

June 29, 2020

## TRL Krosaki Refractories Limited: Ratings reaffirmed

### Summary of rating action

| Instrument*                             | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action                |
|---|-----------------------------------|----------------------------------|------------------------------|
| Fund Based – Term Loan                  | 260.00                            | 260.00                           | [ICRA]AA(Stable); Reaffirmed |
| Fund Based – Working Capital Facilities | 237.00                            | 237.00                           | [ICRA]AA(Stable); Reaffirmed |
| Non-fund Based Limits                   | 170.24                            | 170.24                           | [ICRA] A1+; Reaffirmed       |
| Commercial Paper                        | 75.00                             | 75.00                            | [ICRA] A1+; Reaffirmed       |
| <b>Total</b>                            | <b>742.40</b>                     | <b>742.40</b>                    |                              |

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of the ratings considers the steady financial performance of TRL Krosaki Refractories Limited (TRL) in FY2020, supported by its leadership position in the domestic refractory market with a wide product portfolio of high quality refractories, strong brand image and a large and reputed client base. TRL's top line grew by ~4% in FY2020. While there was a marginal dip in the operating profit margin (OPM) in FY2020 to 10.9%, the capital structure remained conservative, with a gearing of 0.5 times and debt coverage indicators strong with interest cover of 10.9 times. TRL's cost competitiveness in certain categories of refractories due to its captive raw material sources and long-term arrangements with key raw material suppliers also support the operating profile of the company. The ratings also favourably factor in the significant operational and management synergies of TRL with its parent, Krosaki Harima Corporation (KHC; in which Nippon Steel Corporation, rated at Baa2 (Negative) by Moody's, holds a 42.9% stake), which holds a 77.62% stake in the company.

The long-term rating, however, continues to be constrained by the exposure of the company to the cyclicity inherent in the steel industry as ~65% of its revenues is earned through sales to the steel companies. Moreover, the pricing power of the refractory players, including TRL, is limited due to the fragmented industry structure with surplus capacity and competition from imported refractories on the back of low-duty protection. ICRA, however, notes that the focus on Refractory Engineering Management Services (REMS) business has resulted in a differentiated competitive position for the company. Moreover, an increase in the sales volume of products used as consumables in steel making has led to a considerable de-risking of the business model due to reduced dependence on project related business. Notwithstanding the same, with the Covid-19 related disruptions likely to cause a fall in steel production in the domestic and export markets, ICRA expects TRL's financial performance to remain muted in the current year.

ICRA notes that the company is undertaking a sizeable capital expenditure towards capacity expansion of its basic, dolomite and tap hole clay segments and capacity set-up in the black refractory segment, which is being funded by external debt and internal accruals. While a portion of the capex is already completed, the remaining is expected to be incurred by the last quarter of FY2021. TRL's experience in project execution and easy access to established technology from the parent are expected to mitigate project execution and market risks to an extent. Notwithstanding an increase in debt levels expected in the current financial year in the backdrop of the ongoing capex, TRL's capital structure is expected to remain conservative. With healthy cash accruals projected from the business, TRL's risk profile would also continue to remain

strong, going forward. The Stable outlook is underpinned by ICRA's expectations that TRL would continue to maintain its strong position in the refractory business with healthy cash flows relative to its debt service obligations.

## Key rating drivers and their description

### Credit strengths

**Market leader in the domestic refractory market, a reputed client base** – TRL is the largest manufacturer of refractory products in India. It has a comprehensive range of refractory products covering all grades and shapes for industries like steel, copper, cement, aluminium, glass and other non-ferrous industries. TRL is among the largest manufacturers of dolomite refractories in the world and the only manufacturer in India. It is also the leading supplier of silica refractories for coke ovens and glass industry worldwide. The company has a reputed client base, which includes renowned entities like TSL, JSW Steel Ltd etc. The company gets repeat orders from its reputed clientele, reflecting TRL's acceptable quality of refractory products. Moreover, the reputed client base reduces counterparty risk to a large extent.

**Consistent improvement in turnover in recent years, driven by expansion of customer base as well as increased product offerings while maintaining profitability** – The company's operating income grew steadily over the past few years, with a CAGR of around 12% during FY2015-FY2020. A consistent growth in the top line was supported by the company's increasing customer base, coupled with a growth in volumes and foray into new segments like tap hole clay and flow control products. The company's operating profitability also remained stable at around 10-12%, which resulted in healthy accruals.

**Financial profile characterised by healthy capital structure and coverage metrics** – TRL's financial profile has been comfortable, as characterised by its conservative capital structure (gearing of 0.5 times and TOL/TNW of 1.2 times as on March 31, 2020) and healthy debt coverage indicators (interest coverage of 10.9 times and Total Debt/OPBDITA of 1.3 times in FY2020), despite an increase in the debt outstanding in the books of the company to part fund the capex towards augmenting capacity. In addition, availability of surplus cash accruals for part funding of working capital requirements kept the working capital borrowings range bound despite increasing scale of operations. Notwithstanding the increase in debt levels expected in the current financial year in the backdrop of the ongoing capex, TRL's capital structure is expected to remain conservative.

**Strong parentage with significant operational and management synergies** – TRL derives significant operational and management synergies from its parent, KHC, a global leader in the refractories business. Moreover, a 42.9% of KHC's equity is held by Nippon Steel Corporation, a global integrated steel producer. KHC holds a 77.62% stake in TRL at present, after purchasing TSL's stake in the company in December 2018.

### Credit challenges

**Exposure to cyclical inherent in the steel industry** – TRL is exposed to the cyclical inherent in the steel industry as ~65% of its revenues is earned through sales to the steel companies. However, an increase in the sales volume of products used as consumables in steel making has led to a considerable de-risking of the business model due to reduced dependence on project-related business. Notwithstanding the same, with the Covid-19 related disruptions likely to cause a fall in steel production in the domestic and export markets, ICRA expects TRL's financial performance to remain muted in the current year.

**Intense competition in the industry** – The pricing power of the refractory players in India is limited on account of the fragmented industry structure with surplus capacity and competition from imported refractories on the back of low duty protection. To consolidate its position in a fragmented Indian industry, the company has taken over the management of

some of the small domestic refractory manufacturers through management and buyback contracts. The company has also taken measures to diversify its product portfolio by increasing its focus on the Refractory Engineering Management Services (REMS), wherein it produces tailor-made refractories to suit the specific needs of consumers and advises the clients in designing and usage of refractory bricks in the furnace.

**Exposure to fluctuations in supply and prices of main raw materials** – The company imports a large portion of its raw materials, particularly for basic refractories, from China. Following the implementation of new environmental rules in China, prices of fused magnesia had moved up sharply in FY2018 and have stayed firm since then. While TRL’s long-term relationships resulted in stable supply linkages, any disruption in supply may result in an increase in raw material prices going forward, thereby impacting the profitability of the company.

### Liquidity position: Strong

The strong liquidity position is supported by no long-term debt repayments scheduled in the near term, healthy fund flow from operations and adequate buffer in the form of unutilised working capital limits. Notwithstanding the ongoing capex for which the long-term funding is already in place, TRL’s liquidity would continue to remain strong, going forward. The company also enjoys considerable financial flexibility, given its healthy relationship with banks.

### Rating sensitivities

**Positive triggers** – ICRA may upgrade TRL’s ratings if a sustained improvement in end-user demand leads to a significant improvement in turnover and profit margins of the company.

**Negative triggers** – Pressure on TRL’s ratings may arise if profitability and cash accrual are lower than expected due to volatility in raw material prices and weak demand from end-user industries. Specific metrics that could lead to a rating downgrade include RoCE below 15% and/or the interest coverage remaining below 7.0 times on a sustained basis.

### Analytical approach

| Analytical Approach             | Comments  |
|---------------------------------|---|
| Applicable Rating Methodologies | <a href="#">Corporate Credit Rating Methodology</a>   |
| Parent/Group Support            | Parent Company: Krosaki Harima Corporation (KHC)<br>While no direct funding support from the parent is envisaged, TRL enjoys synergies in terms of managerial / operational / technical support from KHC, in which Nippon Steel Corporation holds a 42.9% of the equity capital. In addition, the company’s association with KHC also expands its export opportunities. |
| Consolidation/Standalone        | The rating is based on the standalone financial profile of the company.   |

### About the company

TRL Krosaki Refractories Limited (TRL) was initially established in 1958 under the name of Tata Refractories Limited as a joint venture between Tata Steel Limited (TSL) and Didier Werke AG of Germany. Gradually, Didier exited the operations and TSL had the majority stake of 51%. Between FY2006 and FY2010, TSL increased its stake in the company to 77.46%. In May 2011, TSL sold 51% of its stake in the company to Krosaki Harima Corporation (KHC) of Japan, a subsidiary of Nippon Steel Corporation and the world leader in flow control refractories. The company was subsequently renamed as TRL Krosaki Refractories Limited in 2011. On December 31, 2018, TSL sold its entire 26.62% stake to KHC, thereby raising KHC’s stake in the company to 77.62%.

## Key financial indicators (audited)

|  | FY2019 | FY2020 |
|--|--------|--------|
| Operating Income (Rs. crore)                         | 1593.5 | 1652.9 |
| PAT (Rs. crore)                                      | 84.7   | 100.7  |
| OPBDIT/ OI (%)                                       | 11.5%  | 10.9%  |
| RoCE (%)   | 25.4%  | 23.2%  |
| Total Outside Liabilities/Tangible Net Worth (times) | 1.2    | 1.2    |
| Total Debt <sup>^</sup> / OPBDIT (times)             | 1.2    | 1.3    |
| Interest Coverage (times)                            | 11.7   | 10.9   |
| DSCR   | 8.3    | 8.5    |

Source: TRL; <sup>^</sup>Excludes lease liabilities

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

| Instrument                                  | Type       | Current Rating (FY2021) |  |                   | Chronology of Rating History for the Past 3 Years |                         |                              |                    |                         |
|---|------------|-------------------------|--|-------------------|---|-------------------------|------------------------------|--------------------|-------------------------|
|   |            | Amount Rated            | Amount Outstanding as on 31-March-2020 | Date & Rating     | Date & Rating in FY2020                           | Date & Rating in FY2019 |                              |                    | Date & Rating in FY2018 |
|   |            |                         |  |                   |   | June 2020               | June 2019                    | January 2019       |                         |
| 1 Term Loan                                 | Long Term  | 260.00                  | 87.17                                  | [ICRA]AA (Stable) | [ICRA]AA (Stable)                                 | -                       | [ICRA]AA- (Stable) withdrawn | [ICRA]AA- (Stable) |                         |
| 2 Fund-based Working Capital Facilities     | Long Term  | 237.00                  | -                                      | [ICRA]AA (Stable) | [ICRA]AA (Stable)                                 | [ICRA]AA-&              | [ICRA]AA- (Positive)         | [ICRA]AA- (Stable) |                         |
| 3 Non-fund based Working Capital Facilities | Short Term | 170.24                  | -                                      | [ICRA]A1+         | [ICRA]A1+   | [ICRA]A1+&              | [ICRA]A1+                    | [ICRA]A1+          |                         |
| 4 Commercial Paper                          | Short Term | 75.00                   | -                                      | [ICRA]A1+         | [ICRA]A1+   | [ICRA]A1+&              | [ICRA]A1+                    | [ICRA]A1+          |                         |

Amount in Rs. crore; & - Rating watch with developing implications

## 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](http://www.icra.in)

## Annexure-1: Instrument details

| <b>Instrument Name</b>                    | <b>Date of Issuance / Sanction</b> | <b>Coupon Rate</b> | <b>Maturity Date</b> | <b>Amount Rated (Rs. crore)</b> | <b>Current Rating and Outlook</b> |
|---|------------------------------------|--------------------|----------------------|---------------------------------|-----------------------------------|
| Term Loan                                 | FY2020                             | -                  | FY2025               | 260.00                          | [ICRA]AA (Stable)                 |
| Fund-based Working Capital Facilities     | -                                  | -                  | -                    | 237.00                          | [ICRA]AA (Stable)                 |
| Non-fund based Working Capital Facilities | -                                  | -                  | -                    | 170.24                          | [ICRA]A1+                         |
| Commercial Paper                          | -                                  | -                  | 7-365 days           | 75.00                           | [ICRA]A1+                         |

Source: TRL

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