

December 05, 2019

Nelcast Limited: Long-term rating re-affirmed and outlook revised to Negative; Short-term rating downgraded to [ICRA]A1

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based Limits	160.00	160.00	[ICRA]A+(Negative); re-affirmed and outlook revised from Stable
Short-term Fund-based Limits	20.00	20.00	[ICRA]A1; revised from [ICRA]A1+
Short-term Non-fund Based Limits	9.00	9.00	[ICRA]A1; revised from [ICRA]A1+
Short-term Fund-based sub-limits	(50.00)	(50.00)	[ICRA]A1; revised from [ICRA]A1+
Commercial Paper Programme (CP)	30.00	30.00	[ICRA]A1; revised from [ICRA]A1+
Proposed Long-term/Short-term Fund-based Limits	11.00	11.00	[ICRA]A+(Negative) re-affirmed and outlook revised from Stable; [ICRA]A1 revised from [ICRA]A1+
Total	230.00	230.00	

*Instrument details are provided in Annexure-1

Rationale

The revision in outlook and short-term rating reflects the weaker-than expected performance of Nelcast Limited (Nelcast) in H1 FY2020 on the back of demand slowdown in the domestic automotive industry and its consequent impact on the company's revenues and earnings. Nelcast's revenues and operating profits have declined by around 30% in H1 FY2020, because of a sharp de-growth in supplies to the domestic medium and heavy commercial vehicle (M&HCV) and tractor industry segments (down by ~40% and 30%, respectively). Nelcast's margins and earnings have been protected to an extent in the current fiscal by a steady revenue growth witnessed in the higher-margin exports and railways segments, which now contribute around 25% to sales. While Nelcast's revenues and earnings are expected to de-grow by around 25% in FY2020 because of demand-side pressure, they are likely to register a moderate growth of around 8-10% in FY2021, driven by the growing order book in the tractor and export segments. The lower-than anticipated earnings from operations coupled with the ongoing debt-funded expansion and firm repayment obligations is expected to moderate Nelcast's credit metrics and free cash flows. Its net debt to operating profit is expected to increase to around 3 times in FY2020 (from 1.8 times in FY2019) and subsequently improve to ~2.4 times in FY2021. Nevertheless, its coverage metrics and liquidity position continue to remain at adequate levels, with interest coverage and debt service coverage ratios (DSCR) likely to be at around 4.5 times and 1.75 times, respectively in FY2020 (albeit lower than the FY2019 levels). Its credit profile is supported by the cash reserves held and adequate unutilised lines of credit, lending financial flexibility. The ratings continue to factor in Nelcast's operational strengths, including its established relationships with leading M&HCV and tractor original equipment manufacturers (OEMs) and healthy volume share enjoyed in key products supplied to major customers. The ratings also consider the inherent cyclicity in the key end-user segments (both the domestic M&HCV and tractor segments) that has constrained the operating performance in the past, relatively high customer concentration and intense competition in the domestic foundry industry.

Key rating drivers and their description

Credit strengths

Strong market position in key product categories – Nelcast is an established player in the domestic ferrous castings market, generating majority of its sales from the leading domestic OEMs. Strong volume share, continuous product additions and growing export base have supported Nelcast's performance in the past few fiscals. Nelcast is in the process of expanding its capacity to support growing customer requirements, with capacity utilisation reaching around 90% levels in H1 FY2019. While an 18,000-TPA unit (phase I at Pedapariya, Andhra Pradesh) was commercialised in September 2018, another 42,000 TPA (phase II at the same location) is likely to be completed by Q2 FY2021.

Comfortable debt protection metrics – Despite an increase in long-term debt levels (witnessed since FY2019) to fund the expansion undertaken and lower-than expected earnings from operations witnessed in the current fiscal, Nelcast's coverage metrics remain at comfortable levels. Its interest coverage and DSCR stood at around 6 times and 2 times, respectively for H1 FY2020, further backed by its healthy cash reserves and adequate unutilised lines of credit.

Credit challenges

Ongoing slowdown in the domestic automotive industry – Nelcast's operating performance in H1 FY2020 has been adversely impacted by weak demand witnessed in the domestic M&HCV and tractor segments, which contribute ~75% to its sales. With Nelcast's performance remaining largely dependent on the cyclical automotive demand, any sustained weak demand from its key end-user segments (as witnessed in the recent quarters) would adversely impact its revenues and earnings. The risk is accentuated by the sizeable capacity addition in its second phase of expansion. Presence across two automotive segments, which supported volumes during alternating periods of slowdown (as witnessed over the years), healthy growth in exports and ongoing efforts to further widen its product portfolio to effectively utilise the new capacities provide some comfort.

High customer concentration – Nelcast's top three customers account for around 50% of its revenues. Though revenues in the M&HCV segment are relatively diversified across industry players, a substantial portion of the revenues in the tractor segment is generated from a single customer. This exposes the company's earnings to client concentration risks. Nevertheless, Nelcast's long relationship and strong linkages with the leading OEMs provide comfort.

Liquidity position: Adequate

Nelcast's liquidity position remains comfortable despite funding requirements for the ongoing capital expenditure and lower-than expected earnings from operations. The average utilisation of fund-based limits stood at ~75% in H1 FY2020 and the company has cash reserves of around Rs. 60 crore as on September 30, 2019. While repayment obligations remained firm at around Rs. 15 crore in H2 FY2020 and Rs. 40 crore in FY2021, Nelcast's cash flows are expected to be supported by the cash reserves held, adequate unutilised lines of credit post the recent enhancement of limits and cash accruals of around Rs. 40 crore per annum.

Rating sensitivities

Positive triggers – Given the Negative outlook, a rating upgrade over the next 12 months is less likely. However, a change in outlook or an upward movement in rating may happen if the company demonstrates a sustained growth in revenues and earnings, which in turn would improve its credit metrics. Specific credit metrics that may lead to an upgrade of the

company's rating include TD/OPBDITA reducing to less than 1.5 times and DSCR improving to above 2.5 times on a sustained basis.

Negative triggers – Any sustained pressure on revenues and earnings owing to weak demand conditions, deteriorating its credit metrics, may result in a rating downgrade. Specific credit metrics that may lead to a downgrade of the company's ratings include TD/OPBDITA remaining above 2.5 times and DSCR remaining below 1.5 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	For arriving at the ratings, ICRA has considered the consolidated financial statements of Nelcast and the details of its subsidiary are mentioned in Annexure-2.

About the company

Incorporated in 1982, Nelcast manufactures grey and ductile castings for the M&HCV and tractor industry segments. Key products supplied to the M&HCV segment include wheel hubs, brake drums, axle housing and brackets among others. For the tractor segment, the company's major products are transmission casing, centre housing, axle housing and hydraulic lift cover. It also supplies ribbed plates and brake discs used in Metro Rail projects and Railways. Nelcast has an aggregate installed effective capacity of 118,000 tonnes per annum at its factories at Ponneri in Tamil Nadu and Gudur and Pedapariya in Andhra Pradesh. The capacity would be increased to 160,000 TPA upon commercialisation of its second phase at Pedapariya in the next fiscal.

Key financial indicators (Consolidated and audited)

	FY2018	FY2019
Operating Income (Rs. crore)	746.17	860.23
PAT (Rs. crore)	38.26	38.44
OPBDIT/OI (%)	9.81%	9.28%
RoCE (%)	13.98%	13.62%
Total Outside Liabilities/Tangible Net Worth (times)	0.73	0.96
Total Debt/OPBDITA (times)	1.34	2.50
Net Debt*/ OPBDITA (times)	0.58	1.77
Interest Coverage (times)	13.19	8.54
DSCR	6.60	7.64

*Note: Net debt is total debt adjusted for cash and bank balances held

Source: Nelcast and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Rating (FY2020)				Rating History for the Past 3 Years					
Instrument	Type	Amount Rated	Amount Outstanding	Current Rating 5-Dec-2019	Earlier Rating 1-Aug-2019	FY2019 4-Mar-2019	FY2018 5-July-2018	FY2017 26-July-2017	FY2016 12-July-2016
1 Long-term fund-based limits	Long Term	160.00	-	[ICRA]A+ (Negative)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)
2 Short-term fund-based limits	Short Term	20.00	-	[ICRA]A1	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +
3 Short-term non-fund-based limits	Short Term	9.00	-	[ICRA]A1	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +
4 Short-term fund-based sub-limits	Short Term	(50.00)	-	[ICRA]A1	[ICRA]A1 +	-	-	-	-
5 Commercial paper programme (CP)	Short Term	30.00	-	[ICRA]A1	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +	[ICRA]A1 +
6 Proposed long-term/short-term fund-based limits	Long-Term / Short Term	11.00	-	[ICRA]A+ (Negative) / [ICRA]A1	[ICRA]A+ (Stable) / [ICRA]A1 +	[ICRA]A+ (Stable) / [ICRA]A1 +	[ICRA]A+ (Positive) / [ICRA]A1 +	[ICRA]A+ (Positive) / [ICRA]A1 +	[ICRA]A+ (Stable) / [ICRA]A1 +

Amount in Rs. Crore; Source: Nelcast

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term fund-based Limits	-	-	-	160.00	[ICRA]A+ (Negative)
NA	Short-term fund-based limits	-	-	-	20.00	[ICRA]A1
NA	Short-term non-fund-based Limits	-	-	-	9.00	[ICRA]A1
NA	Short-term fund-based sub-limits	-	-	-	(50.00)	[ICRA]A1
NA	Commercial Paper Programme (CP)	-	-	-	30.00	[ICRA]A1
NA	Proposed Long-term/short-term fund-based limits	-	-	-	11.00	[ICRA]A+ (Negative)/ [ICRA]A1

Source: Nelcast

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
NC Energy Limited	93.44%	Full Consolidation

Source: Nelcast

ANALYST CONTACTS

Jayanta Roy

+91 33 7150 1120

jayanta@icraindia.com

Balaji M

+91 44 4596 4317

balajim@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:

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

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87
Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore + (91 80) 2559 7401/4049
Ahmedabad+ (91 79) 2658 4924/5049/2008
Hyderabad + (91 40) 2373 5061/7251
Pune + (91 20) 2556 0194/ 6606 9999

© Copyright, 2019 ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA.

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. All information contained herein must be construed solely as statements of opinion, and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents