December 08, 2020

Nelcast Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Term Loans	0.00	151.07	[ICRA]A(Negative); reaffirmed
Long-term Fund-based Limits	160.00	160.00	[ICRA]A(Negative); reaffirmed
Short-term Fund-based Limits	20.00	20.00	[ICRA]A1; reaffirmed
Short-term Non-fund Based Limits	9.00	9.00	[ICRA]A1; reaffirmed
Short-term Fund-based Sub-limits	(50.00)	(50.00)	[ICRA]A1 reaffirmed
Commercial Paper Programme (CP)	30.00	30.00	[ICRA]A1; reaffirmed
Proposed Long-term/Short-term Fund-based Limits	11.00	9.93	[ICRA]A(Negative)/[ICRA]A1; reaffirmed
Total	**230.00**	**380.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation reflects the expected improvement in operating and financial performance of Nelcast Limited (Nelcast) in the coming quarters, supported by the steady growth in supplies to key customers across the industry segments. This growth in revenues and earnings is expected to be primarily driven by the recovery in volumes supplied to the medium and heavy commercial vehicles (M&HCV) industry segment on the back of new product additions and an increase in the share of business with key customers, coupled with a steady growth in volumes supplied to the tractor and export segments. The same is expected to result in Nelcast's revenues and earnings in the current fiscal to be largely in line with the FY2020 levels. Further, its strong share of business with the leading domestic original equipment manufacturers (OEMs), an increase in the content per vehicle supplied with new product additions and an expected recovery in industry demand conditions are likely to drive a consistent growth in revenue and earnings over the medium term. This expected improvement in performance is post a period of weak operating performance in FY2020 and H1 FY2021 on the back of demand slowdown in the domestic automotive industry, accentuated by the adverse impact of the pandemic on the industry volumes. Lower earnings, coupled with an increase in debt levels to fund capacity expansion also resulted in a deterioration of its leverage indicators. The Negative outlook reflects ICRA's expectations that Nelcast's credit metrics would remain at moderate levels in FY2021 primarily due to the recent debt-funded capital expenditure incurred by the company. Nelcast's interest coverage and net debt to operating profit are estimated to remain at ~3 times each in FY2021, and subsequently improve to around 4.5 times and 2 times, respectively in FY2022. The improvement in credit metrics would be dependent on a sustained growth in volumes supplied to major customers and would remain a key rating sensitivity. Nelcast's credit profile remains supported by its comfortable liquidity position on the back of adequate cash reserves and unutilised lines of credit held, lending financial flexibility. 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 operating performance in the past, relatively high customer concentration and intense competition in the domestic foundry industry, limiting pricing flexibility.

Key rating drivers and their description

Credit strengths

Strong market position in key product categories – Nelcast is an established player in the domestic ferrous castings market, generating the major portion of its sales from the leading domestic OEMs. Nelcast has long relationships with major M&HCV and tractor OEMs, with a healthy volume share enjoyed in key products supplied to its customers. Its diversified business profile, continuous product additions and a growing export base supported performance over the years (except in the recent quarters when a sharp slowdown in demand across the industry segments adversely impacted performance).

Conservative capital structure and adequate coverage metrics – Despite an increase in the long-term debt levels (to fund the capacity expansion undertaken) and lower-than-expected cash flows from operations witnessed in the recent past, Nelcast's capitalisation levels and coverage metrics have remained at adequate levels. Key ratios including gearing, interest coverage and DSCR stood at around 0.5 times, 5.5 times and 1.8 times, respectively in FY2020, further backed by its healthy cash reserves and adequate unutilised lines of credit. While its coverage metrics are likely to moderate in the current fiscal because of the adverse impact of the pandemic on earnings in H1 FY2021, they are expected to improve to comfortable levels in the coming quarters, as seen in an improvement in profitability in the recent months.

Credit challenges

Moderation in operating performance in the recent past – With Nelcast's performance remaining largely dependent on the cyclical automotive demand (domestic M&HCV and tractor segments contribute ~70% to its sales), sustained weakness in demand from its key end-user segments would adversely impact its earnings and credit metrics (as witnessed in the recent quarters). The risk is accentuated by the demand-side pressure witnessed because of the pandemic and sizeable new capacity commissioned in Q2 FY2021. Nevertheless, Nelcast's diversified presence is likely to support its performance going forward, with stable growth in supplies to the tractor and export segments witnessed coupled with new product additions and share of business gained with key customers.

High customer concentration – Nelcast's top two customers account for around 40% of its revenues. Though revenues in the M&HCV segment are relatively diversified across the industry players, a substantial portion of revenues in the tractor segment is generated from a single customer. This exposes the company's earnings to client concentration risk. Nevertheless, Nelcast's long relationships and strong linkages with the leading OEMs provide comfort.

Liquidity position: Adequate

Nelcast's liquidity position remains comfortable, supported by its free cash and bank balances held and the buffer available in the working capital limits utilised (which together stood at around Rs. 90 crore as on September 30, 2020). The average working capital utilisation stood at ~70% over the last 12 months ending October 2020. While funding requirements are expected to remain high with firm repayment obligations (at around ~Rs. 30 crore over the next 12 months) and the likely increase in working capital requirements, Nelcast's liquidity position is likely to remain adequate, supported by the liquidity buffer held and an expected improvement in earnings from operations from Q3 FY2020.

Rating sensitivities

Positive triggers – Given the Negative outlook, an upgrade in the ratings is unlikely in the near term. However, the outlook may be revised to Stable if there is a strong recovery in volumes and earnings in the coming quarters, which in turn would improve its credit metrics. Specific metrics that may lead to a change in the outlook include net debt to operating profits reducing to less than 2 times and the interest coverage improving to more than 5 times on a sustained basis.

Negative triggers – Ratings may be downgraded if there is a sustained pressure on revenues and earnings in the coming quarters, which would adversely impact its credit metrics and liquidity position. Specific metrics which may result in a downgrade include the net debt to operating profits remaining above 2.5 times and the interest coverage remaining below 4 times on a sustained basis.

Analytical approach

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

About the company

Incorporated in 1982, Nelcast manufactures grey and ductile castings for the M&HCV and tractor industry segments. Around 20% of the overall revenues is also generated from the supplies to various export markets. Key products supplied to the M&HCV segment include wheel hubs, brake drums, axle housing and brackets among others. For the tractor segment, the company's major products are transmission casing, centre housing, 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 160,000 tonnes per annum. Its factories are located at Ponneri in Tamil Nadu and Gudur and Pedapariya in Andhra Pradesh.

Key financial indicators (Consolidated and audited)

	FY2019	FY2020
Operating Income (Rs. crore)	860.23	570.85
PBT (Rs. crore)	57.72	30.81
PAT (Rs. crore)	38.44	36.01
OPBDITA/OI (%)	9.28%	9.17%
PAT/OI (%)	4.47%	6.31%
Total Outside Liabilities/Tangible Net Worth (times)	0.96	0.85
Total Debt/OPBDITA (times)	2.50	4.30
Net debt/OPBDITA (times)	1.77	3.38
Interest Coverage (times)	8.54	4.18

Source: Nelcast and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Amount Rated	Amount Outstanding	Rating (FY2021) 8-Dec-2020	29-Jun-2020	Rating History for the Past 3 Years FY2020 5-Dec-2019	1-Aug-2019	FY2019 4-Mar-2019	5-July-2018	FY2018 26-July-2017
1	Long-term term loan facilities	Long Term	151.07	151.07*	[ICRA]A (Negative)	-	-	-	-	-	-
2	Long-term fund-based limits	Long Term	160.00		[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Positive)
3	Short-term fund-based limits	Short Term	20.00	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Short-term non-fund-based limits	Short Term	9.00	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Short-term fund-based sub-limits	Short Term	(50.00)	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1+	-	-	-
6	Commercial paper programme (CP)	Short Term	30.00	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
7	Proposed long-term/short-term fund-based limits	Long-Term/ Short Term	9.93	-	[ICRA]A (Negative)/ [ICRA]A1	[ICRA]A (Negative)/ [ICRA]A1	[ICRA]A+ (Negative)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A+ (Stable)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+

*Amount in Rs. Crore; Source: Nelcast; *Outstanding as on October 31, 2020*

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 click here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan 1	Mar 2018		Mar 2024	61.44	[ICRA]A (Negative)
NA	Term loan 2	July 2019	-	Mar 2026	89.63	[ICRA]A (Negative)
NA	Cash Credit	-	-	-	160.00	[ICRA]A (Negative)
NA	e-VFS	-	-	-	20.00	[ICRA]A1
NA	LC &BG & CEL	-	-	-	9.00	[ICRA]A1
NA	Export packing credit	-	-	-	(50.00)	[ICRA]A1
NA	Commercial Paper Programme (CP)	-	-	-	30.00	[ICRA]A1
NA	Proposed Long-term/short-term fund-based limits	-	-	-	9.93	[ICRA]A (Negative)/ [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

Source: Nelcast

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About ICRA Limited:

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