**January 06, 2022**

# Siechem Technologies Pvt. Ltd.: Ratings upgraded to [ICRA]A (Stable)/[ICRA]A1

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Fund based facilities | 81.00 | - | - |
| Fund/Non Fund-based facilities | - | 101.00 | [ICRA]A (Stable); upgraded from [ICRA]A- (Stable) |
| Interchangeable Limits | (10.00) | (5.00) | [ICRA]A (Stable); upgraded from [ICRA]A- (Stable) |
| Interchangeable Limits | - | (5.00) | [ICRA]A1; upgraded from [ICRA]A2+ |
| Non-fund based facilities | 47.00 | 27.00 | [ICRA]A1; upgraded from [ICRA]A2+ |
| Long-term/Short-term, Unallocated facilities | 126.00 | - | - |
| **Total** | **254.00** | **128.00** | |

**Instrument details are provided in Annexure-1*

## Rationale

The rating upgrade of Siechem Technologies Private Limited (STPL) favourably factors in the expected increase in turnover and profits in FY2023, supported by pent-up demand for e-beam cables from the Indian Railways and scheduled commissioning of a new manufacturing facility at Sedarapet in Q1 FY2023, which will increase the production capacity by ~75%.

ICRA notes that the Indian Railways remain the largest consumer of e-beam cables, accounting for around 60% of the domestic demand. Given the operational disruption experienced by the railways following the pandemic, the overall production of coaches and locomotives decreased by ~34% year-on-year (YoY) in FY2021, which in turn led to STPL reporting a 33% YoY decline in turnover last fiscal. However, the tendering pipeline from the railways remain healthy, with a combined locomotive production target of 9,096 units and 8,236 units in FY2022 and FY2023, respectively, matching the pre-Covid high of 8,342 units produced in FY2020.

ICRA's channel checks suggest that bulk of the execution of these orders are likely to spill over to FY2023, which would help STPL to comfortably surpass its pre-Covid level of performance next fiscal. In addition, ICRA expects STPL's Sedarapet facility to increase its footprint among auto consumers, which is an important growth avenue for the company, especially in the emerging electric vehicle segment.

The ratings also favourably factor in the experience of the company in specialty cables manufacturing and its diversified customer profile across several industries such as railways, automobile, marine and solar. ICRA notes that ~90% of STPL's product profile consists of specialty-grade cables which fetch better margins. This has kept STPL's operating profit margins at a healthy range of 18.5-25.4% over the last few years, which is significantly better than the industry average. Notwithstanding the 33% YoY decline in turnover last fiscal, STPL's operating margin improved to 25.4% in FY2021 from 19.0% in FY2020, supported by various cost control measures, notably the full waiver of director remuneration amounting to Rs. 16.6 crore during the period.

The ratings are further supported by a healthy financial risk profile with a demonstrated ability to report profits across business cycles, a comfortable gearing, healthy debt coverage indicators and a strong liquidity profile supported by sizeable cash & liquid investment balance of Rs. 233.23 crore as on November 30, 2021 and a healthy buffer in working capital limits. ICRA notes that the company has recalibrated its capex plan owing to the delay in approvals for its greenfield project at Vedavakkam. The company is now in the process of setting up a much smaller facility at Sedarapet (one third of the capacity planned at Vedavakkam) at an investment which is less than 50% of the planned capex at Vedavakkam. The Sedarapet capex is expected to be funded entirely through internal accruals against the debt-funded capex plan at Vedavakkam, supporting STPL's financial risk profile going forward.

The ratings are, however, constrained by the company's exposure to product concentration risks with a sizeable chunk of its earnings being contributed by e-beam cables, and the susceptibility of STPL's margins to the volatility in raw material prices, especially for copper and insulation compounds. ICRA notes that the input costs have spiked sharply in the current fiscal, which would be difficult for domestic cable and wire manufacturers to completely pass on to their customers. This would mean that the operating profit margins for STPL is expected to decline sequentially in FY2022. Additionally, with several new players entering the e-beam manufacturing industry recently, the competitive intensity is expected to increase. This makes ICRA believe that STPL's margins are likely to temper from its previous levels. Absolute growth in earnings would largely emanate from STPL's ability to get a larger pie of the incremental demand for e-beam cables by tapping into the requirements of emerging demand centres and developing products having a higher technical specification. In this context, ICRA notes that STPL has received customer approvals for supplying e-beam cables to the rapidly growing electric vehicle and metro railway coach manufacturing segments, where competition is low. The ratings are also constrained by STPL's stretched receivables and consequently elevated working capital intensity due to its low bargaining power with large institutional customers.

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that STPL will maintain its conservative capital structure and strong liquidity profile going forward, and its revenue growth will be supported by the healthy pipeline of orders from the railway and automobile sectors.

## Key rating drivers and their description

### Credit strengths

**Expected increase in turnover and profits in FY2023 –** The installation of the electron beam accelerator facility has given the company an early-mover advantage and it has got the recognition of being an approved vendor of the Indian Railways. Today, STPL is the largest domestic supplier of e-beam cables to the Indian Railways. The turnover declined in FY2021 owing to lower production of locomotives and coaches by the railways due to the pandemic. However, the order flow has picked up in the current fiscal due to pent-up demand and STPL's turnover is expected to increase in FY2023. Also, to tap the sales potential of the auto sector, the company has decided to set up a manufacturing facility at Sedarapet, Puducherry. This will help increase its scale of operation through new customer acquisitions.

**Established player with considerable experience in cable manufacturing** - Incorporated in 1994, STPL commenced commercial production of specialty cables in 2002. Initially, the company manufactured and marketed jelly-filled cables, which were used in the telecom industry. The company was one of the early adaptors of the electron beam irradiation technology among domestic players used to cure insulation compound for enhancing its abrasion resistance, thermal resistance, flame-propagation resistance and deformation resistance. This brings down the risks of fire from short-circuits, which has been the key reason for the adoption of e-beam cables in the railways, automobiles and marine sectors. Early technology adoption, extensive management experience and in-house research facilities have helped the company to improve quality, control costs and provide customised products, helping it gain new customers over the years.

**Reputed and diversified customer base across various end-user industries** - The company has a diversified customer base across various end-user industries such as railways, solar energy, automotive, marine and aerospace. The customer concentration is moderate, with the top 10 customers accounting for 50% of the sales in FY2021. The company is one of the approved vendors designated by the Research Design and Standards Organisation (RDSO), which allows it to participate in Indian Railways' orders, and enjoys a healthy market share in this segment. Due to its proven track record in the industry, the company gets repeat orders from many customers. Apart from the railways, the company is gradually increasing its revenue share in the automobile and solar sectors. In this context, ICRA notes that STPL has received customer approvals for supplying e-beam cables to the rapidly growing electric vehicle and metro railway coach manufacturing segments, where competition remains low.

**Healthy financial risk profile characterised by healthy profitability and strong debt coverage metrics –** Around 90% of STPL's product profile consists of specialty-grade cables which fetch better margins. This has kept STPL's operating profit margins at a healthy range of 18.5 – 25.4% over the last few years, which is significantly better than the industry average. Notwithstanding the 33% YoY decline in turnover last fiscal, STPL's operating profit margins improved to 25.4% in FY2021 from 19.0% in FY2020, supported by various cost-control measures, notably the full waiver of director remuneration amounting to Rs. 16.6 crore during the period. The company's business return indicators remain attractive, as reflected in a core ROCE of 46.12% in FY2021. Further, STPL has been prudent in funding its expansions largely through internal accruals. Therefore, its external borrowings are limited to its working capital lines and loan from related parties (which remained stable for a long period). This, coupled with the strong growth in its net worth, resulted in a low gearing of 0.21 times as on March 31, 2021. Moreover, STPL's coverage indicators remained healthy with a total debt/OPBDITA of 0.85 times, interest coverage of 40.89 times and debt service coverage ratio (DSCR) of 29.22 times in FY2021.

