December 04, 2023

Sterling Tools Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	59.61	46.35	[ICRA]AA-(Stable); Reaffirmed
Long-term Fund-based – Working capital	120.00	125.00	[ICRA]AA-(Stable); Reaffirmed
Non-fund based limits	2.84	2.84	[ICRA]A1+; Reaffirmed
Unallocated	23.22	30.00	[ICRA]A1+; Reaffirmed
Total	**205.67**	**204.19**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation factors in the continuation of steady operating performance of Sterling Tools Limited (STL/company) aided by its established market position as the second largest automotive fastener manufacturer in India. The steady operating profile provides comfort regarding the company's ability to continue to generate healthy cash flows, going forward, which are expected to help it maintain strong credit metrics. The company enjoys a healthy share of business (SOB) with leading automotive original equipment manufacturers (OEMs), including Maruti Suzuki India Limited (MSIL), Honda Motorcycles and Scooters India Limited (HMSI), Tata Motors Limited (TML), Ashok Leyland Limited (ALL), and Mahindra & Mahindra, among others. Benefitting from its expertise in developing value-added specialised, and critical fasteners including those used in engine and transmission systems, the company has maintained its position as a key supplier for various automotive OEMs.

STL reported healthy consolidated revenues of ~Rs. 772 crore with YoY growth of ~51% and standalone revenues of ~Rs. 598 crore with YoY growth of ~27% during FY2023. This was supported by the improvement in the economic environment and, consequently, higher demand from the automotive industry. The performance continued to remain healthy in H1 FY2024 with 22% YoY growth in revenues on a consolidated basis and 4% YoY growth on a standalone basis. While revenues in the fastener business remained slightly impacted in H1 FY2024 by subdued domestic tractor and two-wheeler (2W) sales volumes and limited growth in commercial vehicle (CV) sales at an industry level, the performance is likely to remain better in H2 FY2024 aided by resilient festive season demand in the auto industry, particularly across the PV sector.

The standalone operating margins (OPM) remained at ~14.5% in FY2023 (~14.9% in FY2022) and 13.7% in H1 FY2024, remaining constrained by inflationary pressures to some extent. The company has been able to pass on the steel price hikes to its customers (with a lag); however, it could not completely pass on the increment in other conversion costs. Further, even as the steel prices have softened over the last one year, the company had bought the inventory at a higher price to maintain sufficient inventory holding, which led to higher raw material (RM) costs. Going forward, its standalone margins are expected to improve supported by easing in RM prices, continued cost control measures and better operating leverage. STL's subsidiary, Sterling G-take E-Mobility Ltd. (SGEM), recorded a healthy top line of ~Rs. 129 crore in H1 FY2024 (~Rs. 174 crore in FY2023) with an OPM of ~7.3%. The sales growth momentum is expected to continue over the medium term aided by a growing demand for electric vehicles (EVs) and new client additions, which would help further diversify the company's business profile.

STL has capex plans of ~Rs. 28 crore for SGEM towards capacity expansion and R&D initiatives, and ~Rs. 20-25 crore mainly for maintenance at STL's (standalone) plants in FY2024, likely to be funded by a mix of debt and internal accruals. Nevertheless, coupled with healthy operating profitability and accruals, the credit metrics are likely to remain comfortable as evidenced by gearing of 0.3x, interest cover of 11.1x and net debt/OPBITDA of 0.7x in FY2023.

ICRA also notes that STL's business profile draws strength from diversified revenue streams, with its presence across various automotive segments insulating its prospects against downturn in any particular industry to an extent. Its customer portfolio is also well diversified with its largest customer accounting for only 19% and its top five customers driving ~58% of its standalone revenues in FY2023. However, with more than 95% of its revenues derived from the domestic markets in FY2023, it remains exposed to the inherent cyclicality of the industry. The rating also remains constrained by STL's limited product diversification; although the company's efforts towards diversifying its product profile by ramping up its motor controller unit (MCU) business for EVs provides some comfort.

The Stable outlook on the long-term rating reflects ICRA's opinion that STL would continue to maintain healthy credit metrics going forward as well, aided by its established market position as a leading fastener manufacturer.

Key rating drivers and their description

Credit strengths

Leading player in the automotive fastener segment – STL is positioned as the second largest automotive fastener manufacturer in India in terms of revenue and market share. Aided by regular investments in product development (with focus on specialised fasteners), the company has been able to enhance its share of business (SoB) with leading automobile OEMs in India. Accordingly, despite stiff competition from both organised and numerous unorganised players in the fastener segment, the company has maintained its market standing over the years.

Diversified revenue profile across automotive and customer segments; healthy relationship with key customers – STL's revenue profile is well-diversified, catering to all major automotive as well as some non-automotive segments. Its dependence on each segment is relatively limited, with CVs accounting for 31% of its standalone OEM revenues (FY2023), followed by PVs (~28%), 2Ws (~22%), and tractors (~16%). This protects the company's revenues to an extent from demand downturns in any particular automotive segment. Further, the company caters to multiple OEMs, enjoying healthy SoB with its leading customers. Its largest customer accounted for only ~19% of its standalone revenues in FY2023, while its top five customers generated ~58%. STL's well-diversified profile coupled with its healthy market position augurs well for its business prospects. ICRA notes that SGEM derives most of its revenues from a single customer in the e-2W segment. However, given that the company is in its initial stage of operations and has already been working with more than 40 active customers, this provides some comfort regarding diversification efforts.

Leading MCU supplier in domestic e-2W market; industry growth prospects aid revenue visibility – SGEM recorded revenues of ~Rs. 129 crore in H1-FY2024 (Rs. 174 crore in FY2023) supported by steady demand. Aided by a healthy order book and growing demand for EVs, it is expected to clock a turnover of ~Rs. 270-290 crore in FY2024. It also plans to expand its capacity to supply 6 lakh MCUs/annum by the end of FY2024 from 3 lakh MCUs/annum in FY2023, to serve its customers in a timely manner. The revenue visibility over the medium term is expected to be driven by steady demand for EVs, addition of new customers as well as a healthy sales volumes and realisations.

Healthy financial risk profile with robust profitability, return indicators and comfortable credit metrics – The company reported a healthy OPM of ~14.5% in FY2023 (~14.9% in FY2022). The OPM has moderated over the past few years due to the company's limited ability to pass on inflationary pressures to its customers. Nevertheless, the management expects the standalone margins to improve by ~50 bps YoY in FY2024 on account of easing in raw material prices and other cost efficiency measures. Despite some moderation in margins, the company continues to maintain a healthy credit profile as it maintains a conservative capital structure with low gearing levels and comfortable coverage indicators. It reported consolidated debt levels of ~Rs. 135 crore[1], as of September 30, 2023, even as it continues to maintain adequate cash and liquid investments, which stood at ~Rs. 73 crore as on September 30, 2023. As of March 31, 2023, at the consolidated level, the gearing ratio was healthy at 0.3x and interest cover and DSCR were 11x and 3x, respectively, during the year. Going forward, with moderate capex

[1] Debt includes debtor bill discounting o/s of Rs 14 crore as of Sep 30, 2023

requirements, the company is likely to maintain healthy financial risk profile and comfortable debt metrics, aided by healthy earnings and better accruals.

Credit challenges

Exposed to inherent cyclicality of domestic automotive industry – With more than 90% of STL's revenues derived from domestic OEMs, it remains exposed to cyclicality in the domestic automobile market. As the auto industry underwent a sharp downturn over FY2020-FY2021, it had significant impact on STL as well. However, the situation progressively improved in FY2022 and further in FY2023 as the domestic automotive market recovered and recorded strong growth, and the company was able to close FY2022 and FY2023 with 43% and 51% YoY growth, respectively, in its consolidated revenues. Going forward, with its exports sales likely to continue to remain subdued in FY2024 (export sales of ~Rs. 12 crore in FY2023 vis-à-vis Rs. 47 crore in FY2022) due to macro-economic challenges in its key market, Europe; the revenues are likely to remain dependent on the performance of the domestic automotive market.

Limited product diversification with fasteners constituting bulk of revenues; ramp up of EV business to partially mitigate the risk – STL has historically operated in a single product category of fasteners, thereby limiting its product diversification and offerings. Nevertheless, the versatility of the product segment, along with STL's strong market position as the second largest player and its healthy presence with its key OEMs, offers comfort regarding the stability of the business. Additionally, the company commenced supplies for MCUs in the EV space through its subsidiary, SGEM, from the start of CY2022, which is expected to augur well for its business prospects as well as product diversification, going forward.

Environmental and Social Risks

Environmental considerations – Even as STL is not directly exposed to climate-transition risks from a likelihood of tightening emission-control requirements, with its products being used across different fuel powertrains, its automotive manufacturing customers remain highly exposed to the same; accordingly, STL's prospects are linked to the ability of its customers to meet tightening emission requirements. The company has been taking steps to reduce its carbon footprint, by enhancing its reliance on renewable sources and other energy saving efforts such as adoption of energy-efficient fixtures/equipment and extensive water recycling. The company's exposure to litigation/ penalties from issues related to waste and water management remains relatively low.

Social considerations – STL, like most automotive-component suppliers, has a healthy dependence on human capital. As such, retaining human capital, maintaining healthy employee relations and supplier ecosystem remain essential for disruption free operations for the entity. STL's annual reports indicate that it has been taking initiatives to support its vendors in upgrading their operations, skills, quality, and technology. Another social risk that STL faces pertains to product safety and quality, wherein instances of product recalls and high-warranty costs may not only lead to a financial implication but could also harm the reputation and create a more long-lasting adverse impact. In this regard, STL's strong track record in catering to leading automotive manufacturers underscore its ability to mitigate these risks to an extent. The company's strong technological capabilities are also likely to help it align its products with any change in customer preferences.

Liquidity position: Adequate

The company has an adequate liquidity position with funds parked in cash and liquid investments (Rs. 73 crore as on September 30, 2023) and sufficient buffer from undrawn working capital limits. Its average working capital utilisation remains low, with an average utilisation of 46% over the past 12 months ending in July 2023. The repayment obligations remain moderate at ~Rs. 24 crore in FY2024 and ~Rs. 19 crore in FY2025 for the existing loans, which are expected to be comfortably serviced from internal accruals. The company has moderate capex plans (~Rs. 20-25 crore for STL and ~Rs. 28 crore for SGEM in FY2024), which are likely to be met through a mix of debt and internal accruals.

Rating sensitivities

Positive factors – For a rating upgrade, sustained improvement in business risk profile, characterised by expansion in product portfolio and significant scale up in operations, while maintaining profitability indicators, credit metrics and liquidity profile at current healthy levels, would be critical.

Negative factors – Sustained pressure on revenues and earnings, leading to a deterioration in credit metrics could lead to a rating downgrade. Specific credit metrics include Total Debt/OPBITDA above 1.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Auto Component Suppliers
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of STL. As on March 31, 2023, the company had two subsidiaries, which are enlisted in Annexure-II.

About the company

Established in 1979, STL manufactures and markets high tensile cold forged fasteners, primarily for the automobile industry. At present, it is positioned as the second largest fastener manufacturer in India. The company caters to leading automotive companies in India and tier-I auto component manufacturers in Europe. STL's product portfolio includes fasteners, which find application in both automotive and non-automotive segments.

STL's manufacturing plants are at Faridabad and Palwal (Haryana) and a third fastener manufacturing plant near Bengaluru (Karnataka). The company has a total manufacturing capacity of approximately 45,324 MT per annum, with an overall capacity utilisation of 73% in FY2023.

STL was founded by the first-generation entrepreneur, Mr. Manohar Lal Aggarwal, and has thereafter been managed by his two sons, Mr. Anil Aggarwal and Mr. Atul Aggarwal. The company is listed on the stock exchanges.

Key financial indicators (audited)

STL Consolidated	FY2022	FY2023	H1-FY2024 (Limited audit)
Operating income	509.6	772.0	430.8
PAT	26.2	47.9	25.5
OPBDIT/OI	13.1%	12.7%	11.8%
PAT/OI	5.1%	6.2%	5.9%
Total outside liabilities/Tangible net worth (times)	0.6	0.6	-
Total debt/OPBDIT (times)	1.9	1.3	-
Interest coverage (times)	9.8	11.1	10.1

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as of Sep 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	
					Dec 04, 2023	Oct 7, 2022	Aug 25, 2021	Jan 7, 2021	May 21, 2020
1	**Term loans**	Long term	46.35	46.35	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Negative)**	**[ICRA]AA- (Negative)**
2	**Cash Credit**	Long term	125.00	--	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Stable)**	**[ICRA]AA- (Negative)**	**[ICRA]AA- (Negative)**
3	**Non-fund Based Limits**	Short Term	2.84	--	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**
4	**Unallocated**	Short Term	30.00	--	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term Loan	Simple
Cash Credit	Simple
Unallocated	Not Applicable
Non-fund Based Limits	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 are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan- I	FY2024*	MCLR linked	FY2025	1.75	[ICRA]AA- (Stable)
NA	Term Loan-II	FY2023*	MCLR linked	FY2024	1.70	[ICRA]AA- (Stable)
NA	Term Loan-III	FY2019	MCLR linked	FY2025	9.80	[ICRA]AA- (Stable)
NA	Term Loan-IV	FY2021	MCLR linked	FY2026	2.50	[ICRA]AA- (Stable)
NA	Term Loan-V	FY2022	MCLR linked	FY2027	18.61	[ICRA]AA- (Stable)
NA	Term Loan-VI	FY2023	MCLR linked	FY2028	11.99	[ICRA]AA- (Stable)
NA	Fund based working capital limits	NA	NA	NA	125.00	[ICRA]AA- (Stable)
NA	Non-fund based working capital limits	NA	NA	NA	2.84	[ICRA]A1+
NA	Unallocated	NA	NA	NA	30.00	[ICRA]A1+

*Source: Company *as per latest renewal letter*

[Please click here to view details of lender-wise facilities rated by ICRA]

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Haryana Ispat Private Limited	100.00%	Full Consolidation
Sterling Gtake E-Mobility Limited	100.00%	Full Consolidation

Source: Sterling Tools Limited

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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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