ICRA

September 21, 2017

Kirloskar Ferrous Industries Limited

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Fund-based Bank Facilities	455.00	[ICRA]AA- (Stable) and [ICRA]A1+; Reaffirmed
Non-fund Based Bank Facilities	690.00	[ICRA]AA- (Stable) and [ICRA]A1+; Reaffirmed
Unallocated	11.00	[ICRA]AA- (Stable); Reaffirmed
Commercial Paper	100.00	[ICRA]A1+; Reaffirmed
Total	**1256.00**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the long-term rating of [ICRA]AA- (pronounced ICRA double A minus) with a 'Stable' outlook and the short-term rating of [ICRA]A1+ (pronounced ICRA A one plus) for the Rs. 455.00 crore[1] fund-based and the Rs. 690.00 crore non-fund based bank facilities of Kirloskar Ferrous Industries Limited (KFIL)[2]. ICRA has also reaffirmed the long-term rating of [ICRA]AA- with a 'Stable' outlook for the Rs. 11.00 crore unallocated amount and the short-term rating of [ICRA]A1+ for the Rs. 100.00 crore commercial paper programme of KFIL.

Rationale

The ratings reaffirmation continues to derive comfort from the established position of KFIL in foundry grade pig iron manufacturing and ferrous castings in the domestic market over the years. The company is a part of the reputed Pune-based Kirloskar Group with a proven management track record. KFIL has generated healthy cash accruals during the last few years on the back of favourable raw material price movement, improved operational efficiency and change in the product mix with increased share of value-added castings. ICRA takes note of the healthy castings demand outlook of the tractor as well as the automotive segment in the near to medium term. The ratings also factor in established relations with the original equipment manufacturers (OEMs) for castings manufactured along with the healthy share of business. KFIL has a competitive cost structure for pig iron manufacturing owing to the presence of a sinter plant and hot blast stoves. Moreover, Hospet foundry enjoys the benefits of backward integration in the form of ready availability of molten pig iron. The company continues to have a comfortable capital structure with low gearing of 0.2x as on March 2017 and comfortable liquidity position characterised by healthy cash accruals and sizeable unused bank lines.

The rating strengths are partially offset by vulnerability of the operating margins to fluctuating raw material prices, given the commodity nature of the business. The operating margins of the company dragged significantly in Q1 FY2018 on account of the sharp increase in coke costs. However, they are likely to improve in the near term due to increased realisations and softened raw material costs. KFIL also faces high client concentration risk in the ferrous castings division (contributing to 48% of overall revenues in FY2017) with top three customers accounting for ~69% of the casting revenues. However, the client concentration risk is mitigated to some extent through healthy share of business with key clients and addition of new clients during the past few years. ICRA also takes note of the company's exposure to

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

foreign currency movement, given the sizeable imports, although, the company adopts conservative hedging policies to minimise the impact of forex risk.

Key rating drivers
Credit strengths

- **One of the leading players in the domestic market** – KFIL is one of the leading players in the foundry grade pig iron manufacturing and ferrous castings in the domestic market. It has established performance track record over the years. The company is part of a reputed Pune-based Kirloskar Group with presence across diversified business segments and proven management track record.
- **Healthy cash accruals and comfortable capital structure and liquidity profile** – KFIL has generated healthy cash accruals over the last few years, driven by favourable raw material price movement, improved operational efficiency and favourable change in the product mix with increased share of value-added castings. It doesn't have any long-term debt on its books and the total debt levels have steadily reduced over the years. This, coupled with healthy cash accruals, results in a comfortable capital structure with low gearing of 0.2x as on March 2017. The liquidity profile of the company remains comfortable, and sizeable unused bank lines further helps the financial flexibility of the company. KFIL has generated positive free cash flows during the last three years.
- **Healthy casting demand outlook; established relations with OEMs** – In the casting division, the company primarily caters to the passenger vehicle (PV), tractor and commercial vehicle (CV) segments. With healthy demand outlook of the PV and the tractor segment in the near to medium term, the revenue growth prospects for the casting division remains healthy. This, coupled with increasing share of value-added castings, is expected to improve the profitability of the division, going forward. KFIL has established relations with OEMs for castings manufactured and has a healthy share of business with them. In the past few years, addition of new clients has led to the improvement in casting volumes.
- **Competitive cost structure –** The company has competitive cost structure for pig iron manufacturing on account of the presence of sinter plant and hot blast stoves. In the casting division, Hospet foundry enjoys benefit of backward integration in the form of ready availability of molten pig iron.

Credit weaknesses

- **Raw material price volatility risk** – Owing to commodity nature of the business, the operating margins of the company remain vulnerable to fluctuations in raw material prices. The operating margins of the company dragged significantly in Q1 FY2018 to 4.3% from 20.1% in Q1 FY2017 on account of a sharp increase in coke costs; however, the operating margins are likely to improve in the near term due to increased realisations and softening of raw material costs.
- **High client concentration risk in the casting division –** The company faces high client concentration risk in the casting division. The top customer contributes to ~44% of the casting revenues while the share of the top three customers is ~69%. However, the company has a healthy share of business with its key customers and in the past few years has added new clients to its portfolio. This mitigates the client concentration risk to some extent.
- **Foreign currency movement risk –** Given the sizeable imports (~34% in FY2017), the profitability of the company remains exposed to foreign currency movement. The company, however, adopts conservative hedging policies to minimise the impact of forex volatility.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

Rating Methodology for Entities in the Ferrous Metals Industry
Corporate Credit Rating Methodology

About the company:
KFIL, incorporated in 1991, is part of the reputed Pune-based Kirloskar Group. KFIL manufactures foundry grade pig iron and ferrous castings such as cylinder blocks, housings, cylinder heads, and transmission parts. It mostly caters to casting requirements of PV, tractor and the CV segment along with sales from group company Kirloskar Oil Engines Limited (KOEL).
KFIL's plants at Hospet (Karnataka) and Solapur (Maharashtra) have a combined casting capacity of 1,50,000 tonnes per annum (TPA) and pig iron capacity of 3,91,400 TPA at Hospet. The company also has three steam turbines with a total power cogeneration capacity of 11.5 megawatt (MW).

In FY2017, the company reported a net profit of Rs. 90.6 crore on an operating income of Rs. 1133.7 crore, as compared to a net profit of Rs. 57.7 crore on an operating income of Rs. 1113.9 crore in FY2016.

Key financial indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	1113.9	1133.7
PAT (Rs. crore)	57.7	90.6
OPBDIT/ OI (%)	13.2%	15.5%
RoCE (%)	16.1%	19.1%
Total Debt/ TNW (times)	0.2	0.2
Total Debt/ OPBDIT (times)	0.7	0.6
Interest Coverage (times)	8.1	15.1
NWC/ OI (%)	10.4%	14.4%

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);
NWC: Net Working Capital

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No.	Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
				September 2017	August 2016	August 2015	December 2014
1	Fund-based Facilities	Long-term/Short-term	455.00	[ICRA]AA- (Stable) and [ICRA]A1+	[ICRA]AA- (Stable) and [ICRA]A1+	[ICRA]AA- (Stable) and [ICRA]A1+	[ICRA]A+ (Stable) and [ICRA]A1+
2	Term Loan	Long-term	-	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)
3	Unallocated	Long-term	11.00	ICRA]AA- (Stable)	-	-	-
4	Non-fund Based Facilities	Long-term/Short-term	690.00	[ICRA]AA- (Stable) and [ICRA]A1+	[ICRA]AA- (Stable) and [ICRA]A1+	[ICRA]A+ (Stable) and [ICRA]A1+	[ICRA]A+ (Stable) and [ICRA]A1+
5	Commercial Paper	Short-term	100.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

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	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
	Fund-based Facilities – CC/STL/OD	-	-	-	455.00	[ICRA]AA- (Stable) and [ICRA]A1+
	Non-fund Based Facilities – LC/BG	-	-	-	690.00	[ICRA]AA- (Stable) and [ICRA]A1+
	Unallocated	-	-	-	11.00	[ICRA]AA- (Stable)
	Commercial Paper	-	-	-	100.00	[ICRA]A1+

Contact Details

Analyst Contacts

Subrata Ray
+91 22 2433 1086
subrata@icraindia.com

Laxmikant Lokhande
+91 20 6606 9920
laxmikant.lokhande@icraindia.com

Gaurav Jain
+91 20 6606 9922
gaurav.jain@icraindia.com

Relationship Contact

L Shivakumar
+91 22 6169 3300
shivakumar@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**

Registered Office
ICRA Limited
1105, Kailash Building, 11th Floor, 26, Kasturba Gandhi Marg, New Delhi 110001
Tel: +91-11-23357940-50, Fax: +91-11-23357014

Corporate Office
Mr. Vivek Mathur
Mobile: +**91 9871221122**
Email: vivek@icraindia.com

Building No. 8, 2nd Floor, Tower A, DLF Cyber City, Phase II, Gurgaon 122002
Ph: +91-124-4545310 (D), 4545300 / 4545800 (B) Fax; +91- 124-4050424

Mumbai **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 3rd Floor, Electric Mansion Appasaheb Marathe Marg, Prabhadevi Mumbai—400025, Board : +91-22-61796300; Fax: +91-22-24331390	**Kolkata** **Mr. Jayanta Roy** Mobile: **+91 9903394664** Email: jayanta@icraindia.com A-10 & 11, 3rd Floor, FMC Fortuna 234/3A, A.J.C. Bose Road Kolkata—700020 Tel +91-33-22876617/8839 22800008/22831411, Fax +91-33-22870728
Chennai **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 5th Floor, Karumuttu Centre 634 Anna Salai, Nandanam Chennai—600035 Tel: +91-44-45964300; Fax: +91-44 24343663	**Bangalore** **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 'The Millenia' Tower B, Unit No. 1004,10th Floor, Level 2 12-14, 1 & 2, Murphy Road, Bangalore 560 008 Tel: +91-80-43326400; Fax: +91-80-43326409
Ahmedabad **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 907 & 908 Sakar -II, Ellisbridge, Ahmedabad- 380006 Tel: +91-79-26585049, 26585494, 26584924; Fax: +91-79-25569231	**Pune** **Mr. L. Shivakumar** Mobile: +**91 9821086490** Email: shivakumar@icraindia.com 5A, 5th Floor, Symphony, S.No. 210, CTS 3202, Range Hills Road, Shivajinagar,Pune-411 020 Tel: + 91-20-25561194-25560196; Fax: +91-20- 25561231
Hyderabad **Mr. Jayanta Chatterjee** Mobile: +**91 9845022459** Email: jayantac@icraindia.com 4th Floor, Shobhan, 6-3-927/A&B. Somajiguda, Raj Bhavan Road, Hyderabad—500083 Tel:- +91-40-40676500	