## Credit challenges

**Product concentration risk with a sizeable chunk of earnings being contributed by the electron beam cables –** The share of specialty grade cables (mostly comprising e-beam cables) in the company's revenue mix has been ~90% in the last three fiscals. Although a high revenue share from e-beam cables has supported STPL's above-average operating margins, it makes the company highly dependent on the demand for one product segment. Any weakening in the demand prospects for e-beam cables in the country would lead to plummeting sales and a painful readjustment.

**Vulnerability of profitability to volatility in raw material prices** - Copper and aluminium are the main raw materials used by the company and account for 80-90% of the overall raw material expenses. While STPL fixes the raw material prices with its suppliers when it gets an order, the profit margin remains susceptible to the volatility in raw material prices because of constrained pricing flexibility, intense industry competition and limited bargaining power with customers. The company is also exposed to high supplier concentration as the Vedanta Group is the major supplier of copper. Earlier, the Sterlite factory at Tuticorin was the major supplier but after its closure in Q1 FY2019, the Group has managed to get copper from other locations and there have been no supply disruptions. Nonetheless, to mitigate the risk, STPL has also started sourcing the product from other suppliers.

ICRA notes that the input costs have spiked sharply in the current fiscal, which would be difficult for domestic cable and wire manufacturers to completely pass on to their customers. This would mean that STPL's operating profit margins are expected to decline sequentially in FY2022. Additionally, with several new players entering the e-beam manufacturing industry recently, the competitive intensity is expected to increase. This makes ICRA believe that STPL's margins are likely to temper from its previous levels. Absolute growth in earnings would largely emanate from STPL being able to get a larger pie of the incremental demand for e-beam cables by tapping into the requirements of the emerging demand centres and developing products having a higher technical specification.

**High working capital intensity -** The company's operations are working capital intensive because of stretched receivable days. The receivable days were in the range of 120 to 170 days over the last few years, which impacted the working capital metrics. The impact is partly mitigated by a flexible credit period, varying from ~50-100 days, it receives from its suppliers. The average inventory holding period is 50-60 days, although the year-end inventory levels are lower.

## Liquidity position: Strong

ICPL's liquidity is expected to remain strong, evident from its track record of healthy free cash flow generation, its sizeable free cash balance and nil scheduled debt repayment obligation. However, STPL's free cash flow is expected to slip in the negative territory in FY2022 and FY2023 as the company will need to fund the working capital requirement as well as the ongoing capex for the new unit at Sedarapet to cater to the growing demand. The company will be financing this deficit from its on-balance sheet available liquidity, keeping its debt levels under check. The company has an overall fund-based working capital limit of Rs. 76.00 crore (reduced from Rs. 91.00 crore in October 2021) and the average utilisation of the bank limits stood low at 34% during November 2020 and October 2021.

### Rating sensitivities

**Positive factors –** ICRA could upgrade the ratings if the operations of the upcoming manufacturing facility stabilise, leading to an increase in scale and overall earnings, while maintaining healthy credit metrics and a strong liquidity profile.

**Negative factors –** Downward pressure on the ratings could emerge if there is a deterioration in the financial profile due to a significant decline in operating profit margins or if a stretch in the working capital cycle adversely impacts the overall liquidity. The ratings could also come under pressure if an elevated level of debt-funded capex weakens the credit metrics. Specific credit metrics that could lead to a rating downgrade is a net debt/OPBDITA being greater than 2.3 times on a sustained basis.

