

August 12, 2024

SKH Marelli Exhaust Systems Private Limited: [ICRA]BBB(Stable)/[ICRA]A3+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long-term - Fund-based – Term loan	13.28	[ICRA]BBB(Stable); assigned
Short-term – Fund based / Working capital facilities	105.00	[ICRA]A3+; assigned
Short-term – Non-fund-based	6.09	[ICRA]A3+; assigned
Total	124.37	

*Instrument details are provided in Annexure-I

Rationale

The ratings assigned factor in the strong business position of SKH Marelli Exhaust Systems Private Limited (SKH Marelli/ the company) in the exhaust manufacturing segment for Maruti Suzuki India Limited (MSIL), the market leader in the passenger vehicle (PV) industry. The ratings also factor in favourably the parentage of the entity, with it being a joint venture between Marelli SPA, Italy and SKH Metals Limited (a Krishna Group company). The parentage of Marelli SPA provides the company access to product development capabilities, which has aided the company in maintaining a strong share of business in supplies to MSIL; the presence of Krishna Group, a leading auto component supplier to various OEMs aids its manufacturing and marketing prospects.

The revenues of SKH Marelli have improved significantly, at a CAGR of 18% over the FY2017 to FY2024, aided by healthy demand from automotive industry. In addition, the company has gained significant business from its major customer - Maruti Suzuki India Limited (MSIL) over the past two years, leading to improvement in its share of business (SOB) with the OEM and aided in substantial revenue growth.

The ratings remain constrained by the company's dependence upon a single customer - MSIL, which constitutes ~95% of its revenues; however, the risk is mitigated to an extent by leadership position of MSIL in the passenger car industry and strong share of business of SKH Marelli for certain models of the original equipment manufacturers (OEM). Although, the company faces risk from a prospective transition to electric vehicles (EV), which would eliminate the need for exhaust systems (the sole product category of the company), ICRA notes that the share from EVs in overall PV industry is expected to remain at moderate levels over the medium term; additionally an expectation of sustained demand growth in the PV industry is expected to support the company's growth prospects over the medium term. The company remains exposed to raw material fluctuation risks, as the major raw material (precious metal – Monolith) price can materially impact its profitability. Monolith contributes to about 90-95% of overall cost and thus any fluctuation in the price can have material impact on its overall profitability. ICRA notes that the company earns a handling charge for Monolith handled, which compensates the company for the carrying cost of holding inventory of the metal.

The Stable outlook on the rating reflects ICRA's expectation that company will continue to maintain a steady scale of operations, aided by a healthy demand in the passenger vehicle market and MSIL's market leadership position. Despite the company's thin profit margins, the credit metrics are likely to remain at healthy levels, in absence of material capex plans.

Key rating drivers and their description

Credit strengths

Strong business position in the exhaust systems segment with MSIL – SKH Marelli is a supplier of exhaust systems for Maruti Suzuki India Limited (MSIL). The company has substantially improved its share of business (SOB) for exhaust systems with MSIL over the years and commands a SOB of ~40-45% currently. Coupled with healthy SOB, MSIL's dominant position in passenger vehicle industry with a healthy market share of ~41% provides ample growth opportunity for the company. Within the backdrop of MSIL's healthy expansion plans and the company's healthy SOB with MSIL, SKH Marelli's scale of operations is expected to grow at a healthy pace.

Access to technical support from parent entity Marelli supports product development capabilities – SKH Marelli enjoys technological support from its JV partner, Marelli S.p.A, Italy, a leading Italian auto component supplier with a diversified presence in segments such as electric powertrain, thermal comfort and solutions, exhausts systems, automotive lighting and sensors and motorsport technology, etc., to various global OEMs. The technological support from Marelli is likely to help SKH Marelli adapt to MSIL's changing technological requirements in terms of research and development and support its business prospects going forward.

Comfortable debt coverage metrics – Led by limited dependence on debt, the coverage indicators for the company have remained healthy for the past few years as indicated by interest cover of 8.2 times and total debt/OPBITDA of 1.5 times for FY2024 (provisional financials). The company availed term loans in FY2023 and had further draw down debt in FY2024 for funding the capital expenditure towards procuring plant and machinery; the same are expected to be repaid by FY2027. An expectation of steady year on year accruals are expected to continue to support the company in maintaining healthy debt coverage metrics going forward.

Credit challenges

Low business diversification; however, MSIL's market leadership mitigates risk to an extent – SKH Marelli's business emanates from a single product segment (exhaust systems) and is majorly derived from a single customer, MSIL. Thus, the company's performance and prospects are closely linked to that of MSIL. Although this results in high client concentration risk, the same is mitigated to a large extent by MSIL's market leadership in the passenger vehicle (PV) segment and SKH Marelli's strong SOB with MSIL. ICRA expects the company's concentration on MSIL to remain high over the medium term, in the absence of any material customer diversification plans.

Profit margins vulnerable to volatility in raw material prices – The company's operating margins are susceptible to fluctuations in the prices of key raw material — a precious metal named Monolith, etc which comprises about 90% of overall cost manufacturing expenses. However, SKH Marelli has demonstrated its ability to largely pass on the increase in raw material costs, which mitigates the risk to an extent. Additionally, ICRA notes that the company earns a handling charge for Monolith handled, which compensates the company for the carrying cost of holding inventory of the metal.

Susceptible to demand slowdown in domestic automotive market and transition to electric vehicles (EVs) – Given its dependence on the automotive segment, SKH Marelli's revenues and earnings are susceptible to the cyclicity in automotive demand from both the domestic and export markets. Going forward, its earnings shall remain exposed to any sharp slowdown in automotive demand apart from major volatility in raw material prices and forex rates. Since SKH Marelli derives its revenues from only exhaust systems, it faces a potential threat from the development of alternative vehicle architectures like EVs, which do not use exhaust systems. However, the share from EVs is expected to remain modest in the PV segment in the medium term and with MSIL's expansion plans towards developing additional capacities through internal combustion engines (ICE), the requirement for exhaust systems is expected to remain intact.

Liquidity position: Adequate

The company's liquidity is expected to remain **adequate**, with buffer of ~Rs.80 crore in the working capital limits as of June 2024. The company maintains minimal free cash of about Rs.1-2 crore at any point of time. Additionally, the company at certain points of time also has funds of ~Rs. 25-30 crore in an escrow account from MSIL; MSIL generally clears invoices on Fridays and the payment to vendors are made on proceeding Mondays. The company has marginal capex plans and debt obligations (~Rs. 4.2 crore in FY2025), which are expected to be comfortably met through the expected cash accruals.

Rating sensitivities

Positive factors – The ratings can be upgraded if there is sustained improvement in earnings leading to improvement in capital structure and coverage indicators.

Negative factors – The ratings would face downward pressure if there is a material decline in profitability leading to moderation in coverage indicators. Any material debt funded capex materially impacting the capital structure would also exert negative pressure on the rating. Specific credit metric that could lead to downgrade includes Interest cover of less than 3.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Auto components
Parent/Group support	Not Applicable
Consolidation/Standalone	Standalone

About the company

SKH Marelli Exhaust Systems Private Limited, incorporated in 2008, is a 50:50 joint venture between Marelli SPA, Italy and SKH Metals Limited. SKH Metals is a part of Krishna Group, which is headed by Mr. Ashok Kapur and his son Mr. Sunandan Kapur. The group is one of the leading suppliers to OEMs for seat sets, door trims, mirror, roof liners, fuel tanks, exhaust systems and suspensions. The company is engaged in the manufacturing of exhaust systems, which primarily comprise of two-parts, hot-end (also known as catalytic converter), which had an installed capacity of 1.2 million units and cold-end (consists of silencer/muffler and tail pipe) with an installed capacity of 0.7 million units. The company derives majority of its revenue from sales to Maruti Suzuki India Limited (MSIL).

Key financial indicators

Standalone	FY2023	FY2024*
Operating income	1,479.2	1,361.1
PAT	10.7	18.3
OPBDIT/OI	1.9%	3.0%
PAT/OI	0.7%	1.3%
Total outside liabilities/Tangible net worth (times)	8.0	5.0
Total debt/OPBDIT (times)	2.1	1.5
Interest coverage (times)	15.5	8.2

Source: Company, ICRA Research; *Provisional numbers; 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

Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years					
	Type	Amount rated (Rs. crore)	FY2025		FY2024		FY2023		FY2022	
			Date	Rating	Date	Rating	Date	Rating	Date	Rating
1 Term loan	Long-term	13.28	Aug 12, 2024	[ICRA]BBB (Stable)	-	-	-	-	-	-
2 Working capital	Short-term	105.00	Aug 12, 2024	[ICRA]A3+	-	-	-	-	-	-
3 Non fund based	Short-term	6.09	Aug 12, 2024	[ICRA]A3+	-	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based – Term Loan	Simple
Short -term – Fund-based - Working capital facilities	Simple
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 I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan	FY2023	NA	FY2027	13.28	[ICRA]BBB(Stable)
NA	Working capital facilities	NA	NA	NA	105.00	[ICRA]A3+
NA	Bank guarantee	NA	NA	NA	6.09	[ICRA]A3+

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

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545328
shamsherd@icraindia.com

Srikumar Krishnamurthy
+91 44 45964318
ksrikumar@icraindia.com

Rohan Kanwar Gupta
+91 124 4545808
rohan.kanwar@icraindia.com

Akshay Dangi
+91 124 4545396
akshay.dangi@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@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

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For more information, visit www.icra.in

ICRA Limited



Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001

Tel: +91 11 23357940-45



Branches



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