July 31, 2020

Bharat Forge Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount	Current Rated Amount	Rating Action
Term Loan/ECB	USD35 Million	USD35 Million	[ICRA]AA+/ Negative Reaffirmed
Fund-based Facilities	Rs. 2100.00 crore	Rs.2100.00 crore	[ICRA]AA+/ Negative Reaffirmed
Non-Convertible Debenture	-	Rs. 500.00 crore	[ICRA]AA+/ Negative assigned
Non-fund Based Facilities	Rs. 700.00 crore	Rs.700.00 crore	[ICRA]A1+ Reaffirmed

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation, along with the Negative outlook, reflects ICRA's expectation that Bharat Forge Limited's (BFL) credit profile will continue to witness pressure in the near term due to the ongoing slowdown in the automotive space (mainly commercial vehicles segment or CVs) as well as the industrial segment across geographies including India, the USA and Europe, coupled with the impact of the Covid-19 pandemic.

The company reported a decline of around 44% in its standalone revenue in Q4 FY2020, compared to Q4 FY2019, due to slowdown across geographies in the domestic as well as US CV market, weakness in oil and gas segment, along with Covid-19 pandemic-related impact on dispatches. Subsequently, the operational deleverage affected its operating profitability, which along with moderation in asset turnover, will have a bearing on its return indicators as well as coverage indicators. BFL's standalone operations are expected to witness sharp contraction in revenue and profitability in Q1 FY2021, driven by the nationwide lockdown.

ICRA expects that the decline in CV as well as oil and gas business at the standalone level, coupled with the expectations of a subdued performance by its subsidiaries will impact the company's financial performance for a major part of FY2021 at the consolidated level. Nevertheless, various cost cutting measures at the organisation shall support its bottom line, to an extent, in the short term and result in economies of scale benefits over the medium to long term. Furlough benefit in its overseas subsidiaries from the local government (especially German and Swedish subsidiaries) should provide some support in keeping wage expenses under check at the subsidiary level. ICRA expects BFL's coverage indicators to weaken in the near term with net debt/OPBIDTA increasing to 2.7-3.0 times in FY2021 from 1.7 times in FY2020. A large share of the company's debt is bill discounting done for its reputed clientele, which have relatively strong credit profile and hence low counterparty risk. Excluding bill discounting, its consolidated net debt/OPBIDTA stood at 0.8 times in FY2020. ICRA believes that the expected recovery in demand, along with cost rationalisation measures, should aid in substantial recovery in operating profits, with net debt/OPBIDTA likely to improve back to 1.5-1.7 times in FY2022.

At present, ICRA has a Negative outlook for multiple automotive segments including PV and CV segments. The novel coronavirus pandemic and the consequent nationwide lockdown significantly impacted economic activity and disrupted the supply chain. ICRA expects volume decline across most automotive segments in FY2021, with sharp double-digit reduction expected in domestic PV and M&HCV segments. The trajectory of demand recovery in CV and industrial segments will be a key monitorable for BFL's credit profile.

The ratings draw comfort from BFL's strong liquidity position with unencumbered cash and liquid investments of over Rs. 2,000 crore as of June 2020 on a consolidated basis, coupled with unutilised bank lines of around Rs. 500 crore, resulting in overall liquidity buffer of over Rs. 2,500 crore. It is expected to raise Rs. 500 crore via issuance of long-term non-convertible debentures, which will support its liquidity position. The ratings continue to reflect BFL's leading position in the global automotive forgings industry, especially in the CV chassis and engine component space. The ratings note its large scale of operations, diversified business portfolio with a strong customer base across auto and industrial segments across geographies, and its technical capabilities.

While diversification across industrial segments have helped in mitigating some impact of the cyclicality in the CV segment during the recent downturn, BFL's dependence on the CV segment (44% of consolidated turnover in FY2019) remains high over the medium term. It is continuously working on diversifying its business portfolio by increasing the share of industrial segment, passenger car segment and aluminium content in its overall revenue pie. Going forward, the company's ability to maintain its cost structure and profitability level, despite headwinds in the underlying end-user industries such as the CV and O&G segments remain a key monitorable.

Key rating drivers and their description

Credit strengths

Leadership position in CV engine and chassis components segment; strong customer base in domestic and international markets facilitated by strategic acquisitions – BFL is the market leader in the domestic chassis and engine component segments for CVs. It is the main supplier to leading domestic CV OEMs. Along with its subsidiaries, the company supplies forged components to all major global CV OEMs. Over the years, it has added new customers and geographies to diversify its business profile and clientele.

Diversified product profile and dual shore capabilities; strong engineering, design and fully-integrated manufacturing capabilities help in maintaining steady share of business with leading OEMs and improved traction in new platform development programmes – BFL's strong market position reflects its large scale of operations (with facilities to supply entire range of auto components). Its research and development infrastructure allows the company to enjoy the status of a complete solution provider right from the conceptualisation and designing stage to the manufacturing and validation stage.

Diversification through investments in industrial components business and favourable demand prospects especially in defence, aerospace and locomotive sector support long-term growth – To de-risk its business model from the cyclicality of the automobile industry, BFL has been increasingly focussing on its industrial business with a varied product mix including forged and machined products. The company has been supplying to industrial segments for applications in oil and gas, wind energy and a range of heavy engineering applications, which accounted for 44% of its consolidated turnover in FY2019.

Strong liquidity profile – BFL's liquidity position remains strong, supported by sizeable liquid investments of over Rs. 2,000 crore, along with healthy cash accruals and unutilised credit lines of around Rs. 500 crore. It is expected to raise Rs. 500 crore via issuance of long-term non-convertible debentures, which will further support its liquidity position.

Credit challenges

High working capital intensity and moderately leveraged capital structure – Owing to high exports, BFL's receivable cycle is stretched, which resulted in high working capital intensity. To improve its cash flows, the company discounts invoices of its overseas customers, as discounting rate is substantially lower than the domestic funding rate. Due to sharp decline in turnover, there will be short-term aberration in working capital cycle (NWC/OI) because of relatively higher receivable cycle compared to its creditor cycle. Consequently, the working capital intensity is likely to deteriorate in the current fiscal.

Challenging operating environment across geographies; though manpower rationalisation efforts has helped in improving break-even levels–With its lean cost structure and superior product mix, BFL has been able to sustain healthy operating margin, despite a decline in volume, amid the challenging demand environment in its end-user industries in the past. Going forward, the company's ability to maintain its cost structure and profitability level, despite headwinds in the underlying end-user industries such as CV and O&G segments remain a key monitorable.

Despite diversification plans, exposure to highly cyclical CV segment both in India and international markets remains high. Anti-dumping duty or any other customs duty on the US auto-component imports can have a bearing on BFL's performance– BFL's revenue can be broadly divided into CV (~44% of consolidated revenue), PV (~12%) and industrial segment (~44%). It is working on diversifying its product base by increasing exposure to PV, locomotive, defence and aerospace components, where the demand is relatively stable compared to the cyclical M&HCV segment. It aims to diversify its business portfolio through product diversification and focussing on the industrial business segment. The auto component industry remains vulnerable to pricing pressures from the large OEMs.

Liquidity position: Strong

The company's liquidity profile is **strong**, supported by large unencumbered cash and liquid investments of over Rs. 2,000 crore and undrawn bank lines of around Rs. 500crore as of June 2020. Despite headwinds in the key end-user industry as well as sizeable capex and investment plans, BFL's liquidity profile is expected to remain healthy due to strong cash accruals. The management has guided to maintain cash and liquid investments to the tune of Rs. 1,500 crore on a sustained basis.

Rating sensitivities

Positive triggers – Given the current scenario, an upgrade in the long-term rating from the current level is unlikely. The outlook on the long-term rating can be revised to Stable in case of sustained improvement in profitability and coverage indicators. The short-term rating is already at the highest level.

Negative triggers – Negative pressure on BFL's rating could arise in case of sustained slowdown in its key end-user industries, thereby exerting pressure on the profitability and coverage indicators. Moreover, large debt-funded acquisition or capacity expansion, which could adversely impact capital structure, would trigger a negative rating action. Moreover, Net Debt/ OPBITDA above 1.5 times, on a sustained basis, may trigger a downward rating revision.

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 financials of Bharat Forge Limited. Subsidiaries details including direct as well as step-down subsidiaries are all enlisted in Annexure-2.

About the company

Incorporated in 1961, BFL is the largest forging company in India and one of the largest players in the world, second only to Thyssen Krupp, in terms of its installed capacity and revenues. It has a diversified global customer base including the top five CV and PV manufacturers in the world. BFL's customer base includes virtually every global automotive OEM and tier-I supplier.

The company's business broadly comprises two segments – (i) auto components (56% of consolidated revenue) and (ii) non-automotive components (44% of consolidated revenue). Within the auto components segment, BFL primarily manufactures forging-based engine and chassis components with focus on crankshafts and front-axle beams. It is one the leading suppliers of crankshafts and front-axle beams to CV OEMs in India, Europe and North America and enjoys a sizeable share of business with the leading OEMs. In terms of its geographical mix, America is the largest market for BFL in terms of turnover, followed by India and Europe. Over the years, BFL has followed a two-pronged diversification strategy. During the first phase, the company diversified its presence across markets through a series of overseas acquisitions and transformed its business model from being a forgings-based auto component company with domestic market presence to an entity with global scale and customer base. Over the next phase, it has diversified its presence in the non-automotive applications.

Key financial indicators

Consolidated	FY2019	FY2020
Operating Income (Rs. crore)	10,145.7	8,055.8
PAT (Rs. crore)	1044.6	392.1
OPBDIT/OI (%)	20.0%	13.8%
RoCE (%)	21.4%	8.1%
Total Debt/TNW (times)	0.7	0.8
Total Debt/OPBDIT (times)	2.0	3.6
Net Debt/OPBIDT (times)	1.1	1.7
Interest Coverage (times)	16.0	6.5

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2020) Type	Amount Rated	Amount Outstanding*	Chronology of Rating History for the Past 3 Years Date & Rating in FY2021 31-July 2020	Date & Rating in FY2020 13-March 2020	Date & Rating in FY2020 23-September 2019	Date & Rating in FY2019 27-July 2018	Date & Rating in FY2018 04-Aug 2017
1	Term Loan	Long-term	USD35 Million	USD 20 Million	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)
2	Fund-based Facilities	Long-term	Rs.2100.00 crore	Rs.1408.00 crore	[ICRA]AA+ (Negative)	[ICRA]AA+ (Negative)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)
3	Non-Convertible Debenture	Long-term	Rs. 500.00 crore	NIL	[ICRA]AA+ (Negative)	-	-	-	-
4	Non-fund Based Facilities	Short-term	Rs.700.00 crore	Rs.249.00 crore	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

*Source: Thecompany; *: Amount outstanding as on March 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 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/ECB	March 2015	3M Libor+65 to 225 bps	March 2021	USD 35 Million	[ICRA]AA+(Negative)
NA	Fund-based Facilities	-	NA	-	2100.00	[ICRA]AA+(Negative)
NA	Non-Convertible Debenture	-	-	-	500.00	[ICRA]AA+(Negative)
NA	Non-fund Based Facilities	-	NA	-	700.00	[ICRA]A1+

Source: The company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Direct Subsidiaries/Joint Ventures/Associates		
Bharat Forge Global Holding GmbH	100.00%	Full Consolidation
Bharat Forge International Limited	100.00%	Full Consolidation
Bharat Forge America Inc.	100.00%	Full Consolidation
BF Infrastructure Limited	100.00%	Full Consolidation
Kalyani Strategic Systems Limited	51.00%	Full Consolidation
Analogic Controls India Limited	100.00%	Full Consolidation
BF Elbit Advanced Systems Private Limited	51.00%	Full Consolidation
Eternus Performance Materials Private Limited	51.00%	Full Consolidation
Kalyani Centre for Precision Technology Limited	100.00%	Full Consolidation
Indigenous Limited	NA	Full Consolidation
Tork Motors Private Limited	48.86%	Equity Method
Tevva Motors (Jersey) Limited	36.51%	Equity Method
Step Down Subsidiaries/Joint Ventures/Associates		
Bharat Forge Holding GmbH	100.00%	Full Consolidation
Bharat Forge Aluminiumtechnik GmbH	100.00%	Full Consolidation
Bharat Forge Kilsta AB	100.00%	Full Consolidation
Bharat Forge CDP GmbH	100.00%	Full Consolidation
Bharat Forge Daun GmbH	100.00%	Full Consolidation
Bharat Forge CDP Trading	100.00%	Full Consolidation
MecaniqueGeneraleLangroise	100.00%	Full Consolidation
Bharat Forge Hong Kong Limited	100.00%	Full Consolidation
Bharat Forge PMT Technologies LLC	100.00%	Full Consolidation
Bharat Forge Tennessee Inc.	100.00%	Full Consolidation
Bharat Forge Aluminium USA, Inc.	100.00%	Full Consolidation
Kalyani Precision Machining, Inc.	100.00%	Full Consolidation
BFIL-CEC JV	100.00%	Full Consolidation
Kalyani Rafael Advanced Systems Private Limited	50.00%	Full Consolidation
Lycan Electric Private Limited	48.86%	Equity Method
Tork Motors (UK) Limited	48.86%	Equity Method
BF Premier Energy Systems Private Limited	50.00%	Equity Method
Aeron Systems Private Limited	22.42%	Equity Method
BF NTPC Energy Systems Limited (under liquidation)	51.00%	Equity Method
TalbahnGmBH	35.00%	Equity Method

FerroviaTransrail Solutions Private Limited	49.00%	Equity Method
Hospet Bellary Highways Private Limited	35.00%	Equity Method
Refu Drive GmbH	50.00%	Equity Method
Refu Drive India Private Limited	50.00%	Equity Method
Tevva Motors Limited	36.51%	Equity Method

ANALYST CONTACTS

Subrata Ray
+91 22 2433 1086
subrata@icraindia.com

Ashish Modani
+91 20 6606 9912
ashish.modani@icraindia.com

Pavan Rajkumar Agrawal
+91 20 6606 9916
pavan.agrawal@icraindia.com

RELATIONSHIP CONTACT

L Shivakumar
+91 226114 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

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,
Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore + (91 80) 2559 7401/4049
Ahmedabad+ (91 79) 2658 4924/5049/2008
Hyderabad + (91 40) 2373 5061/7251
Pune + (91 20) 2556 0194/ 6606 9999