Gravita India Limited

September 06, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	44.79	**CARE BBB+; Stable (Triple B Plus; Outlook: Stable)**	**Revised from CARE A-; Negative (Single A Minus; Outlook: Negative)**
Long-term/Short-term Bank Facilities	209.00	**CARE BBB+; Stable / CARE A2 (Triple B Plus; Outlook: Stable / A Two)**	**Revised from CARE A-; Negative / CARE A2+ (Single A Minus; Outlook: Negative / A Two Plus)**
Short-term Bank Facilities	31.00	**CARE A2 (A Two)**	**Revised from CARE A2+ (A Two Plus)**
Total facilities	**284.79 (Rs. Two Hundred Eighty Four crore and Seventy Nine lakh only)**		

*Details of instruments/facilities in Annexure-1; *The rating assigned to short term bank facility of Rs.12 crore has been withdrawn as the same has not been renewed*

Detailed Rationale & Key Rating Drivers

The revision in the ratings of the bank facilities of Gravita India Limited (GIL) is on account of deterioration in its profitability margins and debt coverage indicators during Q1FY20 along with moderation in its liquidity which has happened on the back of lower than previously envisaged total operating income (TOI) and profitability for FY19 (refers to the period April 1 to March 31).

The ratings continue to derive strength from GIL's experienced management, established track record of operations in lead recycling and smelting industry with wide geographical presence, its operational synergy with subsidiaries at multiple locations and benefit derived from its license to import lead acid battery scrap. The ratings are further underpinned by its moderate capital structure and reputed customer base.

The ratings, however, continue to remain constrained on account of its limited pricing flexibility due to low value addition nature of its business and weak entry barriers; along with susceptibility of its profitability to volatility in lead prices especially in the backdrop of its large inventory holding. The ratings are further constrained on account of risk associated with stabilisation of operations of its on-going and recently concluded projects, customer concentration risk, foreign exchange fluctuation risk, regulatory risk pertaining to duty structure and requirement of compliance with stringent environmental norms and inherent cyclicality associated with the end-user industry.

GIL's ability to significantly improve its profitability on a sustained basis through implementation of effective hedging policy and practices in the backdrop of volatile metal prices leading to improvement in its debt coverage and liquidity indicators shall be the key rating sensitivities. Furthermore, stabilization of operations of its newly constructed facilities and generation of envisaged returns thereof while diversifying its customer base and ensuring continuous compliance with prescribed environmental norms would also remain rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced management: Dr. Mahaveer Prasad Agrawal (Chairman) and Mr. Rajat Agrawal (Managing Director) have vast experience of more than two decades in the lead recycling industry.

Established track record of operations with wide geographical presence: GIL has an established track record of operation in the lead recycling and smelting industry since 1992. Over the period, GIL has set up plants at eight different locations under standalone operations as well as under various subsidiaries (both in India and abroad) in order to be in close proximity to key raw material sources which improves its accessibility and partially mitigates regulatory risk arising from environmental concerns of operating in a single location.

Operational synergy with subsidiaries: Overseas subsidiaries of GIL in African countries have only lead smelting capacity while its subsidiaries in America are largely into PET recycling and scrap collection with major portion of their sales being routed through GIL providing operational synergy. Furthermore, the company has come up with a new lead smelting and refining facility at Ghana as well as a new lead smelting and aluminum recycling facility at Tanzania during current year i.e. FY20. GIL benefits from its license for import of battery scrap in to India. However, its overseas subsidiaries are exposed to geo-political risks given their location in the African regions.

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

Growth in scale of operations in FY19 although the same declined in Q1FY20 on y-o-y basis: GIL's consolidated total operating income (TOI) increased by around 22% on y-o-y basis to Rs.1247.06 crore in FY19 mainly due to increase in sales volume across lead, aluminium and plastic products on account of healthy demand from respective customers. However, the TOI of GIL declined by around 13% on y-o-y basis in Q1FY20 largely on account of decline in sales volume of lead and aluminium products along with decline in average sales realisation of both the commodities, viz., lead and aluminum, in line with decline in their market prices.

Moderate capital structure: GIL's overall gearing though improved; stood moderate at 1.24 times as on March 31, 2019 as against 1.33 times as on March 31, 2018. However, total debt level is likely to increase by end-FY20 on account of its planned drawal of term loan as reimbursement of capex incurred in the past.

Key Rating Weaknesses
Decline in profitability margins and moderation in its debt coverage indicators: PBILDT margin of GIL declined by 333 bps on y-o-y basis to 5.82% in FY19 on account of higher cost of raw material consumed. Declining price trend of lead (at LME) impacted its operating margin as the sales realization on products tends to decline while the scrap procurement expenses and conversion charges which are fixed in nature do not change much. The same was also on account of downward revision in valuation of base inventory which remained un-hedged in FY19. The PBILDT margin continued to moderate on y-o-y basis as reflected from its 179 bps dip to 6.08% in Q1FY20. The profitability of the company remains susceptible to volatility in prices of lead which is driven by international demand-supply scenario. With reduction in profitability along with increase in interest and depreciation expenses, PAT margin also declined by around 313 bps on y-o-y basis to 1.55% in FY19. Gross cash accruals of the company declined from Rs.58.55 crore in FY18 to Rs.36.87 crore in FY19. Furthermore, PAT margin declined by 297 bps on y-o-y basis to 0.95% in Q1FY20 due to increase in interest and depreciation expenses. GIL's debt coverage indicators also exhibited deterioration as reflected from its total debt to GCA of 6.82 times as on March 31, 2019 (4.38 times as on March 31, 2018) while PBILDT interest coverage declined to 2.77 times in FY19 (4.59 times in FY18) and further to 2.34 times during Q1FY20 on account of increase in interest expenses along with decline in operating profit.

Customer concentration; albeit some of them being very reputed: Sales to top 10 customers constituted around 52% of its TOI (consolidated) in FY19 (59% in FY18) depicting moderate customer concentration risk. GIL exports its products to around 29 countries with major exports being made to U.S.A., Japan, Singapore and Indonesia. Some of the customers of GIL are reputed which include Luminous Power Technologies Private Limited, Exide Industries Limited and KEI Industries Limited. GIL has also entered into contract with Amara Raja Batteries Limited (ARBL) for lead acid battery scrap collection and recycling arrangements. Apart from barter arrangement with ARBL, GIL has entered into yearly contract with ARBL for supplying lead ingots. However, the previously envisaged benefit from its contract with ARBL has not materialized.

Raw material price fluctuation risk; albeit management's articulation to fully hedge its inventory going forward: GIL's profitability is vulnerable to volatility in prices of lead which have exhibited high volatility in the past. GIL's profitability got impacted in the past on account of its inability to pass on higher raw material purchase cost to its customers as well as due to part of its inventory remaining un-hedged. In order to mitigate the raw material price volatility risk, the company management has articulated that it uses different hedging policies depending on type of order. In around 50% of its orders from customers who enter into contracts with GIL, the company has back to back raw material procurement arrangement in order to mitigate the said risk. Furthermore, in some cases where the company receives monthly orders from its regular customers, the price is decided as per the average rate of lead battery scrap / lead prevailing in the market in the immediate preceding month. The company procures raw material considering the quantity demanded by these customers which helps in mitigating the volatility in prices of raw materials to an extent. Remaining orders and excess scrap collected used to remain un-hedged which affected the profitability margins. The company has now started hedging the excess scrap collected apart from scrap collected for orders received by booking contracts on LME. Moreover, the company has core inventory of 2900 MT which is available across manufacturing facilities to carry out production uninterruptedly. The company has reinstated the cost of said inventory time to time considering the market price of lead which impacted the profitability margins in FY19. The company management has articulated that now it has completely hedged the said inventory in Q1FY20 which is expected to result in relatively stable profitability margins going forward. GIL's management has further articulated that unlike in the past they plan to actively hedge against aluminium price volatility going forward. Furthermore, the company incurred losses in FY18 and FY19 in the plastics division on account of non-stabilisation of operations. Ability of the company to actively manage the volatility in prices of its key raw materials in an effective manner and timely pass on the increase in raw material prices to its customers so as to improve its profitability margins would be crucial.

Foreign exchange fluctuation risk: The company uses forward contracts to hedge majority of its foreign currency exposure which is in the form of imports, exports and foreign currency borrowings. The company hedges part of its open position apart from the portion which is hedged naturally by entering into forward contracts. Hence, the risk persists for balance un-hedged portion.

Timely implementation and stabilisation risk associated with its projects: GIL is in the process of shifting its lead refining unit from Gandhidham to Mundra which is expected to get completed by September 2019. The same has got delayed on account of delay in receipt of license from government for import of cable scrap at Mundra facility. The company is envisaged to save on logistics cost at Mundra plant as the same would be closer to Mundra port. Further, the company has started commercial production of lead from newly constructed smelting unit at Tanzania with installed capacity of 3000 MT from April 2019 and has commenced recycling of aluminium through smelting facility with installed capacity of 6000 MT in July 2019. Furthermore, the company has also completed construction of lead smelting and refining unit at Ghana under its newly formed subsidiary- Recyclers Ghana Limited and commercial production from the same has started with installed capacity of 6,000 MT in June 2019. The installed capacity of Ghana would be further increased by 6,000 MT by end of August 2019. The company has incurred total cost of around Rs.27 crore up to March 31, 2019 and envisages incurring around Rs.8 crore towards these projects at Ghana and Tanzania during current financial year i.e. FY20. There has been marginal cost overrun and time overrun in these projects which can be mainly attributed to delay in transportation of machinery, delay in installation along with teething problems being faced at the time of installation. Moreover, the company does not envisage any further capex for expansion of capacity (apart from routine capex) in near term and plans for optimum utilisation of its existing capacity. The company had got sanction of term loan of Rs.31.50 crore for capex at Ghana and Tanzania project along with reimbursement with regard to capex already done at Jamaica and Nicaragua in FY18. The company has availed partial amount out of total sanction of Rs.31.50 crore up to date and would avail the balance loan in the current year which would be utilized for remaining capex as well as in meeting its working capital requirement. Ability of the company to stabilize operations at Ghana and Tanzania facilities and derive expected benefits and return on its investments thereon would be crucial.

Regulatory risk pertaining to duty structure and compliance with environmental norms: Lead is hazardous in nature and can cause serious damage to the environment. To safeguard against this, the Ministry of Environment and Forests (MoEF) has framed Batteries (Management and Handling) Rules, 2001. These rules specify that only those who possess environmentally sound management systems and are registered with the MoEF / Central Pollution Control Board (CPCB) are allowed to carry out battery recycling. Although GIL being a CPCB certified company has an advantage over unorganized sector, any violations of stringent pollution control norms can adversely affect the operations of the company. Moreover, any change in duty structure on lead products including battery scrap can impact the viability of its operations. The company has also become a member of International Lead Association (ILA) which is expected to benefit it in terms of worldwide recognition.

Inherent cyclicality associated with end user industry: Lead alloys find its primary application in the manufacturing of lead acid batteries for its use in automobiles, invertors, solar power systems, etc. with automobile industry being the major end user industry for lead acid batteries. Hence, GIL is exposed to inherent cyclicality associated with automobile industry. However, the growth in power back-up industry is likely to have a favourable impact on the lead industry which augurs well for the companies like GIL.

Liquidity: GIL's operations are working capital intensive in nature. The average utilization of its fund-based working capital borrowings stood at 94% during the trailing 12 month period ended July, 2019. Liquidity position of GIL moderated marked by decline in current ratio to 1.08 times as on March 31, 2019 (1.22 times as on March 31, 2018). However, the company had free cash and bank balance of around Rs.15.27 crore as on March 31, 2019 at consolidated level. Its liquidity is also likely to be supported through long-term debt of Rs.17.5 crore that has been sanctioned to it by its lenders towards reimbursement of new as well as completed capex and the proposed term debt of around Rs.12 crore that it plans to avail towards reimbursement of capex already done at Phagi, Jaipur; the same is expected to be utilized for meeting its remaining capex and working capital requirement.

Industry Outlook: The lead industry in India is poised to perform well on the back of good demand prospects in long term. India's growing telecom industry and on-going infrastructure development has boosted the industrial battery demand, as is the case with an expanding photovoltaic market which is planned to reach 227 GW by 2022. The automobile sector, the telecom sector and the power sector (solar, wind and invertors) will be the main demand drivers for lead usage. Lead prices are influenced by the global economic conditions and the geopolitical conditions of the major producing countries & major utilizing countries. Mine and metal demand-supply dynamics, inventory levels and currency fluctuations also play a role in determining lead prices. Price of lead has been declining since the start of FY19. The on-going global trade wars, appreciation of the dollar and fears of a global slowdown have, however, been dragging the prices of lead.
The growth in aluminium consumption is likely to be driven by the growth in power transmission and the automobile sector. Demand from the building & construction activities is also likely to pick up due to the affordable housing for all program;

whereas demand from the packaging sector is likely to support the domestic demand. However, the aluminium prices will continue getting affected due to changing macros on account of recent trade wars which will impact the global demand supply dynamics.
Going forward, organised players with strong sourcing ability with better operating efficiencies, geographically diversified clientele and a conservative forex/working capital management policy are likely to exhibit relatively stable credit profiles.

Analytical Approach - Consolidated. For analysis purpose, CARE has considered the consolidated financials of GIL as there are operational synergies between the parent (GIL) and its subsidiaries and associate. Details of subsidiaries and associate considered in GIL's consolidation have been given in **Annexure 3.**

Applicable Criteria
Criteria on assigning Rating Outlook and Credit Watch
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology-Manufacturing Companies
Factoring Linkages in Ratings
Financial ratios – Non-Financial Sector

About the company
Incorporated in 1992, GIL is a listed public limited company promoted by Dr Mahaveer Prasad Agrawal and Mr Rajat Agrawal. GIL is engaged in the manufacturing and trading of lead and lead-based products. Under manufacturing operations, the company carries out smelting of lead battery scrap to produce secondary lead metal, which is transformed into pure lead, specific lead alloy, lead oxides (lead sub-oxide, red lead, and litharge) and lead products like lead sheets and lead pipes. Over the past few years, the company has also ventured into recycling of aluminium and plastic scrap. The company also provides turnkey solutions for development of plant and machinery for lead manufacturing units.

Brief Financials- Consolidated (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	1018.60	1247.06
PBILDT	93.22	72.55
PAT	47.64	19.39
Overall gearing (times)	1.33	1.24
Interest coverage (times)	4.59	2.77

A: Audited

As per published results on the stock exchange, during Q1FY20, GIL on consolidated basis earned a PAT of Rs.2.52 crore (Q1FY19: Rs.11.99 crore) on a TOI of Rs.264.91 crore (Q1FY19: Rs.305.75 crore).

Status of non-cooperation with previous CRA: None

Any other information: Not Applicable

Rating History (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/ ST-Cash Credit	-	-	-	209.00	CARE BBB+; Stable / CARE A2
Fund-based - LT-Term Loan	-	-	Nov-2024	44.79	CARE BBB+; Stable
Non-fund-based - ST-BG/LC	-	-	-	31.00	CARE A2
Fund-based - ST-Standby Line of Credit	-	-	-	0.00	Withdrawn

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT/ ST-Cash Credit	LT/ST	209.00	CARE BBB+; Stable / CARE A2	1)CARE A-; Negative / CARE A2+ (07-Jun-19)	1)CARE A-; Stable / CARE A2+ (26-Nov-18) 2)CARE A-; Positive / CARE A2+ (08-Oct-18)	1)CARE A-; Positive / CARE A2+ (07-Aug-17)	1)CARE A-; Stable / CARE A2+ (22-Feb-17) 2)CARE A- / CARE A2+ (25-Apr-16)
2.	Fund-based - LT-Term Loan	LT	44.79	CARE BBB+; Stable	1)CARE A-; Negative (07-Jun-19)	1)CARE A-; Stable (26-Nov-18) 2)CARE A-; Positive (08-Oct-18)	1)CARE A-; Positive (07-Aug-17)	1)CARE A-; Stable (22-Feb-17) 2)CARE A- (25-Apr-16)
3.	Non-fund-based - ST-BG/LC	ST	31.00	CARE A2	1)CARE A2+ (07-Jun-19)	1)CARE A2+ (26-Nov-18) 2)CARE A2+ (08-Oct-18)	1)CARE A2+ (07-Aug-17)	1)CARE A2+ (22-Feb-17) 2)CARE A2+ (25-Apr-16)
4.	Fund-based - ST-Standby Line of Credit	ST	-	-	1)CARE A2+ (07-Jun-19)	1)CARE A2+ (26-Nov-18) 2)CARE A2+ (08-Oct-18)	1)CARE A2+ (07-Aug-17)	1)CARE A2+ (22-Feb-17) 2)CARE A2+ (25-Apr-16)

Annexure-3: List of subsidiaries and associate

Name of the subsidiary and associate	% of Holding as on March 31, 2019
Gravita Infotech Limited (Formerly known as M/s Gravita Exim Ltd)	100.00
M/s Gravita Metals	100.00
M/s Gravita Metal Inc	100.00
M/s Gravita Infotech (Formerly known as M/s Gravita Technomech)	100.00
M/s Recycling Infotech LLP	100.00
Gravita Employee Welfare Trust	100.00
Noble Build Estate Private Limited	100.00
Gravita Ghana Limited	100.00
Gravita Mozambique LDA	100.00
Gravita Global Pte Limited	100.00
Navam Lanka Limited	52.00
Gravita Netherlands BV	100.00
Gravita Senegal S.A.U	100.00
Gravita Nicaragua S.A.	100.00
Gravita Jamaica Limited	100.00
Gravita Ventures Limited	100.00
Gravita USA Inc.	100.00
Gravita Mali SA	100.00
Gravita Cameroon Ltd.	100.00
Met Mauritania Recycling SARL	100.00
Recyclers Gravita Costa Rica SA	100.00
Gravita Tanzania Limited	100.00
Recyclers Ghana Ltd.	100.00
Mozambique Recyclers LDA	100.00
Gravita Dominican SAS	100.00
Gravita Peru SAC	100.00
Pearl Landcon Private Limited	25.00

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. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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