October 25, 2019

ZF Steering Gear (India) Limited: Ratings reaffirmed; outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Term Loan	125.00	125.00	[ICRA]A+ reaffirmed; outlook revised from stable to negative
Long-term fund based	1.00	1.00	[ICRA]A+ reaffirmed; outlook revised from stable to negative
Short-term non-fund based	0.35	0.35	[ICRA]A1+; reaffirmed
Total	**126.35**	**126.35**	

**Instrument details are provided in Annexure-1*

Rationale

The long-term outlook revision reflects ICRA's expectation that the credit profile of ZF Steering Gear India Limited (ZFI) could weaken over the near to medium term due to pressure on its core operations given the slowdown in the domestic medium and heavy commercial vehicle (M&HCV) as well as tractor industry. The company reported a 39% drop in sales in Q2FY2020 when compared to Q2FY2019 due to low offtake from key customers because of weak demand in the segment. Owing to sharp decline, ZFI's OPBIDTA margin declined to 13% during H1FY2020 as compared to 18% in FY2019. With ramp-up in greenfield Pithampur (in Madhya Pradesh) unit and consequent impact on fixed overheads, overall profitability indicators (RoCE and OPBIDTA margin) are likely to remain suppressed in current fiscal as well as first half of next fiscal.

Despite weakening in operational profile, the ratings continue to draw comfort from ZF's strong liquidity position, characterized by Rs.128 crore of investments. The company has repaid majority of its debt and it is net debt free as on September 2019. The ratings reaffirmation continues to reflect ZFI's strong position in the domestic power steering segment, established relationship with domestic automobile OEMs and its superior operating efficiencies. ICRA notes that Robert Bosch Automotive Systems which is amongst the largest steering system manufacturers globally, holds 25.89% stake in ZFI. The credit strengths are partially offset by ZFI's modest scale of operations, susceptibility to the inherent cyclicality in the domestic M&HCV and tractor industry and continuous need to upgrade technology in view of technology-intensive nature of products. The company's Pithampur facility will start operation soon. The total project cost is estimated at Rs 127 crore, out of which Rs 90-95 crore has been already incurrent incurred and rest will be invested over next 2-3 quarters.

Key rating drivers and their description

Credit strengths

Strong position in the domestic steering systems industry for HCV and tractors; established relationship with leading OEMs -The Indian steering gear market is primarily dominated by three major players viz JTEKT India Limited (erstwhile Sona Koyo Steering Systems Limited; rated [ICRA]AA/Stable/A1+), Rane TRW Steering Systems Private Limited (Rane; rated [ICRA]AA-/Stable/A1+) and ZFI. While JTEKT is primarily present in the passenger vehicle (PV) segment, ZFI and Rane are mainly present in the commercial vehicle and tractor segment. Overall, the domestic M&HCV and tractor steering system market is primarily duopolistic in nature with ZFI and Rane Group accounting for ~90% of the market share

Comfortable capitalization and coverage indicators- ZF is net debt free, and hence it has comfortable coverage indicators with Total Debt/ OPBDITA of 0.4 time and DSCR of 3.3 times as of September 30, 2019.

Strong liquidity position - The company reported cash, bank balance and investments (including investment in liquid fund, equity shares and other mutual funds) to the tune of Rs. 131 crore as on September 30, 2019.

Credit challenges

Susceptible to inherent cyclicality in the domestic CV and tractor segment; negligible presence in power steering segments of PV and tractor business- ZFI primarily supplies power steering systems for CVs and mechanical steering systems for tractors. The company has underperformed in the mechanical steering supplies for the tractor segment, as demand is gradually shifting towards power steering, where ZFI has a weak market position. Moreover, both M&HCV as well as tractor industry are currently in cyclical downturn which is likely to pressurize revenue as well as profitability indicators of ZFI over next few quarters. The company has limited presence in the PV segment.

