Tube Investments of India Limited

January 10, 2018

Summary of rated instruments

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund based	525.00	[ICRA]AA+ (Stable); Assigned
Short-term fund based - sublimit	(525.00)	[ICRA]A1+; Assigned
Short-term non-fund based	500.00	
Commercial paper	525.00	
Total	**1,550.00**	

*Instrument details in Annexure - I

Rating action

ICRA has assigned [ICRA]AA+ (pronounced ICRA double A plus) rating to the Rs. 525.00 crore long term fund based facilities of Tube Investments of India Limited (TIIL/the company). ICRA has also assigned [ICRA]A1+ to the Rs. 525.00 crore short term fund based facilities (sublimit), the Rs. 500 crore short-term non fund based facilities and the Rs. 525.00 crore commercial paper programme of the company. The outlook on the long-term rating is stable.

Rationale

The assigned ratings favourably factor in from TIIL's diverse product profile and its well-entrenched market position across products. TIIL's product portfolio comprises of cycles (~33% of revenues), tubes and strips (~43% of revenues), chains, doorframes, fineblanking products and railway products (~24% of revenues) at the standalone level and, additionally gears at the consolidated level. In terms of business position, the company is the market leader in CDW (cold drawn welded) tubes and one of the two prime players in chains. Also, the company's 'Diamond', 'Rombo' and 'Razor' brands have high value in the chains replacement market in India. Further, TIIL holds close to 30% market share in the retail clientele for cycles – owning the popular brands BSA, Hercules, Roadeo and Montra.

The company's engineering and metal forming products have grown at a healthy compounded annual growth rate (CAGR) in the last few years – the former at 5% and the latter at 8% CAGR for FY2014-17. These have resulted in high capacity utilization of factories across most products, resulting in cost economies. TIIL is also looking at expanding capacities for a few products in the near to medium term.

The ratings also draw comfort from the company's healthy financial profile marked by conservative capital structure, healthy coverage metrics and adequate liquidity. The company's gearing stood at 0.7 times while its consolidated interest coverage stood at 5.3 times for FY2017/as on March 31, 2017. Due to adequate liquidity, the company utilizes only 65-70% of its working limits/available drawing power currently. The company's strong parentage – by virtue of it being one of the key entities of the Chennai-based Murugappa group – lends it implicit financial flexibility.

However, the ratings are constrained by the moderate profit margins and profitability. The consolidated net margin was sub 4% in FY2017, while its RoCE (return on capital employed) stood sub 15% (also on consolidated basis) in FY2017. Also, the company's margins are exposed to volatility in commodity price movements and its revenues are vulnerable to fluctuations in 2W/passenger car demand. However, the relatively stable margins of the engineering and metal forming divisions in the past – primarily from passing on commodity price increases to customers; and about 17% of TIIL's revenues (excluding cycles) from non-auto businesses (industrial and Railways) mitigate these risks to a large extent.

Going forward, ICRA expects TIIL's engineering/metal forming volumes to witness healthy growth, aided by healthy demand outlook in the end segments (2W and passenger vehicles), increase in export volumes (which currently contribute less than 10% of revenues) and new products; the strong entry barriers from new players will support the company further. While there will be margin improvement with scale economies, higher sale of better margin products and cost saving initiatives undertaken by the company, the increase in margins is likely to remain modest. Nevertheless, TIIL's capital structure and financial profile are expected to remain comfortable going forward as well. The demand for standard cycles has been on a declining trend in the last few years, and TIIL is compensating the decline through higher specials and institutional sales; ICRA notes that delayed payment receipts in institutional orders could stretch debtors.

Outlook: Stable

ICRA believes that TIIL will continue to maintain its dominant market position and that demand for its products from the engineering and metal forming divisions will continue to drive revenues. Further, while the margins are likely to remain stable with the company passing on any increase in raw material prices, TIIL's debt metrics are also expected to remain strong in the medium term, despite moderate capex plans. The outlook may be revised to 'positive' if there is substantial improvement in profit margins, RoCE and debt levels. The outlook may be revised to 'negative' if profit margins or cash accruals are lower than expected; or if there is any major capex or working capital stretch that causes surge in debt levels. Any increase in investments and acquisitions would be rating sensitivities.

Key rating drivers

Credit strengths

Diversified revenue base – At the standalone level, the company has three prime divisions – cycles, engineering and metal formed products; and several products/product categories under these divisions. The engineering division, which manufactures tubes and strips, is the largest contributor to revenues at 43% of net sales. Cycles division manufactures and trades cycles and constituted 33% of standalone sales in H1 FY2018; while metal formed products, through which the company manufactures chains, door frames, fine blanking products and railways products contributed to 24% of net sales during the same period. TIIL also benefits at the consolidated level from additional diversity from gearbox manufacturing, through Shanthi Gears Limited – although the company contributes to less than 5% of consolidated revenues. The diversified revenue base mitigates risks arising from cyclicality in demand and technology changes to a large extent.

Well established market position in all the segments – The company is one of the leading players in cold drawn welded (CDW) tubes – key product in the engineering division. Through its metal forming division, TIIL is also one of the two major suppliers of automotive and industrial chains in India and an establishing player in fineblanking products. The company's replacement brands in the chains segment – 'Diamond', 'Rombo' and 'Razor' are well established in India and have high brand value. In the cycles business, the company is one of the four largest organized players in India and had a market share of close to 30% in the retail segment in H1 FY2018. Also, its cycle brands – BSA, Hercules, Montra and Roadeo – are amongst the best-selling brands in the country. TIIL's market position is expected to remain strong across products over the medium term. The company's customers across divisions (barring cycles which is more retail oriented) are in the marquee category, comprising of reputed tier-I auto suppliers and OEMs.

Healthy increase in volumes in the engineering and metal forming divisions; high capacity utilization –The engineering and metal forming products divisions have witnessed healthy volume growth in the last 3-4 years. Tubes had a CAGR growth of 8.5% by volumes for FY2014-17 while fineblanking products grew by a robust 10% CAGR for the same period. The capacity utilization of factories across most product categories in these two divisions has also been high by virtue of the demand, and TIIL is exploring capacity expansion possibilities.

Healthy demand outlook for various products; new products in pipeline – The healthy demand outlook for 2W and passenger cars for FY2018 and FY2019; strengthening of export presence – where the company is relatively weak (less than 10% of revenues); and relatively high entry barriers for new players in tubes, chains, fineblanking products and railway coach frames are likely to drive volumes. Further, the company is also looking at new products to drive revenue growth going forward. In the cycles division, sale of specials and institutional orders (driven by Government welfare schemes) are expected to support revenue growth, although the overall outlook for the cycle segment is subdued.

Comfortable financial profile marked by conservative capitalization, healthy coverage metrics and adequate liquidity – TIIL's gearing stood at 0.7 times on standalone and consolidated basis, as on March 31, 2017. TIIL's coverage metrics are also healthy with interest coverage of 4.9 and 5.3 times respectively for FY2017. Further, the company had positive free cash flows for FY2017 and its average working capital utilization stood at 65-70% of drawing power/sanctioned limits for the 13-month period Oct 2016 to Oct 2017. The capital structure, coverage metrics and liquidity are likely to remain comfortable going forward.

Strong parentage being one of the flagship entities of the Murugappa group; lends financial flexibility – TIIL is one of the flagship companies of the Chennai based Murugappa group – a conglomerate having presence across sugar, fertilisers, financial institutions and auto components, to name a few. While TIIL's accruals are relatively healthy and the company does not require any financial support from the group, the company enjoys implicit financial flexibility by virtue of it being a key part of the much larger Murugappa group.

Credit challenges

Moderate operating and net margins; moderate profitability – TIIL's standalone and consolidated operating profit margins (OPM) stood at 8.9% and 9.0% respectively for FY2017, while its net margins were sub 4% for the same period. Despite healthy margins—upwards of 10% from engineering and metal forming divisions, sub 5% OPM from the cycles division has resulted in moderation of the overall margins. Further, TIIL's RoCE stood at sub 15% on a standalone and consolidated basis for FY2017, indicating moderate profitability for the healthy market position. While TIIL's margins are likely to improve going forward with increase in scale, better sales of high-margin products and strategic cost saving initiatives, the margin expansion is expected to be modest.

Declining demand from 'standards' in the cycles segment; delayed payments from institutional orders whose volumes are on an increasing trend – Standard cycles are an integral part of the cycle segment (22.7% of cycle sales in FY2017), but its volumes have declined in the last few years due to migration to 2W/motorcycles as a commuting medium from cycles. TIIL used to sell close to 18 lakh standard cycles in FY2014; this has reduced by close to 40% to about 11 lakh cycles for FY2017. The sales volumes of standard cycles are likely to decline further going forward. Although the company has compensated this to a large extent through increase in sale of specials (which is a fast-growing segment) and higher institutional orders, delayed receipt of receivables in the latter is an area of concern and could increase receivables as institutional sales increases.

Exposed to volatility in demand from 2W/passenger car industries – TIIL derives 52% of revenues from the auto segment; of this, about 50% each comes from the 2W and passenger car segments. Any downturn in these segments is likely to impact the company's revenues. However, the healthy outlook for these two segments for FY2018 and FY2019, and presence in non-auto (17% of revenues) – in the industrial and railways businesses mitigates the segment concentration risk to an extent.

Exposed to volatility in commodity price movements, although the company has been able to sustain margins by passing on the same in the past – By virtue of most of its raw materials being linked to various forms/alloys of steel, TIIL's margins are vulnerable to unfavourable commodity price movements. However, the company's demonstrated ability to pass on raw material price increases (albeit with a lag) to its customers has resulted in operating margin stability at 10-12% in engineering and 12-14% in the metal forming division.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below. Also, ICRA has taken a consolidated view of TIIL; its two subsidiaries - Shanthi Gears Limited (SGL, rated [ICRA]AA/Stable/[ICRA]A1+) and Financiere C10 SAS (FC10); and its two joint ventures - TI TSubamex Private Limited (TI Tsubamex) and TI Absolute Concepts Private Limited (TI Absolute Concepts).

Links to applicable criteria:

Corporate Credit Rating Methodology

Rating methodology for Auto Component Suppliers

About the company:

TIIL is one of the flagship companies of the over Rs. 30,000 crore Chennai-based Murugappa group. At the standalone level (which constitutes over 90% of TIIL's consolidated revenues from FY2017), the company has three divisions – cycles, engineering and metal formed products. The cycles segment manufactures standard and special cycles under the brands BSA, Hercules, Montra and Roadeo and trades some imported brands like Bianchi and Schwinn to name a few. The engineering division manufactures ERW (electric resistance welded) tubes, CDW (cold drawn welded) tubes and cold-rolled steel strips (CRSS); while metal formed products comprise of automotive and industrial chains, fine blanking products, doorframes, special products such as agri blades and motor casings, and railway products. The three divisions constituted ~33%, ~44% and ~23% of net sales in H1 FY2018 respectively. TIIL has 16 plants as on date, across the three divisions and is looking at starting another plant for the engineering division from Q1 FY2019.

TIIL has 4 subsidiaries/joint ventures which constitute less than 10% of the consolidated revenues (in FY2017). Shanthi Gears Limited (70.1% subsidiary of TIIL) manufactures standard and customized gears for various engineering and industrial segments, while Financiere C10 SAS (100% subsidiary) manufactures engineering and industrial chains, primarily in France. TI Tsubamex Private Limited is a 75:25 JV between the company and Tsubamex Private Limited, Japan and does large sheet metal stampings die design and engineering in its factory near Chennai. TI Absolute Concepts Private Limited is a 50:50 JV between TIIL and Absolute Speciality Foods Chennai Private Limited and runs 'Ciclo Cafe' – cycle themed cafes in Chennai, Hyderabad and Gurugram. The company also acquired 80% stake in two Sri Lankan companies – Creative Cycles (Private) Limited and Great Cycles (Private) Limited, in December 2017, for backward integration of the mass premium and super premium cycles.

TIIL held about 60% stake in Cholamandalam MS General Insurance Company Limited (rated [ICRA]AA (Stable)) and about 46% stake in Cholamandalam Investment & Finance Company Limited (rated [ICRA]AA (Positive)/[ICRA]A1+)- investments aggregating to over Rs. 900 crore as on March 31, 2016. As part of a demerger arrangement in FY2017, these investments were moved into another listed company —TI Financial Holdings Limited wef. April 01, 2016 (appointed date of demerger) and TIIL currently holds only the manufacturing investments.

Key financial indicators (audited)

Consolidated*	FY2016	FY2017
Operating Income (Rs. crore)	4,602.5	4,493.3
PAT (Rs. crore)	99.9	174.4
OPBDIT/ OI (%)	8.6%	9.0%
RoCE (%)	NA	12.9%
Total Debt/ TNW (times)	1.3	0.7
Total Debt/ OPBDIT (times)	3.7	2.1
Interest coverage (times)	2.8	5.3
NWC/ OI (%)	12%	13%

Source: Company, ICRA research; OPBDITA: Operating Profit before Depreciation, Interest and Taxes; PAT: Profit After Tax; RoCE: Return on Capital Employed; TNW: Tangible Net Worth; NWC: Net Working Capital

*Consolidated financials include financials of TIIL (standalone), Shanthi Gears Limited (SGL), Financiere C10 SAS (FC10), its two joint ventures - TI TSubamex Private Limited (TI Tsubamex) and TI Absolute Concepts Private Limited (TI Absolute Concepts). FY2016 KFIs are based on proforma financials.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2018)				Chronology of Rating History for the past 3 years		
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating January 2018	Date & Rating in FY2017 -	Date & Rating in FY2016 -	Date & Rating in FY2015 Dec 2014
1	Long-term fund based	Long Term	525.00		[ICRA]AA+ (Stable)	-	-	[ICRA]AA (Stable)/ withdrawn
2	Short-term fund based - sublimit	Short Term	(525.00)		[ICRA]A1+	-	-	-
3	Short-term non-fund based	Short Term	500.00		[ICRA]A1+	-	-	-
4	Commercial paper	Short Term	525.00		[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

Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
CC			NA	525.00	**[ICRA]AA+ (Stable)**
EPC / WCDL/ STL/ Buyers Credit				(525.00)	**[ICRA]A1+**
LC/BG				500.00	
Commercial Paper			7-365 Days	525.00	

Source: Tube Investments of India Limited

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About ICRA Limited:

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Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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