September 21, 2020

Kineco Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term, Fund-based facilities	18.00	28.00	[ICRA]BBB-(Negative); Reaffirmed
Long-term, Term Loan/ Working Capital Term loans	36.16	28.78	[ICRA]BBB-(Negative); Reaffirmed;
Long-term/Short-term, Non-fund based	21.00	21.00	[ICRA]BBB-(Negative)/[ICRA]A3; Reaffirmed
Long-term/Short-term, Unallocated Facilities	5.44	2.82	[ICRA]BBB-(Negative)/[ICRA]A3; Reaffirmed
Long-term, Interchangeable limits	(5.00)	(5.00)	[ICRA]BBB-(Negative); Reaffirmed
Short-term, Interchangeable limits	(20.00)	(21.00)	[ICRA]A3; Reaffirmed
Total	**80.60**	**80.60**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings consider Kineco Limited's (Kineco) established track record in the composites industry and its strong parentage with the company being a step-down subsidiary of Indo National Limited (INL), which is one of the market leaders in the zinc carbon batteries segment and has a strong financial profile. The company also has strategic linkages with global major, Kaman Corporation, USA, through a joint venture, Kineco Kaman Composites Indian Private Limited. In the past, Kineco was expected to extend support to Kineco Kaman Composites India Private Limited (KKCI). However, with improvement in KKCI's financial performance, at present, no additional support is expected in the near to medium term. Further, any dividend upstreaming from KKCI to Kineco should be favourable for Kineco's liquidity profile. ICRA also draws comfort from the company's growing business diversification into defence, aerospace and pultrusion industries; although the railways continue to drive ~87% of Kineco's revenues in FY2020.

The ratings are, however, constrained by the company's moderate scale of operations, high customer concentration exposing it to business risk and high working capital intensity due to extended payment cycle from major customers. However, ICRA notes that Kineco's counterparty credit risk is low because of its reputed clientele. In FY2020, the company witnessed revenue growth and profitability improvement, but they were limited by the impact of the pandemic and its resultant lockdown during the fourth quarter, which is typically the strongest season for Kineco's business. The performance during Q1 FY2021 has also been adversely impacted by the lockdown despite healthy orders in hand. However, there has been recovery in operations over the last two months, which is expected to improve further. The company had witnessed healthy order flow in FY2020 from the railways, defence and other industrial sectors. The working capital intensity, however, remained high, partly on account of the pandemic-led disruption, resulting in high utilisation of working capital limits, despite enhancement in limits and additional support from promoters in the form of debt. This also resulted in continued high gearing and stretched coverage indicators. ICRA notes that Kineco's profitability indicators have also remain constrained by its restricted pricing flexibility on account of stiff competition and L1 (lowest bid) tender-based orders from clients.

Going forward, while ICRA expects Kineco's revenues and profitability to improve as the lockdown eases, backed by healthy orders in hand, the liquidity position remains stretched due to high utilisation of existing limits. The company may need additional funds in the form of enhanced limits or additional support from promoters, to be able to execute orders at a higher monthly run rate and scale up, going forward. Further, the order flow in the current year may also be impacted by the pandemic and any intensification of the same and re-imposition of containment measures remain a sensitivity factor.

Key rating drivers and their description

Credit strengths

Part of INL Group – INL holds a majority stake in Kineco through its subsidiary, Helios Strategic System (India) Limited (HSSL). INL enjoys strong brand recall with a pan India presence through its established distribution network for its zinc carbon dry cell batteries, marketed under its own brand, Nippo. Though INL had earlier guaranteed all the bank facilities of Kineco, with the sanctioned debt limits increasing, its bank facilities stand partially guaranteed. Nevertheless, the Group continues to provide need-based funding support to Kineco either in the form of unsecured loans or guarantee for bank limits.

Established track record and considerable experience of promoters in composites industry – Kineco has an established track record in the composites industry and benefits from its strategic linkage with global majors, Kaman Corporation, USA, through a joint venture.

Healthy order book position – Kineco had orders in hand worth ~Rs. 200 crore as on June 30, 2020, which includes orders from the railways, defence and other industrial sectors, providing revenue visibility. Although operations during the first four months of FY2021 were impacted by the lockdown and other restrictions on account of Covid-19, the operations started improving from August 2020 onwards. While, the company is pursuing some large new orders, the overall order flow in the current fiscal may be impacted by the pandemic. Further, the company may need additional funds to operate at a higher monthly run rate and scale up, going forward. The long-term demand outlook for fibre reinforced plastics (FRP) composites is likely to remain favourable, given its wide range of applications.

Credit challenges

Moderate scale of operations – Kineco's credit risk profile is constrained by its moderate scale of operations, which despite its healthy growth in the recent fiscals, continues to remain moderate.

Moderate financial risk profile with leveraged capital structure and moderate debt protection metrics – Kineco's debt protection metrics and coverage indicators had remained moderate owing to net worth erosion till FY2016. Although the equity infusion from INL in FY2017 resulted in a healthy improvement in the company's gearing, its interest coverage and other debt protection metrics remained subdued on the back of high utilisation of working capital facilities. Subsequently, the capital structure and coverage indicators witnessed further deterioration in FY2018 and FY2019 due to subdued profitability and increase in debt owing to higher working capital requirement, in line with growth in scale. In FY2020, although coverage indicators remained subdued, it improved over FY2019 due to better margins, with interest coverage increasing to 2.0 times as on March 31, 2020 against 1.1 times as on March 31, 2019. However, the gearing increased to 3.8 times as on March 31, 2020 over 3.4 times as on March 31, 2019 due to increase in debt levels to meet increased working capital requirement, while the TD/OPBDITA also increased during the period.

Profitability indicators remain constrained and vulnerable to volatility in order flows as well as delays in project execution – Orders from major customers are obtained through L1 tender-based bidding, which limits the pricing flexibility owing to the aggressive bidding from competitors. Stiff competition in the industry characterised by numerous small players limits pricing flexibility and exposes the margins to variation in input costs. Any adverse variation in order flows constrains Kineco's profitability on account of high fixed overheads. Further, any delays in project execution exposes the company to imposition of liquidated damages. While the margins improved in FY2020, it has remained moderate as the improvement was limited by the impact of Covid-19 in Q4 FY2020, as well as due to higher interest expense. While the revenue growth and margin improvement in FY2021 may be impacted by the pandemic, scaling up in subsequent years should result in better absorption of fixed cost and improvement in margins.

High customer concentration risk – Kineco's customer concentration risk remained very high with 80-90% of revenues accruing from the railways (mainly Integral Coach Factory) sector. However, there has been increasing diversification of customer segments in recent years with orders from defence and other industrial sectors. ICRA notes that while the company faced stretched receivable payments from the railway sector, resulting in high working capital intensity, the counterparty risk was low due to its clientele from central public-sector units (PSUs) in the railways and defence sectors, as well as reputed private sector clients.

Liquidity position: Stretched

In the current fiscal, while the cash flows may witness some impact from the pandemic and subdued performance in the first four months, the healthy orders in hand should provide support. Moreover, cash flows are expected to recover from August 2020 onwards with the easing of lockdown measures. The company had also availed moratorium on payments from its lenders as permitted by the RBI due to the Covid-19 pandemic, which supported its liquidity till August 2020. The company has repayment obligations of ~Rs. 10-11 crore for FY2021 and its liquidity profile remains stretched due to high working capital limit utilisation (~89% in last 12 months) and requirement of additional working capital debt to scale up operations, either in the form of enhancement in working capital facilities or unsecured loans from the promoter group. Furthermore, Kineco has no major capex plans in the medium term, which will support its liquidity position.

Rating sensitivities

Positive triggers – A change in outlook to Stable or an upward movement in rating is possible if Kineco demonstrates a sustained improvement in revenue and operating profitability, backed by healthy order flows and improved working capital management. Specific metrics that could lead to an upgrade in ratings include TD/OPBDITA of below 3.0 times and OPBDITA/Interest greater than 3.5 times on a sustained basis.

Negative triggers – Negative pressure on the ratings could arise if the company demonstrates a sustained decline in revenue and margin, or if a stretch in the working capital intensity weakens its liquidity profile or there is substantial moderation in order flow due to the Covid-19 pandemic. Specific credit metrics that could lead to a rating downgrade include OPBDITA/interest lesser than 2.0 times and TD/OPBDITA greater than 4.0 times on a sustained basis. Any significant moderation in the credit profile of the parent, INL, may also put negative pressure on the ratings.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology]()
Parent/Group Support	Parent company: Indo-National Limited INL owns 51% stake in Kineco Limited and has partially guaranteed its bank facilities. INL has extended financial support in the form of unsecured loans and, going forward, ICRA expects INL to provide financial support to Kinceo, should a need arise.
Consolidation/Standalone	The ratings are based on standalone financial statements of the entity.

About the company

Kineco Limited was incorporated in 1994 as Mass Kinematics Private Limited and commenced operations by manufacturing FRP chemical process equipment. The company was renamed as Kineco Private Limited in 2001, and has since diversified into manufacturing custom moulded products and advanced composites. It caters to industries such as aerospace and defence, railways, automotive, and process equipment. It was reconstituted as a public limited company in 2016, with INL picking up stake in Kineco through its wholly-owned subsidiary, Helios Strategic Investments (India) Limited. The company caters to a reputed clientele of industry majors, including Bharat Heavy Electricals Limited, Integral Coach Factory, Bhaba Atomic Research Centre and Research and Development Establishment, Pune, among others.

In FY2020, the company reported a net profit of Rs. 2.1 crore on an operating income (OI) of Rs. 124.5 crore, compared to a net loss of Rs. 1.8 crore on an OI of Rs. 80.0 crore.

Key financial indicators (audited)

	FY2019	FY2020
Operating Income (Rs. crore)	80.0	124.5
PAT (Rs. crore)	-1.8	2.1
OPBDIT/OI (%)	8.9%	15.1%
RoCE (%)	5.2%	13.8%
Total Outside Liabilities/Tangible Net Worth (times)	4.7	5.4
Total Debt/OPBDIT (times)	10.6	4.8
Interest Coverage (times)	1.1	2.0
DSCR	0.4	0.6

Source- Kineco Limited

About the subsidiary company

Kineco Kaman Composites India Private Limited was incorporated in 2012, as a 76:24 joint venture with Kaman Aerospace Group Inc., which is a subsidiary of the US-based aerospace major, Kaman Corporation. KKCI manufactures advanced composites for aerospace, defence, medical imaging and other industries. Its products include composite structural parts for aircrafts and helicopters. In FY2020, the subsidiary reported a net profit of Rs. 10.8 crore on an OI of Rs. 54.4 crore, compared to a net profit of Rs. 12.2 crore on an OI of Rs. 46.6 crore in FY2019.

About the parent company

INL was incorporated by Mr. P. Obul Reddy in 1972 as Nippo Batteries Company Ltd., a joint venture with Matsushita Electric Industrial Co. Ltd. (known as Panasonic Corporation at present) and commenced production of heavy duty zinc carbon dry cell batteries, marketed under its own brand, Nippo. It is the second largest player in the dry cell batteries industry in India, with a market share of ~31%. INL enjoys strong brand recall with a pan India presence through its established distribution network of exclusive distributors, 30 depots, ~5,600 stockists and ~1.7 million retailers across the country. Over the years, the company has diversified its product portfolio and currently includes home UPS and inverters, LED and CFL lamps and bulbs, torches and emergency lights. INL has also set up a 5-MW solar power plant in Polepally village, Telangana, and evacuates power under a PPA to Deccan Hospitals (unit of Apollo Hospitals Enterprise Ltd.) It acquired 51% stake in Kineco in April 2016, through its wholly-owned subsidiary, Helios Strategic System Limited, for a consideration of ~Rs. 40 crore.

In FY2020, at consolidated level, the company reported a net profit of Rs. 10.4 crore on an OI of Rs. 508.2 crore, compared to a net profit of Rs. 26.6 crore on an OI of Rs. 443.2 crore in FY2019.

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2021)					Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Current Rating	Earlier Rating	FY2020	FY2019	FY2017
					21-Sep-2020	19-Jun-2020	13-Nov-2019	28-Sep-2018	07-Mar-2017
1	Cash Credit	Long Term	28.00		[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	[ICRA]BBB-(Stable)	[ICRA]A (SO) (Stable)
2	Term Loan/WCTL	Long Term	28.78	28.78	[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	[ICRA]BBB-(Stable)	[ICRA]A (SO) (Stable)
3	Bank Guarantee	Long Term/ Short Term	21.00		[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Stable)/ [ICRA]A3	-
4	Unallocated Facilities	Long Term/ Short Term	2.82		[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Negative)/ [ICRA]A3	[ICRA]BBB-(Stable)/ [ICRA]A3	-
5	Cash Credit	Long Term	(5.00)		[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	[ICRA]BBB-(Negative)	-	-
6	Letter of Credit	Short Term	(21.00)		[ICRA]A3	[ICRA]A3	[ICRA]A3	[ICRA]A3	[ICRA]A1 (SO)

Amount in Rs. crore

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	-	-	-	28.00	[ICRA]BBB-(Negative)
NA	Term Loan/WCTL	FY2017	-	FY2023	28.78	[ICRA]BBB-(Negative)
NA	Bank Guarantee	-	-	-	21.00	[ICRA]BBB-(Negative)/ [ICRA]A3
NA	Unallocated	-	-	-	2.82	[ICRA]BBB-(Negative)/ [ICRA]A3
NA	Cash Credit	-	-	-	(5.00)	[ICRA]BBB-(Negative)
NA	Letter of Credit	-	-	-	(21.00)	[ICRA]A3

Source: Kineco Limited

Analyst Contacts

K. Ravichandran
+91 4445964301
ravichandran@icraindia.com

Sai Krishna
+91 44 45964300
sai.krishna@icraindia.com

R Gopikrishnan
+91 4445964335
r.gopikrishnan@icraindia.com

Relationship Contact

Jayanta Chatterjee
+91 80 4332 6401
jayantac@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