

August 16, 2021

Indotech Transformers Limited: Ratings reaffirmed; outlook revised to Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based	0.00	11.00	[ICRA]BB (Stable); Reaffirmed and Outlook revised to Stable from Negative
Short-term Non-fund based	74.00	71.79	[ICRA]A4; Reaffirmed
Short-term Unallocated	12.00	9.71	[ICRA]A4; Reaffirmed
Long term Unallocated	6.50	0.00	-
Issuer Rating	-	-	[ICRA]BB (Stable); Reaffirmed and Outlook revised to Stable from Negative
Total	92.50	92.50	

*Instrument details are provided in Annexure-1

Rationale

The revision in rating outlook assigned to Indotech Transformers Limited (ITL) takes into account the company's rebound in financial performance in FY2021. Despite the operational challenges faced by the company in Q1FY2021 and Q2FY2021, the company was able to generate an operating income of Rs. 206.0 crore in FY2021 as against Rs. 205.3 crore in FY2020. Further, the operating margin significantly improved and stood at 5.6% in FY2021 as against 1.0% in FY2020. This is on account of the increased contribution of higher load transforms in the overall sales mix, wherein margins are higher. Furthermore, the company's order book position remains healthy (Rs. 268.0 crore as of March 2021, which is 1.3 times the gross operating income reported in FY2021), thereby providing adequate revenue visibility in the medium term. ICRA also positively takes note of the company's comfortable capital structure, backed by healthy net worth position. Further, the ratings derive comfort from the extensive experience of the new promoter namely Shirdi Sai Electricals Limited (SSEL) and ITL's proven operational track record in the transformers industry spanning nearly three decades. The ratings positively factor in SSEL's established position, with significant scale of operations in the transformer industry, which is expected to provide operational synergies to ITL and lend economies of scale (through joint sourcing, joint lead generation and reduction in manufacturing cost). ICRA expects ITL to derive long-term benefit required for scaling up the operations and improving the gross margin.

However, the ratings are constrained by its linkages with its parent company (SSEL), whose credit profile is relatively weak (rated at [ICRA]BB (Stable)/A4) due to a stretch in liquidity position on account of high receivable position. Further, the rating takes into consideration the company's higher customer concentration risk, where the top-ten customers contributed 65% to the total revenues in FY2022. Nonetheless, the counterparty risk remains low owing to its reputed clientele. Further, ITL operates in the transformer industry, which is highly fragmented and competitive, resulting in pricing pressure to some extent. The ratings also consider the high working capital intensity of operations and the susceptibility of profitability to volatility in raw material prices.

Key rating drivers and their description

Credit strengths

Extensive experience of promoters and ITL's proven track record – ITL's new promoters SSEL have vast experience in the transformers industry, spanning nearly three decades. This coupled with its extensive presence and proven operational track record in the power and distribution transformers industry will facilitate in establishing better relationship with customers and gaining new orders. ITL also derives synergic benefits in terms of raw material procurement at economical prices and economies of scale through joint sourcing, joint lead generations and reduction in manufacturing cost.

Healthy order book position and improvement in margins –The company's order book position remains healthy at Rs. 268.0 crore as of March 2021, which is 1.3 times the gross operating income reported in FY2021, providing adequate revenue visibility in the medium term. Further, the operating margin improved and stood at 5.6% in FY2021 (against 1.0% in FY2020), led by the company's increased focus on the higher load capacity transformer where realisations and margins are better. The healthy order book position and new order inflows are expected to translate into higher turnover and profitability in FY2022.

Comfortable capital structure – ITL's capital structure remains comfortable, aided by its strong net worth position (Rs. 133.2 crore as on March 31, 2021). The capital structure was robust as illustrated by TOL/TNW of 0.4 times as on March 31, 2021 (against 0.6 times on March 31, 2020).

Credit challenges

High client concentration risk– ITL's revenue from the top-ten clients accounted for around 49% and 65% of the total revenues in FY2020 and FY2021, respectively, exposing the company to the client concentration risk. However, the counterparty risk remains low owing to its reputed clientele and LC backed sales to most of the private players. Further, the established relationship with the customers along with execution track record ensures repeat business.

Stiff industry competition– ITL operates in the transformer industry, which is highly fragmented and competitive, resulting in pricing pressure to some extent.

Profitability exposed to volatility in raw material prices – ITL's profitability remains exposed to volatility in raw material prices. Nonetheless, majority of the contracts have price escalation clauses based on the published indices.

Relatively high working capital intensity - ITL exhibits high working capital intensity, as is inherent in the industry it operates in due to high receivable period and inventory requirements. The company recorded working capital intensity of 32% in FY2021 (against 31% in FY2020).

Stretch in liquidity at parent entity- The credit profile of the parent entity (SSEL) is relatively weak due to a stretch in liquidity position on account of a stretch in the receivable position. This in turn constraints the rating assigned to ITL, given the linkages with its parent entity.

Liquidity position: Adequate

ITL's liquidity position is adequate, given the company has cushion in liquidity in the form of unutilised fund-based working capital facility of Rs. 10.00 crore and unencumbered cash of around Rs. 6.2 crore as on June 30, 2021. The company has moderate LC maturities, lined up in the near term. However, estimated cash flows are expected to remain adequate and will facilitate debt obligations going forward.

Rating sensitivities

Positive Factors- The ratings could be upgraded if the company demonstrates a sustained improvement in its scale and margins, while maintaining adequate liquidity position and improving the credit profile of the parent entity.

Negative Factors – The ratings could witness a downward revision if a significant deterioration in scale and profitability weakens key credit metrics or deteriorates SSEL’s credit profile. Also, any stretch in working capital position or any large debt-funded capex that weakens the liquidity position could exert negative pressure on the rating. Specific credit metrics for a downgrade would be TOL/TNW higher than 3.0 times 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
Parent/Group Support	Parent Company: Shirdi Sai Electricals Limited (SSEL); 73.6% stake in ITL. ITL derives operational synergies in the form of joint sourcing of raw materials, leading to generation and reduction in manufacturing cost.
Consolidation/Standalone	The ratings are based on the standalone financial statements of the company

About the company

ITL, incorporated in 1992, is involved in manufacturing power and distribution transformers and various special application transformers, mobile sub-station transformers and sub-stations. The company’s manufacturing plants are located in Chennai and Kancheepuram in Tamil Nadu.

ITL is a subsidiary of Shirdi Sai Electricals Limited, and SSEL held 73.64% stake in ITL as on September 03, 2020. SSEL had bought a majority stake from the ITL’s erstwhile promoters - Prolec GE (a joint venture between a Mexican industrial group, Xignux S.A. de C.V., and General Electric Company (GE)) recently. Shirdi Sai Electricals Limited (SSEL) (rated at [\[ICRA\]BB \(Stable\)/\[ICRA\]A4](#)), incorporated in 1994, is into the business of manufacturing of power and distribution transformers (up to 20 MVA, 66 kV). The company has a transformer manufacturing facility in Kadapa, Andhra Pradesh. It designs and manufactures power and distribution transformers to cater to the needs of electricity utilities as well as private enterprises. SSEL also provides solutions for power transmission and distribution systems through its turnkey projects division.

Key financial indicators (audited)

ITL Standalone	FY2020	FY2021
Operating Income (Rs. crore)	205.3	206.0
PAT (Rs. crore)	1.9	6.3
OPBDIT/OI (%)	1.0%	5.6%
PAT/OI (%)	0.9%	3.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.6	0.4
Total Debt/OPBDIT (times)	0.0	0.0
Interest Coverage (times)	0.8	3.8

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 (FY2022)			Chronology of Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020		Date & Rating in FY2019	
					Aug-16-2021	Sep-29-2020	Feb-17-2020	Aug-28-2019	Nov-08-2018	Jul-12-2018
1	Cash Credit	Long-Term	11.00	-	[ICRA]BB (Stable)	-	[ICRA]BB+ (Negative)	[ICRA]BB+ (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)
2	Bank Guarantee/Letter of Credit	Short-Term	71.79	-	[ICRA]A4	[ICRA]A4	[ICRA]A4+	[ICRA]A4+	[ICRA]A3	[ICRA]A3
3	Unallocated	Short-Term	9.71	-	[ICRA]A4	[ICRA]A4	[ICRA]A4+	[ICRA]A4+	[ICRA]A3	[ICRA]A3
4	Unallocated	Long-Term	0.00	-	-	[ICRA]BB (Negative)	-	-	-	-
5	Issuer Rating	-	-	-	[ICRA]BB (Stable)	[ICRA]BB (Negative)	[ICRA]BB+ (Negative)	[ICRA]BB+ (Negative)	[ICRA]BBB- (Negative)	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based	Simple
Short-term – Non-fund based	Very Simple
Short-term – Unallocated	NA
Long term – Unallocated	NA
Issuer rating	NA

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 analyzing 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, is available on ICRA's website: [Click Here](#)

Annexure-1: Instrument details

ISIN/ Banker name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (RS Crore)	Current Rating and Outlook
Bank of Baroda	Bank Guarantee/ Letter of Credit	NA	NA	NA	26.00	[ICRA]A4
State Bank of India	Bank Guarantee/ Letter of Credit	NA	NA	NA	40.00	[ICRA]A4
Citi Bank	Bank Guarantee/ Letter of Credit	NA	NA	NA	5.79	[ICRA]A4
State Bank of India	Long term – Fund based	NA	NA	NA	10.00	[ICRA]BB (Stable)
Bank of Baroda	Long term – Fund based	NA	NA	NA	1.00	[ICRA]BB (Stable)
NA	Unallocated – Short term	NA	NA	NA	9.71	[ICRA]A4
NA	Issuer Rating	NA	NA	NA	-	[ICRA]BB (Stable)

Source: Company

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

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