

February 20, 2020

Kyungshin Industrial Motherson Private Limited: Rating reaffirmed at [ICRA]AA(Stable)/[ICRA]A1+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Limits	15.00	15.00	[ICRA]AA(Stable) reaffirmed
Non-fund Based Limits	5.00	5.00	[ICRA]A1+ reaffirmed
Unallocated	36.74	36.74	[ICRA]AA(Stable) reaffirmed
Total Bank Line Facilities	56.74	56.74	
Commercial Paper	5.00	5.00	[ICRA]A1+ reaffirmed

*Instrument details are provided in Annexure-1

Rationale

The ratings reaffirmation takes into consideration (i) Kyungshin Industrial Motherson Private Limited's (KIML's) established business position as the sole supplier of wiring harness (WH) assemblies to Hyundai Motor India Limited (HMIL), (ii) its strong parentage as a joint venture (JV) between Kyungshin Industrial Corporation Limited (KIC), South Korea, and Motherson Sumi Systems Limited (MSSL, rated [ICRA]AA+(Stable)/[ICRA]A1+), and (iii) its strong financial risk profile.

KIML was set up as a JV between KIC and MSSL to supply WH assemblies to HMIL in India. Over the years, HMIL has established itself as the second largest passenger vehicle (PV) manufacturer in India, with 18% share of the domestic market and 27% of PV exports from India. Despite its business profile being subject to high customer concentration risks and limited product diversity, KIML has benefited from the high acceptance of HMIL's vehicles in the market, the rising trend of electronic content in PVs resulting in higher content per vehicle and the gradual shift in HMIL's product portfolio towards more high-end models such as 'Creta' and 'Verna'.

As a JV between two established players in the supply of WHs, KIML also benefits from the access to their technical and operational support. Additionally, KIC's well-established global relationships with Korean PV manufacturers have also supported KIML's business prospects with Indian subsidiaries of these PV manufacturers. Accordingly, the company has gained business for the supply of WH assemblies to Kia Motors India (Kia), which launched its first model, 'Seltos', in the Indian market in August 2019. KIML is the sole supplier of WH systems for Kia's Seltos as well, and given the favourable response received by the original equipment manufacturer (OEM) in the market, revenue growth prospects through the new business remains healthy. Over the medium term, business from Kia would lead the company's revenue growth as well as diversification, thereby strengthening its business profile.

Despite the healthy business position with both its customers, ICRA notes that KIML has a limited ability to pass on raw material and forex fluctuations to them through price adjustments. Accordingly, its profitability margins have weakened significantly over the past two years because of cost reductions negotiated by the OEM in an environment of rising input costs. Sharp increase in prices of key raw materials, particularly copper, coupled with depreciation in the Indian Rupee against the Dollar, and steep cost reductions negotiated with HMIL, resulted in

close to 900 bps contraction in operating profit margins (OPM) since FY2017. Nevertheless, the financial risk profile continues to remain strong, characterised by nil debt, healthy cash flow generation and comfortable liquidity. Additionally, return on capital employed continues to remain healthy, in the range of 25-30%. Credit metrics continue to remain strong, given the limited reliance on external borrowings, as even the major requirement of capital expenditure (capex) for Kia Motors was funded by internal cash flow generation and existing cash balances.

ICRA would, however, continue to monitor the company's ability to sustain and improve its profitability metrics and return indicators going forward. Given that it does not have a strong pass-through clause with its customers, which subjects it to adverse fluctuations in currency rates and raw material prices, its ability to protect its margins through value-added value engineering (VAVE) and localisation initiatives remain critical. Additionally, given the high import content in its raw material sourcing mix (72.6% in FY2019), its ability to protect margins from adverse forex fluctuations hinges on appropriate hedging policies.

The Stable outlook on the long-term rating reflects ICRA's expectation that KIML would continue to maintain strong credit metrics going forward as well, despite the contraction in margins over the past two years. Its business prospects over the medium term would be supported by expected scale up in its Kia business, while the financial risk profile would remain supported by a healthy balance sheet and cash generation.

Key rating drivers and their description

Credit strengths

Strong parentage of KIC and MSSL ensures access to technical and operational support of both JV partners – As a JV between MSSL and KIC, Korea, which are both well-established players in the supply of automotive WH assemblies, KIML benefits from the access to their technical and operational support. Furthermore, the global relationships enjoyed by KIC with Korean automakers like Hyundai and Kia augurs well for business prospects with Indian subsidiaries of the OEMs.

Established relationship with HMIL, the second largest PV manufacturer in India, as sole supplier of WH assemblies – As the sole supplier of WH assemblies to HMIL, the second largest PV OEM in India with 18% share of the domestic market and 27% of PV exports from India, KIML's business prospects remain healthy. The OEM has also regularly engaged in launching new models and facelifts to stay relevant in the market and maintain its share of the growing pie.

New business gained from Kia augurs well for strengthening business prospects over medium term – During the current fiscal, KIML began supplying WH assemblies to its second customer, Kia, who launched its Seltos model in India in August 2019. KIML's sole supplier status for WH assemblies with Kia, and favourable response received in the market for the model so far, augur well for KIML's revenue growth prospects over the medium term, as well as overall strengthening of KIML's business profile through diversification of revenue streams.

Strong financial risk profile characterised by a robust balance sheet with nil debt and sizeable cash balances – Despite weakening in its profitability over the past couple of years, KIML continues to enjoy a strong financial risk profile, characterised by nil dependence on external borrowings and healthy cash balances. The capex

requirements for the new Kia business were funded from existing cash balances and internal cash flow generation, resulting in minimal dependence on external borrowings.

Credit challenges

Significant weakening in profitability metrics over past two years due to limited ability to pass on cost pressures

– KIML’s profitability metrics weakened sharply over the past two fiscals, primarily because of cost reductions passed on to the customer, in an environment of rising input costs. While copper prices had increased since FY2017, and Rupee depreciation additionally increased import costs, the company had limited ability to pass on the same to its customer. Accordingly, OPM weakened to 6.6% in FY2019 from 15.4% in FY2017.

Exposed to customer and product concentration risks with 100% of revenues driven by WH supplies to HMIL; however, new business from Kia should reduce dependence on HMIL over the medium term

- The company’s business profile is characterised by concentration risks as a single-customer, single-product company. As per the JV agreement between KIC and MSSL, KIML is restricted from competing with MSSL in supplying to OEMs, wherein the latter has a presence. This limits KIML’s opportunity for reducing its customer concentration. However, given the new business from Kia, which began in the current fiscal, its dependence on HMIL should gradually reduce over the medium term.

Susceptible to cyclicity in the Indian PV market; revenue and earnings growth in current fiscal to be impacted by ongoing slowdown

- With the domestic automotive industry undergoing a period of sharp slowdown, KIML’s revenues and volumes during the current fiscal from its key customer, HMIL, have been lower than expected. Despite this, however, KIML has outperformed the market average with a 14% revenue growth during H1 FY2020, primarily supported by incremental supplies to Kia, which has helped it buck the slowdown trend.

Exposed to foreign exchange fluctuation risks as most of its raw material is imported; any sharp fluctuation in currency movement could impact KIML’s profitability indicators

- The company imports a major proportion of its raw material requirement from its parent company in Korea, resulting in significant import content (72.6% in FY2019) and vulnerability of earnings to adverse forex movements. During FY2019 too, depreciation of the Rupee against the Dollar had a moderating impact on the profitability of the company, which was significant at Rs. 28.7 crore.

Liquidity position: Strong

KIML’s liquidity position is **strong**, supported by healthy cash flow generation from operations of around Rs. 70 crore and adequate buffer in unutilised working capital facilities (Rs. 15 crore of sanctioned limits have been largely unutilised over the years; drawing power of more than Rs. 100 crore). The capex requirements at the greenfield facility in Andhra Pradesh, while sizeable at Rs. 180-200 crore, are expected to be funded by available cash balances (Rs. 151 crore as on March 31, 2019), cash generated from operations, and available credit lines. Additionally, financial flexibility as part of the larger Motherson Group offers comfort regarding its ability to raise funds in a timely manner, if required.

Rating sensitivities

Positive triggers: Given the expectation of gradual ramp up in production at the recently set up facility and its impact on credit metrics, a rating upgrade is unlikely in the near term. Nonetheless, material strengthening of business profile supported by diversification of the customer base, segment and product mixes would be critical for a positive rating movement.

Negative triggers: Downward pressure on the ratings could arise in case of further weakening in profitability or due to significant debt-funded capex, resulting in moderation of ROCE below 20% or TD/OPBITDA above 1.5x on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Impact of Parent or Group Support on an Issuer's Credit Rating Rating Methodology for Auto Component Manufacturers
Parent/Group Support	Parent/Group Company: Motherson Sumi Systems Limited (rated [ICRA]AA+(Stable)/A1+) The ratings are based on the implicit support from its parent company
Consolidation/Standalone	The ratings are based on the standalone financial statements of the issuer

About the company

Incorporated in October 1997, KIML is a 50:50 joint venture between Kyungshin Industrial Corporation Limited, South Korea (KIC), and Motherson Sumi Systems Limited, India (MSSL). The company is the key supplier of wiring harness systems to HMIL in India. Being a global supplier of wiring harness assemblies to Hyundai, KIC followed Hyundai Motor Company (HMC) into India as per the request of the OEM for WH supplies. KIC and MSSL entered into a JV agreement in July 1997, as per which KIML could supply WH to HMIL and any other OEM on mutual agreement between the JV partners. Although the agreement does not obviate KIML from venturing into other OEMs, the opportunities to diversify have been limited, given MSSL's presence as a WH supplier with almost all other major OEMs in India. However, the company has received business from Kia Motors in FY2020, following their entry into the Indian market, as KIC is a supplier of wiring harness components to Kia Motors globally.

In addition to the JV agreement, the JV partners also entered into a technical and licensing agreement in October 1997, so as to import technical know-how from the Korean parent. As part of the agreement, KIML pays royalty to KIC on an annual basis. The company also receives support from the foreign parent in terms of common sourcing of components; accordingly, KIML imports most of its raw material from its parent, KIC, Korea. In addition to royalty payments to KIC, KIML also pays dividends on a regular basis to both its JV partners. In FY2019, the total dividend paid by the company stood at Rs. 41.5 crore.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	1,258.0	1,382.8
PAT (Rs. crore)	84.6	69.2
OPBDIT/OI (%)	9.1%	6.6%
RoCE (%)	37.2%	28.7%
Total Outside Liabilities/Tangible Net Worth (times)	0.5	0.6
Total Debt/OPBDIT (times)	0.0	0.0
Interest Coverage (times)	149.2	214.7
DSCR	120.7	179.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding*	Rating	FY2019	FY2018	FY2017
					20-Feb-2020	25-Jan-2019	15-Dec-2017	10-Jan-2017
1	Fund Based Limits	Long Term	15.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Stable)
2	Non-fund Based Limits	Short Term	5.00	NA	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Unallocated	Long Term	36.74	NA	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Stable)
4	Commercial Paper	Short Term	5.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Amount in Rs. crore

*As on March 31, 2019

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund Based Limits	NA	NA	NA	15.00	[ICRA]AA(Stable)
NA	Non-fund Based Limits	NA	NA	NA	5.00	[ICRA]A1+
NA	Unallocated	NA	NA	NA	36.74	[ICRA]AA(Stable)
NA	Commercial Paper	NA	NA	7-365 days	5.00	[ICRA]A1+

Source: Kyungshin Industrial Motherson Private Limited

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

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