August 22, 2023

LGB Forge Limited: Ratings reaffirmed; outlook on long-term rating revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based facilities	17.00	17.00	[ICRA]BBB- reaffirmed; Outlook revised to Negative from Stable
Short-term non-fund based facilities	10.00	10.00	[ICRA]A3; reaffirmed
Total	**27.00**	**27.00**	

Instrument details are provided in Annexure-I

Rationale

The revision in outlook on the long-term rating follows LGB Forge Limited's ('LGBFL' / 'the company') weaker-than-expected performance in FY2023 and Q1 FY2024, and moderation in ICRA's expectations about the company's performance in FY2024. Backed by established relationships with reputed tier-I auto components suppliers, its diversified segment presence and clientele, and uptick in domestic auto demand, the company was expected to report healthy performance and accruals. However, LGBFL reported operating loss of Rs. 2.4 crore in FY2023 and Rs. 1.0 crore in Q1 FY2024 against an operating profit margin (OPM) of 7.9% in FY2022, impacted by machinery breakdown in the hot forging division, other operating challenges in the machining division and demand volatility in cold forgings. The operating and cash losses have cascaded into stretched coverage metrics as well for the aforementioned period. While the accruals are expected to improve going forward, aided by focussed preventive maintenance measures and operational improvement undertaken, the extent of improvement remains to be seen.

The ratings remain supported by the company's operational and financial flexibility by virtue of it being part of the larger Coimbatore-based LGB Group. The promoters have infused unsecured loans of Rs. 4.5 crore in FY2023 and Rs. 2.0 crore in Q1 FY2024, given the weak operating performance, and are expected to extend timely and adequate financial support, on need basis, to meet the company's operational and financial commitments going forward as well. The company had undrawn working capital lines of Rs. 3.4 crore as on June 30, 2023. Also, LGBFL does not have any term loans along with undrawn general purpose term loan of Rs. 10.0 crore, as on date. However, LGBFL has relatively low market share because of its modest scale, and witnesses competition from other forging players. Also, going forward, the impending electrification of the automotive industry could have a bearing on the company's revenues over the medium term, since LGBFL caters to auto electricals.

Key rating drivers and their description

Credit strengths

Financial and operational flexibility as part of larger Coimbatore-based LGB Group – LGBFL enjoys financial flexibility, lender/investor comfort and operational flexibility by belonging to the larger, Coimbatore-based LGB Group. The promoters owned 73.82% stake in the company as on June 30, 2023, with 28.45% stake held by Mr. V Rajvirdhan, the grandson of Mr. L. G. Balakrishnan. Additionally, Ms. V Rajasri, the granddaughter of Mr. L.G. Balakrishnan, has been LGBFL's Managing Director (MD) w.e.f. February 16, 2023. The promoters have also infused unsecured loans of Rs. 4.5 crore in FY2023 and Rs. 2 crore in Q1 FY2024, given the weak operating performance, and are expected to extend timely and adequate financial support, on need basis, to meet the company's operational and financial commitments going forward as well.

Revenue diversification across segments and clients – LGBFL is a tier-II player and supplies to reputed tier-I auto component suppliers in both the domestic and export markets. Its customer profile is diversified, with no single customer accounting for more than 25% of revenues in FY2023. Further, the company's revenues are diversified across passenger vehicles (PVs), light commercial vehicles (LCVs) and tractors. This insulates revenues from risks arising from downturn in a particular segment or lower volumes from a specific client to an extent.

Credit challenges

Weak performance in FY2023 and Q1 FY2024; stretched coverage metrics – The company reported operating loss of Rs. 2.4 crore in FY2023 and Rs. 1.0 crore in Q1 FY2024 against an OPM of 7.9% in FY2022, impacted by machinery breakdown in the hot forging division, other operating challenges in the machining division and demand volatility in cold forgings. The operating and cash losses have cascaded into stretched coverage metrics as well for the aforementioned periods. While the accruals are expected to improve going forward, aided by focussed preventive maintenance measures and operational improvement undertaken, the extent of improvement remains to be seen.

Modest scale of operations; intense competition from larger, unorganised players restricts pricing flexibility – The company has modest scale of operations with an operating income of Rs. 117.0 crore in FY2023, limiting the benefits from economies of scale. LGBFL is a relatively small player in the highly competitive forging industry, with pressure from larger players restricting its pricing flexibility. It also has relatively low market share with its customers because of its scale. Nonetheless, its established relationships with reputed tier-I auto component suppliers support its revenues to an extent.

Impending electrification of automotive industry could have bearing on LGBFL's revenues – Some of the company's products are auto electrical components, whose usage is expected to be minimised in electric vehicles (EVs) in comparison to those with internal combustion engines. As a result, the move towards electrification of automobiles might impact LGBFL's revenues over the medium to long term. However, LGBFL's segment diversification, presence in components that are unlikely to be impacted by the EV transition, and anticipated addition of new products mitigate the risk to an extent.

Liquidity position: Stretched

The company's liquidity remains stretched, impacted by its relatively weak accruals. It had a minimal cash balance as on June 30, 2023. The company's average fund-based utilisation was 72.2% of sanctioned lines for the 12-month period from July 2022 to June 2023, and it had undrawn working capital lines of Rs. 3.4 crore as on June 30, 2023. Also, as on date, LGBFL has an undrawn general purpose term loan of Rs. 10.0 crore. Further the promoters have committed to extending timely and adequate financial support, on need basis, to meet the company's operational and financial commitments going forward. Against these sources of cash, the company has repayment obligations of Rs. 0.3 crore in FY2024, Rs. 0.5 crore in FY2025, and Rs. 1.0 crore on the sanctioned term loan for FY2024–FY2026, apart from maintenance capex.

Rating sensitivities

Positive factors – The outlook on the long-term rating could be revised to Stable if the company demonstrates a significant improvement in revenues and margins, resulting in improvement in debt protection metrics and liquidity position.

Negative factors – The ratings may be downgraded if there is sustained weak performance, working capital stretch or sizeable debt-funded capex resulting in deterioration in liquidity position or significant rise in debt levels. Specific metrics that could lead to a rating downgrade include Debt/ OPBDITA more than 3.0x on a sustained basis.

Environmental and social risks

Environmental considerations: LGBFL, being an auto component supplier, remains indirectly exposed to climate-transition risks by virtue of its automotive original equipment manufacturer (OEM) customers manufacturing products used across different fuel powertrains. Accordingly, the prospects for LGBFL are linked to the ability of its customers to meet tightening emission requirements. The company also remains exposed to tightening environmental regulations with regard to waste and pollution norms, which can lead to an increase in operating costs and new capacity instalment costs. LGBFL has been taking steps to minimise the impact of environmental risks on its operations and carbon footprint, by enhancing its reliance on renewable sources and other energy saving efforts such as adoption of energy-efficient fixtures/equipment and water recycling.

Social considerations: Social considerations for LGBFL relate primarily to maintaining healthy industrial relations and product safety. Attracting and nurturing skilled manpower is critical as it seeks to keep pace with innovation and technological changes. On the product front, vehicle recalls by OEMs because of defective auto parts could create additional cost burden and liabilities. The company is also exposed to changing consumer preferences, including but not restricted to, increasing awareness of the potential environmental damage from emissions, shift towards EVs, usage of sustainable materials and societal trends like preference for ride sharing.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Suppliers
Parent/Group support	Not Applicable
Consolidation/Standalone	The ratings are based on LGBFL's standalone financial statements.

About the company

LGB Forge Limited is involved in manufacturing forged (hot, warm and cold forgings) and machined components. It is a tier-II auto ancillary player and caters to both domestic (83% of revenues in FY2023) and export markets, including PV, LCV and tractor segments. The company has manufacturing facilities at Coimbatore, Puducherry and Mysore with a production capacity of 6.2 million hot forging components and 8.2 million number of cold forging components per annum in FY2023. It is a part of the larger Coimbatore-based LGB Group, which includes L.G. Balakrishnan & Bros Limited ([ICRA]AA (Stable)/[ICRA]A1+). The promoters owned 73.82% stake in the company as on June 30, 2023.

Key financial indicators (audited)

Standalone	FY2022	FY2023
Operating income	130.5	117.0
PAT	3.4	-9.3
OPBDIT/OI	7.9%	-2.0%
PAT/OI	2.6%	-8.0%
Total outside liabilities/Tangible net worth (times)	1.2	1.8
Total debt/OPBDIT (times)	1.3	-11.3
Interest coverage (times)	4.1	-0.9

Source: Company, ICRA Research; Note: Amount in Rs. crore; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Financial ratios in the report are ICRA adjusted figures and may not be directly comparable with results reported by the company in some instances.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as of June 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021
					Aug 22, 2023	Feb 23, 2023	Aug 19, 2022	Sep 15, 2021	Jun 12, 2020
1	**Fund based/CC**	Long term	17.00	-	**[ICRA]BBB- (Negative)**	**[ICRA]BBB- (Stable)**	**[ICRA]BBB- (Stable)**	**[ICRA]AA (CE)(Stable)**	**[ICRA]AA (CE)(Stable)**
2	**Non-fund Based**	Short term	10.00	-	**[ICRA]A3**	**[ICRA]A3**	**[ICRA]A3**	**[ICRA]A1+ (CE)**	**[ICRA]A1+ (CE)**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund based /CC	Simple
Short -term non-fund based	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Cash credit**	NA	NA	NA	17.00	[ICRA]BBB- (Negative)
NA	**Bank guarantee/Letter of credit**	NA	NA	NA	10.00	[ICRA]A3

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis –Not Applicable

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545 328
shamsherd@icraindia.com

Srikumar K
+91 44 4596 4318
ksrikumar@icraindia.com

Vinutaa S
+91 44 4596 4305
vinutaa.s@icraindia.com

Bikram Keshari Swar
+91 44 4596 4311
bikram.swar@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@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

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches