

January 24, 2020

Subros Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based -Term Loan	108.15	23.50	[ICRA]AA-(Stable); Reaffirmed
Non-fund Based - Working Capital Facilities	140.00	115.00	[ICRA]A1+; Reaffirmed
Fund-based - Working Capital Facilities	0.00	40.00	[ICRA]AA- (Stable)/[ICRA]A1+; Reaffirmed
Fund-based/ Non-fund Based - Working Capital Facilities	0.00	125.00	[ICRA]AA- (Stable)/[ICRA]A1+; Reaffirmed
Fund-based - Working Capital Facilities	35.00	0.00	-
Non-fund Based - Working Capital Facilities	15.00	0.00	-
Fund-based - Working Capital Facilities	110.00	0.00	-
Total Bank Facilities	408.15	303.50	
Commercial Paper Programme	120.00	75.00	[ICRA]A1+; Reaffirmed
NCD Programme	50.00	50.00	[ICRA]AA-(Stable); Reaffirmed
NCD Programme	100.00	-	[ICRA]AA-(Stable); Withdrawn

*Instrument details are provided in Annexure-1

Rationale

The rating reaffirmation continues to factor in the strong market position of Subros Limited (Subros) in the thermal products segment of the passenger vehicle (PV) industry, benefitting from its integrated manufacturing operations and strong product development capabilities (supported by technical support from Denso Corporation). Despite slowdown in automotive demand leading to lower supplies to the PV segment in the current fiscal, Subros's revenue decline is likely to be lower than the industry, led by an improvement in share of business with its key customer, Maruti Suzuki India Limited (MSIL) (aided by shift in preference towards petrol vehicles). Over the years, while the company's revenue-mix has remained skewed towards the PV segment, over the past few years Subros has also expanded its product range to other segments such as commercial vehicle (CV) original equipment manufacturers (OEMs) and home air conditioner (AC) segments besides the Indian Railways. In H1 FY2020, a ramp up in supplies for the home AC segment (post the acquisition of assets of Zamil Air Conditioners India Pvt. Ltd. in Q1 FY2020) aided the company in reporting only a marginal revenue decline (~2.5% YoY) despite sharp contraction in volumes in its end-user automotive industries. A further ramp up in supplies for new segments is expected to support Subros's medium-term revenue growth prospects and aid diversification.

The rating reaffirmation also favourably factors in Subros's healthy financial risk profile, aided by the infusion of Rs. 209.9 crore by its technology partner, Denso Corporation, Japan, in December 2018. The company continues to maintain a conservative capital structure and strong debt coverage indicators as reflected by TD/TNW of 0.4 time and Interest Coverage Ratio of 6.9 times as on FY2019. This is supported by equity infusion as well as moderate capex, which is likely to remain at moderate levels. During the current fiscal, the company's operating profitability indicators have declined owing to low operating leverage, coupled with a change in product mix, which is likely to result in lower generation of cash flows from operations. It may be noted that the receipt of full and final settlement (Rs. 50.6 crore in Q1 FY2020) of its insurance claim in relation to a fire at its Manesar plant (Haryana) has, however, supported the company's return indicators and helped it maintain a strong liquidity profile (with cash and bank balances of ~Rs. 85.3 crore as of December 31, 2019), which provides comfort.

The company's business profile is characterised by high customer concentration risk with sales to MSIL (including indirect sales) accounting for ~75% of the revenues in H1 FY2020. Although the company faces customer and segment concentration risks, but they are mitigated to an extent by its strong share of business with MSIL and the OEM's market leadership in the PV segment. Moreover, business gains from new segments are also expected to lead to some moderation in the segment and client concentration, going forward.

The Stable outlook on the long-term rating reflects ICRA's expectation that the company's revenue and earnings growth are expected to remain at stable levels over the medium term, supported by continued business awards from MSIL and diversification into new segments. ICRA expects the company to continue to maintain a conservative financial risk profile, reflected in limited incremental dependence on external borrowings.

ICRA notes that the proceeds from the rated commercial paper programme are intended to be utilised for funding the working capital requirements, as per the objects of the issue. Any deviation from the above, which has the effect of exerting pressure on the asset-liability position of the company, would be a rating sensitivity.

Key rating drivers and their description

Credit strengths

Strong market share in thermal products segment for PV industry; ramp up in supplies for other business to aid segment diversification - Subros is a leading automotive AC manufacturer in the domestic market. Despite intense competition in the segment, it has successfully maintained a strong market position (an estimated market share of ~45% in the addressable product range in the PV industry), benefitting from its integrated manufacturing operations and strong product development capabilities (aided by a technical collaboration agreement with Denso Corporation). The company's revenue-mix over the years remained skewed towards the PV segment; however, over the last few years, it has expanded its product range to cater to CV OEMs, besides other segments such as home ACs and the Indian Railways. Although the PV segment is likely to remain the mainstay of the company's business prospects, its dependence is expected to reduce over the medium term as supplies for the new business segments scale up.

Technical collaboration with Denso Corporation strengthens product development capabilities and competitive positioning - Subros has a technical collaboration with Denso Corporation, a leading automotive manufacturer in the global market. The company's strong product development capabilities, coupled with its considerable scale of operations and low-cost structure, has enabled it to sustain a strong market position over the years. Its strong parentage (SMC and Denso Corporation hold ~12% and ~20% equity stakes, respectively)

has also helped it to maintain strong business relations with its primary customer, MSIL, while aiding in establishing relationships with new customers.

Healthy financial risk profile, aided by infusion of equity through preferential share issue to Denso Corporation - Subros received an infusion of Rs. 209.88 crore from the issue of equity shares on preferential basis to Denso Corporation, Japan, in December 2018. The company utilised the equity proceeds for part repayment of its debt and creditors, and continues to maintain healthy cash and bank balances (~Rs. 85.3 crore as of December 31, 2019). The financial risk profile of the entity has improved significantly post the equity infusion, characterised by a conservative capital structure (gearing of 0.4 time as of March 31, 2019) and strong debt coverage indicators (Total Debt/OPBDITA of 1.1 times, interest coverage of 6.9 times and NCA/Total Debt of 65.9% in FY2019). The TOL/TNW, also remains at moderate levels of 1.0 time, despite the significant creditors on the company's balance sheet. With capex requirements expected to remain at moderate levels, the equity infusion coupled with an expectation of improved cash accruals is likely to help improve the company's credit profile considerably, with Total Debt/OPBDITA expected to reduce to levels of 0.6-0.7 time by FY2021.

Credit challenges

High client and segment concentration risks with MSIL driving ~75% of the company's sales - The company remains exposed to increased customer concentration risk with sales to MSIL accounting for ~75% (including indirect sales) of total revenues in H1 FY2020. Although the heavy dependence on MSIL results in high client-concentration risk, the same is mitigated to a large extent by the OEM's market leadership in the PV segment and Subros's strong share of business across various model programmes of the OEM. Subros also remains focussed on reducing its segment and client concentration risk through business gains from new segments, such as CVs, home ACs and the railways.

Moderation in profitability and return indicators likely in the near-term - Subros's operating profitability had remained at stable levels of 10.5-11.0% over the past few years, aided by its efforts to increase its localisation levels for improving operational efficiency. The company's operating profitability in FY2020 is, however, likely to moderate from FY2019 levels (10.8%), led by a decline in operating leverage as well as a change in product mix (with higher contribution from the home AC segment, which entails lower margins). The company's net profits in FY2020 remain supported by an extraordinary profit of Rs. 41.3 crore with regards to the full and final settlement of its insurance claim for the fire accident at its Manesar plant (2016). In the absence of this extraordinary gain, the company's return indicators would have remained at moderate levels of 12-13%. The company's operating profitability and return indicators are expected to gradually expand over the medium-term, benefitting from economies of scale, measures to rationalise costs as well as increased localisation.

Liquidity position: Strong

The liquidity position of the entity remains **strong**, supported by sizeable cash and bank balances (~Rs. 85.3 crore as of December 31, 2019), moderate utilisation of working capital facilities (buffer of ~Rs. 20-30 crore from drawing power) and expectation of stable retained cash flows of ~Rs. 130-140 crore annually (expected to be impacted in FY2020 by weak automotive demand). The company has a planned capex of ~Rs. 50-60 crore per annum, and moderate debt repayments (~Rs. 30.4 crore in FY2021), with its cash flows likely to be adequate to help repay the same in a timely manner.

Rating sensitivities

Positive triggers – A sustained improvement in the company’s operational profile through material diversification of its customer and automotive segment mix could trigger a rating upgrade. A healthier-than-expected improvement in RoCE to over 20% on a sustained basis, would be favourably considered for an upward revision in ratings.

Negative triggers – A rating downgrade could be triggered if there is a significant deterioration in the company’s operational profile led by a decline in share of business (SOB) with key OEMs, especially MSIL. Further, deterioration in profitability indicators or a higher-than-expected capital expenditure or acquisition outlay, which adversely impacts the credit profile of the entity, could trigger a downward revision in ratings. Specific credit metrics that could result in a downgrade include Debt/OPBDITA greater than 2.0 times on a sustained basis or enhanced dependence on short-term borrowings/creditors leading to TOL/TNW weakening above 1.0 time on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Suppliers
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Subros Limited. As on March 31, 2019, the company had a subsidiary and a JV, which are enlisted in Annexure-2.

About the company

Incorporated in 1985, Subros Limited is a leading thermal system manufacturer with the capability to manufacture compressors, condensers, hoses and tubes. The company is promoted by the Suri family, which has a presence across other industries as well (education, hospitality and telecom access products). While the company was initially focused on solely providing cooling solutions for the PV segment, over the years it has gradually expanded its product portfolio to include thermal systems for homes, buses, truck cabin and railway driver cabins.

The company’s manufacturing plants at Noida (Uttar Pradesh), Manesar (Haryana), Pune (Maharashtra), Chennai, Sanand (Gujarat) and Karsanpura (Gujarat) have an annual production capacity of ~2.0 million AC kits. Subros has a technological agreement with Denso Corporation, Japan, a leading automotive manufacturer in the global market. Denso Corporation currently also owns a 20% ownership interest in Subros. Suzuki Motor Corporation (SMC), Japan, also holds a ~12% share in the listed entity, with ~36.8% being held by the Suri family.

Key financial indicators (Consolidated)

	FY2018	FY2019
Operating Income (Rs. crore)	1,912.9	2,124.5
PAT (Rs. crore)	60.6	76.2
OPBDIT/OI (%)	11.0%	10.8%
RoCE (%)	18.7%	20.2%
Total Outside Liabilities/Tangible Net Worth (times)	2.2	1.0
Total Debt/OPBDIT (times)	1.8	1.1
Interest Coverage (times)	5.1	5.4
DSCR	1.7	1.9

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Instrument	Type	Current Rating (FY2020)		Chronology of Rating History for the Past 3 Years					
		Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating 24-Jan-20	Date & Rating in FY2019 19-Dec-18	Date & Rating in FY2018		Date & Rating in FY2017	
						22-Dec-17	19-May-17	22-Dec-16	1-Jun-16
1	Fund-based -Term Loan	23.50	23.50	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+&
2	Non-fund Based - Working Capital Facilities	115.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
3	Fund-based - Working Capital Facilities	40.00	-	[ICRA]AA-(Stable)/[ICRA]A1+	-	-	-	-	-
4	Fund-based/ Non-fund Based - Working Capital Facilities	125.00	-	[ICRA]AA-(Stable)/[ICRA]A1+	-	-	-	-	-
5	Fund-based - Working Capital Facilities	-	-	-	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+&
6	Non-fund Based - Working Capital Facilities	-	-	-	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	[ICRA]A+&
7	Fund-based - Working Capital Facilities	-	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
8	Unallocated Limits	-	-	-	-	[ICRA]A+(Positive)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+	[ICRA]A+&/[ICRA]A1+ &
9	Commercial Paper Programme	75.00	75.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+ &
10	NCD Programme	50.00*	10.00	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	-	-

*Rating withdrawn for Rs. 100 crore NCD programme rated earlier

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 No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan	Jan 2018	-	Feb 2023	23.50	[ICRA]AA-(Stable)
NA	Non-fund Based - Working Capital Facilities	-	-	-	115.00	[ICRA]A1+
NA	Fund-based - Working Capital Facilities	-	-	-	40.00	[ICRA]AA-(Stable)/ [ICRA]A1+
NA	Fund-based/ Non-fund Based - Working Capital Facilities	-	-	-	125.00	[ICRA]AA-(Stable)/ [ICRA]A1+
INE287B14933	Commercial Paper	Oct 2019	-	Jan 2020	25.00	[ICRA]A1+
INE287B14941	Commercial Paper	Nov 2019	-	Feb 2020	25.00	[ICRA]A1+
INE287B14958	Commercial Paper	Nov 2019	-	Feb 2020	25.00	[ICRA]A1+
INE287B07010	NCD Program	Aug 2017	-	April 2020	50.00	[ICRA]AA-(Stable)

Source: Subros Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Thai Subros Limited	100.00%	Full Consolidation
Denso Subros Thermal Engineering Centre India Limited	26.00%	Equity Method

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