J.K. Cement Limited

July 09, 2020

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Proposed Non-Convertible Debentures	250.00 (enhanced from Rs.200 crore)	CARE AA; Stable [Double A; Outlook: Stable]	Reaffirmed
Total Facilities	**250.00 (Rs. Two Hundred and Fifty Crore)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The reaffirmation of rating of the non-convertible debentures (NCDs) of J.K. Cement Limited (JKCL) derives strength from the extensive experience of the promoters in cement business, the company's established presence in grey cement across diversified geographical markets and its dominant position in white cement, ensuring healthy margins from the product, and its strong brand image in both segments. The rating also takes into account satisfactory financial performance of the company during the FY20, its comfortable financial profile and its strong liquidity position.

The rating is, however, constrained on account of the timing of the significant capacity expansion which is nearing completion and would come on-stream at a time when the cement industry is impacted on account of the outbreak of Covid-19 pandemic, the incremental debt required for the residual portion of the expansion programme which shall lead to increased overall gearing in the next 1-2 years, support extended by JKCL to its loss-making subsidiary J.K Cement Works Fujairah (JKCWF, rated CARE AA (SO); Stable), cyclicality associated with the cement industry, exposure to volatility in input costs and cement demand dependent on construction activity and infrastructure spend in the economy and the uncertainty regarding the timing of the on-going Covid-19 pandemic clearing out.

Rating Sensitivities: The sensitivities indicate the possible direction of movement of rating in future (positive or negative), on happening of, *inter alia,* the following events:

Positive Factors:

- Improvement in leverage levels, going forward, with overall gearing sustaining below unity, on a consolidated basis.
- Timely stabilization of enhanced capacities such that the overall capacity utilization levels ramp up to 75% -80%
- Sustained growth in top-line by around 15-20% p.a.
- Turnaround of loss-making subsidiary J.K. Cement Works Fujairah
- Sustained profitability in light of volatile input costs

Negative Factors

- Time and cost overruns in the ongoing capex and extended stabilization period for the enhanced capacities amidst the ongoing Covid-19 pandemic
- Increase in leverage levels such that overall gearing, on a consolidated basis, increases beyond 1.50x
- Structural changes in the white cement industry impacting the profitability of the company

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters, established presence and strong brand image

The promoters of JKCL have extensive experience in the business of cement manufacturing and marketing. JKCL also has an experienced and qualified management team, which has facilitated the company's growth over two decades. The company has a strong presence in the grey cement segment across the northern, western and southern markets of India, with presence in more than 10 states and has established brands like '*JK Super Cement*' and '*JK Super Strong Cement*'. Besides, the company has a pan-India presence in white cement and wall putty, which are sold, respectively, under brand names, '*JK White Cement*' and '*JK Wall Putty*'.

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

Dominant position in white cement industry
JKCL is the second largest white cement manufacturer in India with an installed capacity of 0.6 million tonnes per annum (MTPA). The company also produces wall putty, a value-added product of white cement, for which it has an overall capacity of 0.9 MTPA as on March 31, 2020. The white cement segment is characterised by a small industry with significant entry barriers, and consequently a duopoly structure as of now, which ensures healthy operating margins for the manufacturers. Besides, consistently strong growth in the white cement and wall putty segments has created a steady cash flow stream for JKCL and contributed significantly towards its PBILDT over the years.

Consistent improvement in operating and financial performance
During FY20, the company has reported improvement in financial performance. The consolidated operating income of JKLC has grown by around 11% on y-o-y basis to Rs.5,887 crore (Rs.5310 crore in FY19), its PBILDT has increased by around 46% to Rs.1299 crore in FY20 (Rs.890 crore in FY19), and its PAT has increased by 83% to Rs.483 crore in FY20 (Rs.264 crore in FY19). The improvement in performance in FY20 is primarily on account of higher sales realizations and reduced input costs.

JKCL's volume growth in the white cement and wall putty segments continued to be steady at 10% in FY20. The volumes in the grey cement segment declined by 2% during FY20 owing to Covid-19 pandemic, which affected the operations of the company during last 10 days of March 2020. While net sales realization for white cement and putty remained at similar level during FY20 over FY19, the net sales realization in grey cement segment improved by more than 13% during FY20, which has offset the decline in volumes during the FY20.
Owing to nation-wide lockdown, the volumes are expected to be lower in Q1 FY21. It may however, be noted that the company has gradually ramped up its operations on all the plants following partial lifting of the lockdown. The ramp up in rural areas has been moderate which has resulted in increased trade volumes for grey cement subsequent to lifting of lockdown. The sales volume of white cement, however, has declined, with white cement being a high value commodity with demand primarily in urban areas. Cement demand is closely linked to the overall economic growth, particularly the housing and infrastructure sector, which has fallen given the lockdown related restrictions owing to Covid-19 pandemic. Going forward, the ability of the company to sustain or improve its operational performance amidst the ongoing Covid-19 pandemic, and revive its volumes and realizations over the rest of the FY21 shall be a key monitorable.

Comfortable financial risk profile and strong liquidity position
JKCL's financial risk profile improved during the FY19 facilitated by improvements in the capital structure and debt service coverage ratios. The company raised equity aggregating Rs. 510.79 crore in the month of Dec 2018 which has strengthened the company's capital structure. The company's interest coverage ratio stood at 3.41x for FY19, which further improved to 4.70x for FY20 on account of improvement in PBILDT levels. Furthermore, the overall gearing of the company also improved to 1.10x as on March 31, 2020 at the back of healthy profits generation as against 1.12x as on March 31, 2019 , however, drawdown of debt for the ongoing capex would result in some increase in gearing levels in the next year.

Key Rating Weaknesses
Ongoing capital expenditure though satisfactory progress achieved
JKCL had undertaken a brownfield expansion of 4.2 MTPA for a total estimated expenditure of about Rs.1,998 crore, which had started in FY18. The expansion comprises of an additional clinker capacity of about 2.64 MTPA at Mangrol and additional grinding capacity of 1 MTPA each at Nimbahera and Mangrol. Besides, two new split grinding units of 1.5 MTPA at Aligarh, Uttar Pradesh and 0.7 MTPA at Balsinor, Gujarat would be added under the planned expansion. The aggregate project cost is funded in debt equity ratio of 1.86:1. The entire debt has been tied up and drawn to the extent of Rs. 760 crore as on March 31, 2020. Equity has been infused aggregating Rs. 668 crore as on March 31, 2020 as against the total equity requirement of Rs. 698 crore. The company has incurred expenses of Rs.1,480 crore till March 31, 2020.

While the company had commissioned the 1 MTPA grey cement grinding unit at Nimbahera and a 2.64 MTPA grey clinker at Mangrol in September 2019, 1 MTPA Cement Grinding Capacity at Mangrol and 1.5 MTPA at Aligarh has also been commissioned and commercial despatches have since started from February 2020. The balance 0.7 MTPA grinding unit at Balasinor is at an advanced stage and likely to be commissioned by FY21.
While a large part of the capex has been completed, the company remains exposed to project risk for the residual portion of the expansion project, which would be substantially funded through term debt, resulting in increased gearing ratio during the FY21. The timely completion and stabilization of operations of the new capacity shall be a key monitorable.

Furthermore, the capacities would come on-stream at a time when the cement industry is impacted on account of the outbreak of Covid-19 pandemic and the entire industry would grapple with volume ramp-up with normalization of the ongoing scenario. However, this is mitigated to a large extent by the strong brand image enjoyed by the company. Besides, the company expects to enhance its distribution network during the current period which would enable it to increase its supply as and when the demand normalizes.

JKCWF's weak operating performance and financial risk profile
JKCL, under its step-down subsidiary JKCWF, had established a green-field dual process cement plant in September 2014 at Fujairah, UAE, having installed capacity of 0.6 MTPA of white cement or 1 MTPA of grey cement. JKCWF has reported net loss since the commencement of operations (net loss of Arab Emirate Dirhams (AED) 38.15 million and AED 37.23 million in CY 19 and CY18 respectively). The operating levels have remained relatively low due to weak demand in the Gulf countries on account of subdued construction activity. JKCWF remains dependent on infusion of funds from JKCL for meeting its debt obligations in near term. Consequently, operational and financial improvement in performance would remain a crucial rating sensitivity of JKCL.

Exposure to volatility in input costs as well as sales realization prices
While JKCL has fuel supply agreements (FSA) to meet part of the coal requirement, it has a significant dependence on petroleum coke (sourced from domestic markets) and imported coal, thereby exposing the company to any adverse volatility in the prices of commodities. Additionally, the company is meeting part of its fuel requirement through imports, which also exposes it to the risk of any adverse fluctuation in exchange rates. The ability of the company to manage costs and improve realizations remains crucial. Besides, realizations and profitability get impacted by demand, supply, offtake etc., which are inherent risks associated with the cement industry.

Liquidity Position**:** Strong
The liquidity position of the company continues to be strong with free cash balance (including liquid investments) of around Rs.980 crore as on July 1, 2020. The average utilisation of fund-based working capital limits (including commercial paper) was comfortable at 31.95% for 12 months ending May 31, 2020. The company has principal repayments of around Rs.415 crore in FY21 on a consolidated basis vis-à-vis gross cash accruals of Rs.851 crore in FY20.
The company has not availed moratorium for its debt obligations under the COVID-19 - Regulatory Package announced by the RBI on March 27, 2020 and May 22, 2020.

Analytical approach:
Consolidated

Applicable Criteria
Criteria on assigning 'Outlook' and 'Credit Watch' to Credit Ratings
CARE's Policy on Default Recognition
Financial Ratios – Non-Financial Sector
Rating Methodology – Manufacturing Companies
Rating Methodology - Cement Industry
Rating Methodology – Short Term Instruments
Rating Methodology: Factoring Linkages in Ratings
Liquidity Analysis of Non-Financial Sector Entities

About the Company
JKCL (CIN No: L17229UP1994PLC017199), a part of the JK group (North), was incorporated in November 1994. JKCL's installed capacity for grey cement stood at 13.97 MTPA, with facilities located at Nimbahera, Mangrol and Gotan in Rajasthan (aggregating 7.97 MTPA), Jhajjar in Haryana (1.50 MTPA capacity including split grinding unit at Jhajjar, commissioned in FY15), Muddarpur in Karnataka (3.0 MTPA) and Aligarh in Uttar Pradesh (1.50 MTPA). The company's white cement plant has a capacity of 0.6 MTPA is located at Gotan and wall putty plant of 0.5 MTPA is located at Gotan and 0.4 MTPA at Katni, Madhya Pradesh (commissioned on May, 2016 and June 2018).
JKCL, under its step-down subsidiary J.K Cement Works (Fujairah), FZC UAE (JKCWF, rated 'CARE AA (SO)', backed by corporate guarantee from JKCL) , has a dual process cement plant having interchangeable capacity of 0.6 mtpa of white cement or 1 mtpa of grey cement.

Brief Financials (Consolidated) (Rs. crore)	FY20 (A)	FY19 (A)	FY18 (A)
Total operating income	5,886.96	5,310.19	4,887.65
PBILDT	1,298.77	890.10	830.43
PAT	483.39	263.63	285.59
Overall gearing (times)	1.10	1.12	1.51
Interest coverage (times)	4.70	3.41	2.92

A: Audited

Covenants of rated facility: *Detailed explanation of covenants of the rated facilities is given in Annexure-3*

Status of non-cooperation with previous CRA: Not Applicable

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	ISIN	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Proposed Debentures-Non Convertible Debentures	NA	NA	NA	NA	250.00	CARE AA; Stable

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-Cash Credit	LT	375.00	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
2.	Commercial Paper	ST	150.00	CARE A1+	-	CARE A1+ (16-Dec-19)	1)CARE A1+ (08-Oct-18)	1)CARE A1+ (14-Sep-17)
3.	Non-fund-based - ST-BG/LC	ST	350.00	CARE A1+	-	CARE A1+ (16-Dec-19)	1)CARE A1+ (08-Oct-18)	1)CARE A1+ (14-Sep-17)
4.	Debentures-Non Convertible Debentures	LT	31.50	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
5.	Debentures-Non Convertible Debentures	LT	69.00	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
6.	Term Loan-Long Term	LT	2811.68	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
7.	Debentures-Non Convertible Debentures	LT	51.00	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
8.	Debentures-Non Convertible Debentures	LT	200.00	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
9.	Debentures-Non Convertible Debentures	LT	100.00	CARE AA; Stable	-	CARE AA; Stable (16-Dec-19)	1)CARE AA; Stable (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
10.	Debentures-Non Convertible Debentures	LT	-	-	-	-	1)Withdrawn (08-Oct-18)	1)CARE AA; Stable (14-Sep-17)
11.	Debentures-Non Convertible Debentures	LT	250.00	CARE AA; Stable	CARE AA; Stable (June 12, 2020)	-	-	-

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

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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