Kesoram Industries Limited

December 13, 2018

Rating

Facilities	Amount (Rs. Crore)	Rating[1]	Rating Action
Long/Short-term Bank Facilities	906.00 (reduced from 1,100)	**CARE BBB/CARE A3+; Credit watch with developing implications (Triple B/A Three Plus; under Credit watch with developing implications)**	**Continues on Credit watch with Developing Implications**
Short-term Bank Facilities	705.00	**CARE A3+: Credit watch with developing implications (A Three Plus; under Credit watch with developing implications**	**Continues on Credit watch with Developing Implications**
Total	**1,611.00 (Rupees One Thousand Six Hundred and Eleven crore only)**		

Details of facilities in Annexure-1

Detailed Rationale and Key Rating Drivers

The ratings assigned to the bank facilities of Kesoram Industries Limited (KIL) were under rating watch with developing implications due to lack of clarity on the sale or induction of a partner in the tyre division which would have a significant impact on the financial risk profile of the company. The Board of Directors of KIL, at its meeting held on December 4, 2018, has approved the demerger of the tyre division into Birla Tyres Limited (BTL). The Proposed Demerger shall be subject to various necessary regulatory approvals. Post demerger, BTL will be listed with its shareholding pattern being same as KIL. The appointed date of such demerger will be Jan.1, 2019.

The tyre division which is being demerged contributed about 39% of the revenue in FY18 (refers to the period April 1 to March 31). However, it incurred a loss before interest and tax of Rs.128.93 crore in FY18 as against a profit before interest and tax of Rs.127.50 crore earned by the cement division which KIL will continue to operate. Further, with the demerger of the tyre division, the debt level in KIL is expected to reduce substantially.

CARE will take a view on the ratings once the demerger process is completed and exact implications of the above demerger on the credit risk profile of KIL are clear and the ratings continue to remain on watch with developing implications.

The ratings draw strength from the long and established track record of promoters and demonstrated support by the promoters to the company and operational efficiency of the cement division. The ratings also take note of the reduction in quantum of losses in H1FY19 with improvement in performance of the tyre division, though it continued to incur losses. The ratings remain constrained by the leveraged capital structure, losses in tyre division, risk of volatility in raw material prices of tyre division, high competition in the tyre industry and cyclicality of the cement industry.

Detailed description of the key rating drivers

Key Rating Strengths

Long & established track record of the company

KIL, the flagship company of B. K. Birla group, was set up in the year 1919 and has been operating over the last nine decades. B. K. Birla group is a leading industrial group in the country with major interests in tea, cement, tyres, textiles, etc. Mr. B. K. Birla is the promoter & Chairman of KIL and his daughter Smt. Manjushree Khaitan is the vice-chairperson and executive director. As on Sep.30, 2018, the promoters' stake in KIL is around 53.18%.

To support the company in view of losses, the promoters infused equity of Rs.312 crore in March'2018 through preferential allotment and warrants and Rs.23.73 crore was infused as unsecured loan. In H1FY19 also, Rs 150 crore was advanced to KIL through promoter group entities.

Operational efficiency of cement division by way of limestone mines and captive power plant

In the cement segment, KIL sells both PPC and OPC. The ratio of OPC and PPC is around 55:45. KIL sells cement under the brand name 'Birla Shakti' and has presence in Western and Southern regions of the country. KIL sources limestone from its two leasehold mines (one each at both the locations). The limestone reserves at both the mines extend beyond economic life of the respective plants. The said mines are located in proximity of the clinker plants, thereby enabling the company to optimize cost. Cement production, being power intensive, KIL needs uninterrupted supply of power which is ensured by the CPPs installed at its plant locations (aggregate capacity 93MW), which meets the entire annual power

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

requirement of the cement unit. The cheaper cost of power generated in CPPs vis-à-vis power from GRID reduces power cost leading to improvement in operational efficiency of the company.

Key Rating Weaknesses

Continued losses incurred by the company, though the quantum reduced in H1FY19

Though KIL's total operating income remained relatively stable at Rs.3,606.87 crore in FY18 vis-à-vis Rs.3,715.03 crore in FY17, the company incurred operating loss of Rs.53.53 crore in FY18 vis-à-vis operating profit of Rs.68.52 crore in FY17. This was primarily due to increased losses in the tyre division. The profitability of cement division improved during the year despite subdued performance during Q3FY18 on account of lower prices in Maharashtra region (around 50% of its produce is sold in Maharashtra). The division achieved PBILDT of Rs.212 crore in FY18 as against Rs.181 crore in FY17. However, the losses from tyre division increased to Rs.90 crore in FY18 as against Rs.40 crore in FY17. Consequently, with increased overall operational losses and increase in interest cost, the loss before exceptional items increased to Rs.390.29 crore in FY18 (Rs.275.46 crore in FY17). The company incurred exceptional cost of Rs.75.22 crore in FY18 vis-à-vis exceptional income of Rs.121.35 crore in FY17. Accordingly, the net loss increased during the year to Rs.463.51 crore vis-à-vis Rs.154.87 crore in FY17.

However, the losses reduced in H1FY19 and the company reported net loss of Rs.159.65 crore on total income of Rs.1914.73 crore vis-à-vis net loss of Rs.262.18 crore on total income of Rs.1756.47 crore in H1FY18. The operating profitability improved in H1FY19 due to lower losses in tyre division with various measures taken by the company to increase efficiency.

Weak capital structure and debt coverage indicators

The company adopted IND-AS from April 1, 2017 and the networth stood at Rs.845.87 crore as on March 31, 2017 vis-à-vis Rs.193.29 crore as on March 31, 2017 (under previous IGAAP). The increase in networth was primarily due to fair valuation gain on fixed assets. However, despite equity infusion of Rs.312 during FY18, the networth decreased to Rs.773.59 crore as on March 31, 2018 due to net loss of Rs.463.51 crore during the year. The total debt increased from Rs.3,637.70 crore as on March 31, 2017 to Rs.3,895.81 crore as on March 31, 2018. Consequently, the overall gearing increased from 4.30x as on March 31, 2017 to 5.04x as on March 31, 2018. The debt coverage indicators remained weak and the company met its obligations timely through infusion of funds by the promoters.

However, the total debt reduced to Rs.3,413.43 crore as on September 30, 2018 with significant reduction in working capital borrowings.

Losses in tyre division

In the tyre segment, KIL's aggregate installed capacity is around 21.65 lakh tyres per annum. Its product portfolio consists of mainly Truck/Bus Tyre, 2/3 wheelers tyres, Light commercial vehicle tyres. Replacement market accounts for around 65% of the total sales of tyre division. KIL sells tyres (under the brand name of Birla tyres).

The operating loss of tyre division increased to Rs.90 crore in FY18 as against loss of Rs.40 crore in FY17. The performance of the division was impacted during H1FY18 due to high natural rubber prices and low capacity utilisation due to import of Chinese tyres and destocking by dealers prior to implementation of GST. The profitability of division improved during H2FY18 with decline in natural rubber prices and imposition of Anti-Dumping Duty on import of Chinese Tyres. However, the performance of the tyre division remains impacted due to sale of low margin Truck & Bus bias tyres and stiff completion from the established players in the industry.

The Company is setting up a Passenger Car Radial tyre Unit of 80 MT per day at Balasore unit for which it has already incurred around Rs.740 crore.

Risk of volatility in raw material prices

KIL sources majority of natural rubber from the open market which has witnessed volatility in the recent past. Consequently, the performance of KIL depends upon the ability to procure natural rubber at competitive prices. Further, there has been significant volatility in prices of other raw materials such as synthetic rubber, carbon black.

Cyclical nature of cement industry

Cement industry is highly cyclical in nature and depends largely on the economic growth of the country. There is a high degree of correlation between the GDP growth and the growth in cement consumption. Cement being a cyclical industry goes through phases of ups and downs, and accordingly impacts the unit realisations.

Liquidity

The liquidity position of the company has been impacted on account of continuous losses. The company has timely met all its obligations through support extended by the promoters. Rs.312 crore of equity was infused in FY18 and in H1FY19 also advances of Rs.150 crore have been received from the group. The company has liquidity cushion in the form of undrawn lines of credit of about Rs.70 crore as on Dec.1, 2018. Additionally it has receivables of about Rs.140 crore from a vendor which is likely to be received by March 31, 2019.

Analytical approach: Standalone

Applicable Criteria
[CARE's Policy on Default Recognition]
[Criteria for Short Term Instruments]
[Criteria on assigning Outlook to Credit Ratings]
[Financial ratios – Non-Financial Sector]
[Rating Methodology-Manufacturing Companies]
[Rating Methodology - Cement Industry]

About the Company
KIL, the flagship company of the B. K. Birla group, is a diversified conglomerate engaged in manufacturing of tyres & tubes and cement. The primary products are tyre (majorly into Truck & Bus Segment- T& B) and cement, which accounted for 39% and 61% respectively of gross turnover in FY18. KIL's cement manufacturing units have an aggregate capacity of 7.25 million tonnes per annum (MTPA) and are located in Karnataka & Andhra Pradesh. The tyre manufacturing facility of the company is located at Balasore, Orissa, having an installed capacity to produce 21.65 lakh tyres per annum.

Brief Financials (Rs. Crore)	FY17 (A)	FY18 (A)
Total operating income	3,715.03	3,606.87
PBILDT	68.52	-53.53
PAT	-154.87	-463.51
Interest coverage (times)	4.30	5.04
Overall Gearing	0.24	NM

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure-2

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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Annexure-1: Details of Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Non-fund-based - ST-BG/LC	-	-	-	575.00	CARE A3+ (Under Credit watch with Developing Implications)
Fund-based - LT/ ST-CC/Packing Credit	-	-	-	906.00	CARE BBB / CARE A3+ (Under Credit watch with Developing Implications)
Fund-based - ST-Term loan	-	-	March'19	130.00	CARE A3+ (Under Credit watch with Developing Implications)

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Commercial Paper	ST	-	-	-	-	-	1)Withdrawn (03-Apr-15)
2.	Term Loan-Long Term	LT	-	-	-	-	1)Withdrawn (08-Jun-16)	1)CARE A- (Under Credit Watch) (11-Jan-16) 2)CARE A- (Under Credit Watch) (01-Oct-15) 3)CARE A- (Under Credit Watch) (03-Apr-15)
3.	Non-fund-based - ST-BG/LC	ST	575.00	CARE A3+ (Under Credit watch with Developing Implications)	1)CARE A3+ (Under Credit watch with Developing Implications) (22-May-18)	1)CARE A2+ (Under Credit watch with Negative Implications) (20-Feb-18) 2)CARE A2+ (Under Credit	1)CARE A1 (14-Oct-16) 2)CARE A1 (08-Jun-16)	1)CARE A2+ (Under Credit Watch) (11-Jan-16) 2)CARE A2+ (Under Credit Watch) (01-Oct-15)

						watch with Negative Implications) (25-Jan-18) 3)CARE A2+ (Under Credit watch with Negative Implications) (21-Nov-17) 4)CARE A2+ (25-Sep-17) 5)CARE A1 (12-Jul-17)		3)CARE A2+ (Under Credit Watch) (03-Apr-15)
4.	Fund-based - LT/ ST-CC/Packing Credit	LT/ST	906.00	CARE BBB / CARE A3+ (Under Credit watch with Developing Implications)	1)CARE BBB / CARE A3+ (Under Credit watch with Developing Implications) (22-May-18)	1)CARE A- / CARE A2+ (Under Credit watch with Negative Implications) (20-Feb-18) 2)CARE A- / CARE A2+ (Under Credit watch with Negative Implications) (25-Jan-18) 3)CARE A- / CARE A2+ (Under Credit watch with Negative Implications) (21-Nov-17) 4)CARE A-; Negative / CARE A2+ (25-Sep-17) 5)CARE A; Negative / CARE A1 (12-Jul-17)	1)CARE A / CARE A1 (14-Oct-16) 2)CARE A / CARE A1 (08-Jun-16)	1)CARE A- / CARE A2+ (Under Credit Watch) (11-Jan-16) 2)CARE A- / CARE A2+ (Under Credit Watch) (01-Oct-15) 3)CARE A- / CARE A2+ (Under Credit Watch) (03-Apr-15)
5.	Commercial Paper-Commercial Paper (Carved out)	ST	-	-	-	-	-	1)Withdrawn (03-Apr-15)
6.	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (03-Apr-15)
7.	Preference Shares-Convertible Prefrence Shares	LT	-	-	-	1)Withdrawn (12-Jul-17)	1)CARE BBB+ (RPS) (14-Oct-16) 2)CARE BBB+ (RPS) (08-Jun-16) 3)CARE BBB+ (RPS) (Under	-

							Credit Watch) (12-Apr-16)	
8.	Commercial Paper	ST	-	-	-	-	1)Withdrawn (30-Jun-16) 2)CARE A1 (08-Jun-16)	-
9.	Fund-based - LT-Term Loan	LT	-	-	1)Withdrawn (22-May-18)	1)CARE A- (Under Credit watch with Negative Implications) (20-Feb-18) 2)CARE A- (Under Credit watch with Negative Implications) (25-Jan-18) 3)CARE A- (Under Credit watch with Negative Implications) (21-Nov-17) 4)CARE A-; Negative (25-Sep-17) 5)CARE A; Negative (12-Jul-17)	-	-
10.	Fund-based - ST-Term loan	ST	130.00	CARE A3+ (Under Credit watch with Developing Implications)	1)CARE A3+ (Under Credit watch with Developing Implications) (22-May-18)	-	-	-

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CIN - L67190MH1993PLC071691