March 03, 2023

Kesoram Industries Limited: Rating downgraded to [ICRA]BB+; outlook revised to Stable from Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Issuer Rating	-	-	[ICRA]BB+ downgraded from [ICRA]BBB-; outlook revised to Stable from Negative
Non-Convertible Debentures (NCD)	1549.0	1549.0	[ICRA]BB+ downgraded from [ICRA]BBB-; outlook revised to Stable from Negative
Fixed Deposits	190.0	190.0	[ICRA]BB+ downgraded from [ICRA]BBB-; outlook revised to Stable from Negative
Total	**1739.0**	**1739.0**	

**Instrument details are provided in Annexure-I*

Rationale

The rating downgrade factors in the sustained pressure on Kesoram Industries Limited's (KIL's) operating profits in the current fiscal, and lower-than-expected recovery in OPBDITA/MT due to continued cost side pressures and lower sales volumes in the first half of the year. While the sales volume remained flat in Q3 FY2023 on YoY basis in 9M FY2023, the sales volumes reduced by 5% year-on-year (YoY) to 5.0 million MT. Despite an increase in net sales realisation by 6% YoY, OPBITDA/MT[1] dipped by more than 50% in 9M FY2023 to Rs. 368/MT from Rs. 827/MT in 9M FY2022, primarily due to steep increase in the power and fuel cost/MT by 35% on a YoY basis. Consequently, the operating profit margins (OPM) declined to 7.3% in 9M FY2023 from 17.4% in 9M FY2022. ICRA notes that on a QoQ basis, the OPBITDA/MT improved by 22% in Q3 FY2023 to Rs. 473/MT over Rs. 388/MT in Q2 FY2023. However, it still remained moderate and lower than ICRA's expectation. While the moderation in input costs and likely increase in net sales realisations is likely to support the operating performance from Q4 FY2023 onwards, ICRA expects the operating margins for full year FY2023 to remain low by 630-650 bps over FY2022.

The rating continues to remain constrained by the cyclicality inherent in the cement industry, which leads to variability in profitability and cash flows, the 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 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. The company's creditors continue to remain high. 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. Therefore, timely tie-up of working capital facilities will remain a key monitorable. Nonetheless, the infusion of Rs 90 crore of non-convertible cumulative redeemable preference shares (5% coupon) in Q3 FY2023 has supported the company's liquidity and working capital requirements. The company is in the process of monetization of some non-core assets which it plans to use for debt prepayment and working capital requirements. Further, any refinancing of the existing high-cost debt at more favourable

[1] *Excludes other operating income*

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

[3] *Book value of debt as on September 30, 2022 is Rs. 1,645 crore*

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 continues to consider 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, which supported KIL's liquidity and helped the company is reducing its debt. KIL also fully redeemed the OCDs in August 2022 using the rights issue proceeds and cash flow from operations and also converted Rs. 430 crore of zero coupon optionally convertible redeemable preference shares into equity, thereby resulting in reduction in gross debt and thus supporting its capital structure.

The revision in outlook on the long-term rating to stable factors in the expected improvement in operating performance with softening of input costs, adequate liquidity as on December 30, 2022 and ICRA's expectation that KIL will continue to benefit from its established presence in the western and southern region.

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 supported debt prepayments, additional fund fusion in Q3 FY2023 for supporting liquidity – The company launched a rights issue allotment in September 2021 and proceeds of around Rs. 399.4 crore were received as of June 2022, which aided the liquidity position. Of these proceeds, Rs. 50 crore of ICDs infused from promoters in H1 FY2022 were converted into equity as a part of this rights issue, an amount of Rs. 55 crore was used to redeem NCDs in November 2021, while Rs. 293.9 crore was used to prepay OCDs in January 2022. It further prepaid the balance OCDs during March 2022 to August 2022 using a mix of rights issue proceeds and cash flows from operations. KIL 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. Further, the preference share issuance of Rs. 90 crore (non-convertible cumulative redeemable preference shares with 5% coupon) has supported the company's liquidity.

Credit challenges

Deterioration in operating performance in 9M FY2023; vulnerability of revenues to cyclicality in economy – The sustained pressure on operating profits in the current fiscal, and lower-than-recovery in OPBDITA/MT due to continued cost side pressures and lower sales volumes in the first half of the year. While the sales volume remained flat in Q3 FY2023 on YoY basis in 9M FY2023, the sales volumes reduced by 5% year-on-year (YoY) to 5.0 million MT. Despite an increase in net sales realisation by 6% YoY, OPBITDA/MT[4] dipped by more than 50% in 9M FY2023 to Rs. 368/MT from Rs. 827/MT in 9M FY2022, primarily due to steep increase in the power and fuel cost/MT by 35% on a YoY basis. Consequently, the operating profit margins (OPM) declined to 7.3% in 9M FY2023 from 17.4% in 9M FY2022. ICRA notes that on a QoQ basis, the OPBITDA/MT improved by 22% in Q3 FY2023 to Rs. 473/MT over Rs. 388/MT in Q2 FY2023. However, it still remained moderate and lower than ICRA's expectation. While the moderation in input costs and likely increase in net sales realisations is likely to support the operating performance from Q4 FY2023 onwards, ICRA expects the operating margins for full year FY2023 to remain low by

[4] *Excludes other operating income*

630-650 bps over FY2022. 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 a leveraged capital structure and modest coverage indicators, given the high adjusted debt levels. Despite the improvement in OPBIDTA, the large debt and high cost of borrowings resulted in a moderate adjusted interest cover of 2.3 times in FY2022. Although the company 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 times 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 anticipated 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. The company's creditors continue to remain high. The absence of any sanctioned working capital limits may adversely impact its ability to fund the incremental working capital requirements, should the need arise.

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, its 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

The company's liquidity position is adequate supported by available free cash balances and no scheduled principal repayments till August 2023. The company has fully redeemed the OCDs in August 2022 as per the scheduled repayment using the rights issue proceeds and cash flow from operations and only interest obligations pertaining to the NCDs are payable in H2 FY2023. The principal repayment of the NCDs to the tune of Rs. 91.4 crore will be due in FY2024. Further, the company has raised funds to the tune of Rs. 96 crore as on December 31, 2022 through public deposits scheme launched in August 2022 and by issuance of preferential equity share issue of Rs. 90 crore, which also supported the liquidity. Also, the regular capex requirements in the near term are anticipated to be met from internal accruals. The proceeds from the monetisation of non-core assets in H2 FY2023 and available cash and bank balances is likely to support the liquidity.

Rating sensitivities

Positive factors – The rating can be upgraded 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.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for Cement Companies
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 the clinker is 6.3 MTPA and that of cement stood at 10.8 MTPA.

Key financial indicators (audited)

	FY2021 (Audited)	FY2022 (Audited)	9M FY2023 (Unaudited)
Operating Income (Rs. crore)	2,415.2	3,539.6	2,537.3
PAT (Rs. crore)	166.9	(130.0)	(109.6)
OPBDIT/OI (%)	16.3%	15.5%	7.30%
PAT/OI (%)	6.9%	(3.7%)	(4.3%)
Total Outside Liabilities/ Tangible Net Worth (times)	7.3	3.9	
Total Debt/OPBDIT (times)	4.7	3.1	
Interest Coverage (times)	1.6	1.1	0.6

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 on	Date & Rating in FY2022		Date & Rating in FY2021	Date & Rating in FY2020
					Mar 3, 2023	Nov 22, 2022	Jun 20, 2022	Mar 31, 2022	Feb 10, 2022	-	-
1	**Issuer Rating**	Long Term	-	-	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-	-
2	**NCD**	Long Term	1549	1549	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-		
3	**OCD**	Long Term	-	Nil	-	[ICRA]BBB- (Negative); withdrawn	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-		
4	**Fixed Deposits**	Long Term	190	93	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Stable)				

Complexity level of the rated instruments

Instrument	Complexity Indicator
Issuer Rating	NA
NCD	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-I: 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]BB+ (Stable)
INE087A07651	NCD	Mar-21	9.10%*#	Feb-26	1549.0	[ICRA]BB+ (Stable)
NA	Fixed Deposits	NA	NA	NA	190.0	[ICRA]BB+ (Stable)

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-II: List of entities considered for consolidated analysis: Not applicable

ANALYST CONTACTS

Rajeshwar Burla
+91 40 45474829
rajeshwar.burla@icraindia.com

Anupama Reddy
+91 40 45474829
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