

October 27, 2021

Paras Defence & Space Technologies Limited: [ICRA]A- (Stable)/ [ICRA]A2+; Rating reaffirmed and assigned to enhanced amount

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Cash Credit	25.0	49.00	[ICRA]A- (Stable); Reaffirmed/Assigned
Long-term- Term Loan	-	22.00	[ICRA]A- (Stable); Assigned
Long-term/Short-term-Bank Guarantee & LC	-	34.00	[ICRA]A- (Stable) /[ICRA]A2+; Assigned
Short-term-Invoice Discounting	-	5.00	[ICRA]A2+; Assigned
Total	25.0	110.00	

*Instrument details are provided in Annexure-1

Rationale

The assigned rating of Paras Defence & Space Technologies Limited (PDSTL) continues to favourably factor in the healthy order book position at Rs.305 crore as on June 30, 2021, which translates to a comfortable OB/OI ratio of 2.1 times the operating income of FY2021, thereby providing medium term revenue visibility. The rating continues to favourably factor in the strengthening of the company's capital structure, liquidity position and coverage metrics post the equity infusion of Rs. 140 crore through the recent Initial Public Offering (IPO) in September 2021. Apart from part prepayment of the debt outstanding, the proceeds from the IPO are proposed to be used for funding incremental working capital requirements, capital expenditure, and for extending support to subsidiary companies. The rating also draws comfort from the extensive experience of management team with three decades of experience in designing, developing, and manufacturing of a wide range of engineering products and solutions for defence and space sector in the domain of optics, heavy engineering and electronics. PDSTL's long tenure presence in the defence and space sector has helped it to establish strong relationships with its customers as well as suppliers. The Company has developed a strong management and execution team comprising of several ex-employees of Bharat Electronics Limited (BEL), The Defence Research and Development Organisation (DRDO) among others.

The rating, however, continues to remain constrained by the working capital-intensive nature of operations of the company due to a high inventory holding and a long receivable cycle. The sharp increase in inventory levels as on March 31, 2021 is attributable to additional stocking of critical raw materials to avoid any disruption to the delivery schedules in the event of future lockdowns (if any). Consequently, this resulted in high NWC/OI of 115.6% in FY2021. ICRA expects the moderation in the working capital cycle. Going forward, the company's ability to alleviate its working capital intensity, while scaling up its revenues, will be a key rating monitorable. The rating is also constrained on account of the company's moderate scale of operations with Covid-19 pandemic further impacting the revenue in FY2021. However, the healthy order book status of the company provides adequate revenue visibility in the near to medium term. While the client concentration risk remains with top three clients contributing to 71% of the total order book as on March 31, 2021 and top five clients accounting for 63% of revenue in FY2021; thrust on make in India in defence augurs well for PDSTL. The client profile comprises of mostly government organizations with repeat orders received over the years, which mitigates the counter party credit risk to a large extent.

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, comfortable financial risk profile and the extensive experience of management team.

Key rating drivers and their description

Credit strengths

Healthy order-book position provides medium term revenue visibility: The company's fresh order inflows over the past four fiscals has remained adequate, with orders worth Rs. 192 crore added in FY2021. The pending order book of Rs. 305 crore as on June 30, 2021, (OB/OI ratio of 2.1 times the operating income of FY2021) provides medium term revenue visibility.

Comfortable capital structure and healthy coverage indicators: The company's capital structure remains comfortable with gearing being 0.6 times and TOL/TNW being 0.9 times as on March 31, 2021 supported by equity infusion of Rs.51.6 crore in the last four years period from FY2018 to FY2021. The interest coverage stood at 3.5 times and TD/OPBDITA at 2.3 times in FY2021. With the equity infusion of Rs. 140 crore through the recent IPO in September 2021, ICRA expects the capital structure, liquidity position and coverage metrics of the company to strengthen considerably.

Extensive experience of management team: The promoters of the company have more than three decades of experience in designing, developing, and manufacturing of a wide range of engineering products and solutions for defence and space sector in the domain of optics, heavy engineering and electronics. PDSTL's long tenure presence in the defence and space sector has helped it to establish strong relationships with its customers as well as suppliers. The Company has developed a strong management and execution team comprising of several ex-employees of BEL, DRDO among others.

Credit challenges

High working capital intensity due to elongated receivable: The business is working capital intensive with NWC/OI of 90.3% and 115.6% in FY2020 and FY2021 respectively owing to a high inventory holding and a long receivable cycle. The company bills more than 50% of the sales in Q4 of every fiscal, resulting in high working capital cycle in the year end. Since, PDSTL manufactures various kind of products with long cycle time, inventory levels remain high. Further, the sharp increase in inventory levels as on March 31, 2021 is attributable to additional stocking of critical raw materials to avoid any disruption to the delivery schedules in the event of future lockdowns (if any) as the company partly imports raw materials from South Korea and neighbouring countries. The inventory levels are expected to smoothen post normalisation of the Covid situation. The company has been partly managing its working capital cycle by stretching its trade payables by more than 3 months as it has a long-standing relationship with majority 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. ~40% of the IPO proceeds is estimated to be deployed towards working capital requirement, thus reducing the dependence on external borrowings.

Moderate scale of operations: The company's scale of operations continues to be moderate, with the operating income declining by 6% in FY2020 and by 2% in FY2021, after a steady growth from FY2016 to FY2019, as the pandemic-induced lockdown impacted the work progress in Q1FY2021. However, given the healthy order book status, the company is estimated to report healthy revenue growth in the medium term. ICRA expect the company to register a robust revenue growth in FY2022.

High customer concentration risk, though reputed customer base with repeat orders received over the years mitigates the risk to a large extent: While the client concentration risk remains with top three clients contributing to 71% of the total order book as on March 31, 2021 and top five clients accounting for 63% of revenue in FY2021; thrust on make in India in defence augurs well for PDSTL. The client profile comprises of mostly government organizations with repeat orders received over the years, which mitigates the counter party credit risk to a large extent. The company mainly supplies products to Government entities; although some private companies also form part of its customer mix. The company also exports majorly to companies based in Israel, Singapore and USA. The major clientele of the company are reputed government organisations namely Laboratory for Electro-Optics Systems (a unit of ISRO), Bharat Electronics Limited, Instruments Research and Development Establishment (a unit of DRDO) and Private companies like FFS Industries Private Limited and SEC Industries Private Limited. The company has long standing relationships with most of its clientele.

Liquidity position: Adequate

The company has **adequate** liquidity, with unencumbered cash and bank balance of Rs.4.1 crore as of Mar 31, 2021. Further, the company has long-term debt repayments of Rs.9.1 crore in FY2022, which is estimated to be comfortably serviced through cashflows from operations. The average working capital utilisation in the last 15-month period ending June 2021 remained at 81% and non-fund-based utilisation at 78% as on June 30, 2021. The liquid position has strengthened post IPO proceeds of Rs.140 crore in September 2021. The same is estimated to be deployed for funding incremental working capital requirements, capital expenditure, and for extending support to group companies.

Rating sensitivities

Positive factors: ICRA could upgrade the rating if the company demonstrates a significant growth in its overall scale of operations along with improvement in its working capital cycle while maintaining its operating profitability and sustaining its liquidity position.

Negative factors: Negative pressure on PDSTL rating could arise if lower-than-anticipated billing or deterioration in operating profitability or continued elevated working capital cycle impacts the company's liquidity or the overall financial risk profile.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Consolidation and Rating approach
Parent/Group Support	NA
Consolidation/Standalone	Consolidated. The list of companies that are consolidated to arrive at the rating are given in Annexure 2 below.

About the company

Setup in 1971 by Mr. Sharad Shah, Paras Defence & Space Technologies Limited (PDSTL), is engaged in designing, developing, and manufacturing of a wide range of engineering products and solutions for defence and space sector in the domain of optics, heavy engineering and electronics. It has 2 manufacturing facilities, one located in Ambarnath in Thane and the other in Nerul in Navi Mumbai. The major clientele of the company are reputed government organisations namely Laboratory for Electro-Optics Systems (a unit of ISRO), Bharat Electronics Limited, Instruments Research and Development Establishment (a unit of DRDO) and private companies like FFS Industries Private Limited and SEC Industries Private Limited. The day-to-day operations of the company are currently managed by Mr. Munjal Shah (son of Mr. Sharad Shah).

Key financial indicators (audited)

PDSTL - Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	147.6	144.3
PAT (Rs. crore)	19.7	15.8
OPBDIT/OI (%)	27.6%	31.4%
PAT/OI (%)	13.3%	10.9%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	0.9
Total Debt/OPBDIT (times)	2.5	2.3
Interest Coverage (times)	4.0	3.5

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

S. No.	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2021 (Rs. crore)	Date & Rating in		Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					Oct 27, 2021	Sept 30, 2021			
1	Cash Credit	Long-term	49.00	38.2	[ICRA]A-(Stable)	[ICRA]A-(Stable)	-	-	-
2	Term Loan	Long-term	22.00	35.6	[ICRA]A-(Stable)				
3	Bank Guarantee & LC	Long-term/Short-term	34.00	26.7	[ICRA]A-(Stable) / [ICRA]A2+				
4	Invoice Discounting	Short-term	5.00	5.0	[ICRA]A2+				

Source: ICRA research

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Cash Credit	Simple
Long-term- Term Loan	Simple
Bank Guarantee & LC	Very Simple
Invoice Discounting	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, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No/Banker Name	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
Kotak Mahindra Bank	Cash Credit	-	8.70%	-	24.00	[ICRA]A- (Stable)
NKGSB Co-operative Bank Ltd	Cash Credit	-	9.50%	-	25.00	[ICRA]A- (Stable)
Kotak Mahindra Bank	Term Loan	-	8.90%	-	7.52	[ICRA]A- (Stable)
NKGSB Co-operative Bank Ltd	Term Loan	-	9.75%	-	8.00	[ICRA]A- (Stable)
Housing Development Corporation Limited	Term Loan	-	10.77%	-	6.48	[ICRA]A- (Stable)
Kotak Mahindra Bank	Invoice Discounting	-	9.65%	-	5.00	[ICRA]A2+
NKGSB Co-operative Bank Ltd	BG & LC	-	-	-	14.00	[ICRA]A- (Stable) / [ICRA]A2+
Kotak Mahindra Bank	BG & LC	-	-	-	20.00	[ICRA]A- (Stable) / [ICRA]A2+

Source: Company

Annexure-2: 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

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