in revenue mix towards relatively higher profitable products/segments. The working capital intensity decreased in H1 FY2025 (NWC/OI at 93.6%, FY2024: 111.0%) with decline in debtor days and delivery of periscopes resulting in reduced inventory days. This, coupled with the receipt of QIP proceeds of ~Rs. 135 crore in October 2024, supported the company's liquidity position with unencumbered cash balance improving to ~Rs. 62 crore as on October 31, 2024 (against ~Rs. 3.0 crore as on March 31, 2024), with nil fund-based utilisation as on October 31, 2024.

The ratings favourably factor in the healthy and improved order book (OB) of Rs. 850 crore as on September 30, 2024, which translates to a comfortable OB/Operating Income (OB/OI) ratio of 3.35 times (FY2024: 2.49 times) of FY2024 OI, thus providing medium-term revenue visibility. The ratings positively consider the company's low leverage with TOL/TNW of 0.5 times as on September 30, 2024 (FY2024: 0.4 times). The interest coverage improved to 11.5 times in H1 FY2025 (FY2024: 6.8 times) due to reduced dependence on external borrowings to fund its working capital. The ratings draw comfort from the extensive experience of the management team with more than three decades of experience in designing, developing, and manufacturing a wide range of engineering products and solutions for the defence and space sector in the domain of optics, heavy engineering and electronics. PDSTL's long presence in the defence and space sector has helped it to establish strong relationships with its customers as well as suppliers. The company has developed a strong management and execution team comprising several ex-employees of Bharat Electronics Limited (BEL) and Defence Research and Development Organisation (DRDO), among others.

The ratings, however, remain constrained by the company's working capital-intensive nature of operations, which despite posting a downward trend recently, continues to remain high on an absolute basis on account of long receivables cycle and high inventory holding period. This is attributable to stocking of critical raw materials to avoid any disruption in the delivery schedules and high work in progress due to an elongated manufacturing cycle. The ratings are constrained by PDSTL's moderate scale of operations, coupled with client concentration risk, with top three clients contributing to 76% of the total OB as on September 30, 2024. The Government's thrust on 'Make in India' in the defence sector and the strong credit profile of its principal customers augur well for PDSTL. PDSTL's client profile mostly comprises Government organisations with sustained repeat orders, largely mitigating the counterparty credit risk. Going forward, the company's ability to prudently manage its working capital intensity, while scaling up its revenues, with sustenance of its healthy operating margins, will be a key rating monitorable.

Key rating drivers and their description

Credit strengths

Healthy OB provides medium-term revenue visibility – The company's fresh order inflows over the past four fiscals remained adequate, with orders worth ~Rs. 881 crore added in the last 18 months ending September 30, 2024. The pending OB of Rs. 850.0 crore as on September 30, 2024 (OB/OI ratio of 3.35 times of the OI in FY2024) provides medium-term revenue visibility.

Comfortable capital structure and healthy coverage indicators – The company's capital structure remains comfortable with TOL/TNW of 0.4 times as on September 30, 2024, supported by healthy accretion to reserves, coupled with equity infusion in the past and low debt levels. The interest coverage improved to 11.5 times in H1 FY2025 (FY2024: 6.8 times) due to the reduced dependence on external borrowings to fund its working capital. Going forward, ICRA expects the coverage indicators to remain comfortable, benefitting from the scale-up in operations, given the strong order pipeline.

Extensive experience of management team – PDSTL's promoters have more than three decades of experience in designing, developing and manufacturing a wide range of engineering products and solutions for the defence and space sector in the domain of optics, heavy engineering and electronics. Its long presence in the defence and space sector has helped to establish strong relationships with its customers as well as suppliers. It has developed a strong management and execution team comprising several ex-employees of BEL and DRDO, among others.

Credit challenges

Working capital-intensive nature of operations – The business is working capital intensive in nature with NWC/OI of 111.0% and 93.6% in FY2024 and H1 FY2025, respectively, owing to the high inventory holding period and long receivables cycle. The inventory levels are high because of additional stocking of critical raw materials to avoid any disruption in delivery schedules and high work-in-progress due to elongated manufacturing cycle. However, the working capital intensity improved in H1 FY2025 on account of reduction in debtor days and delivery of periscopes resulting in reduced inventory days. PDSTL has been able to manage its working capital cycle through extended credit period by its suppliers and availing mobilisation advance for part orders.

Moderate scale of operations – While the company reported a robust YoY revenue growth of 14% and 56% in FY2024 and H1 FY2025, respectively, supported by healthy OB position and timely execution of orders, the scale of operations still remains moderate. Given the Government's thrust on 'Make in India' in the defence sector, PDSTL has been mainly catering to domestic demand (~85% of OI contributed by domestic orders). Driven by the healthy OB status, ICRA expects the company to sustain its revenue growth in FY2025 and FY2026.

High customer concentration risk, though largely mitigated by reputed customer base and repeat orders – The company faces client concentration risk with top three clients contributing to 76% of the total OB as on September 30, 2024 and top five clients accounting for ~54% of the revenue in FY2024. The client profile mostly comprises government organisations with repeat orders received over the years, largely mitigating the counterparty credit risk. A major part of PDSTL's clientele included reputed government organisations, namely Laboratory for Electro-Optics Systems (a unit of ISRO), BEL, Instruments Research and Development Establishment (a unit of DRDO) and private companies like RRP S4E Innovation Private Limited and Unifab Engineering Project Private Limited. The company has long-standing relationships with most of its clientele. PDSTL also exports to companies based in Israel, Singapore and USA.

Environment and social risks

Environmental considerations – PDSTL is operating in the defence equipment manufacturing industry, which requires various raw materials and also entails sizeable energy and water requirements for running its multiple facilities. To safeguard the environment against the impact of its operations, and possible regulatory action for violation of applicable environmental laws, the company has tied up with State Pollution Control Board authorities for appropriately disposing/recycling solid hazardous waste at its manufacturing sites.

Social considerations – PDSTL is dependent on human capital and hence, retaining talent, maintaining healthy employee relations, as well as supplier ecosystem remains essential for disruption-free operations. Going forward, the company's ability to manage risks related to safety in the areas of process, and occupational health, while developing safety leadership capabilities, will remain a key factor from the social consideration perspective.

Liquidity position: Adequate

PDSTL has adequate liquidity, with an unencumbered cash and bank balance of ~Rs. 62 crore as on October 31, 2024. Further, it had no long-term debt as on October 31, 2024. The average working capital utilisation during the 12-month period that ended on September 30, 2024 remained at 69% for fund-based limits, with adequate cushion available in non-fund based limits (utilisation being ~80%).

Rating sensitivities

Positive factors – ICRA could upgrade the ratings if the company demonstrates a significant growth in its overall scale of operations, along with an improvement in its working capital cycle, while maintaining its operating profitability and sustaining its liquidity position.

Negative factors – Pressure on PDSTL's ratings could arise if lower-than-anticipated billing or a deterioration in the operating profitability or working capital cycle impacts the company's liquidity position and coverage metrics on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	Consolidated; the list of companies that are consolidated to arrive at the ratings are given in Annexure II

About the company

Set up in 1971 by Mr. Sharad Shah, PDSTL designs, develops and manufactures a wide range of engineering products and solutions for the defence and space sector in the domain of optics, heavy engineering and electronics. It has two manufacturing facilities – one in Ambernath (Thane) and the other in Nerul (Navi Mumbai). Reputed government organisations, namely Laboratory for Electro Optics Systems (a unit of ISRO), BEL, Instruments Research and Development Establishment (a unit of DRDO), and private companies like FFS Industries Private Limited and SEC Industries Private Limited, form a major part of the company's clientele. Its day-to-day operations are currently managed by Mr. Munjal Shah (son of Mr. Sharad Shah).

Key financial indicators (audited)

Consolidated	FY2023	FY2024	H1 FY2025*
Operating income (Rs. crore)	222.8	253.6	170.7
PAT (Rs. crore)	36.1	30.1	26.8
OPBDIT/OI (%)	26.3%	21.2%	27.5%
PAT/OI (%)	16.2%	11.9%	15.7%
Total outside liabilities/Tangible net worth (times)	0.3	0.4	0.5
Total debt/OPBDIT (times)	0.3	1.2	0.7
Interest coverage (times)	7.6	6.8	11.5

*Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations*

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)**	**Nov 08, 2024**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**	**Date**	**Rating**
Cash credit	Long term	39.0	[ICRA]A- (Stable)	Apr 05, 2024	[ICRA]A- (Negative)	-	-	Jan 27, 2023	[ICRA]A- (Stable)	Oct 27, 2021	[ICRA]A- (Stable)
										Sep 30, 2021	[ICRA]A- (Stable)
Term loan	Long term	0.0	-		-	-	-	-	-	Oct 27, 2021	[ICRA]A- (Stable)
Bank guarantee & LC	Long term/ Short term	157.75	[ICRA]A- (Stable)/ [ICRA]A2+	Apr 05, 2024	[ICRA]A- (Negative)/ [ICRA]A2+	-	-	Jan 27, 2023	[ICRA]A- (Stable)/ [ICRA]A2+	Oct 27, 2021	[ICRA]A- (Stable)/ [ICRA]A2+
Invoice discounting	Short term	0.0	-		-	-	-	-	-	Oct 27, 2021	[ICRA]A2+
Overdraft	Long Term	5.00	[ICRA]A- (Stable)	Apr 05, 2024	[ICRA]A- (Negative)	-	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based – Cash credit	Simple
Long-term – Fund-based – Overdraft	Simple
Long-term/Short-term – Bank guarantee & LC	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 I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Cash credit**	NA	NA	NA	39.00	[ICRA]A- (Stable)
NA	**BG & LC**	NA	NA	NA	157.75	[ICRA]A- (Stable)/ [ICRA]A2+
NA	**Overdraft**	NA	NA	NA	5.00	[ICRA]A- (Stable)

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Paras Aerospace Pvt Ltd	60.00%	Full Consolidation
Paras Green Optics Pvt Ltd	100.00%	Full Consolidation
Paras Anti Drone Technologies Private Limited	55.00%	Full Consolidation
Ayatti Innovative Private Limited	58.02%	Full Consolidation
OPEL Technologies PTE Ltd	100.00%	Full Consolidation
Krasny Paras Defence Technologies Private Limited	47.50%	Equity Method

Source: Company

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About ICRA Limited:

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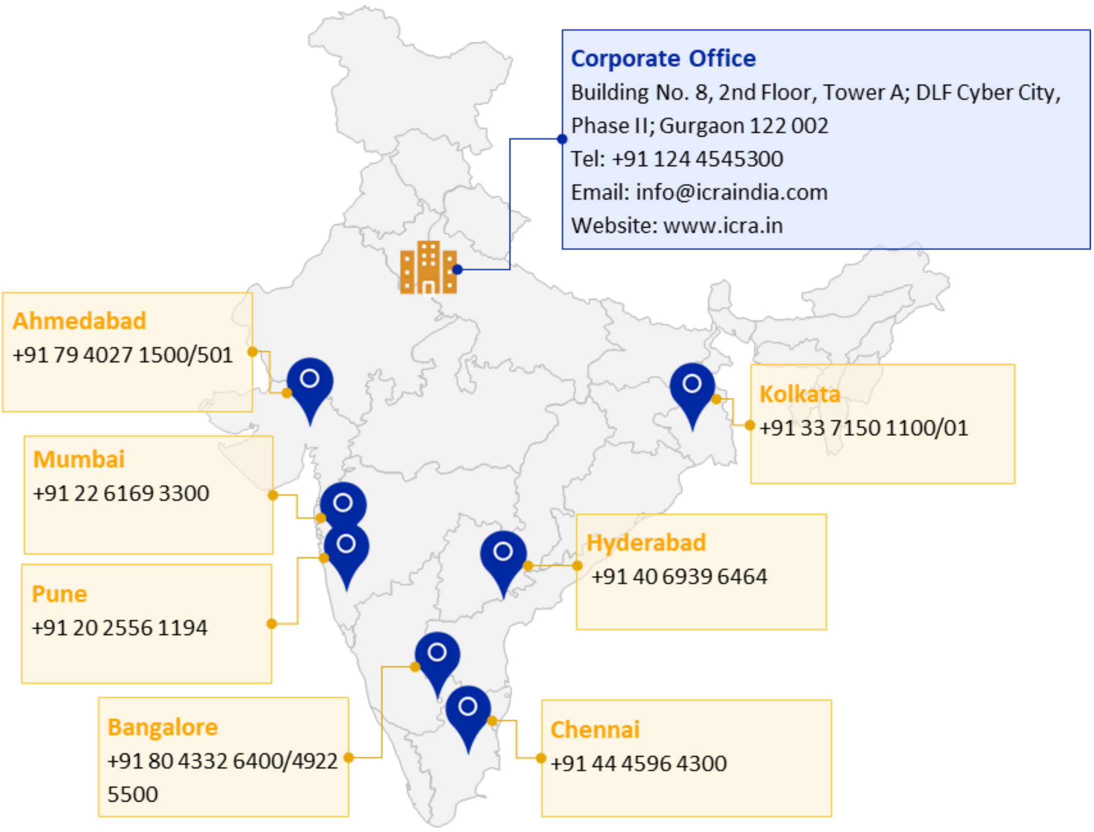

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