January 10, 2023

V.S.T. Tillers Tractors Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based/CC	5.00	5.00	[ICRA]AA- (Positive); reaffirmed
Short-term – Non-fund Based	5.00	5.00	[ICRA]A1+; reaffirmed
Total	**10.00**	**10.00**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation of V.S.T. Tillers Tractors Limited's (VST) factors in its dominant market position in the domestic tiller segment, with a market share of 58%, supported by its established presence and widespread dealer network. The ratings also favourably consider the promoter's extensive experience in the industry, and its strong financial risk profile as evidenced by its continued debt-free status and comfortable liquidity position with sizeable cash and liquid investments of Rs. 279.7 crore as on September 30, 2022.

The ratings also factor in VST's recent operating performance with YoY revenue growth of 11.7% and 10.1% reported in FY2022 and H1 FY2023, respectively, supported primarily by healthy traction in the domestic tiller segment. However, the input cost inflation and supply chain constraints exerted some pressure on margins in the current fiscal, with OPM contracting to 10.5% in H1 FY2023 from 14.8% in FY2022. Going forward, while sequential improvement in margins is expected, supported by price hikes undertaken and cost-optimisation initiatives, the company's ability to scale it back to the FY2022 levels and sustain it would be critical. ICRA also notes that the company's performance in the domestic tractor segment has been lagging behind market trends. Accordingly, its ability to claw back its market share in tractors, supported by its product portfolio and network expansion initiatives, remains critical to diversifying and strengthening its business profile further.

The ratings also consider the cyclicality inherent in the tractor and tiller industry in addition to the competition that limits the company's pricing flexibility to a certain extent, exposing its profitability to fluctuations in input costs. The dependence of the power tiller segment on Government subsidies also exposes VST's revenues and margins to any changes in Government policies. However, the company has made efforts to launch subsidy-neutral tillers and retail finance schemes for its power tillers, which can mitigate the subsidy risk to a certain extent, going forward.

The Positive outlook on the long-term rating factors in the expected growth in VST's revenues and earnings over the medium term, driven primarily by growth in the tiller segment, as well as its efforts to grow other segments such as spares, implements and other allied agricultural products. The company is also expected to continue to maintain its debt-free status and strong liquidity profile, supported by healthy cash accruals from operations.

Key rating drivers and their description

Credit strengths

Established market position in domestic tillers, supported by long presence and widespread dealer network – VST has an established market position and a well-reputed brand presence in the power tiller segment in India with a market share of 58%. Coupled with addition of new dealers to its widespread network of over 500 dealers and increasing penetration of farm mechanisation, this will continue to support the company's business prospects.

Strong financial profile characterised by nil debt and sizeable cash balances and liquid investments – VST's financial profile remains strong, supported by its sizeable net worth of Rs. 764.8 crore as on September 30, 2022, healthy cash flows and debt-free status. The company's liquidity position also remains strong with cash balances and liquid investments of Rs. 279.7 crore as on September 30, 2022. Going forward, given minimal capex requirements and continued healthy cash flow generation, VST is expected to maintain its debt-free status and healthy debt indicators over the medium term.

Healthy revenue growth in FY2022 and H1 FY2023 – In FY2022, VST reported healthy revenue growth of 11.7%, supported by strong demand for tillers, as evidenced in YoY volume growth of 16.3%. The growth momentum continued into the current fiscal as well with 10.3% YoY volume growth during April–November 2022. The trend is expected to sustain going forward as well.

Credit challenges

Exposed to cyclicality in industry with strong linkages to agricultural production and the monsoons – VST derived 54.4% and 27.6% of its revenues from the power tillers and tractors, respectively, in H1 FY2023. Accordingly, its revenues and earnings remain exposed to the cyclicality inherent in these segments owing to dependence on the monsoons and crop production in the country. However, the company is making efforts to diversify into additional segments such as power weeders, brush cutters, electric pumps and spare parts to mitigate this risk to some extent.

Dependence of power tiller segment on Government subsidies – To a large extent, power tiller sales are driven by state government subsidies, which exposes VST's revenues and margins to any adverse changes in Government policies. This was also visible during September–October 2022, when VST's power tiller sales contracted by 19% YoY due to subsidy-related issues in key markets of Odisha and Karnataka. While the company has launched subsidy-neutral tiller and retail finance schemes for its power tillers, which may mitigate the subsidy risk to a certain extent, going forward; their performance will remain a monitorable.

Competition and pricing risks – The tractor and power tiller segments are characterised by intense competition, thus limiting VST's pricing flexibility amid fluctuating input costs. With restriction in imports from countries like China, the pricing scenario has been relatively better, although the competition from domestic players continues to increase.

Environmental and Social Risks

Environmental considerations: Tractor OEMs are exposed to adverse climatic conditions such as droughts, floods etc. as they derive the major proportion of their demand from the rural segment that may be impacted by such environmental factors. Construction/agricultural equipment OEMs also remain exposed to climate transition risks emanating from a likelihood of tightening emission control requirements, with the Government focused on reducing the adverse impact of automobile emissions. Companies in the sector may also need to invest materially to develop products to meet regulatory thresholds, which may have a moderating impact on their return and credit metrics. The change in emission norms from TREM IV to TREM V or TREM VI may lead to a capex outlay towards upgrading its higher HP tractors. However, since most of VST's revenue is derived from selling power tillers and low HP tractors, for which the said norms are not applicable, the credit risk from the same remains low.

Social considerations: OEMs are exposed to risk arising from labour unrest like strikes and lockouts. The company has a labour redressal protocol in place, wherein any unrest is obviated by negotiations and conciliations. The company regularly conducts welfare activities for its employees to mitigate the risk. Another social risk that OEMs face pertains to product safety and quality, wherein instances of product recalls and high warranty costs may not only lead to a financial implication but could also harm their reputation and create a more long-lasting adverse impact on demand.

Liquidity position: Strong

VST's liquidity position is **strong** with a cash and liquid investment balance of Rs. 279.7 crore as on September 30, 2022. Despite regular dividend payouts, the company's liquidity position has remained strong on the back of healthy operating cash flows, which are expected to continue in the future as well. VST remains debt free with moderate capex of Rs. 50-60 crore annually over the medium term, which would be funded comfortably from internal accruals.

Rating sensitivities

Positive factors – The long-term rating could be upgraded on a sustained improvement of the company's scale of operations and earnings profile. VST's ability to achieve business diversification, strengthen market share in the domestic tractor and farm equipment segment aided by product launches and geographical spread shall be a key monitorable.

Negative factors – The ratings may be revised downwards in case of any sharp deterioration in the financial profile of the company from weak earnings and/or deterioration in credit metrics. Any large debt-funded acquisition or capex will also be a critical monitorable. Additionally, the outlook may be revised to Stable if the company reports any continued weakness in operating performance.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Tractor OEMs
Parent/Group Support	Not applicable.
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of VST.

About the company

V.S.T. Tillers Tractors Limited was promoted in 1967 as a 60:20:20 joint venture between Mr. V.T. Velu along with his two brothers in technical and financial collaboration with Mitsubishi, Japan (Mitsubishi Heavy Industries Limited and Mitsubishi Corporation), and Mysore State Industrial Investment Corporation Limited, for manufacturing power tillers and diesel engines. The commercial production of tillers commenced from 1970. Later, an additional technical and financial collaboration was entered into with Mitsubishi Agricultural Machinery Company Limited, Japan, in 1984 for manufacturing 18.5 horse power (HP), four-wheel drive tractors. However, the collaborations with all the above entities have expired. The current shareholding of the Indian promoters in VST is 52.64%, while Mitsubishi's stake is 2.93%, and the rest is held by public shareholders. VST manufactures farm equipment, namely power tillers, tractors, power weeders, diesel engines and other precision agricultural and automotive components. It also trades in certain farm equipment (mainly rice transplanters), which are sourced from China. Headquartered in Bangalore, VST derives approximately 94% of its revenues from the domestic market and has a nationwide network of more than 500 dealers to support sales and provide after-sales services.

Key financial indicators

VST – Standalone	FY2021 Audited	FY2022 Audited	H1 FY2023
Operating income	764.2	853.9	
PAT	90.8	99.3	
OPBDIT/OI	12.6%	14.8%	
PAT/OI	11.9%	11.6%	
Total outside liabilities/Tangible net worth (times)	0.3	0.3	
Total debt/OPBDIT (times)	-	-	
Interest coverage (times)	49.5	78.8	

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 (FY2023)			Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as of March 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Jan 10, 2023	Jan 31, 2022	Nov 27, 2020	May 23, 2019
1	Cash Credit	Long-term	5.0	-	[ICRA]AA- (Positive)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
2	Non-Fund based	Short-term	5.0	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term- Fund Based/CC	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, is available on ICRA's website: Click Here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	5.0	[ICRA]AA- (Positive)
NA	Non-Fund based	NA	NA	NA	5.0	[ICRA]A1+

Source: *Company*

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

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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