### Analytical approach

| Analytical Approach | Comments |
|---|---|
| **Applicable Rating Methodologies** | Corporate Credit Rating Methodology |
| **Parent/Group Support** | Not Applicable |
| **Consolidation/Standalone** | Standalone |

## About the company

STPL was incorporated in 1994 and was promoted by Mr. P Damodaran and his wife Ms. Padma Damodaran. The company began the production of specialty wires and cables from 2002. It has a manufacturing facility in Puducherry with a capacity of 15-20 MT per day and uses the electron beam irradiation technology for cable curing. STPL set up its first e-beam accelerator machine in FY2009. In FY2015, the company set up its second electron beam accelerator to diversify into the railway business. Initially, the company catered specifically to the telecom industry but over the years it has diversified its customer base across several industries, with the railways being a major customer segment.

### Key financial indicators

| STPL (Standalone) | FY2020 (Audited) | FY2021 (Provisional) |
|---|---|---|
| Operating Income (Rs. crore) | 527.87 | 351.42 |
| PAT (Rs. crore) | 77.57 | 55.85 |
| OPBDIT/OI (%) | 19.01% | 25.42% |
| PAT/OI (%) | 14.69% | 15.89% |
| Total Outside Liabilities/Tangible Net Worth (times) | 0.18 | 0.21 |
| Total Debt/OPBDIT (times) | 0.55 | 0.85 |
| Interest Coverage (times) | 50.75 | 40.89 |

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation*

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

# Rating history for past three years

| | Instrument | Current Rating (FY2022) | | | | Chronology of Rating History for the past 3 years | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated (Rs. crore) | Amount Outstanding as on Mar 31, 2021 (Rs. crore) | Date & Rating on | Date & Rating in FY2021 | Date & Rating in FY2020 | | Date & Rating in FY2019 |
| | | | | | 06-Jan-2022 | 30-Nov-2020 | 29-Aug-2019 | 08-Aug-2019 | - |
| 1 | Fund/Non-Fund Based | Long Term | 101.0 | 52.98 | [ICRA]A (Stable) | - | - | | |
| 2 | Fund based Facilities | Long Term | - | - | - | [ICRA]A- (Stable) | [ICRA]A- (Stable) | | |
| 2 | Interchangeable Limits^^ | Long Term | (5.0) | NA | [ICRA]A (Stable) | [ICRA]A- (Stable) | [ICRA]A- (Stable) | | |
| 3 | Interchangeable Limits^^ | Short Term | (5.0) | NA | [ICRA]A1 | - | - | | |
| 3 | Non-Fund Based | Short Term | 27.0 | 10.00 | [ICRA]A1 | [ICRA]A2+ | [ICRA]A2+ | | |
| 4 | Unallocated Facilities | Long Term/ Short Term | - | - | [ICRA]A (Stable)/ [ICRA]A1 | [ICRA]A- (Stable)/ [ICRA]A2+ | [ICRA]A- (Stable)/ [ICRA]A2+ | [ICRA]A- (Stable)/ [ICRA]A2+ | |

*NA: Not Available; ^^sublimit of Fund/Non Fund-Based Limits*

## Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|---|
| Fund/Non Fund-Based Limits | Simple |
| Interchangeable Limits | Simple |
| Interchangeable Limits | Very Simple |
| Non Fund-Based Limits | Very 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 analyzing 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](http://www.icra.in)

## Annexure-1: Instrument details

| ISIN No/Banker Name | Instrument Name | Date of Issuance | Coupon Rate | Maturity | Amount Rated (RS Crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| NA | Fund/Non Based-Limits | NA | NA | NA | 101.00 | [ICRA]A (Stable) |
| | | | | | | |
| NA | Interchangeable Limits^^ | NA | NA | NA | (5.00) | [ICRA]A (Stable) |
| | | | | | | |
| NA | Interchangeable Limits^^ | NA | NA | NA | (5.00) | [ICRA]A1 |
| | | | | | | |
| NA | Non Fund-Based Limits | NA | NA | NA | 27.00 | [ICRA]A1 |

***Source:*** *Company; ^^sublimit of Fund/Non Fund-Based Limits*

### Annexure-2: List of entities considered for consolidated analysis

| Company Name | Ownership | Consolidation Approach |
|---|---|---|
| Not Applicable | | |

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## 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.

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