November 22, 2022

Kesoram Industries Limited: Rating reaffirmed; outlook revised to Negative from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating	-	-	[ICRA]BBB-, reaffirmed; outlook revised to Negative from Stable
Non-Convertible Debentures (NCD)	1549.0	1549.0	[ICRA]BBB-, reaffirmed; outlook revised to Negative from Stable
Optionally-Convertible Debentures (OCD)	167.0	0	[ICRA]BBB-, reaffirmed; outlook revised to Negative from Stable and rating withdrawn
Fixed Deposits	190.0	190.0	[ICRA]BBB-, reaffirmed; outlook revised to Negative from Stable
Total	**1906.0**	**1739.0**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in outlook to Negative factors in Kesoram Industries Limited's (KIL's) expected significant decline in operating profits in FY2023 due to continued cost side pressures and lower sales volumes. In H1FY2023, KIL reported a decline in sales volume by 8% Y-o-Y to 3.2 million MT and the revenues declined by ~2% to Rs. 1608.1 crore. Despite increase in net sales realization by 7% YoY, in H1 FY2023, OPBITDA/MT declined by more than 50% majorly due to steep increase in the power & fuel cost/MT by 45% on a Y-o-Y basis, resulting in a sharp decline in operating profit margins (OPM) to 6.1% in H1 FY2023 (PY: 19.5% in H1 FY2022). While the operating performance from Q3 FY2023 onwards is expected to show some improvement supported by the likely increase in net sales realisations, the operating margins for full year FY2023 are expected to moderate from FY2022 levels. The proposed preferential equity share issue of Rs. 90 crore in H2FY2023 from promoters is likely to aid liquidity.

The reaffirmation of ratings continues to take into account KIL's track record of operations in the cement manufacturing business with established presence in Maharashtra, Telangana and Karnataka. The company's vertically integrated cement operations, with clinkerisation facility of 6.3 MTPA, captive limestone mines and a captive thermal power plant of 94.2 MW also support the rating. Further, the good quality limestone reserves at Sedam in Karnataka aid in cost efficiency. The rating factors in the proceeds from the rights issue of Rs. 399.4 crore as of June 2022 (including Rs. 50 crore of ICD infused by the promoters in H1 FY2022, which has been converted into equity), which has improved KIL's liquidity. Of the rights issue proceeds, Rs. 55 crore was used to repay non-convertible debentures (NCDs) in November 2021 and Rs. 293.9 crore to prepay[1] optionally convertible debentures (OCDs) in January 2022. KIL has fully redeemed the OCDs in August 2022 using the rights issue proceeds and cash flow from operations. It also converted Rs. 430 crore of zero coupon optionally convertible redeemable preference shares into equity in August 2022, thereby resulting in reduction in gross debt and thus supporting its capital structure.

The rating continues to remain constrained by the cyclicality inherent in the cement industry, which leads to variability in profitability and cash flows, company's modest financial risk profile and exposure to refinancing risk. The financial profile is characterised by a leveraged capital structure and modest coverage indicators due to the high adjusted debt[2] levels of around

1 Prepaid on January 31, 2022 against the scheduled repayment date of August 31, 2022

2 Adjusted debt refers to the actual debt outstanding including unpaid premium accrued as against the amortised cost figure reported as per the financial statements prepared as per IndAS accounting

Rs. 1,721.31 crore[3] as on September 30, 2022. Given the decline in OPBIDTA, the adjusted TD/OPBIDTA is likely to remain elevated as on March 31, 2023, however, the lower debt obligations in FY2023 due to prepayment in FY2022 is likely to support the DSCR levels.

KIL is exposed to refinancing risk, with 78% of the debt amortising in February 2026 and high premium payable on redemption. Moreover, the absence of any sanctioned working capital limits may adversely impact the company's ability to fund the incremental working capital requirements, should the need arise. Nonetheless, the company plans to infuse Rs 90 crore of non-convertible cumulative redeemable preference shares (5% coupon) in H2 FY2023 to support its liquidity and working capital requirements. Further, any refinancing of the existing high cost debt at more favourable terms in the near term, could support the debt coverage metrics, going forward. This apart, any incremental investments or support to subsidiaries or Group companies by KIL will remain a key monitorable.

The rating assigned to Rs. 167.0 crore OCD amount have been withdrawn in accordance with ICRA's policy on withdrawal at the request of the company, maturity of OCDs and based on the no dues certificate provided by the trustee.

Key rating drivers and their description

Credit strengths

Established track record in the cement business with integrated manufacturing facilities – KIL has an extensive track record of operations in the cement business with an established presence in Maharashtra, Telangana and Karnataka. The company has a total cement capacity of 10.8 MTPA and the operations remain vertically integrated, supported by clinkerisation facility of 6.3 MTPA, captive limestone mines and a captive thermal power plant of 94.2 MW. Further, good quality limestone reserves at Sedam support cost efficiency.

Proceeds from rights issue have supported debt prepayments – The company launched a rights issue allotment in September 2021 and proceeds of around Rs. 399.4 crore have been received as of June 2022, which aided the liquidity position. Of these proceeds, Rs. 50 crore of ICDs infused from promoters in H1 FY2022 has been converted into equity as a part of this rights issue, an amount of Rs. 55 crore has been used to redeem NCDs in November 2021, while Rs. 293.9 crore has been used to prepay OCDs in January 2022. The company further prepaid the balance OCDs during March 2022 to August 2022 period using a mix of rights issue proceeds and cash flows from operations. The company also converted Rs. 430 crore of zero coupon optionally convertible redeemable preference shares into equity in August 2022, thereby resulting in reduction in gross debt and thus supporting its capital structure. Recently, it has announced infusion of Rs. 90 crore from promoters in the form of non-convertible cumulative redeemable preference shares (5% coupon) which is likely to provide some support to its liquidity.

Credit challenges

Deterioration in operating performance in H1FY2023; vulnerability of revenues to cyclicality in economy – In H1FY2023, KIL reported a decline in sales volume by 8% Y-o-Y to 3.2 million MT and the revenues declined by ~2% to Rs. 1608.1 crore. Despite increase in net sales realization by 7% YoY, in H1 FY2023, OPBITDA/MT declined by more than 50% majorly due to steep increase in the power & fuel cost/MT by 45%, resulting in a sharp decline in operating profit margins to 6.1% in H1 FY2023 (PY: 19.5% in H1 FY2022). While the operating performance from Q3 FY2023 onwards is expected to show some improvement supported by the likely increase in net sales realisations, the operating margins for full year FY2023 are expected to moderate from FY2022 levels. Besides, KIL remains exposed to the demand and pricing dynamics in the cement industry, which are influenced by the cyclical economic trends and capacity additions by the players during such periods.

Modest financial risk profile; exposure to refinancing risk – KIL's financial profile is characterised by leveraged capital structure and modest coverage indicators, given the high adjusted debt levels. Despite the improvement in OPBIDTA, the large

[3] *Book value of debt as on September 30, 2022 is Rs. 1645 crore*

debt and high cost of borrowings resulted in a moderate adjusted interest cover of 2.3 times in FY2022. Although the company has paid/prepaid NCDs and OCDs in FY2022, the adjusted TD/OPBIDTA remained high at ~3.9 times and the adjusted DSCR stood at 0.7 time in FY2022. Given the decline in OPBIDTA, the adjusted TD/OPBIDTA is likely to remain elevated, however, the lower debt obligations in FY2023 due to prepayment in FY2022 is likely to support the DSCR levels. KIL is exposed to refinancing risks with 78% of the debt amortising in February 2026 and high premium on redemption. Further, the absence of any sanctioned working capital limits may adversely impact the ability to fund the incremental working capital requirements, should the need arise. Nonetheless, the proposed preference share issuance of Rs 90 crore in H2 FY2023 is expected to provide support to the company's liquidity position.

Environmental and social risks

Cement manufacturing is an energy intensive process requiring substantial quantities of fuel and thus resulting in greenhouse gas emissions, waste generation, and pollution. Like other cement producers, KIL has had to contend with higher costs to meet the tightening pollution standards. As the standards tighten further, KIL's ability to pass on the increased compliance costs to the customers will be a key monitorable. Further, the industry is exposed to physical climate risks which could impact operations in the absence of sufficient feedstock inventory, given the dependence on limestone mines for raw material.

Social risk in the cement industry stems from the health and safety concerns of employees involved in the mining of limestone and the production of clinker and cement. Entities in the cement industry like KIL are also exposed to labour-related risks and risks of protests/ social issues with local communities, which could impact the manufacturing process, expansion/ modernisation plans.

Liquidity position: Adequate

KIL had free cash balances of Rs. 11.24 crore as on September 30, 2022. In August 2022, KIL has fully redeemed the OCDs as per the scheduled repayment using the rights issue proceeds and cash flow from operations and only NCDs interest obligations are payable in H2FY2023. Further, the company has raised funds to the tune of Rs. 93 crore as on September 30, 2022 through public deposits scheme launched in August 2022, which also supported the liquidity. Also, the regular capex requirements in the near term are anticipated to be met from internal accruals. ICRA expects the company's liquidity position to remain adequate, likely to be supported by proceeds from the proposed preferential equity share issue of Rs. 90 crore in H2 FY2023 and available cash and bank balances.

Rating sensitivities

Positive factors – The outlook could be revised to Stable if the company is able to improve its revenues and earnings, on a sustained basis, leading to an improvement in the debt coverage metrics and liquidity.

Negative factors – Negative pressure on KIL's rating may arise if the revenues and earnings decline on a sustained basis, weakening the credit metrics and liquidity position. Any major debt-funded capex or any incremental support towards subsidiaries/Group companies weakening the credit metrics and liquidity position would pose a downward pressure on KIL's rating. Specific credit metric of adjusted DSCR lower than 1.3 times, on a prolonged basis, may trigger a downward rating revision.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for Cement Companies ICRA's Policy on withdrawal of Credit Ratings
Parent/Group Support	Not Applicable

Consolidation/Standalone	The rating is based on the standalone financial statement of the issuer. This is considering that there are restrictive clauses as per the terms of the NCDs/OCDs for extending support to Group companies without the prior approval of the debenture trustee and further, the corporate guarantee extended by the company to the debt of subsidiary, Cygnet Industries Ltd., had fallen off. ICRA is given to understand that KIL would not extend incremental support to its subsidiaries.

About the company

Kesoram Industries Limited (KIL) was set up in 1919 and is a part of the B.K. Birla Group of Companies, which is a well-diversified conglomerate, having interests in cement, textiles, rayon, chemicals, pulp and paper. The rayon unit has been transferred to Cygnet Industries Limited (wholly-owned subsidiary of KIL) as on March 31, 2016. KIL's tyre manufacturing division was demerged into Birla Tyres Limited from January 1, 2019 (appointed date).

KIL has two integrated cement manufacturing plants at present, one at Sedam (Karnataka) with a clinker capacity of 5.1 MTPA and cement grinding capacity of 9.0 MTPA and the other one at Basantnagar (Telangana) with a clinker capacity of 1.2 MTPA and cement grinding capacity of 1.8 MTPA. As on date, the combined capacity of clinker is 6.3 MTPA and that of cement stood at 10.8 MTPA.

Key financial indicators (audited)

	FY2021 (Audited)	FY2022 (Audited)	H1 FY2023 (Unaudited)
Operating Income (Rs. crore)	2,415.2	3,539.6	1,608.1
PAT (Rs. crore)	166.9	(130.0)	(82.5)
OPBDIT/OI (%)	16.3%	15.5%	6.10%
PAT/OI (%)	6.9%	(3.7%)	(5.1%)
Total Outside Liabilities/ Tangible Net Worth (times)	7.3	3.9	3.6
Total Debt/OPBDIT (times)	4.7	3.1	8.4
Interest Coverage (times)	1.6	1.1	0.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation
Note: All the ratios are based on the reported numbers
Source: Company

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)					Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on September 30, 2022 (Rs. crore)	Date & Rating on	Date & Rating on	Date & Rating in FY2022		Date & Rating in FY2021	Date & Rating in FY2020
					22-Nov-22	20-Jun-22	31-Mar-22	10-Feb-22	-	-
1	Issuer Rating	Long Term	-	-	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-	-
2	NCD	Long Term	1549	1549	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-		
3	OCD	Long Term	167	Nil	[ICRA]BBB- (Negative); withdrawn	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-		
4	Fixed Deposits	Long Term	190	93	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)				

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer Rating	NA
NCD	Simple
OCD	Simple
Fixed Deposits	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-1: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Issuer Rating	NA	NA	NA	-	[ICRA]BBB- (Negative)
INE087A07651	NCD	Mar-21	9.10%*#	Feb-26	1549.0	[ICRA]BBB- (Negative)
INE087A07669	OCD	Mar-21	8.70%	Feb-26	167.0	[ICRA]BBB- (Negative); withdrawn
NA	Fixed Deposits	NA	NA	NA	190.0	[ICRA]BBB- (Negative)

Source: KIL

Interest of 9.10% p.a. for 1-18 months, 11.30% p.a. for 19-36 months and 13.10% p.a. from 37th month onwards.

Annexure-2: List of entities considered for consolidated analysis: Not applicable

ANALYST CONTACTS

Rajeshwar Burla
+91 40 4067 6527
rajeshwar.burla@icraindia.com

Mathew Kurian Eranat
+91 80 4332 6415
mathew.eranat@icraindia.com

Anupama Reddy
+91 40 4067 6516
anupama.reddy@icraindia.com

Tushar Bharambe
+91 22 61693347
tushar.bharambe@icraindia.com

Nijara Kalita
+91 22 61693343
nijara.kalita@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3400
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.

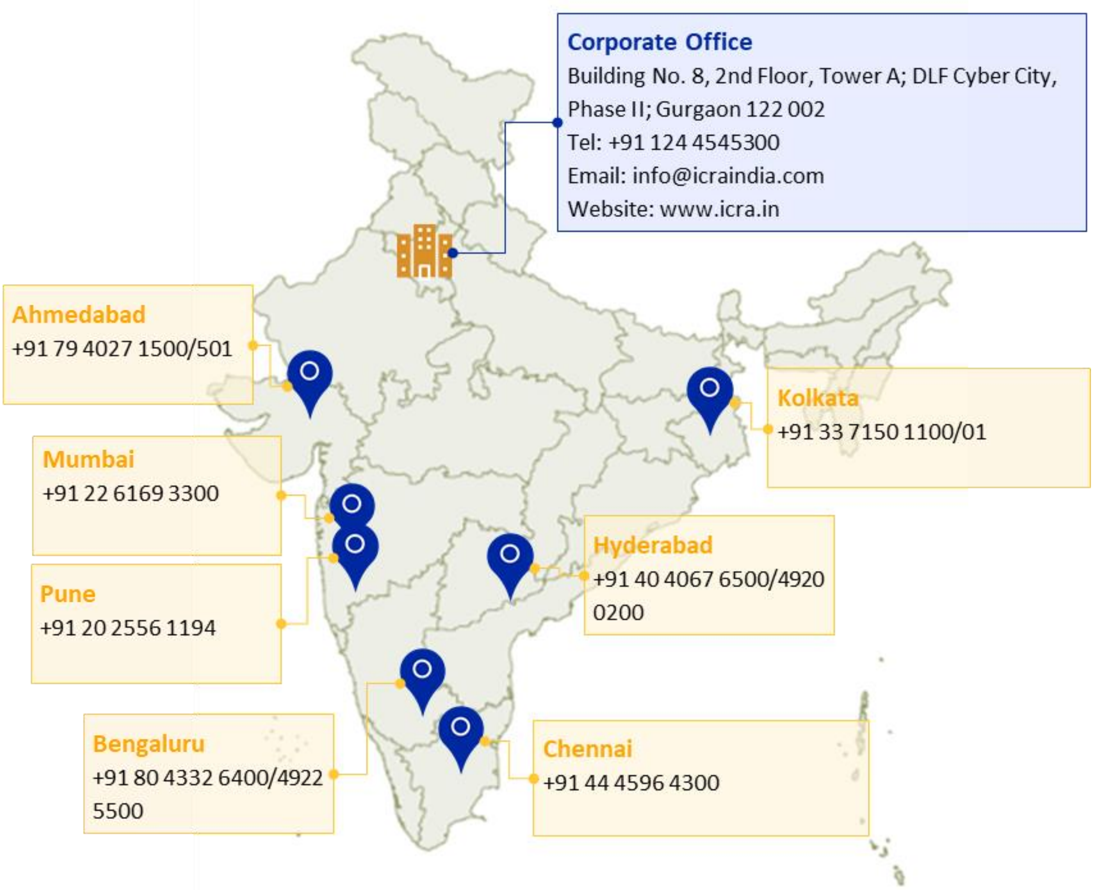
For more information, visit www.icra.in

ICRA Limited

Registered Office

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

Branches



ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents.