

Rating Rationale

October 28, 2022 | Mumbai

Lucas-TVS Limited

Rating outlook revised to 'Stable'; Ratings reaffirmed

Rating Action

Total Bank Loan Facilities Rated	Rs.359.5 Crore
Long Term Rating	CRISIL AA+/Stable (Outlook revised from 'Negative'; Ratings Reaffirmed)
Short Term Rating	CRISIL A1+ (Reaffirmed)
Rs.150 Crore Commercial Paper	CRISIL A1+ (Reaffirmed)

1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has revised the outlook on the long term bank facility of Lucas-TVS Limited (Lucas-TVS) to '**Stable**' from '**Negative**' while reaffirming the rating on the same at '**CRISIL AA+**'. The ratings on the short-term bank facilities and commercial paper programme have also been reaffirmed at '**CRISIL A1+**'.

The rating on follows the better than anticipated improvement in the business performance in fiscal 2022, and continued good performance expected in fiscal 2023, supported by healthy demand for electrical components and alternators from original equipment manufacturers (OEMs), aftermarket and exports. The company is expected to register on a consolidated basis revenues of over Rs.4000 crores, supported also by improving performance at its subsidiary, Lucas Indian Service Ltd (LISL, rated '**CRISIL AA/Stable/CRISIL A1+**'), and its step down subsidiary, India Nippon Electricals Ltd (INEL). LISL acquired additional stake in INEL in fiscal 2022, following which INEL became its subsidiary. Operating profitability is expected to settle at between 7-7.5%, supported by focus on higher margin products including from INEL, automation initiatives and better operating leverage leading to improved cash generation. Steady business performance is also expected over the medium term.

The improved performance in fiscal 2022 is after two consecutive years of decline in performance due to a prolonged slowdown across business segments in the automotive industry which was been exacerbated by the COVID-19 pandemic. Revenues grew by 30% on year in fiscal 2022 driven by healthy offtake from passenger vehicle (PV), commercial vehicle (CV) and tractor OEMs, strong aftermarket demand, gain in market share with auto OEMs and higher exports. Consequently, operating profitability also improved to 6.5% in fiscal 2022 from ~6% in fiscal 2021, driven by continued benefits of cost cutting measures, improved capacity utilisation leading to rationalization of fixed costs and higher exports.

The company continues to maintain a strong financial risk profile, as is net debt free at present. It also has sizeable cash surpluses of Rs.300 crore, which though are likely to be deployed in ongoing capital expenditure of ~Rs.125 crore in fiscal 2023, as the company is also investing in wiper capacity expansion as well as motor line for supplying motors for consumer durables.

Besides, the company will also incur about Rs.30-40 crore in fiscal 2023 in its subsidiary, TVS Indeon Ltd (TVS Indeon), which is setting up a factory to manufacture lithium ion batteries based on 24M Technologies Inc, USA's patented lost cost semi-solid technology. Capex spend on the battery project will be initially incurred at Lucas TVS and later moved to TVS Indeon. Total capex for the battery plant is about Rs.2500 crore and the plant will be constructed across phases over the next few years. Phase 1 of the project is expected to be completed in the 2-3 years and will involve modest investment, which will be funded largely through internal accruals and liquid surpluses of Lucas-TVS. While debt protection metrics are likely to remain healthy in the next 2-3 years in the absence of material increase in debt, the large overall investment by Lucas-TVS in a new product does expose it to project related risks. The extent of debt funding for the project for subsequent phase and the extent of initial losses of the new unit will remain key monitorables.

The ratings continue to reflect Lucas-TVS's leadership position in India's auto electrical products segment, diversified revenue, and strong financial risk profile. These strengths are partially offset by exposure to risks related to cyclicality in automotive demand, susceptibility to pricing pressure on account of large exposure to automobile OEMs and volatility in input prices, and project related risks owing to sizeable investment in a lithium ion battery plant.

Analytical Approach

For arriving at the ratings, CRISIL Ratings has combined the business and financial risk profiles of Lucas-TVS and its wholly-owned subsidiaries, LISL and TVS Automotive Systems Ltd (TVS Auto) as these companies have the same business, common management and operational linkages. Besides CRISIL Ratings will consolidated INEL and its

subsidiaries from fiscal 2023 since LISL acquired majority stake in INEL on March 30, 2022. INEL is in similar line of business as LISL and there are significant operational linkages between the entities. The new subsidiary, TVS Indeon housing the lithium ion battery plant has also been consolidated

Please refer Annexure - List of entities consolidated, which captures the list of entities considered and their analytical treatment of consolidation.

Key Rating Drivers & Detailed Description

Strengths:

- **Leading position in India's auto electricals market:** Lucas-TVS is the largest player in India's auto electrical products market, with strong design and development capabilities, established brand, diversified revenue profile across market and customer segments and longstanding relationships with customers. Besides, in-house capabilities have enabled the company to make product improvements according to the requirements of its key customers and sustain its leading market position despite increasing competition in the auto electrical industry. As in the case of peers with slowdown in automotive industry and impact of COVID-19, the company faced headwinds in fiscal 2020 and 2021, as well as in the initial months of fiscal 2022. However, thereafter, steady demand from all segments enabled revenues register a healthy recovery, which is continuing in the current fiscal. Besides, improving performance of LISL (revenues of over Rs.600 crore in fiscal 2022), which trades in components in the aftermarket mainly, and consolidation of INEL (revenues of over Rs.550 crore in fiscal 2022) is also expected to contribute to healthy revenue growth in the near to medium term.
- **Diversified revenue profile:** Lucas-TVS has presence in all segments of the auto component sector—domestic OEMs, aftermarket, and export, with OEMs accounting for about 71% of revenue. Within OEMs, it caters to all segments and has a strong market position, particularly in the PV, CV, and tractor segments. Diverse presence across segments and customers has helped Lucas-TVS to mitigate the slowdown. LISL and INEL are also expected to contribute to over a third of consolidated revenues from fiscal 2023, adding further diversity to revenues. The company has begun manufacture and sale of energy efficient fans under the TVS Green brand in fiscal 2023, while it is also planning to supply motors for consumer durables to a leading OEM. These businesses are part of the management's initiative to enhance product offerings.
- **Strong financial risk profile:** The financial risk profile remains strong, backed by comfortable capital structure and solid financial flexibility. Steady cash generation, moderate capex and prudent working capital management have helped maintain gearing at ~0.02 times as of March 31, 2022. Other debt protection metrics are also comfortable. Liquidity continues to be supported by largely unutilized working capital limit and healthy build-up in liquid surplus in excess of Rs 300 crore as on March 31, 2022. With ongoing capex at Lucas-TVS and step up of capex for the battery plant, substantial portion of liquid surpluses and future accruals will be used up in the next 2-3 years. Debt metrics will however continue to remain healthy, in the absence of material increase in debt.

Weaknesses:

- **Susceptibility to volatility in raw material prices and pricing pressures from OEMs:** Raw material cost accounts for 70-73% of overall revenue. Operating profitability has been impacted in the past due to increase in input prices, which were only partially passed on to OEMs due to limited pricing power and intense competition. Net-net, operating profitability remains below 8%, which is below the average levels typically seen in the automotive component sector. Due to modest profitability, return on capital employed has been below 12% since fiscal 2013 (except in fiscal 2019 when it was 14.1%).
- **Demand cyclicality due to large exposure to automotive OEMs:** Lucas-TVS's high dependence on the OEM segment renders its performance partly vulnerable to the inherent cyclicality in the automobile industry. For instance, revenue, which grew at a compound annual rate of 25% between fiscals 2009 and 2012, moderated to a modest 3% between fiscals 2012 and 2017. Revenue growth again picked up to 17% in fiscal 2018 and 14% in fiscal 2019 following healthy demand from OEMs but fell 17% in fiscal 2020 and 10% in fiscal 2021, before recovering again in fiscal 2022. While presence in the aftermarket and export segments provides some respite, these segments together account for only ~30% of overall revenue. Thus, given the sizeable share of business from OEMs and only minor share of revenues expected from new initiatives (motors for consumer durables), the company will remain susceptible to inherent cyclicality and any prolonged slowdown in demand from the automotive sector.
- **Project related risk due to implementation of lithium ion battery manufacturing plant:** Lucas-TVS will fund phase 1 of the capex for the lithium-ion battery manufacturing project at Gummidipoondi, near Chennai, largely from its own funds and will be using patented semi-solid technology from 24M. Pilot projects are underway in Thailand and Norway based on the same technology, which is expected to be cost effective. The project under TVS Indeon is expected to be carried out in phases, spreading funding risk over a longer period. In fiscal 2022, Lucas TVS took ~60 acres on long term lease from the government of Tamil Nadu, and land preparation activities are being carried out in fiscal 2023.

The overall project cost for is Rs.2500 crore is substantial relative to Lucas TVS' current scale of operations. Lucas TVS is likely to resort to debt funding for later stages of the project and also induct partners and investors for the same. Its ability to source customers will be critical to monetize investments in the battery project, which is expected to make losses in the initial 2 year of operations. Nevertheless, timely implementation of the project and demand for lithium-ion batteries, as well as availability of substitutes over the medium term will remain key monitorables.

Liquidity: Strong

Lucas TVS enjoys strong liquidity driven by expected annual cash accruals of Rs 200 -250 crore per annum in the medium term (~Rs.163 crore in fiscal 2022), against which there are no long term obligations. The company has only short term debt outstanding. Cash and equivalent were in excess of Rs 300 crore as on March 31, 2022; however, these are expected to gradually decline over the medium term, due to funding needs of the new lithium ion batteries project under the subsidiary. The company however has fund-based limits of Rs 203 crore which were sparingly utilised and are more than sufficient to

fund incremental working capital needs. On account of low debt, Lucas-TVS has sufficient headroom to raise additional funds, if required. Besides, it also has investments in other TVS group entities, which can be monetised in case of requirement.

Outlook: Stable

CRISIL Ratings believes Lucas-TVS's business performance will benefit from its established market position, increasing customer base, and good segmental spread of revenues, which along with improving operating efficiencies, will lead to higher cash generation. Financial risk profile is expected to remain healthy, despite large capex plans, due to minimal reliance on debt for funding.

Rating Sensitivity factors

Upward factors:

- Sustained strong double digit revenue growth, and operating profitability of over 10%, resulting in better than anticipated cash generation
- Completion of phase 1 sizeable capex (lithium iron battery plant) without material cost and time overruns, and stabilization thereafter
- Sustenance of strong financial risk profile

Downward factors:

- Lower-than-expected recovery in revenues and operating profitability sustaining below 6%, including due to higher than expected losses from the lithium iron battery plant
- Significant additional debt-funded capex or acquisitions, leading to material impact on debt metrics

About the Company

Lucas-TVS was set up in 1961 as a joint venture between Lucas Industries PLC, UK, and TV Sundaram Iyengar & Sons Ltd (TVS), India, to manufacture auto electrical systems. Currently, TVS, along with group companies, has more than 80% equity stake in Lucas-TVS. The company supplies products to major OEMs across all auto segments and has a wide presence in the aftermarket segment. It has seven manufacturing plants: one each at Padi and Maraimalai Nagar in Tamil Nadu, Eripakkam and Thiruvandarkoil in Puducherry, Rewari in Haryana, Chakan in Maharashtra, and Rudrapur in Uttarakhand.

The TVS group, with more than 50 companies, is among India's top 20 business groups, and has recently restructured its shareholding. This restructuring has had no impact on Lucas TVS and its subsidiaries. The company continues to be run by Mr TK Balaji (Chairman), his son, Mr Arvind Balaji (Managing Director) and daughter, Ms Priyamvada Balaji (Executive Director).

LISL, a 100% subsidiary of Lucas-TVS, was incorporated in 1930 as an overseas venture of Lucas Industries PLC, UK. The company sells and services auto electrical components manufactured by Lucas-TVS and diesel fuel injection equipment manufactured by Delphi-TVS Diesel Systems Ltd. TVS Automotive is a 100% subsidiary of LISL with limited operations. INEL became a step down subsidiary of LTVS in fiscal 2022, and is engaged in the manufacture of auto-electricals.

Key Financial Indicators

Particulars	Unit	2022	2021
Revenue	Rs crore	2940	2175
Profit after tax (PAT)	Rs crore	110	70
PAT margin	%	3.8	3.2
Adjusted debt / adjusted networth	Times	0.02	0.02
Interest coverage	Times	67.16	49.53

Any other information: Not applicable

Note on complexity levels of the rated instrument:

CRISIL Ratings' complexity levels are assigned to various types of financial instruments and are included (where applicable) in the 'Annexure - Details of Instrument' in this Rating Rationale.

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Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of allotment	Coupon rate (%)	Maturity date	Issue size (Rs crore)	Complexity Level	Rating assigned with outlook
NA	Cash Credit	NA	NA	NA	53.0	NA	CRISIL AA+/Stable
NA	Packing Credit	NA	NA	NA	150.0	NA	CRISIL A1+
NA	Proposed Short Term Bank Loan Facility	NA	NA	NA	156.5	NA	CRISIL A1+
NA	Commercial paper	NA	NA	7-365 days	150.0	Simple	CRISIL A1+

Annexure – List of entities consolidated

Names of entities consolidated	Extent of consolidation	Rationale for consolidation
Lucas Indian Service Ltd	Fully consolidated	Strong business and financial linkages
Indo Nippon Electrical Ltd	Fully consolidated	Step down subsidiary; Strong business and financial linkages
Synergy Shakthi Private Ltd	Fully consolidated	Strong business and financial linkages
TVS Automotive Systems Ltd	Fully consolidated	Strong business and financial linkages
TVS Indeon Ltd	Fully consolidated	Strong business and financial linkages

Annexure - Rating History for last 3 Years

Instrument	Type	Current		2022 (History)		2021		2020		2019		Start of 2019
		Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Fund Based Facilities	LT/ST	359.5	CRISIL AA+/Stable / CRISIL A1+		--	29-10-21	CRISIL AA+/Negative / CRISIL A1+	31-10-20	CRISIL AA+/Negative / CRISIL A1+	05-11-19	CRISIL AA+/Stable / CRISIL A1+	CRISIL AA+/Stable / CRISIL A1+
Commercial Paper	ST	150.0	CRISIL A1+		--	29-10-21	CRISIL A1+	31-10-20	CRISIL A1+	05-11-19	CRISIL A1+	CRISIL A1+

All amounts are in Rs.Cr.

Annexure - Details of Bank Lenders & Facilities

Facility	Amount (Rs.Crore)	Name of Lender	Rating
Cash Credit	3	State Bank of India	CRISIL AA+/Stable
Cash Credit	50	HDFC Bank Limited	CRISIL AA+/Stable
Packing Credit	150	HDFC Bank Limited	CRISIL A1+
Proposed Short Term Bank Loan Facility	156.5	Not Applicable	CRISIL A1+

This Annexure has been updated on 28-Oct-22 in line with the lender-wise facility details as on 08-Dec-21 received from the rated entity.

Criteria Details

Links to related criteria
CRISILs Approach to Financial Ratios
Rating criteria for manufacturing and service sector companies
CRISILs Bank Loan Ratings - process, scale and default recognition
Rating Criteria for Auto Component Suppliers
CRISILs Criteria for rating short term debt
CRISILs Criteria for Consolidation

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