Pursuant to SEBI notifications, CRISIL Limited (CRISIL) has transferred its Ratings business to its wholly owned subsidiary, CRISIL Ratings Limited (CRISIL Ratings), with effect from December 31st 2020. Any reference to CRISIL in the documents published by the Ratings division of CRISIL, such as Rating Rationales, Credit Rating Reports, Press Releases, Criteria, Methodology, FAQs, Policies and Disclosures, shall henceforth refer to CRISIL Ratings.

Rating Rationale

May 07, 2020 | Mumbai

Sundaram-Clayton Limited

'CRISIL AA-/Stable/CRISIL A1+' assigned to debt instruments

Rating Action

Total Bank Loan Facilities Rated	**Rs.708.56 Crore**
Long Term Rating	**CRISIL AA-/Stable (Reaffirmed)**
Short Term Rating	**CRISIL A1+ (Reaffirmed)**

Rs.100 Crore Non Convertible Debentures	**CRISIL AA-/Stable (Assigned)**
Rs.100 Crore Commercial Paper	**CRISIL A1+ (Assigned)**

1 crore = 10 million
Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL has assigned its **'CRISIL AA-/Stable/CRISIL A1+'** ratings to the Rs.100 crore non-convertible debentures and Rs.100 crore commercial paper of Sundaram-Clayton Limited (SCL). CRISIL has also reaffirmed its ratings on the bank facilities at 'CRISIL AA-/Stable/CRISIL A1+.

Fiscal 2020 has been a challenging year for the Indian automobile industry amidst a wider consumption slowdown, liquidity crunch and transition to stringent BS-VI emission norms. The situation was further aggravated due to the spread of Coronavirus (N-Covid 19) in the last quarter of fiscal 2020 in both domestic and overseas markets.

SCL's revenues declined by 28% during nine-month period of fiscal 2020 over the corresponding previous period due to lower off-take from original equipment manufacturers (OEM) in line with the volume decline in the end markets (both domestic and exports). Operating profitability during this period, however improved to 12.1% compared to 9.3% during the comparable period of the previous year due to internal cost optimization measures and transition benefits of declining input prices.

CRISIL expects SCL's business performance to remain subdued in fiscal 2021 as well due to Covid induced slowdown leading to continued decline in off-take from original equipment manufacturers (OEMs) in both domestic and export markets. However, performance should gradually revive over the medium term with expected demand recovery from OEMs in fiscal 2022 coupled with increased offtake from new customers. Besides, despite the potential decline in volumes, operating margins should also remain stable at around 9-11% benefitting from various cost reduction initiatives taken by the company, thereby lending stability to the business risk profile.

SCL's financial risk profile and liquidity are expected to remain healthy, despite moderation in cash accruals, owing to reduced capital expenditure (around Rs 25-30 Cr per annum), prudent working capital management and stable dividend income from TVS Motor Company Ltd (TVS Motor). CRISIL also factors in the significant market value of SCL's 57% holding in TVS Motor, moderate bank line utilisation and SCL's ability to raise debt at competitive interest rates and flexible repayment periods from banks.

CRISIL's ratings on the bank facilities of Sundaram-Clayton Ltd (SCL) continue to reflect the company's diverse customer base across automobile sub-segments and geographies, and adequate operating efficiency. These strengths are partially offset by high revenue dependence on the cyclical CV segment, and on original equipment manufacturers (OEMs), which limits pricing power; and exposure to increasing competition.

Analytical Approach

For arriving at its rating, CRISIL has considered SCL's standalone business and financial risk profiles, and has not combined the business and financial risk profiles of TVS Motor and other investment subsidiaries as they are in different business lines. Need-based financial support has been factored in case of investment subsidiaries. Also, financial flexibility arising from sizeable value of stake in TVS Motor has been factored into the rating assessment of SCL.

In fiscal 2013, SCL entered into a non-cancellable sale and lease-back agreement for assets of Rs.84 crores. The assets comprise customised machinery. CRISIL has, therefore, considered the transaction as a financial lease, and capitalised the present value of SCL's future lease rental obligations as fixed assets. Accordingly, the lease rental payable every year has been bifurcated into interest and depreciation for analysing SCL's financials.

Key Rating Drivers & Detailed Description

Strengths:

*** Diverse customer base, spread across automotive sub-segments and geographies**

SCL's customer base is diverse, spread across sub-segments of the auto sector, such as two-wheelers, passenger cars, and CVs, and across geographies. Healthy demand growth from two-wheeler and domestic CV segment in fiscal 2018, and for most of fiscal 2019, has enabled good growth in domestic volumes for SCL, besides offsetting impact of sluggish demand from passenger vehicle OEMs. Albeit, a moderation in aluminium prices in recent months (which is a pass through) has impacted realisations. The company has enhanced its production capacity, including for passenger OEM customers, which should enable it capture market share during a potential recovery from fiscal 2022. Albeit, fiscal 2021 is expected to witness temporary volatility in volumes in both domestic and export markets due to the Covid impact and continued lower capacity utilization rates.

Healthy share of exports also enhances SCL's revenue and geographic diversity. While the company's share of export revenue declined to 35-37% in fiscals 2017 and 2018, from over 40% in fiscal 2016 due to sluggish demand from European customers, better demand from US markets helped exports recover to over 40% of revenues in fiscal 2019. However, export growth in fiscal 2020 is expected to be moderate due to a gradual moderation in CV growth rates in the USA, and continued muted demand from Europe.

Presence across sub-segments and geographies, partially offsets the impact of cyclicality inherent in the business. The diverse customer base and increased demand from export as well as domestic customers, and increased contribution from recently expanded capacities should support revenue growth over the medium term.

*** Adequate operating efficiencies**

Operating profitability has been largely stable at 9-12% since fiscal 2010 (except a temporary blip in fiscal 2018), backed by ability to pass on changes in raw material prices onto end customers. Implementation of industry-wide best practices, such as Total Quality Management, enterprise resource planning and other internal automation measures, help products meet the rigorous standards of the top global auto manufacturers. Despite limited technological collaboration, SCL has maintained steady business with most customers, on the back of its adequate operating capabilities. During fiscal 2020, SCL has implemented proactive cost optimization measures in low cost automations, employee consolidation, recycling of materials etc. which has facilitated better cost management during the downturn.

*** Adequate financial risk profile and healthy financial flexibility**

SCL's financial risk profile is adequate marked by healthy net worth (Rs 686 crore in fiscal 2019), comfortable capital structure and debt protection metrics. SCL had undertaken large capital expenditure in fiscals 2018 and 2019 which was partly funded through debt. This in turn led to moderation in capital structure with gearing increasing to 1.06 times as of March 31, 2019. However, with completion of the large capex in fiscal 2019 and only nominal capital spends expected over the next two fiscals, gearing should remain less than 1 time over the medium term, with progressive repayment of debt obligations. Debt protection metrics like interest cover and net cash accruals to total debt (NCATD) ratios should also sustain at over 4-5 times and 0.15-0.20 times respectively over the medium term (as compared to 5.2 times and 0.22 times respectively in fiscal 2019) albeit temporary moderation expected in fiscal 2021 due to the moderation in business cash flows. Besides, strong re-financing capabilities arising from SCL's investment in TVS Motor (market value of over Rs 8,900 crore as on April 30, 2020) enhance its financial flexibility, while steady dividend flows from TVS Motor support SCL's cash accruals, besides partially mitigating impact of volatile business cash flows.

Weaknesses:

*** Significant exposure to cyclical CV segment:**

SCL has a high exposure to the CV segment given that it almost derives its entire export revenues from the CV segment, although the domestic customer base is spread across automotive industry sub-segments. Any cut in production schedules by key CV customers could result in a decline in capacity utilisation, and return on capital employed (RoCE), especially with specific lines being devoted to key customers.

While SCL has enhanced its production capacity and hence will be able to manage sudden surge in offtake by customers over the medium term, it remains vulnerable to cyclical offtake mainly by the CV segment, which could affect both revenue and profitability.

*** Susceptibility to pricing pressure from OEMs**

SCL is highly dependent on offtake by Tier-I auto component suppliers as well as OEMs, in both the domestic and export markets. High exposure to OEMs exposes the company to significant pricing pressure. While SCL is able to pass on key raw materials costs to its customers, it has limited flexibility in passing on increase in conversion costs like power costs, employee costs etc., although the continuous cost control measures and process improvements over the years have partly mitigated the impact.

Liquidity Strong

Liquidity is strong largely supported by steady cash accrual (estimated annually at over Rs.80-120 crore) and adequate headroom in bank lines (average utilization of about 26% on sanctioned bank limits of Rs 861 crore over the last 12 months ended March 2020). Accruals in fiscal 2021 will remain inadequate to meet higher repayment obligations at over Rs.150 crore in fiscal 2021, which will require part refinancing. Nevertheless, refinancing risk is expected to be limited considering SCL is the majority stakeholder in India's fourth-largest motorcycle manufacturer, TVS Motor; with market value of SCL's investments in TVS Motor (about Rs 8,900 crore as on April 30th, 2020) substantially enhancing financial flexibility. CRISIL believes SCL is unlikely to dilute its stake in TVS Motor; the market value of the stake will continue to underpin SCL's financial flexibility, in addition to providing steady dividend income.

Outlook: Stable
CRISIL believes that despite business challenges which are expected to continue in fiscal 2021, SCL's credit risk profile will continue to remain supported by its diversified business risk profile and adequate financial risk profile. Moreover, its financial flexibility remains strong, supported by material market value of its holdings in TVS Motor.

Rating Sensitivity factors
Upward factors:
* Compounded annual revenue growth of 12-15% over the medium term driven by increased market share in both domestic and overseas markets.
* Stronger than anticipated growth in cash accruals (over Rs.200 crore annually) on sustained basis, supported by improved business performance
* Prudent capital spending and working capital management, which along with routine debt repayment and better cash accruals would strengthen credit metrics; for instance, gearing to under 0.5 times

Downward factors:
* Further deterioration in revenues owing to continued slowdown in demand from domestic and export markets, and decline in operating margins to less than 7% owing to sub-optimal capacity utilization and higher overheads
* Large debt funded capex or acquisition or significant stretch in working capital levels denting capital structure; for instance, gearing deteriorating to over 1.5 times.

About the Company
SCL was incorporated in Chennai in 1962 and is part of the TVS group led by Mr. Venu Srinivasan. The company is a leading manufacturer of aluminium die-casting components. It supplies to major automotive OEMs including TVS Motor, the Cummins group, the Volvo group, Hyundai Motor India Ltd (rated 'CRISIL A1+), Ford Motors, the Daimler group, and to component suppliers such as Wabco India Ltd and the Visteon group. SCL was set up by the TVS group and the UK-based Clayton Dewandre Holdings Ltd. The TVS group holds 75% stake in SCL, with the balance held by mutual funds (12%), public, and others.

Until fiscal 2007, SCL's financials included the CV brakes business. With effect from March 28, 2008, the Madras High Court approved the de-merger of the brakes business into a separate company, Wabco India Ltd. The non-brakes business (aluminium die-casting) and investments in the TVS group entities remained with SCL. The company has its main die-casting component production facilities at Padi, Mahindra City, and Oragadam in Chennai, and Belagondapalli at Hosur, in Tamil Nadu. During fiscal 2012, SCL restructured its businesses, hiving off the non-automotive businesses into its erstwhile subsidiary, Sundaram Investments Ltd (SIL).

For the first nine months of fiscal 2020, SCL's profit after tax (PAT) was Rs. 7 crore on net sales of Rs. 1,023 crore, against PAT of Rs. 69 crore on net sales of Rs. 1,426 crore for the corresponding period of previous fiscal.

Key Financial Indicators

As on/for the period ended March 31	Unit	2019	2018
Revenue	Rs.Crores	1833	1643
Profit after tax (PAT)	Rs.Crores	120	55
PAT margins	%	6.5	3.3
Adjusted debt/adjusted networth	Times	1.06	1.04
Interest coverage	Times	5.2	3.4

Any other information: Not applicable

Note on complexity levels of the rated instrument:
CRISIL complexity levels are assigned to various types of financial instruments. The CRISIL complexity levels are available on www.crisil.com/complexity-levels. Users are advised to refer to the CRISIL complexity levels for instruments that they consider for investment. Users may also call the Customer Service Helpdesk with queries on specific instruments.

Annexure - Details of Instrument(s)

ISIN	Name of Instrument	Date of Allotment	Coupon Rate (%)	Maturity Date	Issue Size (Rs cr.)	Rating Assigned with Outlook
NA	Bank Guarantee	NA	NA	NA	6	CRISIL A1+
NA	Cash Credit#	NA	NA	NA	210	CRISIL AA-/Stable
NA	External Commercial Borrowings	NA	NA	Feb-2024	172.56	CRISIL AA-/Stable
NA	FCNR (B) Long Term Loan	NA	NA	Sep-2022	145	CRISIL AA-/Stable
NA	Letter of Credit	NA	NA	NA	75	CRISIL A1+
NA	Rupee Term Loan	NA	NA	Dec-2022	100	CRISIL AA-/Stable
NA	Non-Convertible Debentures*	NA	NA	NA	100	CRISIL AA-/Stable
NA	Commercial Paper	NA	NA	7-365 days	100	CRISIL A1+

#Interchangeable with packing credit in foreign currency (PCFC)/Bills Discounting/Short Term Loans
**Not yet Issued*

Annexure - Rating History for last 3 Years

	Current			2020 (History)		2019		2018		2017		Start of 2017
Instrument	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Commercial Paper	ST	100.00	CRISIL A1+		--		--		--		--	--
Non Convertible Debentures	LT	0.00 07-05-20	CRISIL AA-/Stable		--		--		--		--	--
Fund-based Bank Facilities	LT/ST	627.56	CRISIL AA-/Stable			24-12-19	CRISIL AA-/Stable	18-01-18	CRISIL AA-/Stable			CRISIL AA-/Stable
						06-02-19	CRISIL AA-/Stable					
Non Fund-based Bank Facilities	LT/ST	81.00	CRISIL A1+			24-12-19	CRISIL A1+	18-01-18	CRISIL A1+			CRISIL A1+
						06-02-19	CRISIL A1+					

All amounts are in Rs.Cr.

Annexure - Details of various bank facilities

Current facilities			Previous facilities		
Facility	Amount (Rs.Crore)	Rating	Facility	Amount (Rs.Crore)	Rating
Bank Guarantee	6	CRISIL A1+	Bank Guarantee	6	CRISIL A1+
Cash Credit#	210	CRISIL AA-/Stable	Buyer`s Credit*	40	Withdrawn
External Commercial Borrowings	172.56	CRISIL AA-/Stable	Cash Credit#	210	CRISIL AA-/Stable
FCNR (B) Long Term Loan	145	CRISIL AA-/Stable	Cash Credit#	25	Withdrawn
Letter of Credit	75	CRISIL A1+	External Commercial Borrowings	172.56	CRISIL AA-/Stable
Rupee Term Loan	100	CRISIL AA-/Stable	FCNR (B) Long Term Loan	145	CRISIL AA-/Stable
--	0	--	Letter of Credit	75	CRISIL A1+
--	0	--	Letter of Credit	75	Withdrawn
--	0	--	Proposed Long Term Bank Loan Facility	103.24	Withdrawn
--	0	--	Rupee Term Loan	100	CRISIL AA-/Stable
Total	708.56	--	Total	951.8	--

#Interchangeable with packing credit in foreign currency (PCFC)/Bills Discounting/Short Term Loans
**Interchangeable with cash credit*

Links to related criteria
CRISILs Approach to Financial Ratios
CRISILs Bank Loan Ratings - process, scale and default recognition
Rating criteria for manufaturing and service sector companies
Rating Criteria for Auto Component Suppliers
CRISILs Criteria for rating short term debt

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