

July 28, 2023

L.G. Balakrishnan & Bros 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	150.00	150.00	[ICRA]AA (Stable); reaffirmed
Short-term – Non-fund Based Facilities	100.00	100.00	[ICRA]A1+; reaffirmed
Fixed Deposit Programme	40.00	40.00	[ICRA]AA (Stable); reaffirmed
Total	290.00	290.00	

*Instrument details are provided in Annexure-I

Rationale

The ratings outstanding on the bank lines of L.G. Balakrishnan & Bros Limited (LGB/the company) consider the company's strong business and financial profile and ICRA's expectation of a sustained financial performance in the near to medium term, supported by its dominant market position, significant replacement presence and strong liquidity. The company has market share of over 60% in the domestic two-wheeler (2W) chain segment, with healthy share of business across 2W OEMs. Further, it derives over 30% of its revenues from the domestic aftermarkets, thus insulating its revenues to an extent from any downturns in the domestic 2W space. LGB's operating margins continue to be healthy at 17.4% in FY2023 (PY: 18.7%) and it has remained net debt negative, with unencumbered cash and bank balances of Rs. 474.1 crore as on March 31, 2023. ICRA expects LGB's financial profile and liquidity position to remain strong going forward as well.

LGB's revenues grew by ~4.8% in FY2023 and derived over 80% of its revenues from the domestic 2W industry. Over the medium term, the company's revenue could be vulnerable to risks arising from the impending electrification of vehicles, due to minimal usage of chains in electric 2Ws in comparison to internal combustion driven 2Ws. However, its product diversification plans, sizeable portion of revenues from the replacement segment and anticipated e-2W penetration of only 10-12% of new vehicle sales by FY2025 mitigate the risk to an extent. Also, while LGB's margins are susceptible to variations in commodity prices, the company's practice of negotiation-based pass-throughs for raw materials price increases, has historically capped the moderation in margins to the largest extent. Also, LGB has benefitted from improved operating leverage and periodic cost-optimisation measures, and these are likely to continue going forward as well.

Key rating drivers and their description

Credit strengths

Dominant market position in domestic 2W chains – LGB manufactures and markets chains and allied components (around 79% of operating income (OI) in FY2023) primarily for 2Ws and metal forming products (around 21% of OI in FY2023) for 2Ws, passenger vehicles (PVs) and commercial vehicles (CVs). The company remains an established player in the domestic 2W chain segment with market share of over 60%. It is a tier-I supplier and has healthy share of business across 2W OEMs with no OEM constituting more than 15% of LGB's topline.

Significant presence in the replacement segment – The company sells chains and sprockets under the brand, 'Rolon', in the replacement market and derives over 30% of its revenues from aftermarkets. This insulates its revenues from downturns/lower production volumes in the domestic 2W space, to an extent. Further, domestic aftermarket products command better margins than the domestic OEM segment.

Strong financial profile – LGB operating margins continue to be healthy at 17.4% in FY2023 (PY: 18.7%), supported by its relatively high value addition, higher share of replacement revenues, operating leverage benefits and cost-optimisation measures. As a result of its healthy accruals, moderate working capital requirements and moderate capex over the years, LGB has remained net debt negative since FY2021, and its debt protection metrics continue to be strong, with an interest coverage of 58.1 times in FY2023 (PY:42.6 times). The company also had unencumbered cash and bank balances of Rs. 474.1 crore and adequate buffer of Rs. 95.0 crore against sanctioned working capital lines as on March 31, 2023. ICRA expects LGB's financial profile to remain strong going forward as well.

Credit challenges

Impending electrification of automotive industry may impact revenues – The move towards electrification of automobiles could impact the company's revenues over the medium to long-term owing to minimal usage of chains in electric 2Ws in comparison to internal combustion driven 2Ws. However, the company has diversified its product portfolio by re-entering into the industrial chains segment. Further, LGB is in the process of acquiring Ruchi Strips & Alloys Limited (RSAL), and completion of the same (which is expected by Oct 2023) will widen the company's product portfolio. Sizeable portion of revenues from the replacement segment and anticipated e-2W penetration of only 10-12% of new vehicle sales by FY2025, also mitigate the risk to an extent.

High dependence on the 2W industry – LGB derives over 80% of its revenues from the domestic 2W industry, thereby making its revenues susceptible to any demand slowdown in the segment. However, the company's established presence, low client concentration and sizeable revenues from the replacement segment mitigate the risk to an extent.

Margins susceptible to increase in raw material prices – LGB's margins are susceptible to variations in commodity prices. However, the company's practice of negotiation-based pass-throughs for raw materials price increases, has historically capped the moderation in margins. Also, LGB has benefitted from improved operating leverage and periodic cost-optimisation measures, and these are likely to continue going forward as well. The company is a net exporter and, hence, would not be impacted by the depreciation of the INR against the USD.

Environmental and social risks

Environmental considerations – LGB, being an auto component supplier, remains exposed to climate-transition risks because of its automotive OEM customers' manufacturing products being used across different fuel powertrains. Accordingly, the prospects for LGB are linked to the ability of its customers to meet tightening emission requirements. The company also remains exposed to tightening environmental regulations regarding waste and pollution norms, which can lead to an increase in operating costs and new capacity instalment costs. However, LGB has been taking steps to minimise its carbon footprint by enhancing its reliance on renewable sources and other energy saving efforts such as adoption of energy-efficient fixtures/equipment and water recycling.

Social considerations – Social considerations for LGB relate primarily to maintaining healthy industrial relations and product safety. Attracting and nurturing skilled manpower is critical as it seeks to keep pace with innovation and technological changes. On the product front, vehicle recalls by OEMs because of defective auto parts could create additional cost burden and liabilities. The company is also exposed to changing consumer preferences, including but not restricted to increasing awareness of the potential environmental damage from emissions, shift towards EVs, usage of sustainable materials and societal trends like a preference for ridesharing.

Liquidity position: Strong

LGB's liquidity is strong, supported by healthy anticipated cash flow from operations and unencumbered cash and bank balances of Rs. 474.1 crore as on March 31, 2023. The company has adequate buffer in working capital lines with an average working capital utilisation of 36.6% of sanctioned limits and 17.4% of drawing power for the 12-month period April 2022–March 2023. Going forward, LGB has minimal repayment obligations of Rs. 7.6 crore in FY2024, Rs. 6.5 crore in FY2025 and

Rs. 1.4 crore in FY2026 for its existing term loans and fixed deposits. Although the company has significant capex plans of Rs. 210.0 crore in FY2024, Rs. 200.0 crore in FY2025 and Rs. 200.0 crore in FY2026, predominantly for product diversification, capacity enhancement partly through debottlenecking and maintenance capex, it is likely to be funded through internal accruals. Overall, ICRA expects LGB to meet its medium-term commitments through internal sources of cash and yet be left with sufficient cash surplus.

Rating sensitivities

Positive factors – ICRA could upgrade LGB’s rating if the company demonstrates significant growth in its scale of operations and there is sustained improvement in profitability, along with product diversification. Specific metrics that could lead to an upgrade would be RoCE improving above 25% on a sustained basis.

Negative factors – Negative pressure on LGB’s rating could arise if the company’s net debt levels increase significantly, resulting in deterioration of net debt/OPBITDA over 1.5 times on a sustained basis. Any significant decrease in the top line owing to electrification of vehicles could also exert pressure on the ratings.

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 ratings are based on the consolidated financial profile of the L. G. Balakrishnan & Bros Limited and its subsidiaries as mentioned in Annexure-2.

About the company

LGB is among the largest manufacturers of 2W automotive chains in India (marketed under the brand, ‘Rolon’). It derived 79% of operating income (OI) in FY2023) primarily for 2Ws and metal forming products (around 21% of OI in FY2023) for 2Ws, passenger vehicles (PVs) and commercial vehicles (CVs). In terms of its business segments, 2W constitutes over 80% of its consolidated revenues, while over 30% comes from the replacement segment. The company has a subsidiary, LGB USA Inc., which manufactures fine blanking products. LGB (standalone) accounted for 95% of the consolidated revenues and 89% of the consolidated debt in FY2023. The company has 23 manufacturing facilities across Tamil Nadu, Maharashtra, Uttarakhand, Karnataka, Haryana, Rajasthan and Pondicherry in India and one facility in the US, at the consolidated level.

Key financial indicators (Audited)

Consolidated	FY2022	FY2023
Operating income	2102.1	2203.0
PAT	245.7	252.3
OPBDIT/OI	18.7%	17.4%
PAT/OI	11.7%	11.5%
Total outside liabilities/Tangible net worth (times)	0.5	0.4
Total debt/OPBDIT (times)	0.3	0.3
Interest coverage (times)	42.6	58.1

Amount in Rs crore; Source: Company, ICRA Research; Financial ratios in this document are ICRA adjusted figures and may not be directly comparable with results reported by the company in some instances; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; total debt includes lease liabilities

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2024)		Chronology of rating history for the past 3 years				
		Amount rated (Rs. crore)	Amount outstanding as of March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021
				Jul 28, 2023	Jul 07, 2022	Jun 13, 2022	Aug 30, 2021	Aug 28, 2020
1 Term Loan	Long term	-	-	-	-	-	-	[ICRA]AA (Stable)
2 Long-term Fund-based Facilities	Long term	150.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)
3 Short-term – Non-fund Based Facilities	Short term	100.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4 Fixed Deposit Programme	Long term	40.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	MAA (Stable)	MAA (Stable)
5 Unallocated	Long term	-	-	-	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fixed Deposits	Simple
Fund based facilities	Simple
Non-fund Based 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 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	Fixed Deposit Programme	2016	6.0-8.5%	2025	40.00	[ICRA]AA (Stable)
NA	Long-term Fund-based Facilities	NA	8.3-10.9%	NA	150.00	[ICRA]AA (Stable)
NA	Short-term – Non-fund Based Facilities	NA	NA	NA	100.00	[ICRA]A1+

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
LGB USA, Inc	96.00%	Full Consolidation
GFM Acquisition LLC^	98.47% by LGB USA, Inc	Full Consolidation
GFM LLC^	100.00% by GFM Acquisition LLC	Full Consolidation

Source: Company; ^step down subsidiaries

ANALYST CONTACTS

Shamsher Dewan
+91 124 4545 328
shamsherd@icraindia.com

Srikumar K
+91 44 4596 4318
ksrikumar@icraindia.com

Vinutaa S
+91 44 4596 4305
vinutaa.s@icraindia.com

Bikram Keshari Swar
+91 44 4596 4311
bikram.swar@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
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

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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



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