August 04, 2022

Shanthi Gears Limited: Ratings reaffirmed at [ICRA]AA (Stable)/[ICRA]A1+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit	1.00	1.00	[ICRA]AA (Stable); reaffirmed
Long term non-fund based	30.00	28.00	[ICRA]AA (Stable); reaffirmed
Short term- Interchangeable	(28.00)	(11.00)	[ICRA]A1+; reaffirmed
Short term fund based	-	2.00	[ICRA]A1+; reaffirmed
Total	**31.00**	**31.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation factors in Shanthi Gears Limited's (SGL/the company) strong parentage by virtue of being a subsidiary of Tube Investments of India Limited (TIIL, rated [ICRA]AA+(Stable)/[ICRA]A1+) and its healthy financial profile characterised by nil borrowings and sizeable cash and liquid investments of Rs. 94.4 crore, in addition to investments in tax free bonds to the tune of Rs. 22.2 crore as on March 31, 2022. The company's operating margins for FY2022 were also healthy at 17.9% aided by operating leverage and cost optimisation initiatives, despite the impact of commodity inflation. Further, the ratings draw comfort from SGL's established presence in the industrial gears segment across various sectors and its diversified client portfolio.

SGL continues to have a moderate scale, with an operating income (OI) of Rs. 337.1 crore in FY2022, despite healthy improvement over the years. While close linkage to capex cycles exposes revenues to cyclicality in end-user industries, considerable share of revenues from the replacement segment and presence across multiple segments with no segment contributing to more than 30% of the revenues in FY2022, mitigate the risk to an extent. Further, the company had healthy pending order book of Rs. 280 crore as on March 31, 2022. While SGL's margins are exposed to volatility in raw material prices and competitive pressures, it would benefit from better absorption of costs as revenues scale going forward.
With no major debt-funded capex plans in the medium term, ICRA expects the company's debt coverage metrics and liquidity to remain strong.

Key rating drivers and their description

Credit strengths

Strong parentage – TIIL, the flagship company of the Murugappa Group, acquired 70.12% stake in SGL in 2012. Ever since, the company has benefitted from the strong management support and the operational synergies derived as a subsidiary of TIIL. On April 9, 2019, SGL undertook a share buyback of 50 lakh equity shares, following which TIIL's stake has increased to 70.47%.

Strong financial profile characterised by healthy margins, sizeable cash and liquid investments and nil borrowings – The company's operating margins for FY2022 stood at 17.9% (PY: 12.5%) aided by operating leverage and cost optimisation initiatives, despite the impact of commodity inflation. Adjusted for Q1 FY2021 impact, the margins grew by 160 bps on YoY basis for Q2-Q4 FY2022. Also, SGL has remained debt free since FY2013, primarily aided by healthy cash flows from operations (Rs. 31.7 crore in FY2022) and sizeable cash and liquid investments (Rs. 94.4 crore as on March 31, 2022). Besides, it has investments worth Rs. 22.2 crore in tax-free bonds. Consequently, the company has strong capital structure and healthy

coverage metrics. Further, with no major debt-funded capex plans in the medium term, SGL's capital structure and debt coverage metrics are expected to remain comfortable going forward as well.

Healthy order book providing revenue visibility to an extent– SGL's pending order book position stood at Rs. 280 crore (PY: Rs. 225.0 crore) as on March 31, 2022, supported by demand from both OEM and replacement segments. The healthy order book provides revenue visibility for the next few quarters.

Established presence in industrial gears; diversified clientele and end-use sectors support revenue stability – SGL has extensive presence in the industrial gears segment for five decades and caters to a reputed clientele from diversified sectors such as general engineering, steel, cement, railways, power and material handling, among others. It has a diversified client base with its top 10 customers accounting for only one-fifth of its revenues in FY2022, thereby insulating its revenues from the customer concentration risk.

Credit challenges

Moderate scale of operations – The company has a moderate scale of operations with revenue of Rs. 337.1 crore in FY2022, despite healthy improvement. A higher scale would enhance resilience to volatility in demand and enable better cost absorption. Nevertheless, the company's pending order book position of Rs. 280 crore as on March 31, 2022 and healthy demand prospects for industrial gears are likely to support revenue growth, going forward.

Close linkage to capex cycle exposes revenues to cyclicality in end-user industries – SGL's revenues are exposed to the cyclicality in the domestic capex cycles and any economic slowdown could impact its revenues as witnessed earlier. However, considerable share of revenues from the replacement segment and presence across multiple segments with no segment contributing to more than 30% of the revenues in FY2022, mitigate the risk to an extent.

Margins susceptible to fluctuations in raw material prices – SGL's major raw materials include steel and steel components. The company's margins are susceptible to fluctuations in raw material prices, given its limited pricing flexibility for procured orders. Nonetheless, SGL's ability to pass through the increase in raw material prices in new orders and advance procurement of raw material for the existing orders mitigates the risk to an extent. Further, the company's margins are also likely to benefit from the operating leverage, although competitive pressures remain. While the company's proportion of raw material costs increased in FY2022 with multi-year high steel prices during the year, the recent softening of commodity prices is likely to provide some relief.

Liquidity position: Strong

SGL's liquidity position remains **strong** with a healthy cash flow from operations of Rs. 31.7 crore in FY2022, and cash and liquid investments of Rs. 94.4 crore as on March 31, 2022. Besides, it has investments of Rs. 22.2 crore in tax-free bonds. The company has remained debt free and the fund-based working capital utilisation has been nil over the last nine years. In relation to these sources of cash, SGL has moderate capex plans for FY2023 and FY2024 and does not have any debt repayment obligations. Further, it enjoys strong financial flexibility and lender comfort as a subsidiary of TIIL and as part of the well-established Murugappa Group. This is expected to continue going forward as well.

Rating sensitivities

Positive factors – ICRA could upgrade SGL's ratings if it demonstrates significant growth in its scale of operations and earnings, while sustaining its healthy debt protection metrics and liquidity profile.

Negative factors – Negative pressure on the company's ratings could arise if it witnesses a sharp deterioration in its earnings or significant rise in net debt; or weakening in the parent's credit profile or SGL's operational/financial linkages with the parent, TIIL.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	Tube Investments of India Limited (TIIL, rated [ICRA]AA+(Stable)/[ICRA]A1+ holds 70.47% in SGL.
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company.

About the company

Commencing its business as a gear manufacturer for the textile industry in 1969, SGL diversified into manufacturing standard (off-the-shelf) and customised (non-standard) gears over the years. It caters to a reputed clientele from diversified sectors such as general engineering, steel, cement, railways, power and material handling, among others. SGL's product portfolio encompasses a range of customised gear boxes, loose gears, worm gear boxes and helical gear boxes. It has manufacturing facilities (including a foundry) located in and around Coimbatore, Tamil Nadu. The company was founded in 1969 by Mr. P Subramanian, a first-generation entrepreneur from Coimbatore. In July 2012, Murugappa Group's TIIL (rated [ICRA]AA+ (Stable)/ [ICRA]A1+) announced the acquisition of the promoter's entire 44.12% stake in SGL. The acquisition was completed in September 2012. Subsequently, by tendering an open offer, TIIL increased its stake in the company to 70.12%. In April 2019, the company bought back shares, increasing TIIL's shareholding to 70.47%. Following the acquisition, SGL is now a subsidiary of TIIL, with minority shareholding by public and financial institutions.

Key financial indicators

Standalone	FY2021	FY2022
Operating Income (Rs. crore)	215.5	337.1
PAT (Rs. crore)	20.2	42.5
OPBDIT/OI (%)	12.5%	17.9%
PAT/OI (%)	9.4%	12.6%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.3
Total Debt/OPBDIT (times)	-	-
Interest Coverage (times)	112.0	251.2

Source: *Company, ICRA Research; Note: Amounts in Rs. crore; Financial ratios in the report are ICRA adjusted figures and may not be directly comparable with results reported by the company in some instances*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of March 31, 2022 (Rs. crore)	Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					Aug 04, 2022	Jul 05, 2021	Jun 15,2020	Jul 05,2019
1	Cash Credit	Long term	1.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
2	Non-fund based limits	Long term	28.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
3	Interchangeable	Short term	(11.00)	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Fund based	Short term	2.00	-	[ICRA]A1+	-	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+

Complexity level of the rated instrument

Instrument	Complexity Indicator
Long-term Fund-based – Cash Credit	Simple
Long term non-fund based	Very Simple
Short term- Interchangeable	Very Simple
Short term Fund based	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's 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	Cash Credit	NA	NA	NA	1.00	[ICRA]AA (Stable)
NA	Non-fund based limits-Long term	NA	NA	NA	28.00	[ICRA]AA (Stable)
NA	Interchangeable – Short term	NA	NA	NA	(11.00)	[ICRA]A1+
NA	ST- fund-based facilities	NA	NA	NA	2.00	[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis – Not applicable

ANALYST CONTACTS

Shamsher Dewan
+91-124-4545 328
shamsherd@icraindia.com

Srikumar K
+91-44-4596 4318
ksrikumar@icraindia.com

Vinutaa S
+91-44-4596 4305
vinutaa.s@icraindia.com

Rashmi Gole
+91-20-6606 9917
rashmi.gole@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@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.

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.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches

© Copyright, 2022 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.