

January 27, 2023

Paras Defence & Space Technologies Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term cash credit	49.00	39.00	[ICRA]A- (Stable); Reaffirmed
Long term – Term loan	22.00	0.00	-
Long term/Short term – Bank guarantee & LC	34.00	71.0	[ICRA]A- (Stable) /[ICRA]A2+; Reaffirmed
Short term – Invoice discounting	5.00	0.0	-
Total	110.00	110.00	

*Instrument details are provided in Annexure I

Rationale

The reaffirmation of the ratings of Paras Defence & Space Technologies Limited (PDSTL) continues to favourably factor in the healthy order book position as on December 31, 2022, which translates to a comfortable Order Book/Operating Income (OB/OI) ratio of 3.3 times the operating income of FY2022, thereby providing medium-term revenue visibility. The ratings continue to favourably consider the company's comfortable capital structure with a gearing of 0.1 times and TOL/TNW of 0.3 times as on September 30, 2022, supported by an equity infusion of Rs. 162.3 crore in the last two years. The interest coverage stood at 6.4 times and TD/OPBDITA at 0.6 times in FY2022, representing a significant improvement compared to FY2021 due to the prepayment of term debt and limited dependence on external borrowings to fund its working capital.

The ratings also 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 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 with NWC/OI of 107.4% and 126.7% in FY2022 and H1 FY2023, respectively, due to the high inventory holding period and long receivables cycle. The inventory levels are high because of the additional stocking of critical raw materials to avoid any disruption in the delivery schedules in the event of future lockdowns (if any). Going forward, the company's ability to alleviate its working capital intensity, while scaling up its revenues, will be a key rating monitorable. The ratings are also constrained by PDSTL's moderate scale of operations. While the scale of operations is expected to improve over the medium term, the company's ability to judiciously manage its working capital remains crucial from a credit perspective, given the stretched cash conversion cycle.

Client concentration risk remains high with the top three clients contributing 74% to the total order book as on March 31, 2022. 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. The client profile mostly comprises government organisations with sustained repeat orders, largely mitigating the counterparty credit risk.

The Stable outlook reflects ICRA's opinion that PDSTL will continue to benefit from the healthy order book position, which provides medium-term revenue visibility, the comfortable financial risk profile and the extensive experience of the management team.

Key rating drivers and their description

Credit strengths

Healthy order book provides medium-term revenue visibility – The company's fresh order inflows over the past four fiscals have remained adequate, with orders worth Rs. 268 crore added in FY2022. The pending order book as on December 31, 2022 (OB/OI ratio of 3.3 times the operating income of FY2022) provides medium-term revenue visibility.

Comfortable capital structure and healthy coverage indicators – The company's capital structure remains comfortable with a gearing of 0.1 times and TOL/TNW of 0.3 times as on September 30, 2022, supported by the equity infusion of Rs. 162.3 crore in the last two years. The interest coverage stood at 6.4 times and TD/OPBDITA at 0.6 times in FY2022, representing a significant improvement compared to FY2021 due to the prepayment of term debt and limited dependence on external borrowings to fund its working capital. Going forward, ICRA expects the coverage indicators to remain comfortable, benefitting from the scale-up of the 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. PDSTL's long presence in the defence and space sector has helped it 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

High working capital intensity due to elongated receivables cycle – The business is working capital intensive with NWC/OI of 107.4% and 126.7% in FY2022 and H1 FY2023, respectively, owing to the high inventory holding period and long receivables cycle. The company bills more than 50% of its sales in the fourth quarter of every fiscal, resulting in a high working capital cycle towards year-end. As PDSTL manufactures various kinds of products with a long cycle, the inventory levels remain high. Further, the sharp increase in the inventory levels, as on September 30, 2022, was attributable to the additional stocking of critical raw materials. This was done to avoid any disruption in the delivery schedules in the event of future lockdowns (if any) as the company partly imports raw materials from South Korea and India's neighbouring countries. PDSTL has been partly managing its working capital cycle by stretching its trade payables by more than three months as it has a longstanding relationship with most of its suppliers. Going forward, the company's ability to alleviate its working capital intensity while scaling up its revenues will be a key rating monitorable.

Moderate scale of operations – Though the company reported a robust YoY revenue growth of 27% and 29% in FY2022 and H1 FY2023, respectively, supported by the healthy order book and the timely execution of the same, the scale remains moderate. Given the favourable defence offset policy amid the 'Make in India' thrust, PDSTL has been mainly catering to domestic demand (~90% of OI contributed by domestic orders). ICRA expects the company to register a robust revenue growth in FY2023, supported by the healthy order book status.

High customer concentration risk, though largely mitigated by reputed customer base and repeat orders – The company faces client concentration risk with the top three clients contributing 74% to the total order book as on March 31, 2022 and the top five clients accounting for 58% of the revenue in FY2022. However, the Government's thrust on 'Make in India' in the defence sector augurs well for PDSTL. The client profile mostly comprises government organisations with repeat orders received over the years, largely mitigating the counterparty credit risk. The company mainly supplies products to Government entities, although some private companies also form a part of its customer mix. It also exports to companies based in Israel, Singapore and USA. A major part of PDSTL's clientele comprises 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 longstanding relationships with most of its clientele.

Liquidity position: Adequate

PDSTL has adequate liquidity, with an unencumbered cash and bank balance of Rs. 36.2 crore as of September 30, 2022. Further, it had no long-term debt as on September 30, 2022. The average working capital utilisation during the 12-month period ended November 2022 remained at 55% and the non-fund based utilisation was 59%.

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 continued elevated working capital cycle impacts the company’s liquidity.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Consolidation and Rating Approach
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, Paras Defence & Space Technologies Limited (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 Ambarnath (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	FY2021	FY2022	H1 FY2023*
Operating income	144.3	183.5	96.5
PAT	15.8	27.1	15.1
OPBDIT/OI	31.4%	29.1%	26.3%
PAT/OI	10.9%	14.8%	15.6%
Total outside liabilities/Tangible net worth (times)	0.9	0.2	0.3
Total debt/OPBDIT (times)	2.3	0.6	0.7
Interest coverage (times)	3.5	6.4	31.3

Source: Company, ICRA Research

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

* Provisional

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

S. No.	Instrument	Current Rating (FY2023)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2022 (Rs. crore)	Date & Rating	Date & Rating in FY2022		Date & Rating in FY2021	Date & Rating in FY2020
					Jan 27, 2023	Oct 27, 2021	Sept 30, 2021	-	-
1	Cash credit	Long term	39.0	29.2	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-	-
2	Term loan	Long term	0.0	0.0	-	[ICRA]A- (Stable)	-	-	-
3	Bank guarantee & LC	Long term/ Short term	71.0	23.8	[ICRA]A- (Stable) / [ICRA]A2+	[ICRA]A- (Stable) / [ICRA]A2+	-	-	-
4	Invoice discounting	Short term	0.0	0.0	-	[ICRA]A2+	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term – Cash credit	Simple
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	-	-	-	39.00	[ICRA]A- (Stable)
NA	BG & LC	-	-	-	71.00	[ICRA]A- (Stable)/[ICRA]A2+

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	Consolidated Approach
Paras Aerospace Pvt Ltd	60%	Full Consolidation
Paras Green Optics Pvt Ltd	100%	Full Consolidation
Paras Anti- Drone Technologies Private Limited	55%	Full Consolidation
OPEL Technologies PTE Ltd	100%	Full Consolidation
Krasny Paras Defence Technologies Private Limited	47.50%	Equity Method

Source: Company

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