November 14, 2024

Sterling Tools Limited: Ratings reaffirmed; outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	44.22	44.82	[ICRA]AA- (Positive); reaffirmed and outlook revised to Positive from Stable
Long-term Fund-based – Working capital	125.00	144.00	[ICRA]AA- (Positive); reaffirmed and outlook revised to Positive from Stable
Non-fund-based limits	2.84	2.84	[ICRA]A1+; reaffirmed
Unallocated	32.13	12.53	[ICRA]A1+; reaffirmed
Total	**204.19**	**204.19**	

**Instrument details are provided in Annexure-I*

Rationale

The revision in the outlook on the long-term rating to Positive factors in the expected improvement in Sterling Tools Limited's (STL) business risk profile, going forward, aided by a ramp-up in contribution from the electric vehicle (EV) components segment. Even though the fasteners segment is expected to record a healthy growth on the back of steady automotive demand, the company's foray into the EV components segments is likely to drive its revenue growth, leading to an increased diversification of the company's earnings. STL is likely to continue to maintain a strong financial risk profile, aided by expectation of steady cash flows and limited capex and investment plans.

The ratings factor in favourably the continuation of steady operating performance of STL, aided by its established market position as the second largest automotive fastener manufacturer in India. 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 consolidated revenues of ~Rs. 932 crore with a YoY growth of ~21% and standalone revenues of ~Rs. 608 crore with a YoY growth of ~2% in FY2024. The growth in the consolidated revenues was driven by the company's wholly owned subsidiary, Sterling Gtake E-mobility Limited (SGEM), which contributed ~35% to the consolidated revenues in FY2024. The performance continued to remain healthy in Q1 FY2025, with a 28% YoY growth in revenues on a consolidated basis and 9% YoY growth on a standalone basis. While revenues in the fastener business were impacted in FY2024 due to decline in domestic tractor segment and subdued demand in the commercial vehicle (CV) industry, revenues were supported by growth in the two-wheeler and passenger vehicle segment.

The standalone operating profit margin (OPM) stood at 14.0% in FY2024 (14.5% in FY2023) and 13.9% in Q1 FY2025, constrained by inflationary pressure 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 rise in other conversion costs. Though steel prices have softened over the last one year, the company had bought the inventory at a higher price to maintain sufficient holding, which led to higher raw material (RM) costs. Going forward, its standalone margins are expected to be stable, supported by stable raw material 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. 324 crore in FY2024 (~Rs. 174 crore in FY2023) with an OPM of ~7.1%. The sales growth momentum is expected to continue over the medium term, aided by 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. 60 crore (including SGEM) towards capacity expansion and R&D initiatives and maintenance in FY2025, 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 0.3 times, interest cover of 11.4 times and net debt/OPBITDA of 0.1 times in FY2024.

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 ~21% and its top five customers driving ~59% of its standalone revenues in FY2024. Further, the company has announced another foray into the EV segment with the recently executed MoU with South Korean firm, Yongin Electronics, to produce a full range of magnetic components for automotive and electronic industries such as magnetic components. Yongin designs and manufactures EV components like transformers, chokes, filters and other subcomponents for the EV industry. The partnership is expected to aid in improvement in product and customer diversification over the medium-to-long term as the partnership is expected to start production from end FY2025.

However, with ~98% of its revenues derived from the domestic markets in FY2024, STL remains exposed to the inherent cyclicality of the automotive industry. Even as the company's limited product diversification has remained a constraining factor, the company's efforts towards diversifying its product profile by ramping up its motor controller unit (MCU) and other components for EVs provides comfort.

Key rating drivers and their description

Credit strengths

Leading player in the automotive fastener segment – STL is 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 SoB with leading automobile OEMs in India. 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. In FY2024, the CV segment accounted for ~22% of its standalone revenues, while PV (~27%), two-wheeler (~24%) and tractor (13%) segments contributed to the rest. This protects the company's revenues to an extent from demand downturn 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 ~21% of its standalone revenues in FY2024, while its top five customers generated ~59%. 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. As the company is in its initial stage of operations and has already been working with more than 40 active customers, it enjoys some comfort regarding diversification efforts.

Leading MCU supplier in domestic e-2W market; industry growth prospects aid in revenue visibility – SGEM recorded revenues of ~Rs. 324 crore in FY2024 (~Rs. 174 crore in FY2023), supported by steady demand. A healthy order book and growing demand for EVs provided additional support. It also plans to expand its capacity to supply ~6 lakh MCUs/annum by the end of FY2025 from ~4 lakh MCUs/annum in Q1 FY2025 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 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% in FY2024 (~14.5% in FY2023). The OPM has moderated over the past few years due to the company's limited ability to pass on inflationary pressure to its customers. Nevertheless, the management expects the standalone margins to improve in FY2025 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. 117 crore, as of March 31, 2024, even as it continued to maintain adequate cash and liquid investments, which stood at ~Rs. 103 crore during the same period. As of March 31, 2024, at the consolidated level, the gearing ratio was healthy at 0.3 times and interest cover and DSCR stood at 11 times and 3 times, respectively, during the year. Going forward, with moderate capex 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 ~99% of STL's revenues derived from domestic sales, it remains exposed to cyclicality in the domestic automobile market. As the auto industry underwent a sharp downturn over FY2020-FY2021, it had a 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 a strong growth, and the company was able to close FY2022 and FY2023 with 43% and 51% YoY growth, respectively, in its consolidated revenues. In FY2024, a downturn in the commercial vehicle and tractor segment led to a muted growth in the fastener business, with the standalone revenues witnessing a marginal growth of 2% compared to the overall industry growth of 12.5%.

High geographical concentration with major portion of revenues derived from domestic automotive industry – The company's revenues from exports have materially declined in the past three years and accounted for 1% of the consolidated revenues in FY2024 and 2% in Q1 FY2025 from 7-9% during FY2020-FY2022. As its exports sales are likely to continue to remain subdued in FY2025 (export sales of ~Rs. 9 crore in FY2024 vis-à-vis ~Rs. 12 crore in FY2023 and ~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 components business to help mitigate the risk – STL has historically operated in a single product category of fasteners, limiting its product diversification and offerings. Nevertheless, 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, provided comfort about 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 and recorded a healthy ramp-up in revenues over the past two fiscals. More recently, STL has announced another foray into the EV segment with the recently executed MoU with the South Korean firm, Yongin Electronics, to produce a full range of magnetic components for automotive and electronic industries such as magnetic components. The diversification into EV components is expected to augur well for the company's revenue growth prospects, going forward.

Environmental and Social Risks

Environmental considerations – Though STL is not directly exposed to climate transition risks from the likelihood of tightening emission control requirements, with its products 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 lower.

Social considerations – STL, like most automotive component suppliers, has a healthy dependence on human capital. As such, retaining human capital, maintaining healthy relationships with employees and suppliers 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 lead to financial implication and affect 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: Strong

The company has a strong liquidity position with funds parked in cash and liquid investments (Rs. 104 crore as on March 31, 2024) and a healthy buffer from undrawn working capital limits. Its average working capital utilisation remains low. The repayment obligations remain moderate at ~Rs. 30.5 crore in FY2025 and ~Rs. 18.4 crore in FY2026 for the existing loans, which are expected to be comfortably serviced from internal accruals. The company has moderate capex plans (~Rs. 60 crore in FY2025), which are likely to be met through a mix of debt and internal accruals.

Rating sensitivities

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

Negative factors – Sustained pressure on revenues and earnings, resulting in a deterioration in credit metrics, could pave way for a revision in the long-term outlook to Stable. Specific credit metrics for ratings downgrade 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 Components
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of STL. As on March 31, 2024, the company had three 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. It is the second largest fastener manufacturer in India, after Sundaram Fasteners. The company's business profile is characterised by high segment as well as customer diversification. In FY2024, the CV segment accounted for ~22% of its standalone revenues, while PV (~27%), two-wheeler (~24%) and tractor (13%) segments constituted the rest. The company caters to leading automotive companies in India. STL's product portfolio includes fasteners, which find application in both automotive and non-automotive segments.

STL had manufacturing plants in Faridabad and Palwal (Haryana) and set up the third fastener plant near Bengaluru (Karnataka) in 2019. There is also a wire drawing plant at Ballabhgarh, where the company performs the job work of Faridabad, Palwal and Bangalore plants. The Bangalore unit ramped up its capacity over the years and the annual capacity currently stands at ~9,600 MT. The overall capacity across all the plants stands at 60,531 MT, with an overall capacity utilisation of 55% as of FY2024.

In FY2018, STL entered business collaboration with the Japanese fastener manufacturer, Meidoh Co. Ltd, to enhance its design and development capabilities in the automotive fastener segment and strengthen its business prospects with the Indian subsidiaries of Japanese OEMs. The Japanese company acquired a 5% stake in STL at a consideration of Rs. 44.3 crore, as a part of the business collaboration agreement.

STL formed a 100% owned subsidiary, SGEM, in January 2020, to manufacture and supply MCUs for the emerging high speed 2W, 3W and LCV EV markets. An MCU is an electronic module that interfaces between batteries and motor to control the EV's speed and acceleration based on throttle input. The entity benefits from the technical support that it receives from the Chinese entity, Gtake, as well as management and financial support from STL. SGEM's manufacturing facility is at Faridabad, Haryana, the annual production capacity of which stood at 4.0 lakh MCUs as of FY2024. Its main customer is Ola Electric, which contributed more than 94% to its sales in FY2024.

In FY2025, the company announced that it had signed an MoU with South Korea's Yongin Electronics Co. Ltd., a major supplier of components to the Hyundai Kia Motor Group, for manufacturing electronic components in the EV space like chargers, both onboard and off-board chargers, and battery management systems.

Key financial indicators (audited)

STL Consolidated	FY2023	FY2024
Operating income	772.0	932.0
PAT	47.9	55.4
OPBDIT/OI	12.7%	11.6%
PAT/OI	6.2%	5.9%
Total outside liabilities/Tangible net worth (times)	0.6	0.6
Total debt/OPBDIT (times)	1.3	1.1
Interest coverage (times)	11.1	11.4

Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. Crore; 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 (FY2025)				Chronology of rating history for the past 3 years		
		Type	Amount Rated (Rs Crore)	Date & rating in FY2025		Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022
				Nov 14, 2024	Jul 10, 2024	Dec 04, 2023	Oct 07, 2022	Aug 25, 2021
1	Long-term Fund-based – Term loan	Long Term	44.82	[ICRA]AA-(Positive)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)
2	Long-term Fund-based – Working capital	Long Term	144.00	[ICRA]AA-(Positive)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)
3	Non-fund-based limits	Short Term	2.84	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Unallocated	Short Term	12.53	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based – Term loan	Simple
Long-term Fund-based – Working capital	Simple

Non-fund-based limits	Not Applicable
Unallocated	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**	FY2019	NA	FY2025	1.25	[ICRA]AA- (Positive)
NA	**Term Loan-II**	FY2024	NA	FY2029	10.00	[ICRA]AA- (Positive)
NA	**Term Loan-III**	FY2019-FY2024	NA	FY2025-FY2029	33.57	[ICRA]AA- (Positive)
NA	**Fund based working capital limits**	NA	NA	NA	144.00	[ICRA]AA- (Positive)
NA	**Non-fund-based working capital limits**	NA	NA	NA	2.84	[ICRA]A1+
NA	**Unallocated**	NA	NA	NA	12.53	[ICRA]A1+

Source: Company;

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
Sterling Gtake E-Mobility Limited	100.00%	Full Consolidation
Haryana Ispat Private Limited*	100.00%	Full Consolidation
Sterling Advanced Electric Machines Pvt Ltd	100.00%	Full Consolidation

*Source: Sterling Tools Limited; annual report; *the entity is under amalgamation process with and into STL*

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545328
shamsherd@icraindia.com

Srikumar Krishnamurthy
+91 44 4596 4318
ksrikumar@icraindia.com

Rohan Kanwar Gupta
+91 124 4545 808
rohan.kanwar@icraindia.com

Akshit Goel
+91 124 4545 857
akshit.goel@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

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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