
Rating Rationale for Brassco Estates Private Ltd.'s proposed secured Non Convertible Debenture (NCD) Issue of ₹ 440 crore

NCD Issue Rating: BWR AA (SO)

Outlook : Stable

Brickwork Ratings (BWR) has assigned 'BWR AA (SO)' [Pronounced BWR AA (Structured obligation)] Rating for **Brassco Estates Pvt. Ltd's (Brassco)** proposed ₹ 440 crore secured NCD Issue. 'BWR AA (SO)' stands for an instrument that is considered to offer High credit quality / safety in terms of timely servicing of principal and interest obligations.

Background

Brassco Estates Private Limited (Brassco) is an associate company of Amtek Auto Limited (19% shareholding). Promoter, Mr. Arvind Dham & family hold balance stake in the company.

Brassco is engaged in manufacturing, fabrication, distribution and imports & exports of automotive engine parts and spare parts of tractors, automobiles, locomotives, etc. It undertakes design, manufacturing, marketing and maintenance of components and machinery for automobiles, aircraft etc including devices for transport machinery. It also provides services for setting up integrated forging manufacturing and marketing facilities.

For the period ended May 31, 2010, Brassco posted a PAT of 0.46 crore on net sales of ₹ 1.22 crore as against a PAT of ₹ 0.22 crore on net sales of 0.59 crore for the year ending March 31, 2009. (For summary financials of Brassco, please refer Annexure I)

Brassco proposes to issue secured NCDs for ₹ 440 Crore and utilize the proceeds for investment in the Amtek Group Companies. Amtek Auto Ltd., the flagship Company of the Group will provide an unconditional and irrevocable undertaking to purchase the shares acquired out of the issue proceeds.

The rating for the said NCDs factors, inter alia, the Amtek Auto's established position in the auto component segment, integrated global operations, diverse product profile and healthy financial profile. The rating is however tempered by the company's presence in the highly competitive and fragmented auto component industry and concentration of revenues from the automobile segment.

Security for the NCD issue, Structure and Use of funds

Brassco will utilise part of the issue proceeds towards investments including in group companies. The acquired redeemable preference shares would be pledged to the Debenture Trustee, IDBI Debenture Trusteeship Services. Amtek Auto will provide an unconditional and irrevocable undertaking to purchase the shares acquired out of the issue proceeds. Amtek Auto will give a put option to Brassco to purchase the shares acquired at a pre-determined price (1.15 times). Brassco, in turn will assign this option to the trustee.

Repayment Mechanism

Days	Action	Conditions	Remarks
T-5	Notice to Brassco by Trustee		Brassco to send a confirmation by T-4 whether it would be able to fund the designated account by T-3 days
T-3	Undertaking invoked	If confirmation is not received from Brassco till T-3 days or company confirms its inability to pay by T-3 days	Amtek Auto to credit the designated account within 1 day of receipt of notice
T-3		If Brassco does not credit the designated account with the interest payment amount by T-3 days or an event of default is called, which is not cured within the allowed cure period.	

Note- T refers to interest payment date or the redemption date as the case may be

In case Brassco fails to make the interest payment with respect to the first interest payment date as per the Repayment Mechanism provided above, then the trustee will exercise the undertaking in full and would do either of the following based on written instructions from majority debenture holders:

- (a) Redeem the debentures or
- (b) Pay the interest due to debenture holders and keep the balance in a fixed deposit with the designated bank for the balance tenor of the debentures till all dues on the debentures are serviced

Put / Call Option:

The investors will have a Put Option at the end of (and continuing thereafter upto maturity):

1. 21 months to the extent of 7.5% of the issue amount
2. 27 months to the extent of 12.5% of the issue amount
3. 33 months to the extent of 22.5% of the issue amount
4. 39 months to the extent of 22.5% of the issue amount
5. 42 months to the extent of 35.0% of the issue amount

In case any Put Option is not exercised on the above dates, it will not expire and can be exercised by the investors at any point in time after that date. The investors will provide a notice of 5 business days for invocation of the put option.

BWR has relied upon the company's declaration as regards the description, titles, value of assets and nature of charges to secure the proposed NCD issue and no independent verification or assessments thereof have been made by BWR. A legal opinion from a reputed solicitor firm in this regard has confirmed that the transaction complies with the applicable law in force and the security/ structure is enforceable.

Business

Amtek Auto, established in 1987 by Mr. Arvind Dham, is a leading international manufacturer of automotive components and assemblies with production facilities located strategically across North America, Europe & India. Amtek Auto is the flagship company of the Amtek group. The group's extensive manufacturing capabilities encompass sub assemblies, iron & aluminium castings, forgings and complex machining.

Integrated Operations: Amtek Auto is a leading global auto component manufacturer and is among the large component manufacturers globally, with integrated facilities across India, US and Europe. The company is an established player in the industry with leadership position in a number of its product categories. Amtek Auto's business is further strengthened by its various technical collaborations and joint ventures with global leaders in the auto component space for

superior technology as also by its in house design and product development capabilities. The company has undertaken capacity expansion across its manufacturing locations and product categories in the last 2-3 years. The capacity additions are coming on stream in a phased manner and are expected to help Amtek Auto cater to the increased requirements of auto Original Equipment Manufacturers (OEM's) in line with the growth in the automotive sector.

Amtek Auto's various subsidiaries, primarily in the auto component space include Ahmednagar Forgings, Amtek Crankshafts Ltd., Amtek Ring Gears Ltd., Smith Jones Inc (USA) etc, or investment vehicles viz. Amtek Investments (US), Amtek Investments (UK) etc.

Amtek Auto has entered into a share purchase agreement to acquire 40.2% stake in Amtek India Ltd. (Amtek India). The company has already acquired 26.25% stake in Amtek India. Amtek Auto has made an open offer to the public to acquire 20% additional stake in the company. *(BWR has considered the combined consolidated financials of Amtek Auto Ltd. & Amtek India Ltd. for the purpose of its analysis)*

Diverse Product Profile: Amtek Auto has a diverse product and customer profile catering to all the verticals in the automotive segment (two wheelers, cars, commercial vehicles, tractors). Its product profile spans across forging, aluminium and iron castings, machining and sub-assemblies. Amtek Auto's product portfolio includes 300 varieties of components and assemblies and specializes in the manufacture of the key automotive engine components including connecting rods, crankshafts, cylinder blocks, cylinder heads and camshafts flywheel ring gears etc.

Its customer base includes leading players in the domestic and global automotive industry viz. BMW, Chrysler, Ford, Hyundai, Jaguar Land Rover, Nissan, Tata, Toyota, Volkswagen, Ashok Leyland, Eicher, etc. Exports contributed about 40% of Amtek Auto's revenues in FY09. On the non automotive segment, its customer profile includes railways, defense and equipment and engine manufacturers like JCB, Kawasaki, LG etc. A strong customer base with long term relationships with leading players in the industry ensures steady revenue stream for the company.

The company operates primarily in the highly competitive and fragmented auto component industry comprising numerous unorganised players. Auto component and automobile industry are directly linked with performance of auto components depending on the auto industry. Auto component companies thus diversify into supplying to industrial segments to de-risk from the cyclicity of the auto industry. For Amtek, the automotive segment constitutes ~90% of its revenues (FY09). Amtek is also diversifying into defence, industrial, railway wagons and aerospace segments thereby increasing revenue contribution from non automotive segment in the near to medium term. Players also face pricing pressures from both the raw material suppliers and OEM customers in both the domestic and export markets. Further, unorganized and Chinese products pose stiff competition in the replacement market.

Financial Performance: Amtek Auto

Amtek Auto has a strong networth (combined with Amtek India) of ₹ 4,362 crore, net cash accruals of about ₹ 550 crore in FY2009. Its capital structure in FY2009 stood comfortable with debt equity ratio at 1.06x. The company undertook FCCB buyback/conversion to improve leverage and also reduced debt in overseas subsidiaries. The company's operating efficiencies are reflected in its healthy margins with EBITDA at 21.04% and PAT at 5.82% in FY09. RoCE was moderate at ~6.7% in FY09. Decline in revenues and margin is due to impact of economic downturn leading to lower offtake by automobile OEM's, rising input costs and higher interest costs towards debt taken for expansion.

Key Financials: Amtek Auto (consolidated) (excluding Amtek India)

Year ending June 30,	2009	2008	2007
Net Sales (INR Crs.)	3,439	4,657	3,721
EBITDA (INR Crs.)	700	960	812
PAT (INR Crs.)	190	465	428
Networth (INR Crs.)	2,854	2,877	2,005
Total Debt (INR Crs.)	3,898	2,899	1,813
Equity Capital (INR Crs.)	28	28	26
Total Debt/Tangible Networth (x)	1.37	1.01	0.90
Interest Coverage (x)	4.60	8.30	9.74
Debt-Service coverage ratio (x)	2.93	3.01	4.57
Operating Margins (EBITDA/ Op Income) (%)	20.37	20.61	21.84
Profitability margins (PAT/Op Income) (%)	5.54	9.98	11.51
Return on capital employed (%)	6.33	12.97	17.26
Net cash accruals to total debt (x)	0.11	0.22	0.31
Current ratio (x)	2.37	2.23	2.51

Nine Months Consolidated Results – Amtek Auto (excluding Amtek India)

Period ending Mar 31,	9M FY2010		9M FY2009	
	₹ Cr.	%	₹ Cr.	%
Net Sales	2,694	100	2,823	100
OPBDIT	649	24.1	458	16.2
PAT	197	7.3	120	4.3

For the nine months ending 31st March 2009, revenues were ₹ 2,694 crore down 5% from ₹ 2,823 crore in the corresponding previous period while net profits grew to ₹ 197 crore from ₹ 120 crore for the same period. During the period, the company undertook significant cost control and cost reduction measures and size rationalization which helped in improvement of margins. EBITDA margins increased from 16.2% to 24.1% during the period. (Refer Annexure II for summary financials of Amtek India).

Industry Background

Indian auto component industry is highly fragmented and unorganised with large number of small local players. The organised sector comprises about 77% of the total industry size but has only about 400-450 players catering primarily to OEM's, exports and replacement market. The auto component industry covers a comprehensive range of products including suspension & braking parts, engine parts etc. Amtek Auto's product basket covers about 50% of the product range (viz. engine parts, drive transmission & steering parts, etc).

The Indian auto ancillary industry is about USD 18.7 bn (FY2009) growing at a 23% CAGR (2004-2009). (Source: ACMA)

The Auto component industry's performance is directly linked to the automobile industry. Passenger car, 2/3 wheeler & commercial vehicles segment constitute about 90% of sales in the segment. The economic slowdown in 2008-09 resulted in decline in revenues & profitability of players due to lower offtake for OEM's and weak export markets.

The industry is raw-material intensive with input costs accounting for ~60% of the value of the product. The prices of key raw-materials – pig iron, steel and rubber softened in H1FY2010, but rose thereafter. Key raw material prices are expected to firm up in the near term placing a downward pressure on margins of players.

Rating Outlook

With India fast becoming the global auto hub, prospects for auto ancillary industry also looks bright. Global players setting shop in India allows auto ancillaries to cater to global OEMS in the domestic market itself. Over the medium term, automobile industry and consequently the auto component industry looks positive on the back of healthy demand from auto OEM's in domestic market and improvement in demand in the replacement market. Export markets have just started to pick up in the recent quarters.

Amtek Auto is poised to register good growth in revenues with its capacities coming on stream at a time when the automotive sector looks buoyant and on the growth trajectory. Margins, however, will continue to remain under pressure with prices of key inputs like rubber, steel and aluminium expected to rise.

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Annexure I

Summary Financials: Brassco Estates Private Ltd.

	31-5-2010	31-03-2009
Net Sales (₹ Crs)	1.22	0.59
EBIDTA (₹ Crs)	0.78	0.42
Interest (₹ Crs)	-	0.02
PAT (₹ Crs)	0.46	0.22
NCA (₹ Crs)	0.58	0.30
Networth (₹ Crs)	4.42	3.95
Total Debt (Pref. Shares) (₹ Crs)	-	19.10
Net Fixed Assets (₹ Crs)	3.78	3.89
Investments (₹ Crs)	1.10	1.10
Ratios		
EBITDA Margin	64%	72%
PAT Margin	38%	37%
RoCE	15%	1%
Current ratio	0.50	1.26

Note – During the year financial year end was changed from March 31 to May 31

Annexure II

Summary Financials: Amtek India Ltd (Consolidated)

Year ending June 30,	2009	2008	2007
Net Sales (INR Crs.)	831	1,319	938
EBITDA (INR Crs.)	198	516	240
PAT (INR Crs.)	58	353	129
Networth (INR Crs.)	1,508	1,440	820
Total Debt (INR Crs.)	720	708	581
Equity Capital (INR Crs.)	22	22	18
Total Debt/Tangible Networth (x)	0.48	0.49	0.71
Interest Coverage (x)	4.48	16.84	9.43
Operating Margins (EBITDA/ Op Income) (%)	23.80	39.12	25.59
Profitability margins (PAT/Op Income) (%)	7.01	26.76	13.74
Return on capital employed (%)	5.71	21.50	14.51
Net cash accruals to total debt (x)	0.18	0.57	0.27
Current ratio (x)	3.48	3.99	3.95