October 04, 2019

Ramkrishna Forgings Limited: [ICRA]A/A1 ratings reaffirmed; outlook revised to Negative

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Fund-based-Term Loan	443	443	[ICRA]A reaffirmed; Outlook revised to Negative from Stable
Fund-based- Working Capital Facilities	460	460	[ICRA]A reaffirmed; Outlook revised to Negative from Stable
Non-fund based-Working Capital Facilities	239	239	[ICRA]A1 reaffirmed
Total	**1142**	**1142**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in the outlook factors in the slowdown in the domestic medium and heavy commercial vehicle (M&HCV) industry, which in turn may impact RKFL[1]'s overall credit metrics, going forward. ICRA notes that over 50% of RKFL's sales are generated from the sale of components to the M&HCV segment, which has contracted by ~30% during the first five months of FY2020. Consequently, RKFL's sales and profits along with its debt coverage indicators are likely to witness a deterioration as compared to FY2019 and earlier envisaged for FY2020. The impact of a substantial slowdown in the domestic M&HCV industry would be, however, cushioned for the company by the expanding sales in the export market - both in terms of new geographies being catered to, as well as newer components being supplied overseas. In addition, the company is also looking at increasing the sales to the non-auto industries in the domestic market. The trend in performance of the domestic M&HCV industry over the balance period of the year coupled with the success of the company's plans to increase sales in the export market and domestic non-auto industry would be the key factors determining the financial risk profile of the company in FY2020. While revising the outlook, ICRA also takes cognisance of RKFL's proposed acquisition of ACIL Limited. While the acquisition is likely to provide the company an opportunity in diversifying its sectoral and customer base going forward, debt for the acquisition would lead to some deterioration in the capital structure of the consolidated entity over the short to medium term. Moreover, the quality of the assets being taken over, the time required to turn around the performance of the company along with any additional investments required would be the key factors impacting the credit quality of the company.

The assigned ratings factor in the healthy performance of RKFL in FY2019 following a strong growth in sale of components in the domestic market as well as an increase in its exports business. Consequently, debt coverage indicators were healthy with an interest cover of ~ 4.6 times and Total Debt to OPBDITA at 2.4 times. The ratings continue to 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 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 M&HCV, which is more prone to economic cycles. In addition, with the CV division of Tata Motors Limited (TML) and its

[1] *Ramkrishna Forgings Limited*

wholly-owned subsidiaries accounting for a significant portion of the domestic revenues and a single client accounting for a major portion of the company's export orders, RKFL remains exposed to client concentration risks. The above 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/Negative & [ICRA]A1+) having the largest market share in the domestic CV industry, thus reducing the counterparty risks. ICRA also positively factors in the importance of RKFL as a supplier to these counterparties, given the criticality of the components supplied. Moreover, RKFL's recent efforts in acquiring new customers, particularly in Europe, have helped the company diversify its customer base to an extent. ICRA expects the company to diversify its export base further, going forward and thus reduce its dependence on the US market.

While re-affirming the ratings, ICRA has taken into account the company's planned capex of ~Rs. 485 crore to diversify its product base by setting up new press lines and a ring rolling unit. The capex is proposed to be part funded by a debt of ~Rs. 275 crore, thus implying a project debt-to-equity ratio of 1.3:1. The incremental term debt along with higher working capital debt, a necessity as the company increases its scale (given its working capital intensive nature of operations), would limit the scope of an improvement in the capital structure over the medium term. However, an extended back-ended (proposed) repayment of the new debt and the competitive cost of debt would support RKFL's debt coverage indicators as well as liquidity. Moreover, ICRA expects the company to judiciously phase its capex to ensure adequate liquidity in the present scenario of a downturn in the domestic CV industry. While ICRA expects RKFL's cash flows to remain adequate, relative to its debt service commitments, going forward its ability to diversify sectoral and geographical revenue bases, acquire new customers and scale up the export business would be the key drivers determining the overall risk profile of the company.

Key rating drivers

Credit strengths

Established supplier of forged components to the domestic automobile industry – RKFL is an established auto-components supplier, operating in the industry for over the last 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 higher 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.

Increasing export sales – RKFL's export sales are increasing, which helped the company steadily increase its capacity utilisation level. A sustained and profitable improvement in export levels with adequate liquidity support would benefit the overall credit profile of the company.

