Nelcast Limited

March 04, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based Limits	72.00	72.00	[ICRA]A+(reaffirmed); outlook revised to Stable from Positive
Long-term/Short-term Fund-based sub-limits#	(72.00)	(72.00)	[ICRA]A+/[ICRA]A1+ (reaffirmed); outlook to Stable from Positive
Proposed Long-term/Short-term Fund-based Limits	18.00	18.00	[ICRA]A+/[ICRA]A1+ (reaffirmed); outlook to Stable from Positive
Short-term Fund-based Limits	18.00	18.00	[ICRA]A1+ (reaffirmed)
Short-term Non-fund Based Limits	9.00	9.00	[ICRA]A1+ (reaffirmed)
Commercial Paper Programme (CP)	30.00	30.00	[ICRA]A1+ (reaffirmed)
Total	**147.00**	**147.00**	

*Instrument details are provided in Annexure-1

Rationale

The revision in outlook reflects the higher-than-expected increase in debt levels of Nelcast Limited (Nelcast) in the current fiscal, which is expected to result in weaker credit metrics compared to earlier anticipated levels over the medium term. Nevertheless, leverage indicators and coverage metrics of the company are expected to remain comfortable and in line with the category medians, supported by steady earnings from operations. Key ratios including net debt to operating profits and interest coverage are expected to be at around 2 times and 6 times respectively for FY2020. Nelcast's long-term debt levels have increased during the recent quarters to part fund its ongoing Rs. 230-crore capacity expansion at Pedapariya (Andhra Pradesh). Apart from the expansion in scope of the project by around Rs. 35 crore, the increase in net debt levels have been higher than expected because of the change in the funding pattern. The capital expenditure is now fully funded through debt and internal accruals against earlier expectations that a considerable portion of funds would be raised through qualified institutional placement (QIP) route. The ratings reaffirmation also factors in Nelcast's consistent performance, characterised by steady growth in volumes and revenues, its established relationships with leading medium & heavy commercial vehicle (M&HCV) manufacturers and tractor original equipment manufacturers (OEMs), its wide product portfolio and moderate business diversification across segments. The company's revenue growth of more than 20% in FY2018 and 9M FY2019 has been supported by steady demand along with Nelcast's increasing share of business with key customers. However, the company's operating profit margins remain at moderate levels on the back of limited pricing flexibility and firm operating costs. With the expected increase in fixed costs against the gradual ramp-up in utilisation of the new capacities coming onstream, operating margins and return indicators are likely to stabilise at around 10% and 12% respectively over the next 12 to 24 months. The ratings also consider the inherent cyclicality in the key end-user segments (both the domestic M&HCV and tractor segments) that has constrained the company's operating performance in the past, relatively high customer concentration and intense competition in the domestic foundry industry. The ability of the company to sustain its revenue growth and improve margins and return indicators would be the key rating sensitivities going forward.

Outlook: Stable

Stable demand prospects from key business segments, established client relationships and the on-going capacity addition are likely to support Nelcast's performance, going forward. The outlook may be revised to Positive if revenues and earnings significantly exceed estimates and strengthen the financial risk profile. The outlook may be revised to Negative if the earnings are weaker than expected and consequently result in higher dependence on debt to fund the ongoing expenditure program, which would result in adverse impact on the credit metrics.

Key rating drivers

Credit strengths

Consistent performance, aided by strong market position – Nelcast is an established player in the domestic ferrous castings market, generating ~85% of its sales from the leading domestic OEMs spread across both the M&HCV and tractor segments. Steady demand, improving volume share with major customers and product additions have aided in consistent volume growth over the years. Nelcast had recently expanded its capacity to support growing customer requirements – with 18,000 TPA (phase I at Pedapariya, Andhra Pradesh) commercialised in September 2018 and is in the process of further increasing it by another 42,000 TPA in the coming quarters.

Comfortable financial profile – Nelcast's financial profile remains comfortable, characterised by conservative capital structure and adequate credit metrics. Despite the increase in long-term debt levels by around Rs. 120-130 crore to part fund the Rs. 230-crore expansion undertaken, consistent earnings from operations and net worth base have supported the capital structure and coverage metrics. Gearing, net debt to operating profits and interest coverage are expected at around 0.4 times, 2 times and 11 times, respectively in FY2019.

Credit challenges

Operating performance exposed to inherent cyclicality in the key end-user segments – Nelcast derives ~90% of its sales from the domestic M&HCV and tractor segments, which are both exposed to inherent demand cyclicality. Further, the sizeable capacity being added in its second phase of expansion also exposes earnings to demand risks post commercialisation in case of any slowdown in orders from key customers or end-user segments. Presence across two automotive segments, which has supported volumes during alternating periods of slowdown (as witnessed over the years) and ongoing efforts to widen its product portfolio to effectively utilise the new capacities, provide some comfort.

High customer concentration – Nelcast's top-three customers account for around 50% of its revenues. Though revenues in the M&HCV segment are relatively diversified across the key industry players, a substantial portion of the revenues in the tractor segment is generated from a single customer. This exposes the company's earnings to concentration risks. Nevertheless, Nelcast's long relationship with the leading OEMs in both the segments provides comfort.

Liquidity position

Nelcast's liquidity position remains comfortable, supported by internal accruals, despite the funding requirements towards the ongoing capital expenditure (cash balance of around Rs. 53 crore as on September 30, 2018). The average utilisation of fund-based limits was at around 65% for the 12-month period ending December 2018. While the expected increase in working capital requirements with growing scale of operations and ongoing capital expenditure could limit the quantum of free cash flows generated, steady growth in earnings expected, cash reserves held and adequate unutilised lines of credit post the recent enhancement of limits are likely to support the liquidity position of the company.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Construction Equipment Manufacturers
Parent/Group Support	Not applicable
Consolidation	For arriving at the ratings, ICRA has considered the consolidated financial statements of Nelcast and the details of its subsidiary are mentioned in Annexure-2

About the company

Incorporated in 1982, Nelcast manufactures grey and ductile castings for the M&HCV and tractor industry segments. Key products supplied to the M&HCV segment includes wheel hubs, brake drums, axle housing, shackles and brackets among others. For the tractor segment, the company's major products would be transmission casing, centre housing, rear axle housing and hydraulic lift cover. It also supplies ribbed plates and brake discs used in metro rail projects and railways. Nelcast has an aggregate installed effective capacity of 118,000 tonne per annum at its factories at Ponneri in Tamil Nadu and Gudur and Pedapariya in Andhra Pradesh. The capacity would be increased to 160,000 TPA upon commercialisation of its second phase at Pedapariya by September 2019.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	575.95	746.17
PAT (Rs. crore)	34.12	38.26
OPBDIT/OI (%)	11.36%	9.81%
RoCE (%)	13.31%	13.80%
Total Debt/TNW (times)	0.23	0.27
Total Debt/OPBDIT (times)	1.18	1.34
Interest coverage (times)	7.28	13.19

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2019) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating March 2019	Chronology of Rating History for the past 3 years: Date & Rating in FY2019 July 2018	Date & Rating in FY2018 July 2017	Date & Rating in FY2017 July 2016	Date & Rating in FY2016 June 2015
1	Fund-based Limits	Long Term	72.00	-	[ICRA]A+ (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)	[ICRA]A (Stable)
2	Fund-based sub-limits	Long-Term/ Short Term	(72.00)	-	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A (Stable)/A1
3	Proposed Fund-based Limits	Long-Term/ Short Term	18.00	-	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A (Stable)/A1
4	Fund-based Limits	Short Term	18.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA] A1
5	Non Fund-based Limits	Short Term	9.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA] A1
6	Commercial Paper	Short Term	30.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA] A1

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	Fund-based Limits	-	-		72.00	[ICRA]A+(Stable)
NA	Fund-based sub-limits	-	-		(72.00)	[ICRA]A+(Stable)/A1+
NA	Proposed Fund-based Limits	-	-		18.00	[ICRA]A+(Stable)/A1+
NA	Fund-based Limits	-	-		18.00	[ICRA] A1+
NA	Non Fund-based Limits	-	-		9.00	[ICRA] A1+
NA	Commercial Paper				30.00	[ICRA] A1+

Source: Nelcast

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
NC Energy Limited	93.44%	Full Consolidation

ANALYST CONTACTS

Jayanta Roy
+91 33 7150 1120
jayanta@icraindia.com

Balaji M
+91 44 4596 4317
balajim@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@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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ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
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