February 14, 2020

KPIT Technologies Limited: Ratings assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loan ($ million) *	7.5	[ICRA]AA-(Stable); Assigned
Long-term/Short-term – Fund-based/Non-fund based	265.0	[ICRA]AA-/Stable/[ICRA] A1+; Assigned
Total	**265.0** **$7.5 million**	

**Instrument details are provided in Annexure-1*

Though a part of the long-term loans of KPIT are denominated in foreign currency, ICRA's ratings for the same are on national rating scale, as distinct from an international rating scale

Rationale

The ratings reflect the healthy business risk profile of KPIT Technologies Limited (KPIT) with its niche offerings, strong position in the automobile engineering and mobility solutions supported by its established relationships with top global original equipment manufacturers (OEMs). Further, the company's financial profile remains strong with healthy profitability, strong capitalisation and debt protection metrics along with a strong liquidity profile. These strengths are, however, partially offset by the client and industry concentration risks as the company focuses only on the automotive industry with about 84% of its revenue generated by its top 17 customers in Q3 FY2020.

ICRA notes that the company's focus on the automotive segment exposes it to the inherent cyclicality of the auto industry. However, the company is involved in emerging technologies, such as autonomous driving, vehicle connectivity and electric vehicles, which provide healthy revenue visibility. Nevertheless, a prolonged slowdown in the auto industry may adversely impact technological spending by its customers.

ICRA notes that KPIT's offering are niche in nature, focusing on entrenched relationships with its top 25 global automobile players. However, this exposes the company to client concentration risk as the revenue loss from its top clients may impact its revenue and profitability.

The Stable outlook on the [ICRA]AA- rating reflects ICRA's opinion that KPIT will continue to benefit from its long track record of operations, its established relationship with top auto companies and healthy financial risk profile.

Key rating drivers and their description

Credit strengths

Healthy operational profile driven by its niche offerings and strong relationships with top global automotive OEMs and tier-I suppliers – KPIT's business is focused entirely on the mobility industry with its niche offerings in the power train, autonomous and connectivity categories. Further, KPIT enjoys an established client base with BMW, Eaton and other global OEMs and tier-I suppliers to whom it offers multiple services. KPIT's niche offerings and strong relationships have driven a healthy revenue growth over the years.

Strong financial risk profile characterised by low gearing, strong debt coverage and comfortable liquidity – KPIT's financial risk profile is supported by low gearing of 0.2 time as on end September 2019, Gross debt/OPBITDA of 0.7 time and Interest coverage of 13.6 times for H1 FY2020. The company's debt outstanding (excluding leases) was Rs. 132.3 crore and Rs. 92.6 crore at end FY2019 and end H1 FY2020, respectively. The cash and liquid investment (including current investment) stood at Rs. 271.1 crore in FY2019 and Rs. 329.1 crore in H1 FY2020 on a consolidated basis, leading to net cash position. The net cash position is expected to continue, though any large scale, debt-funded acquisition needs to be evaluated on a case-to-case basis.

ICRA notes the application of INDAS 116 on accounting of operating leases in the current financial year has led to recording a lease liability of Rs. 122.5 crore. This has impacted the financial risk profile, albeit remaining comfortable.

Increased R&D expense by global auto companies in view of Government regulations from different countries on electric vehicles provides revenue visibility - The company's constant high growth in automobile engineering (22.9% in FY2019) is supported by increased R&D expenses from the OEMs and tier-I suppliers on emerging technologies such as Autonomous vehicle, electric vehicle and as well as by its addition of new features in vehicles to stay competitive in the industry. The demand for electric vehicles are increasing around the globe owing to high carbon emission by conventional vehicles, leading Governments across countries to incentivise electrical mobility. ICRA believes these factors provide better revenue visibility for KPIT over the near to medium term.

Credit challenges

Client and segment concentration in revenue – KPIT derives its revenues from the auto sector with its top 17 customers contributing about 84% of revenue in Q2 FY2020. So, slowdown in the auto segment or decrease in technology spending by its top clients can have significant bearing on its growth. However, the risk is mitigated to a certain extent by its established relationships with its top global auto OEM clients and its niche offering in mobility solutions. KPIT's strategy is to focus on its top automobile clients (OEMs and tier-I suppliers), in line with the concentrated nature of the industry to drive revenues by offering multiple services.

Margins vulnerable to wage inflation and foreign exchange fluctuations - KPIT's profit margins are susceptible to wage inflation and forex fluctuation. Being in a highly labour intensive business, the availability and retention of a skilled workforce are its key challenges. KPIT is also exposed to the hiring norms of the countries it operates in. KPIT's revenue and margins are exposed to forex risks, although its hedging mechanisms mitigate this risk to an extent.

Liquidity position: Strong

KPIT's liquidity is **strong** with expected healthy fund flow from operations of nearly Rs. 230-250 crore, with planned capex of about ~3% of revenue at about Rs. 60-65 crore. The liquidity is supported by significant cash and cash equivalents (including current investment)of Rs. 271.1 crore at end FY2019 (Rs. 329.1 crore at end H1 FY2020) and unutilised fund-based limits. KPIT's debt repayments at about Rs. 35 crores ($2.5 million) in FY2020 also remain modest.

Overall, ICRA expects KPIT to be able to meet its near-term commitments through internal sources and yet be left with sufficient cash surpluses.

Rating sensitivities

Positive triggers – ICRA could upgrade KPIT's rating if the company demonstrates a sustained improvement in its revenue led by diversification in its business profile with improvement in margins.

Negative triggers – Negative pressure on KPIT's rating could arise if the company's revenue and profitability declines owing to loss of any of its top customers or due to prolonged slowdown in the auto industry. Any debt-funded capex or acquisition that may adversely impact its liquidity profile will also lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology] [Rating Methodology for Entities in the Information Technology (IT) Service Industry]
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on consolidated financial statements of the rated entity.

About the company

KPIT Technologies Limited (erstwhile KPIT Engineering Limited) is a technological company focused on automobile engineering and mobility solutions. It was listed on the National Stock Exchange (NSE) and the Bombay Stock Exchange (BSE) in April 2019.

The company offers technology solutions to automobile OEMs under different practices such as power trains (conventional and electrical), connectivity, autonomous (vision and control systems) and diagnostics. Each of its practice areas offer software IP, software integration, feature development, and verification and validation services.

In H1 FY2020, the company reported a net profit of Rs. 67.7 crore on an operating income (OI) of Rs. 1,049.8 crores compared to a net profit of Rs. 55.0 crore on an OI of Rs. 641.3 crore in FY2019.

Key financial indicators

	FY2019 (Audited)	H1-FY2020
Operating Income (Rs. crore)	641.3	1049.8
PAT (Rs. crore)	55.0	67.7
OPBDIT/OI (%)	14.7%	14.0%
RoCE (%)	13.5%	16.7%
Total Outside Liabilities/Tangible Net Worth (times)	0.7	0.6
Total Debt/OPBDIT (times)	1.4	0.7
Interest Coverage (times)	13.6	13.9
DSCR	15.9	4.1

Note : The appointed date of merger and demerger being 1st January 2019, the full year financial results for FY19 for KPIT technologies Limited are for Q4 of the demerged entity (engineering business) and nine months of KPIT's engineering limited.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years - Not Applicable

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					14-Feb-20	1-Aug-2018	14-Aug-2017	10-Jul-2016
1	Term Loan (USD Million	Long Term	7.5	7.5	[ICRA]AA-(Stable)	-	-	-
2	Working capital Facilities	Long Term/Short term	265.0	-	[ICRA]AA-(Stable)/[ICRA]A1+	-	-	-

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	Current Rating and Outlook
NA	Term Loan (USD Million)	March-2016	6month LIBOR+160 bps	March- 2021	7.50	[ICRA]AA- (Stable)
NA	Long-term/Short-term Fund based/Non-fund based (RS crore)	NA	NA	NA	265.00	[ICRA]AA- (Stable)/A1+

Source: KPIT Technologies Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Impact Automotive solutions Limited	100%	Full Consolidation
KPIT Technologies(UK)Limited	100%	Full Consolidation
KPIT Technologies Inc.	100%	Full Consolidation
KPIT Technologies Holding Inc.	100%	Full Consolidation
KPIT (Shanghai) Software technology company Limited, China	100%	Full Consolidation
KPIT Technologies Netherland B.V	100%	Full Consolidation
KPIT Technologies GK, Japan	100%	Full Consolidation
KPIT technologies Gmbh, Germany	100%	Full Consolidation
KPIT technology Pte Limited	100%	Full Consolidation
Microfuzzy KPIT TECNOLOGIALTDA, Brazil	99.9%	Full Consolidation
Microfuzzy industrie Elektronic Gmbh	87.5%	Full Consolidation

Analyst Contacts

Subrata Ray
+91 22 6114 3408
subrata@icraindia.com

Gaurav Jain
+91 20 6606 9922
gaurav.jain@icraindia.com

Pawan Mundhra
+91 20 6606 9918
Pawan.mundhra@icraindia.com

Relationship Contact

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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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For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999

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