Continuous need to upgrade technology to avoid obsolescence - Steering systems, being critical automobile components, are however subject to marginal changes in design during the transition between emission norms or change in fuel and, hence, requires frequent investments in technology to prevent obsolescence

Liquidity position: Strong

The company has cash and liquid investments to the tune of Rs.131 crore as of September 30, 2019. While net profits are likely to weaken significantly due to moderation in operating margin as well as high depreciation expense, it is expected to generate cash profits of over Rs 30 crore. Given modest debt level and adequate cash profits, company's liquidity position is likely to remain strong in the near to medium term.

Rating sensitivities

Positive triggers – ICRA could upgrade ZF's rating if there is substantial improvement in scale of operations, with turnover more than Rs 500 crore with a ROCE of over 20% on sustained basis, along with reduced dependency on cyclical CV & tractor segment.

Negative triggers – There could be downward pressure on rating if ZF's operating performance weaken further or return indicator (RoCE) continue to remain below 10%-12% over the medium term. Dilution in promoter's stake in the entity due to stake sale or invocation of pledged shares is another key monitorable.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Autocomponent Manufacturers
Parent/Group Support	Not applicable
Consolidation/Standalone	The rating is based on Standalone financial statements of ZFI

About the company

ZF Steering Gear (India) Limited was founded by the Munot family and ZF Lenkystene GmbH. Later, Robert Bosch Automotive Steering GmbH acquired ZF Lenkystene GmbH and renamed the company as Robert Bosch Automotive Steering GmbH. The company manufactures, assembles and deals in steering gears with an installed manufacturing capacity of 2.0 lakh mechanical steering gear units and 3.75 lakh hydraulic power steering gear units per annum. ZFI's manufacturing plant is at Vadu Budruk Village in the Tal Shirur district of Maharashtra.

The company's steering gears are used in buses and are supplied to various state transport undertakings as well as to heavy vehicles like dumper and haulage trucks. Buses fitted with power steering gears reduce the drivers' efforts in steering the vehicle and add to their safety. As on September 30, 2019, promoter group holds 67.39% stake in family wherein Munot family holds 41.5% stake in the company and RBAS holds 25.89% stake. Munot family has pledged their 16.53% stake in ZFI as on September 2019.

In FY2019, ZFI reported a net loss of Rs. 1.3 crore on an operating income (OI) of Rs. 439.4 crore, as compared to a net profit of Rs. 47.1 crore on an OI of Rs. 424.6 crore in the previous year

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	424.6	439.4
PAT (Rs. crore)	47.1	(1.3)
OPBDIT/OI (%)	20%	18%
RoCE (%)	15%	-3%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.3
Total Debt/OPBDIT (times)	0.7	0.6
Interest Coverage (times)	26.9	39.8
DSCR	9.2	8.0

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2020)					Rating History for the Past 3 Years				
		Type	Amount Rated	Amount Outstanding	Current Rating	Earlier Rating	FY2019			FY2017	FY2016
					25-Oct-2019	10-June-2019	28-Feb-2019	30-Oct-2018	05-Apr-2018	03-Mar-2017	10-Mar-2016
1	Term Loan	Long Term	125.0	13.7	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+&	[ICRA]A+&	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
2	Fund based limit	Long Term	1.0		[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+&	[ICRA]A+&	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)
3	Non-fund based limit	Short Term	0.35		[ICRA]A1+	[ICRA]A1+	[ICRA]A1+&	[ICRA]A1+&	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Amount in Rs. Crore

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
	Term Loam	FY2017	8.5%	FY2022	50.00	[ICRA]A+(Stable)
	Term Loan	FY2017	8.5%	FY2022	75.00	[ICRA]A+(Stable)
	Fund based Limit				1.00	[ICRA]A+(Stable)
	Non-fund based limit				0.35	[ICRA]A1+

Annexure-2: List of entities considered for consolidated analysis - NA

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About ICRA Limited:

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