June 01, 2020

Ramkrishna Forgings Limited: Ratings downgraded to [ICRA]A-(Negative)/A2+

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
LT - Fund-based-Term Loan	490.05	490.05	Downgraded from [ICRA]A to [ICRA]A- Outlook is Negative
LT-Fund-based- Working Capital Facilities	655	655	Downgraded from [ICRA]A to [ICRA]A- Outlook is Negative
LT/ST - Fund-based- Working Capital Facilities	55	55	Downgraded from [ICRA]A/A1 to [ICRA]A-/A2+ Outlook is Negative
ST - Non-fund based-Working Capital Facilities	330	330	Downgraded from [ICRA]A1 to [ICRA]A2+
Total	**1530.05**	**1530.05**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in the ratings considers the higher-than-estimated deterioration in the credit metrics of Ramkrishna Forgings Limited (RKFL) in FY2020 as a result of the slowdown in the domestic medium and heavy commercial vehicle (M&HCV) industry, as well as weaker-than-anticipated sales in the export market and risks of further slippages in FY2021. The company's overall business environment, including demand prospects in both the domestic and international markets, continues to remain adverse post the outbreak of Covid-19. Given the adverse outlook, the trend in sales velocity of the company along with its ability to maintain adequate liquidity would be the key factors in determining the financial risk profile of the company, going forward.

While RKFL has adequate short-term liquidity in place, its overall debt levels are currently at an elevated level, thereby impacting capital structure and debt coverage indicators. ICRA also notes that as on May 28, 2020, the promoters held 44.91% equity stake in RKFL, of which around 27.94% was pledged, which could weigh on the company's financial flexibility. The shares have been pledged for a loan of Rs 15.75 crore at the holding company level as against the current market valuation of the pledged shares at ~Rs 63 crore as on date. Going forward, RKFL's ability to scale up its operations profitably, both in the new geographies that it intends to enter, as well as supply of newer components, would be the key rating sensitivities. The performance trend of the domestic M&HCV industry coupled with the outcome of the company's plans to increase sales in the export market and domestic non-auto industry would be the key factors in determining the financial risk profile of the company in FY2021 and beyond.

The ratings continue to factor in the established position of the company as a supplier of forged components with an increasing proportion of value-added products in its portfolio. Besides, the location-specific advantage derived from its proximity to raw-material sources helps in controlling the freight costs. The company's ability to pass on the rise in raw-material prices to most of its customers resulted in steady contribution levels over the years. RKFL reported a healthy performance in FY2019 following a strong growth in sale of components in the domestic market as well as an increase in its exports business. The ratings are, however, constrained by the company's sales concentration in the domestic commercial vehicle (CV) segment, particularly to the M&HCV, which is more prone to economic cycles. The current downturn in the M&HCV industry has materially impacted RKFL's performance, as indicated by a fall in component sales in volume terms by ~38% in 9M FY2020. Consequently, the company's return on capital employed (RoCE) is likely to have deteriorated to less than 8% in FY2020 from ~16% in FY2019. Given the current situation, following the Covid-19 pandemic, there is heightened risk of a further impact on domestic M&HCV volumes in FY2021. In addition to the sectoral concentration risk, RKFL also remains exposed to the client concentration risk with the CV division of Tata Motors Limited (TML) and its wholly owned subsidiaries, accounting for a significant portion of the domestic revenues and a single client accounting for the major portion of the company's export orders. Such risks are partially offset by the established market position of the export customer in the global auto-ancillary industry as well as the established market position of TML (rated at [ICRA]AA-/Negative & [ICRA]A1+), having the largest market share in the domestic CV industry, thus reducing the counterparty risk. ICRA also positively factors in the importance of RKFL as a supplier to these counterparties, given the criticality of the components supplied. In addition, the company is also planning to increase sales to the non-auto industries in the domestic market. Moreover, RKFL's recent efforts of acquiring new customers, particularly in Europe, have helped the company diversify its customer base to an extent. ICRA expected an uptick in export sales beginning Q4 FY2020, but, given the outbreak of the pandemic, the same is likely to be delayed. ICRA expects the company to diversify its export base, going forward, and reduce its dependence on the US market. However, success and timing of the same will be monitored. While revising the ratings, ICRA also takes cognisance of RKFL's proposed acquisition of ACIL Limited. While the acquisition is likely to provide the company with an opportunity to further diversify its sectoral and customer base going forward, debt for the acquisition would lead to a further deterioration in the capital structure of the consolidated entity over the short to medium term. Moreover, the quality of the assets being taken over, the time required to turn around the performance of the company, along with any additional investments required would be the key factors in determining the returns from the acquisition.

While revising the ratings, ICRA has considered the company's plan to delay its ongoing capex. ICRA expects the company to judiciously phase its capex to ensure adequate liquidity in the present scenario of a downturn in the business. While ICRA expects RKFL's cash flows to remain adequate relative to its debt service commitments, going forward, its ability to diversify sectoral and geographical revenue bases, acquire new customers and scale up the export business would be the key drivers in determining the overall risk profile of the company.

Key rating drivers and their description

Credit strengths

Established supplier of forged components to the domestic automobile industry – RKFL is an established auto-components supplier, operating in the industry for over 30 years. The acceptance of the company's products is established by the long relationship that the company has with some of the leading auto manufacturers in the country.

Expanded portfolio and higher proportion of value-added products – RKFL has expanded its product portfolio after commissioning large press lines. Such products include front axle beams, knuckles etc, which can also cater to the multi-axial vehicle segment in the domestic as well as the export markets. Capability to manufacture such products has enhanced the company's operating profile.

Increasing export sales – RKFL's export sales are increasing, which helped the company steadily increase its capacity utilisation level in FY2019. A sustained and profitable improvement in export levels with adequate liquidity support would benefit the overall credit profile of the company. The company has tied up with some of the leading commercial vehicle OEMs in Europe, which is likely to convert into sales, going forward.

Counterparty risks are low, however, sales and geographical concentration risks for export orders remain high – The established business position of RKFL's customers from the domestic and export markets reduces counterparty risks. ICRA also positively factors in the importance of RKFL as a supplier to these counterparties, given the criticality of the components supplied. However, sales concentration risks are high, as most of its sales are made to the commercial vehicle industry both in the domestic as well as the export markets. While over 56% of its domestic sales are derived from TML, ~60% of its export sales came from one single large order in the US. RKFL's recent efforts in acquiring new customers, particularly in Europe, have helped the company in diversifying its customer base. Supplies to such new customers were expected to begin from Q4 FY2020 / Q1 FY2021, but now, the same has been delayed. Pick-up of supplies is expected to diversify its export base, going forward.

Credit challenges

Deterioration in performance in FY2020; risks of further slippages in FY2021 post outbreak of Covid-19 – The company's overall business environment, including demand prospects in both the domestic and international markets, remains adverse in FY2021, post the outbreak of Covid-19, which in turn would delay any material improvement in the debt protection metrics.

Exposed to the cyclicality inherent in CV and steel industries – RKFL's cash flows remain exposed to the cyclicality inherent in the domestic commercial vehicle industry. The slowdown in the domestic CV industry had impacted sales in 9M FY2020, which witnessed a YoY decline of ~38% notwithstanding steady export sales.

Moderate level of return on capital employed – RKFL's overall return on capital employed remained moderate at ~16% in FY2019 and estimated to have contracted to less than 8% in FY2020. The overall RoCE is expected to remain under pressure in FY2021 because of weak asset utilisation prospects.

High working capital intensity of the export business; low cost of working capital debt likely to keep coverage indicators favourable – RKFL's export sales are highly working capital intensive because of the large receivable cycle for these sales. ICRA, however, factors in the competitive cost of foreign currency debt, which keeps the debt coverage indicators at moderate levels.

Liquidity position: Adequate

RKFL's liquidity is adequate on account of its adequate cash flow from operations and prolonged debt repayment schedule. The overall liquidity position receives support from unutilised working capital facilities of ~Rs. 100 crore. The company has annual debt repayment liabilities of Rs. 90-100 crore in the next few financial years. ICRA expects RKFL to generate adequate cash flows vis-a-vis its debt repayment liabilities.

Rating sensitivities

Positive triggers – Given the Negative outlook, an upgrade in the near term is unlikely. The Outlook can be revised to Stable if there is an improvement in the overall liquid position and visibility in demand and cash flows.

Negative triggers – The company's ratings can be downgraded further if weak domestic demand scenario persists for an extended period. Lower-than-anticipated export sales could also be a trigger for a rating revision. RKFL's ratings would come under pressure if Total Debt/EBITDA rises significantly above 3 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	The rating is based on the consolidated financial profile of the company. As on March 31, 2019, the company had one operating subsidiary that is enlisted in Annexure 2.

About the company

Incorporated in 1981, RKFL commenced its operations in 1984 primarily as a forging manufacturer for the Indian Railways. Manufacturing from two facilities located in and around Jamshedpur and another small unit near Kolkata, the company's existing forging facility comprises hammer forge and up-setter forge with a total capacity of 46,000 MTPA, a ring-rolling unit with a capacity of 24,000 MTPA and four press lines of total 80,000 MTPA capacity. RKFL commissioned two of its four press lines of 3,150 tonnes (T) and 4,500 T in July 2014. The third press line of 6,300 T was commissioned in August 2015 and the fourth and the heaviest press line of 12,500 T started commercial operations in December 2015.

RKFL recorded a profit after tax (PAT) of Rs. 119.3 crore on an operating income (OI) of Rs. 1,797.3 crore in FY2019 against a PAT of Rs. 94.7 crore on an OI of Rs. 1,428.9 crore in FY2018.

In 9M FY2020, RKFL reported a PAT of Rs. 15.9 crore on an OI of Rs. 892.2 crore.

Key Financial Indicators (Standalone, Audited)

	FY2018	FY 2019	9M FY2020[1]
Operating Income (Rs. crore)	1428.9	1797.3	892.2
PAT (Rs. crore)	94.7	119.3	15.9
OPBDIT/ OI (%)	19.5%	20.6%	18.7%
RoCE (%)	14.0%	16.4%	
Total Outside Liabilities/Tangible Net Worth (times)	1.7	1.5	
Total Debt/OPBDIT (times)	3.0	2.4	
Interest coverage (times)	4.0	4.6	3.0
DSCR	1.7	2.0	

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

[1] Provisional

Rating history for last three years

	Instrument	Current Rating (FY2021) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating 01-Jun-20	Chronology of Rating History for the past 3 years Date & Rating in FY2020 20-Dec-19	Date & Rating in FY2020 22-Nov-19	Date & Rating in FY2020 04-Oct-19	Date & Rating in FY2019 29-Mar-19	Date & Rating in FY2019 26-Jul-18	Date & Rating in FY2018 28-Feb-18	Date & Rating in FY2018 18-Dec-17
1	Term Loan	Long Term	490.05	490.05	[ICRA]A- (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Fund based-Working Capital Facilities	Long Term	655	655	[ICRA]A- (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
3	Fund based-Working Capital Facilities	Long Term/Short Term	55	55	[ICRA]A- (Negative)/A2+	[ICRA]A (Negative)/A1	-	-	-	-	-	-
4	Non-fund based-Working Capital Facilities	Short Term	330	330	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+	[ICRA]A2+

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	Term Loan	2015-2018	NA	2024	490.05	[ICRA]A- (Negative)
NA	Fund based- Working Capital Facilities	NA	NA	NA	655	[ICRA]A- (Negative)
NA	Fund based- Working Capital Facilities	NA	NA	NA	55	[ICRA]A- (Negative)/A2+
NA	Non-fund based-Working Capital Facilities	NA	NA	-	330	[ICRA]A2+

Source: Ramkrishna Forgings Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Globe Forex & Travels Limited	100.00%	Full Consolidation

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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

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