Incap Contract Manufacturing Services Private Limited

April 05, 2019

Summary of rating action

Instrument*	Previous Rated Amount(Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Long-term - Fund-based - Cash Credit	5.00	5.00	[ICRA]A- (Stable)upgraded from [ICRA]BBB+ (Stable)
Long-term - Fund-based - Term Loan	2.70	2.70	[ICRA]A- (Stable)upgraded from [ICRA]BBB+ (Stable)
Short-term -Fund based	17.30	17.30	[ICRA]A2+; upgraded from [ICRA]A2
Total	**25.00**	**25.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings upgrade for Incap Contract Manufacturing Services Private Limited's (ICPL) takes into account the significant growth in the revenues in FY2018 and 6M FY2019, aided by increased orders from the existing customers as well as new customer additions. The ratings upgrade also takes into account the company's strong financial profile characterised by healthy gearing and coverage metrics and improvement in operating margins owing to benefits arising from economies of scale. The ratings continue to positively factor in the management's extensive experience in the electronics manufacturing services (EMS) industry, the technical and marketing support provided by the parent company, Incap Corporation, Finland, as well as ICPL's track record with reputed clients in the international and domestic markets.

However, the ratings remain constrained by the company's high dependence on the top five customers, accounting for ~91% of the revenues in FY2018. However, the established client relationships supported ICPL in generating repeat orders. The ratings are also constrained by the intense competition in the EMS industry, which restricts the pricing flexibility and margins to some extent. It is also exposed to significant foreign currency exposure risk as it derived about ~75% of its revenues from exports in FY2018. However, import of ~60% of the raw materials provides a natural hedge to an extent. This apart, ICPL's working capital cycle remains long with high inventory and debtor levels.

Outlook: Stable

The Stable outlook reflects ICRA's expectation that ICPL will continue to benefit from the extensive experience of the management, the technical and marketing support provided by the parent company, Incap Corporation, Finland and its established relationship with a reputed clientele. The outlook may be revised to Positive if there is a substantial increase in the scale of operations or if there is sustainable improvement in the profitability indicators. Conversely, the outlook may be revised to Negative, if there is any weakening of the profitability or coverage indicators or any weakening of the liquidity position due to an increase in working capital intensity or higher-than-anticipated capital expenditure.

Key rating drivers

Credit strengths

Significant growth in the revenues in FY2018 and 6M FY2019 - ICPL's revenues witnessed a strong growth of ~21% and improved to Rs. 253.67 crore in FY2018 from Rs. 210.39 crore in FY2017. The revenues further improved to Rs. 182.12 crore in 6M FY2019, with an annualised growth of ~44%. This was driven by increased order volume from its existing customers, coupled with new client addition. Further, an increase in the company's installed capacity also supported the revenue growth.

Comfortable financial profile with strong debt coverage, low gearing and sufficient liquidity - ICPL's financial profile remained healthy with a low gearing of 0.17 times as on March 31, 2018. Its coverage indicators stood healthy with a total debt/OPBDITA of 0.44 times, interest coverage of 18.16 times and DSCR of 6.71 times in FY2018. Further, the liquidity profile also remains comfortable with healthy cash accruals from operations.

Established relationship with reputed clientele enhances business opportunities - The company's customers consist of manufacturers of power electronic devices, such as Victron Energy B.V., GE Appliances, Hitachi Hi-Rel, Emerson Network Power, etc. ICPL has a strong relationship with these customers from the time of its incorporation and enjoys repeat revenues from these customers providing sufficient medium-term revenue visibility.

Technical and marketing support provided by the parent company - ICPL is a subsidiary of Incap Corporation, Finland, which is involved in contract equipment manufacturing for the power electronics sector for over three decades. The company receives technical and marketing support from its parent and pays ~5% of the export revenues as commission to the parent.

Credit challenges

High customer concentration with the top five customers accounting for 90% of revenues in FY2018 - ICPL derived ~66% of its revenues from its top customer Victron Energy B.V. and the top five customers contributed to ~91% of the revenues in FY2018. As a result, the customer concentration risk remains high and any volatility in order flow from its top customers can significantly impact its revenues.

Stiff competition from other contract manufacturers limits pricing flexibility - ICPL remains a mid-sized player, which faces intense competition in the electronic contract manufacturing services industry. As the company is not involved in the designing of the PCBs but only assembles the components based on the designs provided by its customers, the value addition in its operations remains limited. This restricts its pricing flexibility and bargaining power with customers.

Exposure to foreign currency fluctuation risk due to export revenues despite natural hedge from sizeable imports - With 75% of the revenues in FY2018 derived from exports, the company's margins remain exposed to fluctuations in foreign exchange rates. However, it imports about 60% of its raw materials and also has foreign currency term loans, which provide a natural hedge to an extent.

Risk of technological obsolescence necessitates continuous upgrade to sustain competitive advantage - The electronic products industry is characterised by continuous product and process innovation and rapid adoption of new technology. Given the risk of technological obsolescence, the industry players are required to undertake continuous upgrades to sustain the competitive advantage.

Liquidity position

Aided by healthy operating margins of 13.10%, ICPL reported net cash accruals of Rs. 21.98 crore in FY2018. It had Rs. 4.24-crore term loan outstanding as on September 30, 2018. Moreover, the repayment obligation on the term loan remains low at Rs. 2.05 crore for FY2019 resulting in a comfortable cash flow position. The liquidity profile remains healthy with buffer from the unutilised working capital facilities and adequate cash and bank balance.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation / Standalone	Standalone financial statements of the issuer.

About the company

Incorporated in 2007, ICPL is involved in providing EMS mainly to companies operating in the power electronics segment. The company, which started its operations by taking over TVS Electronic Limited's contract manufacturing services division, is a 100% subsidiary of Incap OYJ, Finland. It manufactures products based on the design specifications given by its customers at its manufacturing facility in Hirehalli (near Bangalore). Its major products are inverters, printed circuit board assemblies (PCBA), uninterruptible power supply systems (UPS) and emergency rescue devices (ERD). The company derives a predominant share of its income through exports to companies based in Netherlands and Switzerland.

In FY2018, the company reported a net profit of Rs. 18.12 crore on an OI of Rs. 253.67 crore compared to a net profit of Rs. 12.72 crore on an OI of Rs. 210.39 crore in the previous year.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	210.39	253.67
PAT (Rs. crore)	12.72	18.12
OPBDITA/OI (%)	11.25%	13.10%
RoCE (%)	27.93%	33.63%
Total Debt/TNW (times)	0.19	0.17
Total Debt/OPBDITA (times)	0.55	0.44
Interest Coverage (times)	14.87	18.16

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2020)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs.crore) as on March 31, 2018	Date & Rating April 2019	Date & Rating in FY2019 April 2018	Date & Rating in FY2018 -	Date & Rating in FY2017 Jan 2017
1	Cash Credit	Long Term	5.00	-	[ICRA]A- (Stable)	[ICRA]BBB+ (Stable)	-	[ICRA]BBB+ (Stable)
2	Term Loan	Long Term	2.70	2.16	[ICRA]A- (Stable)	[ICRA]BBB+ (Stable)	-	[ICRA]BBB+ (Stable)
3	Fund based	Short Term	17.30	-	[ICRA]A2+	[ICRA]A2	-	[ICRA]A2

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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				5.00	[ICRA]A- (Stable)
NA	Term Loan	June 2015	-	FY2020	2.70	[ICRA]A- (Stable)
NA	Fund based	-	-	-	17.30	[ICRA]A2+

Source: Incap Contract Manufacturing Services Private Limited

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About ICRA Limited:

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