September 06, 2021

Ramkrishna Forgings Limited: Ratings upgraded to [ICRA]A(Stable)/[ICRA]A1

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based-Term Loan	490.05	490.05	Upgraded to [ICRA]A from [ICRA]A-; Outlook revised to Stable from Positive
Fund-based- Working Capital Facilities	655	655	Upgraded to [ICRA]A from [ICRA]A-; Outlook revised to Stable from Positive
Fund-based- Working Capital Facilities	55	55	Upgraded to [ICRA]A/[ICRA]A1 from [ICRA]A-/[ICRA]A2+; Outlook revised to Stable from Positive
Non-fund based-Working Capital Facilities	330	330	Upgraded to [ICRA]A1 from [ICRA]A2+
Total	**1530.05**	**1530.05**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings upgrade factors in a sustained improvement in operating and financial performances of Ramkrishna Forgings Limited (RKFL or the company) on the back of a favourable demand outlook for the Medium & Heavy Commercial Vehicle (M&HCV) industry in both the domestic as well as the export markets, a trend which ICRA expects to continue in the near-to-medium term. RKFL's adequate capacity and product reach to cater to this rising demand also remain key credit positives. Increased share of high-margin export volumes in RKFL's sales mix led to improved operating profitability, which rose further to ~23% in Q1 FY2022 compared to ~20.8% in Q4 FY2021 and is expected to remain healthy going forward. Additionally, RKFL's capex cycle is nearing completion. Going forward, with the reduction in overall debt levels due to scheduled repayments and improved capacity utilisation levels, the capital structure and the debt coverage indicators are also expected to improve.

The ratings continue to favourably factor in the established position of the company as a supplier of forged components with an increasing proportion of value-added products in its portfolio. Besides, the location-specific advantage derived from its proximity to raw-material sources helps in controlling the freight costs. The company's ability to pass on the rise in raw material prices to most of its customers resulted in a steady contribution levels over the years.

The ratings are, however, constrained by the company's sales concentration in the domestic commercial vehicle (CV) segment, particularly to the M&HCV, which is more prone to the economic cycles. In addition to the sectoral concentration risk, RKFL remains exposed to the client concentration risk with the CV division of Tata Motors Limited (TML) and its wholly-owned subsidiaries, accounting for a significant portion of domestic revenues and a single client accounting for the major portion of the company's export orders. Such risks are partially offset by the established market position of the export customer in the global auto-ancillary industry as well as the established market position of TML (rated at [ICRA]AA-/Stable & [ICRA]A1+), which has the largest market share in the domestic CV industry, thus reducing the counterparty credit risk. In addition, the company is planning to increase sales to the non-auto industries in the domestic market, which would further reduce concentration risks. Moreover, RKFL's recent efforts of acquiring new customers, particularly in Europe, have helped the company diversify its customer base to an extent. The ratings, however, remain constrained due to moderate levels of return on capital employed and high working capital intensity of business, mainly on account of long receivable period for its export orders. Nevertheless, RKFL's overall liquidity position is comfortable with sufficient unutilised working capital facilities and a sanctioned long-term loan with an extended repayment schedule, a part of which is yet to be drawn.

ICRA also notes the recent enabling resolution passed by RKFL's board to raise ~Rs. 500 crore of funds through equity or debt. Going forward, the funding pattern, end use of funds and its impact on the capital structure of the company will remain key rating factors.

ICRA also takes cognisance of RKFL's proposed acquisition of ACIL Limited. While the acquisition is likely to provide the company with an opportunity to further diversify its sectoral and customer base going forward, debt for the acquisition would impact the capital structure of the consolidated entity over the short to medium term. Moreover, the quality of the assets being taken over, time required to turn around the performance of the company, along with any additional investments required would be the key factors in determining the returns from the acquisition.

Key rating drivers and their description

Credit strengths

Substantial improvement in financial performance expected in FY2022 given a favourable demand outlook for M&HCV industry in both domestic as well as export markets – RKFL has reported healthy operating and financial performances in Q1 FY2022, driven by strong demand from domestic as well as export markets. RKFL primarily caters to the M&HCV segment. A favourable demand outlook for the segment in the near to medium term augurs well for the company. ICRA also notes that RKFL's high-margin export sales are increasing, which helped the company steadily increase its capacity utilisation levels and improve the operating margins to ~23% in Q1 FY2022, which is expected to remain healthy, going forward. A sustained and profitable improvement in domestic as well as export volumes would benefit the overall credit profile of the company in the near term.

Established supplier of forged components to the domestic automobile industry – RKFL is an established auto-components supplier, operating in the industry for over 30 years. The acceptance of the company's products is established by the long relationship that the company has with some of the leading auto manufacturers in the country.

Expanded portfolio and high proportion of value-added products – RKFL has expanded its product portfolio after commissioning large press lines. Such products include front axle beams, knuckles etc, which can also cater to the multi-axial vehicle segment in the domestic as well as the export markets. Capability to manufacture such products has enhanced the company's operating profile. Moreover, the company is at the end of its capex cycle and would be in a position to leverage its additional capacity at a time of market expansion, going forward.

Counterparty risks are low, however, sales and geographical concentration risks for export orders remain high – The established business position of RKFL's customers from the domestic and export markets reduces counterparty credit risks. ICRA also positively factors in the importance of RKFL as a supplier to these customers, given the criticality of the components supplied. However, sales concentration risks are high as most of its sales are made to the commercial vehicle industry both in the domestic as well as the export markets. While ~50% of its domestic sales are derived from TML, historically ~55-60% of its export sales came from one single large order in the US. RKFL's recent efforts in acquiring new customers, particularly in Europe, is progressively helping it diversify its customer base.

Credit challenges

Exposed to the cyclicality inherent in CV and steel industries – RKFL's cash flows remain exposed to the cyclicality inherent in the domestic commercial vehicle industry. Slowdown in the domestic CV industry had impacted sales in FY2020 and H1 FY2021. However, with a turnaround in demand conditions, the company's sales have recovered since Q3 FY2021, and continued to improve since then. Moreover, RKFL's sales were superior than the market trend, which indicates that the company was able to beat the industry downturn to an extent by adding new customers and products in its portfolio. With a further improvement in demand conditions, the favourable momentum is likely to sustain, going forward.

Moderate level of return on capital employed – Historically, RKFL's overall return on capital employed remained at a moderate level of ~10-15%. In FY2020, given the contraction in demand, it declined to 6% and remained at similar levels in FY2021 with the capacity utilisation levels remaining sub-optimal, notwithstanding the recovery in H2 FY2021. In FY2022, the RoCE is likely to improve as the demand prospects are expected to remain favourable.

High working capital intensity of the export business; low cost of working capital debt likely to keep coverage indicators favourable – RKFL's export sales are highly working capital intensive because of the large receivable cycle. ICRA, however, factors in the competitive cost of debt (net of subvention), which keeps the debt coverage indicators at moderate levels

Liquidity position: Adequate

RKFL's liquidity is adequate on account of its healthy cash flow from operations and prolonged debt repayment schedule. The overall liquidity position receives support from the unutilised working capital facilities of ~Rs. 150-200 crore and undrawn term loan of ~Rs. 95 crore. The company has annual debt repayment liabilities of ~Rs. 100-150 crore in the next few financial years. ICRA expects RKFL to generate adequate cash flows vis-a-vis its debt repayment liabilities.

Rating sensitivities

Positive factors – RKFL's long-term rating can be upgraded if the company achieves a healthy increase in scale and sustenance of healthy margins along with diversification in its customer base. Specific triggers for a rating upgrade would be interest cover of over 6 times on a sustained basis.

Negative factors – The company's ratings can be downgraded in case of a delay in recovery of cash flows. Lower-than-anticipated export sales could also be a trigger for a rating revision. RKFL's ratings would come under pressure if TOL/TNW remains above 1.4 times on a sustained basis. Additionally, any large debt-funded capex/acquisition, adversely impacting the capital structure and debt coverage indicators, would remain a key rating sensitivity.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Suppliers
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the consolidated financial profile of the company. As on March 31, 2021, the company had one operating subsidiary that is enlisted in Annexure 2.

About the company

Incorporated in 1981, RKFL commenced operations in 1984 primarily as a forging manufacturer for the Indian Railways. Manufacturing from its two facilities located in and around Jamshedpur and another small unit near Kolkata, the company's existing forging facility comprises hammer forge and up-setter forge with a total capacity of 46,000 mtpa and a ring-rolling unit with a capacity of 24,000 mtpa. Additionally, RKFL has four press lines having a cumulative capacity of 80,000 mtpa. The press lines were commissioned between FY2015 and FY2016 and helped the company expand its product portfolio.

RKFL has a 100% subsidiary, Globe Forex & Travels Limited (GFTL). Incorporated in 1994, GFTL, is involved in the travel and ticketing business and organises corporate leisure trips, conferences and others.

In FY2021, RKFL reported a standalone net profit of Rs. 27.9 crore on an operating income of Rs. 1,288.4 crore. In FY2020, RKFL registered a standalone net profit of Rs. 9.6 crore on the back of net sales of Rs. 1,089.8 crore.

Key financial indicators (audited, Standalone)

RKFL – Standalone	FY2020	FY2021
Operating Income (Rs. crore)	1089.8	1288.4
PAT (Rs. crore)	9.6	27.9
OPBDIT/OI (%)	17.2%	17.8%
PAT/OI (%)	0.9%	2.2%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	2.0
Total Debt/OPBDIT (times)	5.1	5.2
Interest Coverage (times)	2.5	3.0

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Key financial indicators (audited, Consolidated)

RKFL – Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	1194.5	1288.9
PAT (Rs. crore)	9.7	31.7
OPBDIT/OI (%)	16.03%	17.3%
PAT/OI (%)	0.81%	1.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	2.1
Total Debt/OPBDIT (times)	5.2	5.1
Interest Coverage (times)	2.4	2.8

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 (FY2022)					Chronology of Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Mar 31, 2021 (Rs. crore)			Date & Rating in FY2021		Date & Rating in FY2020		Date & Rating in FY2019
					Sep 06, 2021	Jun 28, 2021	Mar 30, 2021	Jun 1, 2020	Dec 20, 2019	Oct 4, 2019 Nov 22, 2019	Jul 26, 2018 Mar 29, 2019
1	Term Loan	Long Term	490.05	490.05	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A- (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Stable)
2	Fund based-Working Capital Facilities	Long Term	655	300	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A- (Negative)	[ICRA]A (Negative)	[ICRA]A (Negative)	[ICRA]A (Stable)
3	Fund based-Working Capital Facilities	Long Term/Short Term	55	-	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A- (Positive)/ [ICRA]A2+	[ICRA]A- (Stable)/ [ICRA]A2+	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A (Negative)/ [ICRA]A1	-	-
4	Non-fund based-Working Capital Facilities	Short Term	330	-	[ICRA]A1	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A1	[ICRA]A1	[ICRA]A1

Complexity level of the rated instrument

Instrument	Complexity Indicator
Term Loan	Simple
Fund based- Working Capital Facilities	Simple
Fund based- Working Capital Facilities	Simple
Non-fund based-Working Capital Facilities	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 analyzing 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, is available on ICRA's 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	2015-2018	NA	2025	490.05	[ICRA]A(Stable)
NA	Fund based- Working Capital Facilities	NA	NA	NA	655	[ICRA]A(Stable)
NA	Fund based- Working Capital Facilities	NA	NA	NA	55	[ICRA]A(Stable)/[ICRA]A1
NA	Non-fund based- Working Capital Facilities	NA	NA	-	330	[ICRA]A1

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis:

Company Name	Ownership	Consolidation Approach
Globe Forex & Travels Limited	100.00%	Full Consolidation

ANALYST CONTACTS

Jayanta Roy
+91 33 7150 1120
jayanta@icraindia.com

Sumit Jhunjhunwala
+91 33 7150 1111
sumit.jhunjhunwala@icraindia.com

Priyesh Ruparelia
+91 22 61693328
Priyesh.ruparelia@icraindia.com

Maitri Vira
+91 33 7150 1103
maitri.vira@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:

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ICRA Limited

Registered Office

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

Branches