

## Everest Kanto Cylinder Limited

December 17, 2020

### Ratings

Facilities	Amount (Rs. crore)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	103.57 (Reduced from 128.67)	CARE BBB-; Positive (Triple B Minus; Outlook: Positive )	Revised from CARE BB+; Stable (Double B Plus; Outlook: Stable)
Short Term Bank Facilities	69.92 (Enhanced from 54.92)	CARE A3 (A Three)	Revised from CARE A4+ (A Four Plus)
<b>Total Bank Facilities</b>	<b>173.49</b> <b>(Rs. One Hundred Seventy-Three Crore and Forty-Nine Lakhs Only)</b>		

*Details of instruments/facilities in Annexure-1*

### Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities of Everest Kanto Cylinder Limited (EKCL) reflects its sustained improvement in the operating performance reported over FY20 and past two quarter, i.e. Q1FY21 and Q2FY21 inspite of operational constraints due to CoVID-19. The improvement was majorly driven by the growth in the demand of industrial cylinder majorly in form of oxygen cylinder resulting in substantial improvement reported at PBILDT and PAT levels. During FY20 due to higher raw material prices, moderation in demand from its end user segment primarily the auto segment in India, and muted performance in its subsidiaries resulted in lower PBILDT margin on a consolidated basis, however same has improved in H1FY21. The cash flow too improved during the above period utilised to reduce the total debt by way of optimisation of working capital limit utilisation along with prepayments made towards the servicing of term loans resulting in improvement in coverage and leverage ratios. The company does not envisage to go for any debt led capex over next 2 years.

The ratings continue to derive strength from the promoter's experience, established market position of the company in high pressure seamless cylinder industry and diversified customers mix.

These rating strengths are however partially offset by working capital intensive nature of operations and exposure to volatility in commodity prices/ foreign exchange rates. CARE also takes a note of breach in financial covenants reported in its step down subsidiaries in FY20 though same has not resulted in any accelerated debt repayments or impact on liquidity. EKCL expects proceeds from sale of China subsidiary to materialize in Q4FY21 as the process is in advanced stages. The proceeds would be utilized for further debt reduction and improvement of its liquidity profile.

### Outlook: Revised from Stable to Positive

The revision in the outlook factors in CARE's belief of sustained improvement in the operating profit margins owing to growth in the demand of high pressure cylinder leading to sustained improvement in the capacity utilization along with improvement in the return on capital employed which had been lower than 10% previously.

The outlook may be revised back to stable in case EKCL is not able to sustain the growth in operating margins or faces any liquidity stress due to the breach in the financial covenants in its step down subsidiary or any further delay in getting China proceeds in EKCL.

### Rating Sensitivities

#### *Positive Factors*

- Sustained improvement in TOI above Rs.900 crores along with improvement in PBILDT margins over 16%.
- Improvement in ROCE (Return On Capital Employed) over 14% on sustained basis
- Realisation of proceeds from divestment of China subsidiary translating into lower gearing

<sup>1</sup>Complete definition of the ratings assigned are available at [www.careratings.com](http://www.careratings.com) and other CARE publications

### Negative Factors

- Sustained decline in its RoCE below 9%
- Any large debt funded capex/ acquisition thereby deteriorating the Total Debt / EBITDA over 1.0x on sustained basis.

### Detailed description of the key rating drivers

#### Key Rating Strengths

**Experienced promoters:** EKCL was incorporated in 1978 by late Mr. P.K. Khurana, who had an experience of over three decades in the cylinder manufacturing business. Presently, the business is managed by his sons, Mr. Pushkar Khurana (Chairman) and Mr. Puneet Khurana (Managing Director), both have been in the business for about 15 years. The key management personnel have been associated with the industry since more than 2 decades and thus have been instrumental in business expansion and forging client relationships.

**Established market position in High Pressure Seamless Cylinders and diversified customer mix:** EKCL is one of the largest player in high pressure cylinders in India with presence of over 4 decades in the industry. Revenue has grown at a compounded annual growth rate of around 10% in the past 3 years through March 2020, driven by healthy demand. Further, EKCL has diversified customer mix consisting of OEM (Original Equipment Manufacturers) such as Bajaj Auto Limited, Tata Motors Limited, Ashok Leyland, VE Commercial Vehicles Limited (Eicher Motors), CEV Engineering Pvt Ltd (Hyundai), etc. The customers also include some of the large industrial gas manufacturers like PraxAir, fire fighting product companies such as Tyco, Siemens, Minimax etc and city gas distribution companies like Adani Gas, Mahanagar Gas, Indraprashta Gas etc. Further, the company has manufacturing facilities in Dubai and USA apart from India. EKCL exports to countries in Middle East, Africa, Europe, South America and CIS countries.

**High entry barriers and regulated nature of industry:** The existing stringent regulation w.r.t testing and clearance at multiple levels as per the directive of Petroleum and Explosive Safety Organization poses an entry barrier for new entrants to the high pressure seamless cylinder manufacturing industry. Further, the companies also need to take approval of the Chief Controller of Explosives (CCOE) for import in India. Also, the companies operating in this industry are to follow stringent quality standards for manufacturing the cylinders. Thus the industry is exposed to high entry barriers.

**Healthy TOI growth in H1FY21 and FY20; Albeit muted performance in overseas subsidiaries:** EKCL's Total Operating Income (TOI) on a consolidated basis grew by 7% on a YoY basis to Rs.763.09 crore in FY20, driven by volume growth in CNG (Compressed Natural Gas) cylinders sold to OEMs (Original Equipment Manufacturers). Growth was also driven by increased prices of imported steel tubes and pipes which being the key raw material consumed by EKCL translated in to higher realisation. The growth in TOI continued in H1FY21 by 12.32% Y-o-Y to Rs. 422.66 crore owing to sustained growth in the sales volume of CNG cylinders along with increase in the demand for industrial cylinders. While demand across both the subsidiaries in Dubai and USA continues to remain weak in recent months, sharp bounce back is expected during H2FY21.

**Sharp improvement in PBILDT margins in H1FY21 though expected to moderate:** EKCL on consolidated basis, reported a sharp improvement in PBILDT margins in H1FY21 to 22.02% as against 13.46% y-o-y. Improvement in PBILDT margins was driven by higher sales realisation resulting from increase in the demand of mostly industrial cylinders along with moderation in the raw material prices. On standalone basis too, EKCL booked substantial improvement in PBILDT margins of 29.14% as against 22.65% in H1FY20. The margins on consolidated level were moderated due to weaker performance of the subsidiaries due to CoVID-19 impact which led to weaker demand in overseas market. Further, in line with increase in the PBILDT margin in H1FY21, the PAT margin also witnessed a sharp improvement. During FY20, EKCL continued to report decline in PBILDT margins y-o-y due to wide fluctuation in the raw material prices along with lower utilisation of capacities leading to increased share of overhead cost in revenues.

**Improved leverage indicators albeit; moderation in debt coverage indicators:** EKCL's financial risk profile continues to remain moderate marked by low gearing and moderate debt coverage indicators. EKCL's overall gearing improved marginally to 0.59x as on March 31, 2020 as against 0.65x as on March 31, 2019, on a consolidated basis, led by

scheduled repayment as well as pre-payment of long term borrowing. Going forward, in the short to medium term, the overall gearing is expected to improve further given no major debt funded capex planned by the company.

Due to decline in PBILDT margins by 251 bps, the PBILDT interest coverage too deteriorated to 2.55x in FY20 as compared with 2.80x for FY19. However, due to improvement in operating margins in H1FY21, the interest coverage too improved to 6.83x as compared to 3.00x in H1FY20. Further, driven by improved GCA (Gross Cash Accruals) of Rs 50.40 crore in FY20 as against Rs.31.63 crore in FY19, TDGCA ratio improved to 6.25x as compared to 10.64x in FY19. The TDCGA is expected to improve in FY21 with expectation of improvement in the overall financial performance on back of improvement in the sales realisation along with strong market demand.

#### Key Rating Weaknesses

**Working capital intensive nature of operations:** EKCL's operations are inherently working capital intensive in nature due to procurement of majority of its raw material (Seamless Steel Tubes) requirement from China which takes a lead time of 3- 6 months coupled with relatively smaller credit period and maintenance of inventory. As a result of this, average utilization fund based facility was healthy at 74% for the last 12 months ended October 2020.

**Volatility of raw material prices and foreign exchange fluctuation risk:** Raw material (imported seamless steel tubes) constitutes majority of operating expenses of EKCL. Fluctuations in raw material prices, therefore, tend to impact the PBILDT margins. Any adverse change in the exchange rate between the US Dollar and the Indian rupee will have a negative impact on EKCL's financial performance as the seamless steel tubes (basic raw material) are fully imported. EKCL does not hedge its foreign currency exposure thus exposing itself to currency risk. However, with some of the OEM's, EKCL inbuilt escalation clause in the contracts in order to amend variation in raw material prices or exchange rate.

**Liquidity: Adequate:** EKCL's liquidity position remained adequate marked by expected GCA of ~Rs.85-90 crore during FY21 on a consolidated basis, as against scheduled debt repayment of ~Rs.54 crore. EKCL has already reported ~Rs.54 crore of gross cash accruals in H1FY21. The company had a moderate unencumbered cash balance of Rs.15.67 crore as on March 31, 2020. The company had availed moratorium from one of its lenders against the term loan during COVID 19 and has started paying the instalments as per the schedule. The company has already paid the instalment due in October 2020 in the month of September 2020 itself. The working capital cycle continued to remain elongated. However, its average working capital utilisation improved to ~74% during the past 12 months ended October 2020. The breach of financial covenants in its US-based step down subsidiary could impact the liquidity position on consolidated basis if it triggers accelerated repayment of the entity's debt facility; CARE however notes that till date, the accelerated repayment clause has not been invoked.

**Analytical approach:** Consolidated, while arriving at the rating care has considered consolidated financials as all its subsidiaries are in the similar line of business and are under the same management. Following are the list of companies considered in consolidation along with their holdings by EKCL as on March 31, 2020 is provided below.

Name of the subsidiary	Country	Holding
EKC International FZE	UAE	100
CP Industries Holdings, Inc.	USA	100
EKC Industries (Tianjin) Co. Ltd.*	China	100
EKC Industries (Thailand) Co. Ltd.	Thailand	100
Calcutta Compressions and Liquifaction Eng. Ltd.	India	100
EKC Hungry Kft.	Hungary	100
Next Gen Cylinder Pvt. Limited	India	100
EKC Europe GmbH	Germany	100

\*EKCL along with its UAE subsidiary had entered into an agreement to sell its entire stake in China subsidiary to a company in China, for an aggregate consideration of RMB 93.50 Million (approx. Rs.100 crore). The sale process has commenced wherein EKCL is in advanced stage of consummation of the agreement.

**Applicable Criteria**
[Criteria on Consolidation and Factoring Linkages](#)
[Criteria on Rating Outlook and Credit Watch](#)
[CARE's Policy on Default Recognition](#)
[CARE's methodology for Short-term Instruments](#)
[Rating Methodology – Manufacturing Companies](#)
[Financial ratios – Non-Financial Sector](#)
[Liquidity Analysis- Non-Financial Sector](#)
**About the Company**

Incorporated in 1978, EKCL is engaged in the manufacturing of high pressure seamless cylinders for industrial gases and CNG applications, large diameter high pressure seamless vessels, large seamless cylinders, jumbo cylinders and jumbo skids for the storage and bulk transportation of CNG and various other industrial and specialty gases like Nitrogen, Helium, Argon, etc. The products manufactured by EKCL find application in domestic and international markets like aerospace, chemical processing, construction, food production, industrial controls, medicine, nuclear and power propulsion systems, CNG City Gas Projects, etc. The company has two facilities to manufacture cylinders in India (located at Tarapur in Maharashtra and Kandla in Gujarat) as well as Outside India (located at Dubai & USA).

Brief Financials (Rs. crore)	FY19A	FY20A	H1FY21
Total operating income	713.15	763.09	422.66
PBILDT	105.07	93.26	93.09
PAT	73.12	6.73	36.02
Overall gearing (times)	0.65	0.59	0.50
Interest coverage (times)	2.80	2.55	6.83

A: Audited, Financials are classified as per CARE Standards.

**Status of non-cooperation with previous CRA:** Not Applicable

**Any other information:** Not Applicable

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

**Annexure-1: Details of Instruments/Facilities**

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	April 2021	12.57	CARE BBB-; Positive
Fund-based - LT-Cash Credit	-	-	-	91.00	CARE BBB-; Positive
Non-fund-based - ST-BG/LC	-	-	-	69.92	CARE A3

## 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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	12.57	CARE BBB-; Positive	-	1)CARE BB+; Stable (19-Feb-20)	1)CARE BB+; Positive (15-Feb-19)	1)CARE BB; Positive (16-Nov-17)
2.	Fund-based - LT-Cash Credit	LT	91.00	CARE BBB-; Positive	-	1)CARE BB+; Stable (19-Feb-20)	1)CARE BB+; Positive (15-Feb-19)	1)CARE BB; Positive (16-Nov-17)
3.	Non-fund-based - ST-BG/LC	ST	69.92	CARE A3	-	1)CARE A4+ (19-Feb-20)	1)CARE A4+ (15-Feb-19)	1)CARE A4+ (16-Nov-17)
4.	Term Loan-Long Term	LT	-	-	-	-	1)Withdrawn (15-Feb-19)	1)CARE BB; Positive (16-Nov-17)

## Annexure 4: Complexity level of various instruments rated for this Company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Fund-based - LT-Term Loan	Simple
3.	Non-fund-based - ST-BG/LC	Simple

**Note on complexity levels of the rated instrument:** CARE has classified instruments rated by it on the basis of complexity. This classification is available at [www.careratings.com](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications.

## Contact us

### Media Contact

Mradul Mishra  
Contact no. – +91-22-6837 4424  
Email ID – [mradul.mishra@careratings.com](mailto:mradul.mishra@careratings.com)

### Analyst Contact-1

Group Head Name: Mr. Arti Roy  
Contact No: +91-22-6754 3451  
Email ID- [arti.roy@careratings.com](mailto:arti.roy@careratings.com)

### Analyst Contact-2

Rating Head Name: Mr. Sudarshan Shreenivas  
Contact No: +91-22-6754 3566  
Email ID- [sudarshan.shreenivas@careratings.com](mailto:sudarshan.shreenivas@careratings.com)

### Relationship Contact

Name: Mr. Saikat Roy  
Contact no. +91-22-6754 3404  
Email ID: [saikat.roy@careratings.com](mailto:saikat.roy@careratings.com)

### About CARE Ratings:

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