

April 13, 2023

## D&H Secheron Electrodes Private Limited: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term – Fund-based – Cash credit	17.00	17.00	[ICRA]BB+ (Stable); reaffirmed
Short term - Non-fund-based - Others	7.00	7.00	[ICRA] A4+; reaffirmed
<b>Total</b>	<b>24.00</b>	<b>24.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The ratings reaffirmation factors in the track record of DSEPL in its core business of manufacturing welding consumables, giving a wide-ranging acceptability for its products. The ratings continue to take into account the extensive sales distribution network of nearly 450-500 dealers across India and a diversified segment mix with its products catering to various industries. Further, the ratings derive comfort from the company's well-diversified and reputed clientele base. The ratings favourably consider the improved steady and order inflow during the previous as well as current fiscal, resulting in healthy revenue growth for the company. ICRA notes that the company is expanding its production capacity to support increased order execution, driven by healthy order inflow in the near to medium term, thus resulting in a higher scale of operations and healthy cash accruals for the business.

The ratings, however, remain constrained by the moderate operating profit margin of the company. DSEPL has sizeable debt repayment obligations against the cash accruals. This, coupled with the moderated operating profit of the company, has resulted in continued weak coverage indicators for FY2022 as well. ICRA notes that the company's sizeable capital is deployed in non-core business activities like investments in real estate and Group entities, generating modest returns, which continue to adversely affect its liquidity and return metrics. DSEPL's profitability remains modest, being exposed to the adverse fluctuation in raw material prices and intense competition from organised and unorganised players in the industry.

The Stable outlook on the rating reflects ICRA's opinion that DSEPL's revenues and accruals will be supported by the healthy order inflow and improved execution. Also, the company will continue to benefit from its established track record in the welding consumables business.

### Key rating drivers and their description

#### Credit strengths

**Well-diversified product portfolio supported by comprehensive sales and distribution network** – DSEPL has a robust product profile with more than 300 electrode variants. Most of its products are approved by internationally accepted inspection agencies. The company has an established dealership network of nearly 450-500 dealers across India. As a variety of welding consumables are used in different industries, DSEPL benefits from a wide product portfolio and a comprehensive distributor network.

**Diversified customer profile with reputed client base** – DSEPL has a well-diversified and reputed customer base. The top five customers contribute to nearly 10–15% of its annual sales. The extensive presence of the promoters in the industry has helped the company establish strong relationships with suppliers and customers.

**Healthy order inflow and moderate scale of operations-** The company's order inflow scaled up to Rs. 370 crore in FY2022, improving from the stagnant order inflow of nearly Rs. 200 crore over the past years. Further, the company has received orders of nearly Rs. 464 crore for FY2023. The improved order inflow because of a wider distributor network and an enhanced production capacity have resulted in better order execution. DSEPL reported a healthy revenue of Rs. 258 crore in FY2022, a YoY growth of 39%. The healthy revenue growth trend continued during FY2023 as well with the company achieving a revenue of Rs. 371 crore for FY2023. DSEPL is further enhancing its production capacity, which coupled with the improved order inflow in the coming fiscal, is expected to ramp up the company's scale of operations, resulting in healthy cash accruals.

### Credit challenges

**Modest operating margin profile and weak coverage metrics** –DSEPL has a modest operating margin profile in the range of 2-4% mainly due to intense competition in the welding industry and the high volatility in raw material prices. The operating profit margin of the company stood at 2.42% in FY2022, declining from 3.96% in FY2021, adversely affected by increase in raw material prices. As a result, the coverage indicators deteriorated with interest coverage at 1.16 times, total debt/OPBDITA at 8.52 times and DSCR at 0.86 times in FY2022. However, with the expected ramp up in the company's scale of operations, driven by healthy order inflow, softening of raw material prices and various optimisation measures being taken by the company, the operating profit margin is expected to improve in the near term, though will remain in the range of 3-4%. The improvement in operating profit margin may improve the coverage metrics with an interest coverage metrics of around 2-3 times and DSCR of 1.5-2 times in the near term.

**Substantial funds blocked in low-yielding investments** – DSEPL's capital is deployed in non-core assets like investments in real estate and in its various Group companies that constrain its liquidity position, evident from the high utilisation of working capital limits. The company has invested ~Rs. 40 crore in residential properties which are generating modest lease rentals of Rs. 0.9 crore p.a. In addition, the company has investments worth ~Rs. 27.7 crore in its various Group entities, which are not yielding any returns. Such large capital blockage in assets, which are not generating any meaningful returns, continues to affect its RoCE, besides keeping the debt levels elevated and the liquidity position stretched.

**Vulnerability of profitability to price fluctuation risks** – Mild steel (MS)/stainless steel (SS) wires, nickel wires, ferro alloys and minerals are the primary raw materials for producing welding consumables. With a widely diversified product portfolio, DSEPL is required to maintain a high level of inventory for continuous operations. The increased volatility in the prices of ferro alloys and steel exposes DSEPL to raw material price risks. The company's operating margins continue to be modest, led by a moderate level of value addition.

**Intense competition in fragmented industry** – The welding consumables industry is highly fragmented due to the presence of a large number of organised and unorganised players. The stiff competition in the industry limits the pricing flexibility of the industry participants, including DSEPL, thus affecting the operating margins.

### Liquidity position: Stretched

DSEPL has a stretched liquidity profile owing to the high working capital requirements of the business with minimal cushion available in working capital limits and sizeable debt repayments as a significant part of cash generation is parked in illiquid investments. The company has an overdraft limit of Rs 5 crore which is currently unutilised and may be used by the company as per the business requirements. The company is also undertaking capex to enhance its production capacity, partially funded through its internal accruals. Further, ICRA notes that the company has diverted substantial funds towards non-core business activities like investments in real estate, which has increased the company's dependence on debt. However, the company generates modest rental income from the investments in real estate, thus providing some comfort on the debt repayments for the debt taken on these properties.

## Rating sensitivities

**Positive factors** – ICRA could upgrade DSEPL’s ratings if a sustained improvement in revenues and profitability as well as liquidity leads to an improvement in the debt coverage indicators.

**Negative factors** – Pressure on the ratings could emerge if a substantial decline in the revenues and operating margins results in subdued cash accruals. Any significant debt-funded capital expenditure further deteriorating its credit profile, or any significant outflow towards real estate, or inability to improve its liquidity position could lead to a negative revision of the ratings. Specific credit rating metrics that may lead to a negative rating action include interest coverage below 2 times on a sustained basis.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on the company’s standalone financial profile

## About the company

DSEPL was incorporated in 1966 as a joint venture (JV) between the Switzerland-based Secheron Group and Mr. Dalamal and Mr. Hiranandani. The business was taken over by Mr. Ashok Maheshwari in 1986, after the expiry of the technical collaboration. At present, the promoter and his family members control the entire shareholding. DSEPL manufactures welding consumables such as manual metal arc welding (MMAW) electrodes, submerged arc welding (SAW) wires and flux, flux cored arc welding wires and CO2 welding wires at its multiple manufacturing units in Indore, Madhya Pradesh.

### Key financial indicators (audited)

D&H Secheron Electrodes Private Limited	FY2021	FY2022
Operating income (Rs. crore)	185.1	258.2
PAT (Rs. crore)	0.5	0.3
OPBDIT/OI (%)	3.96%	2.42%
PAT/OI (%)	0.3%	0.1%
Total outside liabilities/Tangible net worth (times)	1.3	1.7
Total debt/OPBDIT (times)	6.1	8.5
Interest coverage (times)	1.5	1.2

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

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

**Any other information: None**

### Rating history for past three years

	Instrument	Current rating (FY2024)			Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding (Rs. crore)	Date & rating on	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					April 13, 2023	-	Feb 25, 2022	Nov 18, 2020
1	Fund based – Cash credit	Long Term	17.00	-	[ICRA]BB+ (Stable)	-	[ICRA]BB+ (Stable)	[ICRA]BBB- (Stable)
3	Non-fund-based- Others	Short Term	7.00	-	[ICRA]A4+	-	[ICRA]A4+	[ICRA]A3

### Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund based – Cash credit	Simple
Non-fund based - Others	Very 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	Long term - Fund based- Cash Credit	-	-	-	17.00	[ICRA]BB+ (Stable)
NA	Short Term- Non-fund-based- Others	-	-	-	7.00	[ICRA] A4+

Source: D&H Secheron Electrodes Private Limited

[Please click here to view details of lender-wise facilities rated by ICRA](#)

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

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