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. The current slowdown in the domestic CV industry has impacted sales in Q1 FY2020, which witnessed a YoY decline of ~8% and likely to further impact the performance of the company in Q2 FY2020. RKFL's increasing sales in the export market mitigates such risks to an extent

High sales concentration risks; however, counterparty risks low – RKFL has high sales concentration risks, both in the domestic as well as the export markets as most of its sales are made to the commercial vehicle industry. While over 56%

of its domestic sales are derived from TML, ~60% of its export sales came from one single large order. However, the established business position of these customers reduces counterparty risks. ICRA also positively factors in the importance of RKFL as a supplier to these counterparties, given the criticality of the components supplied.

Geographical concentration risks for export orders – A major portion of the company's exports sales takes place in the US market, which results in high geographical concentration risks. RKFL's recent efforts in acquiring new customers, particularly in Europe, have helped the company in diversifying its customer base. While it is slowly diversifying into other markets, an increase in sales to other geographies would be a credit positive.

Moderate level of return on capital employed – RKFL's overall return on capital employed remains moderate as on date as the new press lines are yet to reach optimal capacity utilisation levels. Nevertheless, with a steady improvement in asset utilisation levels, RoCE has witnessed a steady improvement as well.

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 for these sales. ICRA, however, factors in the competitive cost of foreign currency debt, 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. Cash flow from operations is expected to remain sizeable despite the slowdown in sales in the current financial year. Overall liquidity position receives support from unutilised working capital facilities of ~Rs 270 crore. The company has annual debt repayment liabilities of Rs 90-100 crore in the next few financial years. ICRA expects RKFL to generate adequate cash flows vis-a-vis its debt repayment liabilities even under a stretched scenario of domestic sales de-growth.

Rating sensitivities

Positive triggers – Given the Negative outlook, an upgrade in the near term is unlikely. In the medium to long term, ICRA could revise RKFL's rating upwards if the company is able to profitably scale up its sales while maintaining adequate liquidity. A sustained correction in leverage and improvement in coverage indicators could also be a trigger for an upgrade.

Negative triggers – The company's ratings can be downgraded if the weak demand scenario in the domestic M&HCV industry continues. Less-than-anticipated export sales could also be a trigger for a rating revision. RKFL's ratings would come under negative pressure if Total Debt/EBITDA exceeds beyond 3 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Manufacturers
Parent/Group Support	Not Applicable
Consolidation / Standalone	While revising the rating outlook, ICRA has considered the standalone financials of RKFL.

About the company

Incorporated in 1981, RKFL commenced operations in 1984 primarily as a forging manufacturer for the Indian Railways. Manufacturing from 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, a ring-rolling unit with a capacity of 24,000 MTPA and four press lines of total 80,000 MTPA capacity. RKFL commissioned two of its four press lines of 3,150 T and 4,500 T in July 2014. The third press line of 6,300 T was commissioned in August 2015 and the fourth and the heaviest press line of 12,500 T started commercial operations in December 2015.

RKFL recorded a profit after tax (PAT) of Rs. 119.3 crore on an operating income (OI) of Rs. 1,797.3 crore in FY2019 against a PAT of Rs. 94.7 crore on an OI of Rs. 1,428.9 crore in FY2018.

During Q1 FY2020, RKFL reported a PAT of Rs 13.47 crore on an OI of Rs 379.3 crore.

Key Financial Indicators (Standalone, Audited)

	FY2018	FY 2019	Q1 FY2020[2]
Operating Income (Rs. crore)	1428.9	1797.3	379.3
PAT (Rs. crore)	94.7	119.3	13.5
OPBDIT/ OI (%)	19.5%	20.6%	19.0%
RoCE (%)	14.0%	16.4%	
Total Outside Liabilities/Tangible Net Worth (times)	1.7	1.5	
Total Debt/OPBDIT (times)	3.0	2.4	
Interest coverage (times)	4.0	4.6	3.6
DSCR	1.7	2.0	

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

[2] Provisional

Rating history for last three years:

	Instrument	Current Rating (FY2020) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating 04-October 2019	Chronology of Rating History for the past 3 years: Date & Rating 29-March 2019	Date & Rating in FY2019 26-July 2018	Date & Rating in FY2018 28-February 2018	Date & Rating in FY2018 18-December 2017	Date & Rating in FY2017 02-November 2016
1	Term Loan	Long Term	443	443	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
2	Fund based-Working Capital Facilities	Long Term	460	460	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
3	Non-fund based-Working Capital Facilities	Short Term	239	239	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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	2015-16	NA	2021-22	443	[ICRA]A (Negative)
NA	Fund based- Working Capital Facilities	NA	NA	NA	460	[ICRA]A (Negative)
NA	Non-fund based-Working Capital Facilities	NA	NA	-	239	[ICRA]A1

Source: Ramkrishna Forgings Limited

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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.

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