

Klassic Wheels Limited

June 14, 2018

Summary of rated instruments

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based – Term Loan	7.63	6.52	[ICRA]BBB+ (Stable); Upgraded from [ICRA]BBB(Stable)
Fund-based – Cash Credit	10.30	10.30	[ICRA]BBB+ (Stable); Upgraded from [ICRA]BBB(Stable)
Non-fund based – Letter of Credit	3.00	3.00	[ICRA]A2; Upgraded from [ICRA]A3+
Unallocated	-	6.11	[ICRA]BBB+(Stable)/[ICRA]A2; Upgraded from [ICRA]BBB (Stable)/[ICRA]A3+
Fund-based – Proposed Loan	5.00	-	-
Total	25.93	25.93	

Rating action

ICRA has upgraded the long-term rating to [ICRA]BBB+ (pronounced ICRA triple B plus) from [ICRA]BBB (pronounced as ICRA triple B) for the Rs. 16.82 crore¹ fund-based limits of Klassic Wheels Limited (KWL or the company)². ICRA has also upgraded the short-term rating to [ICRA]A2 (pronounced ICRA A two) from [ICRA]A3+ (pronounced ICRA A three plus) for the Rs. 3.00-crore non-fund based facility of KWL. ICRA has also upgraded the long-term and short-term rating to [ICRA]BBB+(Stable)/[ICRA]A2 to the unallocated facility of Rs. 6.11 crore. The outlook on the long-term rating is Stable.

Rationale

The rating upgrade takes into account the healthy growth in topline as well as expansion in margins, with process improvement measures, as well as modernisation of plant and machinery undertaken. Along with price variation agreements with its key customers, the same led to improvement in profitability metrics in FY2017 and 9M FY2018. The rating upgrade also factors in KWL's reputed client base and dominant market share in the two (2W) and three-wheeler (3W) segments and the company's proposed diversification into hybrid and alloy wheels, which will help cater to passenger cars in the four-wheeler (4W) segment, going forward. The rating continues to factor in the healthy financial profile of the company marked by conservative capital structure despite regular capital expenditure, improving asset turnover ratio, strengthening coverage indicators following lower reliance on external debt and healthy cash flow position over the period under study. The ratings continue to take comfort from the longstanding promoter experience of more than three decades in the industry, along with the presence of group companies in the auto ancillary business.

The ratings, however, remain constrained by high client concentration risk because the majority share of revenues (~67%) is generated by a single customer, Honda Motorcycle and Scooter India (HMSI); although the market leadership position of HMSI in the scooter segment mitigates this risk to some extent. The company also faces stiff competition from well

¹ 100 lakh = 1 crore = 10 million

² For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

entrenched players in the industry as well as substitutes to steel wheel rims, considering the increased usage of alloy wheels in lieu of steel wheel rims in the auto industry.

Going forward, the company's timely and successful transition to align with industry developments like greater penetration of alloy wheels, along with diversification in product as well as customer portfolio, with increase in market share in the scooter segment, will remain a key monitorable.

Outlook: Stable

ICRA expects KWL to continue to benefit from its extensive experience in wheel rim manufacturing and its established relations with reputed original equipment manufacturers (OEMs) in the 2W and 3W segments. The outlook may be revised to Positive if substantial revenue growth is reported with sustainable improvement in profitability and better working capital management strengthens the financial risk profile. The outlook may be revised to Negative if profitability weakens, or if any stretch in the working capital cycle weakens liquidity, or if any large capex without commensurate returns leads to cash flow mismatches.

Key rating drivers

Credit strengths

Established promoter track record of more than three decades in the industry; group companies also involved in the auto ancillary business - The company is promoted by Ahmednagar based -Munot family which is present in auto ancillary business since last two generations. The promoters are technically qualified and have wide industrial experience in the auto ancillary segment. The group companies Sumesh Industries, Kaygee Foam Private Limited and Sushant Industries are also involved in the auto ancillary business mainly in manufacturing.

Reputed client base with majority of revenues generated by HMSI, a market leader in the scooter segment ensuring stable demand; sole supplier status for 2W and 3W models for various OEMs - KWL has depicted a reputed client base over the years which includes OEMs such as HMSI, Yamaha, Suzuki, Mahindra, and Piaggio among others. The company is a single source supplier for automotive OEMs such as Suzuki, Yamaha, Mahindra, Piaggio, Atul Auto and has significant share (at ~66%) as a portion of HMSI's total requirement, which is the market leader in scooter segment, which ensures stable demand prospects. HMSI currently holds ~57% market share in the Indian scooter industry in FY2018. While 2W segment currently generates 87% of the revenues in FY2018, with the addition of Bajaj Auto Limited the share of 3W segment in the sales mix has increased from 7% in to 11%.

Process improvement in the manufacturing process led to expansion in margins in FY2017 and 9M FY2018 - The company has undertaken capex for automation of processes and upgradation of machinery leading to better process flow and manpower reduction. The same has resulted in sustainable reduction in manufacturing overheads, and thus has led to improvement in operating margins from 17.8% in FY2016 to ~20.4% in FY2017 and 9M FY2018. The net margin of the company improved to 9.0% in FY2017 as compared to 6.6% in FY2016 which was in line with the improvement in operating margins and also supported by reduced interest expenses in line with decline in external debt levels and higher non-operating income (primarily interest income).

Conservative capital structure despite regular capital expenditure and strengthening of coverage metrics following reducing reliance on working capital borrowings; healthy cash flows position - KWL's management has been historically conservative which is evidenced from a comfortable capital structure of the company and y-o-y reducing reliance on external debt for funding the working capital requirements. Its gearing stands at 0.57 times as on 31st March, 2017 and 0.32 times as on 31st December, 2017. The interest coverage indicators and debt coverage metrics strengthened given the improvement in profitability with an interest coverage of 10.85 times, total debt to OPBDITA of 0.90 times and net cash

accruals (NCA) to total debt of 71.8% as on March 31, 2017 (6.17 times, 1.27 times, 50.2% respectively as on March 31, 2016). Supported by healthy margins, low working capital intensity, the company has consistently generated positive free cash flows during last four years despite regular capex incurred. ICRA notes that KWL has a planned capex of ~Rs. 20 crore in FY2019 which will lead to capacity addition and will be partly funded through debt and internal accruals. In spite of the same, the capital structure and cash flow position is likely to remain comfortable going forward due to anticipated steady cash accruals and improvement in net worth base.

Favourable outlook for 2W industry provides revenue visibility - In FY2018, production volumes of 2W segment displayed a growth of 16% over the past fiscal supported by strong double-digit growth in domestic and export markets. Domestic sales for the 2W segment grew by 14.8% in FY2018 over the previous fiscal with the growth in scooters standing at 19.9%. In April 2018, production of scooters was higher by 10.1% in comparison to April 2017. Scooter sales are expected to grow at a sharp pace led by the increased disposable incomes amidst positive economic factors coupled with increasing penetration in the rural market and an increase in women participation.

Credit challenges

Moderate scale of operations; business diversification will be key to scale up - KWL has clocked a turnover of Rs. 182 crores in 9M FY2018 (provisional). Currently, the product diversification is low as the company manufactures steel wheel rims for 2W and to a small extent for the 3W segment. In terms of business diversification, sales to aftermarket accounts for less than 15% of total revenues. Going forward, the key to scale up will be to diversify across segments and depict greater customer diversification. ICRA, however, positively factors in the company's capex plan in FY2019 to set up an automated facility in Ahmednagar, Maharashtra to increase the capacity of wheel rims (including steel, alloy and hybrid wheels) and plans to cater to the 4W segment additionally.

Client concentration risk arising from single customer contributing significant portion of revenues - The company derives major share of revenues (at ~66%) in FY2018 from HMSI which introduces client concentration risk and vulnerability of business performance of KWL to the performance and market share of HMSI. Nevertheless, in view of market leader status of HMSI in scooter segment, the risk is mitigated to an extent. In the scooter segment, Honda continues to lead with market share of 64.1% during April 2018.

Threat of substitutes with increased usage of alloy wheels replacing steel rims in the 2W industry, though the same has not picked up much in the scooters segment; product and segment diversification remain crucial - Since KWL predominantly manufactures cost-efficient steel rims, it is susceptible to threat of substitutes with increased usage of better aesthetics, light weight and superior heat conduction alloy wheels in the 2W³ scooter segment. The dip in the market share for Suzuki's Access to 50% has been caused by alloy wheels being used instead of regular steel wheel rims. Nonetheless, the company has witnessed steady and increasing demand for steel rims from HMSI, its key customer; but the shift to alloy or hybrid wheels is imminent. To address the same, KWL is diversifying into manufacturing hybrid wheels in technical collaboration with Grimeca, Italy, with patented technology. These wheels will directly compete with alloy wheels, being similar in appearance and utilisation, but are expected to be cheaper than alloy wheels. While the company has received small orders for the same, the scaling up of orders for the new product and acceptability from existing as well as new customers remain to be seen.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

³ Includes motorcycles, scooters and mopeds

Links to applicable criteria:[Corporate Credit Rating Methodology](#)[Rating Methodology for Auto Component Manufacturers](#)**About the company:**

Incorporated in 1994, Kclassic Wheels Limited has been involved in the manufacturing of steel wheel rims for two and three wheeler vehicles. The company has two manufacturing units at MIDC Ahmednagar, Maharashtra. KWPL supplies its products to reputed automotive OEMs in India, including Honda Motorcycle & Scooters India Private Limited, India Yamaha Motor Private Limited, Suzuki Motorcycle India Private Limited, Piaggio Vehicles Private Limited, Bajaj Auto Limited and Mahindra Two Wheelers Limited. The company is promoted by the Ahmednagar-based, Munot family. The family has been present in the auto ancillary business over the last two generations.

In FY2017, the company reported a net profit of Rs. 13.63 crore on an OI of Rs. 151.45 crore, as compared to a net profit of Rs. 8.66 crore on an OI of Rs. 131.54 crore in the previous year.

Key financial indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	131.54	151.45
PAT (Rs. crore)	8.66	13.63
OPBDIT/ OI (%)	17.76%	20.44%
RoCE (%)	28.63%	36.50%
Total Debt/ TNW (times)	0.84	0.57
Total Debt/ OPBDIT (times)	1.27	0.90
Interest Coverage (times)	6.17	10.85

Status of non-cooperation with previous CRA: Not applicable**Any other information: None**

Rating history for last three years:

Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years		
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating Jun 2018	Date & Rating in FY2018	Date & Rating in FY2017 Jan 2017	Date & Rating in FY2016 Nov 2015
1 Term Loan	Long Term	6.52	6.52	[ICRA]BBB+ (Stable)	-	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)
2 Cash Credit	Long Term	10.30		[ICRA]BBB+ (Stable)	-	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)
3 Letter of Credit	Short Term	3.00		[ICRA]A2	-	[ICRA]A3+	[ICRA]A3+
4 Unallocated	Long Term/ Short Term	6.11		[ICRA]BBB+ (Stable)/ [ICRA]A2	-	-	-

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 and Outlook
NA	Term Loan	FY2014	-	FY2023	6.52	[ICRA]BBB+ (Stable)
NA	Cash Credit	-	-	-	10.30	[ICRA]BBB+ (Stable)
NA	Letter of Credit	-	-	-	3.00	[ICRA]A2
NA	Unallocated	-	-	-	6.11	[ICRA]BBB+ (Stable)/ [ICRA]A2

Source: KWL

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