Dalmia Refractories Limited

November 19, 2021

Ratings

Facilities/Instruments	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	133.00	CARE A (CWD) (Single A) (Under Credit watch with Developing Implications)	Revised from CARE A- (Single A Minus); Revision in credit watch from Positive Implications to Developing Implications
Long Term / Short Term Bank Facilities	40.00	CARE A / CARE A1 (CWD) (Single A / A One) (Under Credit watch with Developing Implications)	Revised from CARE A- / CARE A2+ (Single A Minus / A Two Plus); Revision in credit watch from Positive Implications to Developing Implications
Total Bank Facilities	**173.00 (Rs. One Hundred Seventy-Three Crore Only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Dalmia Refractories Limited (DRL) factors in the improvement in the financial risk profile of the company marked by improvement in total operating income and profitability during H1FY22 (refers to period April 01 to Sep 30) and progress achieved on the amalgamation of scheme wherein refractory businesses of DRL, GSB Refractories India Private Limited (GSB India), Dalmia Bharat Refractories Ltd. (DBRL, erstwhile Sri Dhandauthapani Mines And Minerals Limited), Dalmia OCL Limited (DOL, erstwhile Ascension Commercio Private Limited) and refractory business of Dalmia Cement Bharat Limited (DCBL) will be consolidated into a single entity which is expected to further strengthen the financial risk profile and increase business capabilities of the ultimate consolidated entity.

Further, the credit watch has been revised to developing implication from credit watch with positive implications on considering the progress achieved in scheme of amalgamation, however approval from National Company Law Tribunal (NCLT) of scheme of arrangement is still under process. CARE shall evaluate the ratings once the process of amalgamation is completed in entirety.

The ratings continue to derive strength from the strong parentage of the Dalmia group, long track record of operations, reputed clientele, captive mines for sourcing of a part of the raw material requirements and adequate liquidity. These rating strengths are, however, partially offset by its significant dependence on the cement industry which is inherently cyclical, fragmented and competitive nature of the refractory industry and susceptibility of profitability margins to volatility in raw material prices and exchange rate fluctuations.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Timely execution of the amalgamation schemes with requisite regulatory approvals.
- Expansion in the scale of operations and improvement in the profitability margins (PBILDT margin of more than 11%) leading to improvement in the financial risk profile on a sustained basis.
- Ability of the company to manage its working capital requirements while timely realizing its debtors.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Any higher then envisaged debt funded capex incurred by the company adversely impacting the capital structure with the overall gearing exceeding 1.50x on a sustained basis.
- Decline in PBILDT margin of more than 3% from the current levels on a sustained basis going forward.

Detailed description of the key rating drivers

Key Rating Strengths

Improvement in financial risk profile during H1FY22

During H1FY22, the company reported improvement in financial risk profile characterized by healthy growth in total operating income and profitability. The company reported a growth of 80% in total operating revenue to Rs.148.40 crore as

[1]*Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

compared to revenue of Rs.81.41 crore registered in H1FY21. The company EBIDTA margin improved in H1FY22 stood at 9.40% as compared to 7.22% in FY21. The company also reported growth in PAT and GCA of Rs.7.25 crore and Rs.10.15 crore respectively in H1FY22 as compared to Rs.3.10 crore and Rs.6.32 crore respectively in H1FY21.
The company, however, reported moderation in total income in FY21 due to Covid-19 lockdown at Rs.221.11 crore. However, post lifting of lockdown the company performance saw improvement from Q3FY21 onwards.
The overall gearing of the company also improved and stood at 0.11x as on March 31, 2021 as compared to 0.21x as on March 31, 2020 on lower working capital utilization and no term debt. The total debt of Rs. 28.93 cr as on March 31, 2021 comprise of lease liabilities of Rs. 1.70 cr and Inter-corporate deposits (ICDs) from Dalmia Cement Bharat Ltd (DCBL, group company) of Rs.23.50 crore. The debt protection metrics stood comfortable characterised by comfortable interest coverage and total debt / GCA ratio of 5.27x (PY: 11.11x) and 2.28 years (PY: 1.55 years) in FY21 respectively.
For the acquisition of the German entities during FY19, DRL has extended SBLC to its foreign subsidiary. DRL had a total of non-current investments in associates/subsidiary companies for Rs. 151.25 crore (PY: Rs.71.02 crore) as on March 31, 2021. The adjusted overall gearing of DRL (incorporating outstanding foreign currency term loan amount advanced against SBLC facility to foreign subsidiary and adjusting the net worth for the investments made in subsidiaries/associates) stood at 1.05x as on March 31, 2021 (PY: 1.18x).

Strong parentage and long track record of operations
Dalmia Refractories Limited (DRL) belongs to Dalmia Bharat Group which operates in various industries including cement, sugar, power and refractory. The Dalmia Bharat Group is one of the leading Indian conglomerates with strong business track record of more than 75 years. The Group’s presence spans across various countries and industries with an employee strength of over 9,000. DRL has been engaged in the refractories business for over four decades and enjoys strong market positioning in the refractories segment for the cement industry. The company was promoted by Late J.H. Dalmia and Mr Y.H. Dalmia. DRL leverages the strong presence of Dalmia Bharat Group in the cement sector through the flagship company Dalmia Cement Bharat Limited (DCBL) and through its refractory division and has strong and sustainable customer relationships across the spectrum of various user industries. Mr. Sameer Nagpal, CEO of refractories division of Dalmia Bharat Group is the managing director of DRL, with over 28 years of industry experience in business strategy and transformation. He is ably supported by the management team comprising of industry professionals having significant experience in the related domain of business operations.

Reputed Clientele providing repeat business
With its long track record of operations and owing to its association with Dalmia Bharat Group, DRL has built its reputation as one of the established players in the refractory business and receives repeat orders from large and reputed players in the cement industry. DRL leverages the wider product portfolio of DCBL and thus is able to source different variants of refractory bricks such as silica bricks, alumina-silicon-carbide bricks, magnesia carbon/chrome bricks etc. from DCBL. This enables DRL to offer diversified and comprehensive product offerings to its customers as per their requirements and specifications. In addition to this, DRL also supplies refractories to DCBL. The refractory products manufactured by DRL and DCBL are sold under the common brand name of ‘Dalmia OCL”, further enabling DRL to leverage the brand equity of DCBL and gain acceptance of the new clients.
The consolidated entity (post the amalgamation process) is expected to offer more diverse product offerings to the clientele with the manufacturing of other variants of refractory bricks such as magnesia carbon, silica bricks and monolithics etc., with the end use application not only in cement but also in steel, coke over and glass industries.

Captive mines for sourcing of a part of raw material requirements
The primary raw materials used in the manufacturing of refractories are bauxite and clay (which together comprise of 70-80% of consumption by volume). For the sourcing of the bauxite, DRL maintains an optimal mix of imports and domestic procurements, considering the requirements and specifications of the customers, the quality and material required, cost specifications and lead time to delivery and supply. The company majorly imports high grade bauxite from China, which is used in the production of the high value products and domestically procures bauxite from Rajasthan and Gujarat. In addition to this, the Group also owns 5 bauxite mines in Khambalia, Gujarat. These bauxite mines have total reserves of 6250 KMT and are available till 2098. This insulates the Group from raw material price fluctuations to certain extent. Out of these, currently 3 mines are being owned by DCBL and another 2 by DRL, however, with the completion of the amalgamation process, all the 5 mines would come under the ownership of the consolidated entity.

Key Rating Weaknesses
Significant dependence on the cement industry which is inherently cyclical
The company produces high alumina bricks and castables and mainly caters to the cement industry, which is cyclical in nature and hence, the company’s performance is largely dependent on the performance and growth in the cement industry. During FY21, the COVID-19 pandemic has adversely impacted the demand of the cement industry leading to decline in the capacity utilization of cement companies. However, post Covid-19, the cement sector has shown a growth path with more

infrastructure related activities are implemented. In addition to this, the consolidated entity (post amalgamation) is expected to offer diverse product offerings including magnesia carbon, silica bricks, monolithics etc. in order to cater to steel and glass industries as well. This is expected to capture the demand from steel sector, the largest consumer of refractories product and minimize the impact from cyclicality of cement sector.

Fragmented and competitive nature of the refractory industry
The refractory industry is highly fragmented with more than 150 players of which around 15-16 are major players. The industry is highly competitive due to excess capacity available for refractory production in India and increased imports of refractory products. Indian refractory industry faces a huge threat in the form of competition from cheap refractory products dumped from China which has captured more than 25% of the total market. Due to highly competitive nature of the refractory industry, players experience limited pricing flexibility as they deal with large cement players and hence, work under high margin pressure. The consolidated entity (post amalgamation) would also have higher bargaining power with its customers owing to increase in scale of operations and diverse product portfolio being offered.

Susceptibility of profitability margins to volatility in raw material prices and exchange rate fluctuations
The major raw materials used by DRL are bauxite and clay, the prices of which are volatile. The raw materials costs constituted ~62% of the total operating income of DRL for the past 3 years; hence any volatility in the prices of the raw materials has a direct impact on the profitability margins of the firm.
The company majorly imports high grade bauxite from China, which is used in the production of the high value products and sources bauxite domestically from Rajasthan and Gujarat, while maintaining a mix of imports and domestic purchases based on prices, supply of materials and availability of time.
With procurement in foreign currency and sales realization in domestic currency, the company is exposed to the fluctuation in exchange rates. DRL uses foreign exchange forward contracts to hedge the risks, which varied from one purchase order to another, depending on the views of the bankers and internal forex team of the company. In addition to this, DRL's proportion of exports increased during FY21 to Rs. 33.72 crore (~15% of total operating income) as compared to Rs. 32.06 crore (~11% of total operating income) during FY20, which acted as a natural hedge for DRL to a certain extent. DRL reported net foreign exchange gain of Rs.0.38 crore in FY21 as compared to gain of Rs. 0.42 cr during FY20.

Liquidity: Adequate
The liquidity profile of DRL is adequate with its current ratio at 1.21x with cash and bank balances of Rs. 5.71 crore as on March 31, 2021. The cash and bank balances stood at Rs. 1.81 crore as on Sep 23, 2021. The company is generating healthy accruals and does not have any major capex plans with the overall gearing of 0.11x as on March 31, 2021. The annual repayment for the FCTL guaranteed by DRL is Rs. 3.52 crore for FY22. The operations of the company are working capital intensive majorly owing to the large inventory requirements particularly of raw materials, whereby the company has to maintain sufficient amount of inventory of various raw materials (major being bauxite and clay) used in the manufacturing of refractories as per the client's specifications. DRL has the sanctioned working capital limits (including CC limits and non-fund based limits) for an amount of Rs. 80 crore for the business operations. The utilization of the working capital limits for the last 12 months ending Sep 21 stood moderate with average utilization of ~10%. The company also availed ICDs from its group company Dalmia Cement Bharat Ltd of Rs.23.50 crore for working capital purpose.

Analytical approach: Standalone. The ratings however take into account the strong operational & management linkages DRL has with its group companies and financial support it has extended to its foreign subsidiary.

Applicable Criteria
CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Criteria for Short Term Instruments
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
Rating Methodology - Manufacturing Companies

About the company
DRL, formerly Shri Nataraj Ceramic and Chemical Industries Ltd, belongs to Dalmia Group which has presence in various industries including cement, sugar, power and refractory. The name of the company was changed to Dalmia Refractories Limited on March 28, 2014, to reflect the group and the brand 'Dalmia Refractories' under which the company's products are marketed. DRL produces high alumina refractory bricks and castables which are supplied to cement, steel, coke oven and glass industries. Presently, the company has 2 manufacturing units located at Dalmiapuram (Tamil Nadu) and Khambalia (Gujarat). The current installed capacity as on March 31, 2020 stands at 1,08,600 metric tons per annum (MTPA) for Refractory and 24,000 MTPA for Calcined Bauxite. The company used to previously undertake job work for Dalmia Bharat Ltd

(DBL) which has been discontinued w.e.f. April 1, 2014 and the refractories produced are directly marketed to the user industries by DRL.
DRL and DCBL, at their respective Board meetings held on 14th November 2019, have approved Schemes of Arrangement through which their respective refractory businesses will be consolidated under a single operating entity. The final approval from NCLT is awaited.

Brief Financials (Rs. crore)	FY20 (A)	FY21 (A)	H1FY22
Total operating income	292.19	221.11	148.40
PBILDT	29.39	15.96	13.95
PAT	17.53	7.14	7.25
Overall gearing (times)	0.21	0.11	0.13
Adjusted Overall gearing (times)	1.24	1.05	-
Interest coverage (times)	11.11	5.27	9.05

A: Audited;
*The adjusted overall gearing has been computed by incorporating outstanding foreign currency term loan amount advanced against SBLC facility to foreign subsidiary and adjusting the net worth for the investments made in subsidiaries/associates.

Status of non-cooperation with previous CRA: NA

Any other information: NA

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Cash Credit	-	-	-	-	40.00	CARE A (CWD)
Non-fund-based - LT/ ST-BG/LC	-	-	-	-	40.00	CARE A / CARE A1 (CWD)
Non-fund-based - LT-Standby Letter of Credit	-	January 07, 2019	-	-	93.00	CARE A (CWD)

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Fund-based - LT-Cash Credit	LT	40.00	CARE A (CWD)	-	1)CARE A- (CWP) (01-Sep-20)	1)CARE A- (CWP) (28-Feb-20) 2)CARE A- (CWD) (25-Nov-19) 3)CARE A-; Stable (27-Sep-19) 4)CARE A-; Stable (03-Apr-19)	1)CARE A-; Stable (03-Apr-18)
2	Non-fund-based - LT/ ST-BG/LC	LT/ST*	40.00	CARE A / CARE A1 (CWD)	-	1)CARE A- / CARE A2+ (CWP) (01-Sep-20)	1)CARE A- / CARE A2+ (CWP) (28-Feb-20) 2)CARE A- / CARE A2+ (CWD) (25-Nov-19) 3)CARE A-; Stable / CARE A2+ (27-Sep-19) 4)CARE A-; Stable / CARE A2+ (03-Apr-19)	1)CARE A-; Stable / CARE A2+ (03-Apr-18)
3	Non-fund-based - LT/ ST-Loan Equivalent Risk	LT/ST*	-	-	-	-	-	1)Withdrawn (03-Apr-18)
4	Non-fund-based - LT-Standby Letter of Credit	LT	93.00	CARE A (CWD)	-	1)CARE A- (CWP) (01-Sep-20)	1)CARE A- (CWP) (28-Feb-20) 2)CARE A- (CWD) (25-Nov-19) 3)CARE A-; Stable (27-Sep-19)	-

** Long Term / Short Term*

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: NA

Annexure 4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1	Fund-based - LT-Cash Credit	Simple
2	Non-fund-based - LT-Standby Letter of Credit	Simple
3	Non-fund-based - LT/ ST-BG/LC	Simple

Annexure 5: Bank Lender Details for this Company

To view the lender wise details of bank facilities please [click here]

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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