Rating Rationale

Kalyani Forge Limited

Rating outlook revised to 'Stable'; ratings reaffirmed

Rating Action

Total Bank Loan Facilities Rated	**Rs.100 Crore**
Long Term Rating	**CRISIL BBB+/Stable (Outlook revised from 'Negative' and rating reaffirmed)**
Short Term Rating	**CRISIL A2 (Reaffirmed)**

1 crore = 10 million

Refer to annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has revised its outlook on the long-term bank facilities of Kalyani Forge Ltd (KFL) to 'Stable' from 'Negative' while reaffirming the rating at 'CRISIL BBB+'. The rating on the short-term bank facilities has been reaffirmed at 'CRISIL A2'.

The revision in outlook reflects restoration in the business risk profile on back of higher-than-expected revenue and improvement in operating margin in fiscal 2021 supported by demand recovery. The lockdown and other measures taken by the Centre and various state governments towards containment of the Covid-19 pandemic had resulted in weakening of demand and performance during Q1 FY21. However, with gradual recovery in demand from auto segment as well as non-auto segment (such as power, engineering, etc.) led to steady recovery in revenue. Hence, company reported an operating income of Rs.181.56 crore in fiscal 2021. Operating margin too recovered to 7.3% in fiscal 2021 (from 4.9% in fiscal 2020). The demand from customers continues to remain comfortable, as reflected in revenue of Rs 118.95 crore during H1 FY 2022. With the improvement in revenue, operating margin has also further improved to 8.4% during the same period and is expected to improve further to around 8.8-9.0%, in-line with historical levels. Company reported net profit of Rs 1.89 crore during H1 FY 2022, as against net loss during the last two fiscals ended 2021. The overall credit risk profile continues to be supported by the company's healthy financial risk profile and adequate liquidity.

The ratings continue to reflect KFL's established market position in the domestic forging and machining industry and healthy financial risk profile. These strengths are partially offset by large working capital requirements, modest return on capital employed (RoCE) and susceptibility to cyclicality in the automotive (auto) sector, volatility in raw material prices and intense competition.

Key Rating Drivers & Detailed Description

Strengths:

* **Established market position:** A presence of around four decades in the domestic forging and machining industry has enabled the promoters to develop a healthy relationship with reputed original equipment manufacturers (OEMs) in the auto segment. Company has a diversified customer base, with top 5 customers contributing to 30-35% of the total revenue. The heavy dependency of customers on KFL will continue to support its business risk profile.

* **Healthy financial risk profile:** Gearing, and total outside liabilities to tangible networth ratio were low at 0.27 time and 0.80 time as on March 31, 2021, supported by healthy networth of Rs 100.16 crore and controlled working capital debt. Backed by lower interest outgo and recovery in operating margin, interest cover has improved to 4.72 times in fiscal 2021. Net cash accruals to adjusted debt ratio was 0.39 time in fiscal 2021.

Weaknesses:
* **Susceptibility of operating margin to cyclicality in the auto sector, volatility in raw material prices and intense competition, and modest RoCE:** Operating margin remains susceptible to volatile raw material prices with any increase being passed on to customers with some time lag. Further, most of the revenue (around 70-80%) comes from the auto sector, which is cyclical. Moreover, there is intense competition from auto ancillary manufacturers, which limits bargaining power with customers. Operating margin was 8.4% for H1 FY22 and is expected to be around 8.8-9.0% over the medium term. The RoCE is expected to recover to 6.5-8.0% over the medium term supported by recovery in profitability but expected to remain low because of moderate profitability.

* **Large working capital requirement:** KFL has large working capital requirements as reflected in gross current asset days in the range of 175-235 days over the last five fiscals ended 2021. GCA days increased to 233 days as on March 31, 2021 (from 187 days in previous fiscal) due to increase in debtor days to 136 days (from 103 days in previous fiscal) and increase in inventory days to 97 days (from 76 days in previous year) due to stretch in debtor collection because of Covid-19 pandemic and slow movement of products during fiscal 2021 because of the Covid-19 induced disruptions, respectively. However, the debtor days and inventory days have come under control in the current fiscal and were at 101 days and 83 days, respectively, on Sept 30, 2021. The working capital requirements are expected to remain large with GCA days of 190-200 days over the medium term.

Liquidity: Adequate
Net Cash accruals are expected to be in the range of Rs 15-19 crore per fiscal and will be more than adequate against debt repayments of Rs 1.2-2.3 crore per fiscal over the medium term. The company has access to working capital limits of Rs 40 crore, which have been utilized at an average of 69% over the 12 months ended November 2021. Unencumbered cash and bank balance was Rs 0.10 crore as on March 31, 2021 and this has revived to Rs 1.63 crore as on Nov 30, 2021. Company will be undertaking debt funded capital expenditure of Rs 15 crore over fiscal 2022 and 2023. CRISIL Ratings believes KFL's net cash accruals, unutilized bank limits and cash and cash equivalent will be sufficient to fund incremental working capital, debt repayment and capex requirements over the medium term.

Outlook: Stable
CRISIL Ratings believes KFL will continue to benefit from its established position in the forging and machining industry.

Rating Sensitivity factors
Upward factors:
- Sustained revenue growth with operating margin of over 10%; resulting in net cash accruals above Rs 25 crore on a sustained basis

- Sustained improvement in working capital cycle

Downward factors:
- Decline in revenue or operating margin resulting in net cash accruals below Rs 10 crore
- Stretch in working capital requirements
- Larger-than-expected, debt-funded capital expenditure (capex) or acquisition; or more-than-expected dividend payout, weakening the financial risk profile, particularly liquidity

About the Company
Established in 1979, KFL is led by Ms. Rohini G Kalyani, as the managing director. The company manufactures high-quality, hot-warm and cold-forged products at its plants in Koregaon Bhima and Sanaswadi in Pune, Maharashtra.

Key Financial Indicators

Particulars	Unit	2021	2020
Revenue	**Rs crore**	**181.56**	**202.15**
Profit after tax (PAT)	**Rs crore**	**-1.76**	**-6.93**
PAT margin	**%**	**-0.97**	**-3.43**
Adjusted debt/adjusted networth	**Times**	**0.27**	**0.31**
Interest coverage	**Times**	**4.72**	**1.90**

Annexure - Details of Instrument(s)

ISIN	Name of instrument	Date of Allotment	Coupon Rate (%)	Maturity date	Issue Size (Rs crore)	Complexity levels	Rating Assigned with Outlook
NA	Cash Credit	NA	NA	NA	40.00	NA	CRISIL BBB+/Stable
NA	FCNR (B) Long Term Loan	NA	NA	Sep-2021	1.22	NA	CRISIL BBB+/Stable
NA	Foreign Exchange Facility	NA	NA	NA	1.00	NA	CRISIL A2
NA	Letter of credit & Bank Guarantee	NA	NA	NA	22.00	NA	CRISIL A2
NA	Term Loan	NA	NA	Mar-2027	11.50	NA	CRISIL BBB+/Stable
NA	Proposed Fund-Based Bank Limits	NA	NA	NA	24.28	NA	CRISIL BBB+/Stable