

July 05, 2019

EFTEC (India) Private Limited: Ratings downgraded to [ICRA]BBB(Stable)/[ICRA]A3+ and removed from Issuer Not Cooperating category

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term Fund-based/Non-fund Based	17.00	16.00	[ICRA]BBB(Stable)/[ICRA]A3+ downgraded from [ICRA]BBB+ (Stable)/[ICRA]A2; removed from Issuer Not Cooperating category
Long-term/Short-term Unallocated Facility	-	1.00	[ICRA]BBB(Stable)/[ICRA]A3+ downgraded from [ICRA]BBB+ (Stable)/[ICRA]A2; removed from Issuer Not Cooperating category
Total	17.00	17.00	

*Instrument details are provided in Annexure-1

Rationale

The rating revision takes into account the decline in EFTEC (India) Private Limited's (EIPL's) operating income in FY2019 on account of slowdown in demand and the continued weakening of its profitability metrics since FY2017 with rising prices of raw materials, which are mainly crude oil derivatives. The company's profitability is also susceptible to fluctuations in foreign exchange rates owing to sizeable raw material imports. Substantial dividend pay-outs to the parent company amounting to Rs. 17.69 crore and Rs. 10.02 crore in FY2018 and FY2019, respectively, resulted in negative net cash accruals in the last two fiscals. Furthermore, the rating remains constrained by EIPL's high client and geographical concentration risks with limited presence in the after-market segment. The company's revenues are dependent on the revival of demand in the passenger vehicle (PV) segment of the automobile industry, which is cyclical in nature and remains its major revenue driver.

The rating, however, continues to draw comfort from the company's strong parentage as a wholly-owned subsidiary of the Switzerland-based EMS Group. The rating also factors in the strong financial, technical and marketing support from its parent, its established market position in bonding, coating, sealing and damping adhesives used in the domestic automobile industry backed by reputed OEMs (including Tata Motors Limited (TML), Renault-Nissan Automotive India Private Limited (RN) and General Motors India Private Limited or GM, etc), and its medium to long-term contracts with them. The rating also factors in the high entry barriers in the business (owing to its speciality products and technology, combined with the stringent vendor approval process of OEMs) and EIPL's strong financial profile with low gearing and healthy coverage indicators. Also, the addition of new clients in the current fiscal is likely to boost the company's revenue over the medium to long-term.

Going forward, EIPL's revenue growth and overall profitability will be contingent upon the revival of demand in the PV segment of the automobile industry.

Outlook: Stable

ICRA expects EIPL to continue to benefit from its strong parentage as a wholly-owned subsidiary of the Swiss EMS Group and its established market position in the adhesives segment catering to the automobile industry. The outlook may be revised to Positive if a substantial growth in revenue and profitability strengthens the overall financial risk profile. The outlook may be revised to Negative if any deterioration in margins, continued substantial dividend pay-out, or a stretch in the working capital cycle weakens the company's liquidity position.

Key rating drivers

Credit strengths

Wholly-owned subsidiary of EMS Group; strong financial, technical and marketing support from parent - The EMS Group (CHF 2.3 billion sales in CY2018) operates globally in high performance polymers and speciality chemicals. It has 26 production sites in 16 different countries and is represented throughout the world by owned-sales companies or distributors/traders. In April 2012, the EMS Group acquired the Shroff Group's entire stake, making EIPL the former's wholly-owned subsidiary.

Established market position in sealing/bonding solutions for domestic automobile industry - The EMS Group is the global leader in providing sealing-bonding solutions for the auto industry. EIPL has an established position in the domestic market backed by its parent's long-standing relationships with international OEMs in India, resulting in a strong and stable clientele of reputed automotive OEMs (including TML, RN, GM, etc). It supplies to various manufacturing facilities of these OEMs, catering primarily to PV and utility vehicle (UV) segments.

Reputed client base of leading automobile manufacturers; client additions to boost revenues - The company has long-term contracts ranging between three and five years with its customers, ensuring optimal capacity utilisation and sustained revenue growth. Its client base includes TML, RN and GM, among others, with whom it enjoys long-term associations. The addition of Maruti Suzuki India Limited (MSIL) to the customer mix in FY2020 will boost its revenues in the near to medium term.

Strong financial profile with low gearing and healthy coverage indicators; funds infused by parent strengthen capital structure - The company's capital structure remains strong on the back of minimal dependence on outside funding combined with adequate accruals, which are further supported by compulsory convertible debentures (CCD) and external commercial borrowing (ECB) from the parent. The funds infused by the parent company resulted in a significant drop in the external debt levels during the last five fiscals. In FY2019, EIPL's interest coverage and debt protection metrics remained strong, with interest coverage of 11.13 times and gearing of 0.09 time (in line with low debt levels and adequate accruals).

High entry barriers owing to speciality products and technology; exclusive supplier for catered OEMs - EIPL receives strong research and development (R&D) and technical support from its parent, leading to better performance, quality products and healthy share in most of the products supplied to different plants of the OEMs. Its long track record, high speciality products, and technological and contractual agreements with clients act as high entry barriers in the industry.

Credit challenges

Gradual decline in operating margins amidst slowdown in automobile industry - The automobile industry registered a substantial degrowth in sales across PVs in April 2019, with subdued buyer interest and poor market sentiments. High fuel prices, low fund availability and escalating acquisition costs have led to disinterest in most rural places, while urban customers are finding more convenience in shared mobility, which is increasingly replacing new car ownership in the country's key Tier 1 cities. Evidently, EIPL's operating income registered a decline of ~3% in FY2019 to Rs. 113.99 crore.

EIPL is exposed to the inherent cyclicality in the automobile industry, with decline in production and sales volume of the PV segment in FY2019. In Q2 FY2019, the growth muted to 4.3% on a YoY basis, impacted by flooding in a few regions, high base in Q2 FY2018, delayed festive season and bearish consumer sentiments, amidst rising fuel prices and interest rates. In H2 FY2019, the production declined by 6.2% on a YoY basis with increase in on-road prices (due to higher insurance costs) also being a sales deterrent. The decline in production continued in April 2019 as well.

Since the last two fiscals, EIPL's cost structure has worsened with an increase in prices of raw materials, which are predominantly crude oil derivatives, leading to a decline in operating margins to 7.94% in FY2019 from 17.11% in FY2017. In line with the drop in operating margins, the net margins fell to 3.67% in FY2019 from 10.24% in FY2017.

High customer and geographical concentration risks; limited presence in aftermarket segment - EIPL has high customer and geographical concentration risks, with the top five customers accounting for more than 80% of its total revenues in FY2018 and H1 FY2019. RN and TML comprised over 50% of the total revenue share in FY2018 and H1 FY2019. The company has a limited presence in the aftermarket segment. Addition of new customers, like MSIL, is expected to reduce the customer concentration risk to some extent.

Profitability susceptible to fluctuations in raw material prices; sizeable exposure to currency movement with ~40% of raw materials imported - The total import content has increased over the years due to addition of new clients who have insisted on imported content and are more demanding than domestic clients in terms of product quality and performance. The company's profitability is exposed to fluctuations in raw materials prices, which constitute ~65-80% of the overall cost structure. Raw material prices are linked to crude oil prices, which are susceptible to volatility and affected by both global and domestic factors (including economic growth, OPEC production decisions, demand-supply gap, oil future contracts, global oil inventories, etc). Due to these factors, the company has low bargaining power in terms of raw material pricing. The company's products are indirect materials for its clients and hence, there is no structured contract for raw material price escalation and benefit pass on; however, in the past, with mutual negotiations with customers, the company received/passed on benefits of raw material price rise/fall. With continuing increase in raw material prices as a percentage of output, the dip in operating margins remained.

Substantial dividend outflows in last two fiscals draining retained cash flows - The company paid dividends of Rs. 17.69 crore and Rs. 10.02 crore (including tax on dividend), translating to more than 100% of net profits in FY2018 and FY2019, respectively. The extent of dividend declared is determined by the holding company, and has constrained its accretions to net worth and accumulation of liquid reserves (cash and cash equivalents).

Liquidity position

The company has no major capex plans in the near term, and has a repayment obligation of ~Rs. 2 crore in FY2020. It generated sufficient cash flows in the past to meet its working capital requirements, as evident from the low average working capital utilisation of 3% during the 12-month period ended May 2019. However, the retained cash flows remained negative during the last two years on account of high dividend payout ratio. The financing requirement was met through previous year's cash and bank balances. The company's liquidity position remains modest, with an unencumbered cash and bank balance amounting to Rs. 4.77 crore in FY2019 and an undrawn line of credit of Rs. 13.00 crore as of May 2019. However, the cash accruals will remain sensitive to the level of dividend pay-outs.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Manufacturers
Parent/Group Support	Parent Group – EMS Group
Consolidation/Standalone	The ratings are based on the standalone financial statements of the issuer.

About the company

EIPL operates in the niche segment of manufacturing and supplying bonding, coating, sealing and damping adhesives to the automobile industry. It is a wholly-owned subsidiary of the EMS Group, Switzerland. The company has a manufacturing unit at MIDC Ranjangaon in the Pune district of Maharashtra.

In FY2019, the company reported a net profit of Rs. 4.18 crore on an operating income of Rs. 113.99 crore (as per provisional numbers), compared to a net profit of Rs. 9.67 crore on an operating income of Rs. 117.49 crore in the previous year.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	112.92	117.49
PAT (Rs. crore)	11.57	9.67
OPBDIT/ OI (%)	17.11%	13.72%
RoCE (%)	38.56%	31.89%
Total Debt/ TNW (times)	0.13	0.12
Total Debt/ OPBDIT (times)	0.33	0.28
Interest Coverage (times)	24.26	15.67

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Instrument	Current Rating in FY2020			Chronology of Rating History for the past 3 years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating Jul 2019	Date & Rating in FY2019 Apr 2018	Date & Rating in FY2017 Oct 2016	Date & Rating in FY2016 Apr 2015
1 Fund-based/ Non-fund Based	Long Term/ Short Term	16.00	-	[ICRA]BBB (Stable)/ [ICRA]A3+	[ICRA]BBB+ (Stable)/ [ICRA]A2; ISSUER NOT COOPERATING	[ICRA]BBB+ (Stable)/ [ICRA]A2	[ICRA]BBB+ (Stable)/ [ICRA]A2
2 Unallocated Facility	Long Term/ Short Term	1.00	-	[ICRA]BBB (Stable)/ [ICRA]A3+	-	-	-

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating
NA	Cash Credit/ Letter of Credit	-	-	-	16.00	[ICRA]BBB(Stable)/ [ICRA]A3+
NA	Unallocated Limits	-	-	-	1.00	[ICRA]BBB(Stable)/ [ICRA]A3+

Source: EIPL

Annexure-2: List of entities considered for consolidated analysis: Not applicable

ANALYST CONTACTS

Mr. K. Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Mr. Suprio Banerjee
+91 22 6114 3443
suprio.b@icraindia.com

Ms. Rupa Pandey
+91 22 6114 3456
rupa.pandey@icraindia.com

Ms. Aprajita Singh
+91 22 6169 3364
aprajita.singh@icraindia.com

RELATIONSHIP CONTACT

Mr. Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

© Copyright, 2019 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents