

India Ratings Downgrades Titagarh Wagons to 'IND A+' / Negative; Rates New CP

20

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India Ratings and Research (Ind-Ra) has downgraded Titagarh Wagons Limited's (TWL) Long-Term Issuer Rating to 'IND A+' from 'IND AA-'. The Outlook is Negative. The instrument-wise rating actions are as follows:

Instrument Type	Date of Issuance	Coupon Rate	Maturity Date	Size of Issue (million)	Rating/Outlook	Rating Action
Fund-based working capital limits	-	-	-	INR1,400	IND A+/Negative/IND A1	Downgraded
Non-fund-based limits	-	-	-	INR6,008	IND A1	Downgraded
Commercial paper (CP)	-	-	360 days	INR500	IND A1	Assigned

The rating action reflects deterioration in TWL's operating performance and credit profile in 9MFY18 with high reliance on bank borrowings to fund its working capital requirement.

Ind-Ra continues to take a consolidated view of TWL and its subsidiaries, referred to as the Titagarh group, while arriving at the ratings, due to strong operational, legal and strategic interlinkages among them in the form of common management, similar line of business and strong support extended by TWL towards its subsidiaries.

KEY RATING DRIVERS

Waning Operating Performance: In 9MFY18, revenue declined to INR9.6 billion (9MFY17: INR10.6 billion; FY17: INR17.1 billion, FY16: 9.6 billion) due to execution of inherited lower realisation foreign orders, along with lack of execution of higher realisation electric multiple units (EMU)/mainline EMU orders. EBITDA margins declined to 0.9% in 9MFY18 (FY17: 6.8%, FY16: 4.2%) due to lower realisation of orders in its foreign entities, coupled with a one-time adjustment of INR313.4 million arising from provision/write-off of losses incurred/to be incurred by its Italian subsidiary, Titagarh Firema Adler S.p.A. (TFA). This was owing to re-estimation of certain long-term contracts inherited at the time of acquisition. Excluding the one-time adjustment, the EBITDA margins stood at 4.0% in 9MFY18.

As per 3QFY18 audits, penalties of INR502.7 million are likely to arise in the near term due to delays in inherited contracts in TFA. This could further dent the EBITDA margins. Any improvement in the operating performance is dependent upon TWL's ability to manage its working capital borrowings and securing higher margin contracts backed by advances.

Weak Credit Metrics: Net adjusted leverage (net adjusted debt/EBITDAR) deteriorated to 35.9x in 9MFY18 (FY17: 2.5x, FY16: 1.4x) driven by an increase in debt to support the rise in working capital requirements, resulting from a prolonged elongation of the net working capital cycle (FY17: 98 days, FY15: 63 days). The increase in the working capital cycle was largely due to a delay in recovery of unbilled revenue from TFA and the decline in the operating profitability. Consolidated unbilled revenue was around INR5.4 billion in FY17 (FY16: INR1.9 billion). An increase in wagon orders from the Indian Railways (not backed by advances) and lack of supply of free supply items would also result in a higher working capital requirement in FY19.

Ind-Ra, however, expects net adjusted leverage to return to about 4.0x by FY20 due to increased scale of operations, and receipt and execution of higher margin and advance backed orders, leading to an improvement in the margins and lower working capital debt requirement.

Moderate Liquidity: The company has been reporting negative cash flow from operations since FY16 due to higher working capital requirement. Cash and cash equivalents declined to INR1.0 billion (FY16: INR2.04 billion).. Any delay in improvement in the net working capital cycle would impact the cash balances, and consequently its debt servicing ability. However, a sustained increase in the profitability levels backed by positive cash flow from operations would lead to an improvement in the liquidity position.

Revenue Visibility; Customer Concentration: Order book declined to INR26.0 billion at end-December 2017 (1.5x of FY17 revenue) from INR28.7 billion at end-September 2016 (2.9x of FY16 revenue) because of a delay in securing new orders from its foreign operations, leading to a decline in its foreign order book. At end-December 2017, nearly 42.0% of the total order book (70% as of September 2016) comprised orders from TFA, of which 50% consisted low margin orders, inherited at the time of the acquisition. With the new sanction of orders worth INR5.5 billion from the Indian Railways in November 2017, the order book from Indian Railways' wagon segment increased to 27.7% of the overall order book at December 2017 (11.7% at September 2016), reflecting increased dependence on the volatile Indian Railways wagon segment.

Established Market Position: TWL is among the largest wagon manufacturers in India in terms of capacity. TWL and Cimmco Limited (a 74.7% subsidiary of TWL; 'IND A+'**Negative**), together accounted 15%-20% of the wagon orders from the Indian Railway over the past few years. The group secured the highest order (around 25%) in the tender floated by the Indian Railways in November 2017. The Indian Railways' wagon procurement process provides for allocation of 40% of the orders based on the past performance; thus resulting in high entry barriers.

Moreover, the group is diversifying its presence into various business segments such as defence, shipbuilding, metros, bridges, electrification and propulsion works, for which it has ventured into acquisitions with some of the foreign entities to acquire technical expertise and qualifications.

RATING SENSITIVITIES

Positive: Timely execution of existing orders coupled with replenishing of order book with higher margin and advance backed orders, leading to EBITDA margins sustaining at 7%-8% and net adjusted leverage improving to about 4.0x by FY20 could result in the Outlook being revised to Stable.

Negative: Change in expectation of net adjusted leverage not reverting to about 4.0x by FY20 due to lower scale of operations, driven by a delay in tying up of working capital facilities, coupled with order book composition skewed towards lower margin and non-advance backed orders could lead to a negative rating action.

COMPANY PROFILE

Incorporated in 1997, TWL manufactures various types of wagons, EMUs, bailey bridges, heavy earthmoving and mining equipment, and steel and spheroidal graphite iron castings. The company has three manufacturing facilities, two in Titagarh and one in Uttarpara, with a combined manufacturing capacity of 6,000 wagons and 36 EMU rakes.

Cimmco, has a manufacturing facility in Bharatpur, Rajasthan, with an annual capacity of 2,400 wagons. Titagarh Agrico Private Limited (a wholly-owned subsidiary of TWL), has set up a tractor manufacturing plant in Bharatpur with an annual capacity of 2,400 units. The capacity can be ramped up based on demand. |

France-based wagon manufacturer and subsidiary of TWL, Titagarh Wagons AFR has an annual manufacturing capacity of 2,000 wagons. TFA, a step-down subsidiary of TWL, manufactures coaches and was merged with Cimmco in FY17.

FINANCIAL SUMMARY

Particulars	9MFY18	FY17	FY16
Revenue (INR million)	9,667.70	17,136.00	9,591.70
EBITDA (INR million)	86.7	1,165.60	400.8
EBITDA margin (%)	0.9	4.2	6.8
Total adjusted debt (INR million)	6,012.60	4,071.70	2,679.60
Cash and cash equivalent (INR million)	1,864.20	1,041.50	2,037.40
Net debt (INR million)	4,148.50	3,030.20	642.20
Source: TWL (consolidated)			

RATING HISTORY

Instrument Type	Current Rating/Outlook			Historical Rating/Outlook	
	Rating Type	Rated Limits (million)	Rating	30 December 2016	9 October 2015
Issuer rating	Long-term	-	IND A+/Negative	IND AA-/Stable	IND AA-/Stable
Fund-based facilities	Long-term	INR1,400	IND A+/Negative/IND A1	IND AA-/Stable/IND A1+	IND AA-/Stable/IND A1+
Non-fund-based facilities	Short-term	INR6,008	IND A1	IND A1+	IND A1+
CP	Short-term	INR500	IND A1	-	-

COMPLEXITY LEVEL OF INSTRUMENTS

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Applicable Criteria

[Corporate Rating Methodology](#)

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