February 15, 2024

Happy Forgings Limited: Long-term rating upgraded to [ICRA]AA(Stable); short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term loan	245.00	0.00	-
Long-term/ Short -term – Fund based	240.00	210.00	Long-term rating upgraded to [ICRA]AA(Stable) from [ICRA]AA-(Stable); short-term rating reaffirmed at [ICRA]A1+
Total	**485.00**	**210.00**	

**Instrument details are provided in Annexure-I*

Rationale

Happy Forgings Limited's (HFL) long-term rating upgrade factors in the improvement in its financial risk profile following the equity infusion from the recently concluded Initial Public Offering (IPO). The company raised ~Rs. 400 crore of funds (primary issuance) via the IPO, which have lowered debt levels and would help it fund its growth capex over the near term. The enhanced manufacturing capacity/capabilities are likely to increase the company's scale of operations going forward, and help it further diversify its operational profile. The company has reported a sustained improvement in scale of operations and stability of its profitability indicators over the past few years. ICRA expects the company to continue to record a healthy operating performance over the medium term, aided by healthy order flows and its effort to gain new business from new customers, benefitting from its established relationships and strong share of business (SOB) with reputed tier-I automotive ancillaries and original equipment manufacturers (OEMs).

HFL's revenues grew by ~39% in FY2023 on a YoY basis and reported a revenue of ~Rs. 1,015 crore for 9M FY2024, driven by steady demand for its key end-user segments. Aided by an improving proportion of sales emanating from the relatively profitable machining segment and heavy forged components, the company's operating profitability remained at robust levels (29.2% in 9M FY2024). The company benefits from steady demand trends in the catered automotive segments, with its established relationships and strong SOB with various customers likely to help it record a moderate-to- healthy revenue growth over the medium term. The company has recently gained business from multiple new customers (including some non-automotive ones); a ramp-up in supplies for these customers is expected to help diversify the company's business profile, augment its company's cash accruals and improve its credit profile.

The company continues to maintain a conservative capital structure (gearing of 0.2 times as on March 31, 2023), aided by healthy accretion to reserves and pre-payment of long-term debt post fund raise during the recently concluded IPO. HFL's operating profitability metrics and low debt levels have helped it maintain strong debt coverage indicators (Total Debt/OPBDITA of 0.6 times and NCA/Total Debt of ~123% in FY2023). Despite the ongoing capex programme to enhance capacity/capabilities (capex outlay of ~Rs. 200-250 crore/annum expected over the next 2-3 years), an expectation of healthy operating performance is likely to help limit HFL's dependence on external debt to fund its substantial capex plans, while helping it maintain strong return indicators and debt metrics.

The ratings remain constrained by the susceptibility of HFL's revenue generation to the cyclicality in the CV and agri-machinery segments, as they contribute ~75% to the company's revenues. While dependence on these segments is expected to remain high over the medium term, HFL's established relationships and strong SOB with various customers provides comfort. ICRA also notes that while the new 14,000T press line will help the company cater to relatively new product categories, thereby leading to diversification of its revenue profile, HFL's ability to achieve healthy capacity utilisation levels for the enhanced capacity would remain monitorable.

The Stable outlook on the rating reflects ICRA's expectations that the entity's capex plans to further expand its capacity will be funded in a manner, that it is able to durably maintain its debt protection metrics commensurate with the existing rating level.

Key rating drivers and their description

Credit strengths

Established relationships with tier-I component manufacturers and OEMs – HFL is a Ludhiana-based manufacturer of forged and machined components, which are primarily supplied to the CV and tractor segments of the automotive industry. The promoters have over four decades of experience in the forging industry. The company enjoys established relationships and a strong SOB with reputed OEMs such as Ashok Leyland Limited, JCB India Limited, VE Commercial Vehicles Limited, and Escorts Limited as well as reputed tier-I automotive ancillaries, such as Graziano Transmission India Private Limited. The established relationships provide healthy revenue visibility for the company. The company has recently gained business from multiple new customers like Tata Motors Limited, Mahindra and Mahindra Limited, American Axle & Manufacturing (AAM India), Bonfiglioli etc., further strengthening its operational profile and revenue growth prospects.

Strong operating profitability and return indicators – HFL's operating margin continued to be strong at ~29% in 9M FY2024 and 28.9% in FY2023, aided by healthy realisations, cost-efficiency measures and a timely ramp-up in capacity utilisation of the press lines and machining facilities. The profitability has also remained supported by supplies for heavier components post the commercialisation of 8,000T and 14,000T press lines. The average realisations for the company's sales in FY2023 increased because of a combination of factors i.e., higher contribution from machining products & export sales (both commanding higher realisations) along with increase in steel prices.

Healthy financial risk profile, aided by infusion of funds via IPO – Happy Forgings Limited concluded its Initial Public Offering (IPO) and got its shares listed on the stock exchanges on December 27, 2023. The IPO primary issue size was ~Rs. 400 crore (additionally there was an OFS of Rs. 608.6 crore) and a part of the proceeds from that IPO has been used to payout the long term and short-term debt ~Rs. 153 crore, as was stated in the objects of the offer. The same will help improve the debt and coverage metrices of the company in the future. Apart from that, the remaining funds (~Rs. 220 crore post issue expenses) are expected to be used for funding the company's capital expansion, to enhance forging capacity to expand the product and client portfolios. The company's strong operating profitability metrics, coupled with moderate debt levels (no term debt as on December 31, 2023), have helped the company report robust debt coverage indicators, with Total Debt/OPBDITA of 0.7 times and NCA/Total Debt of 107.5% in H1 FY2024. The debt coverage indicators are expected to remain at healthy levels going forward, aided by an expectation of strong cash accruals and consequent decline in debt levels.

Credit challenges

Key end-user segments remain exposed to cyclicality – HFL is primarily a supplier of forged and machined components to the CV and tractor segments of the automotive industry. Together, these two segments constitute ~75% of its total revenues. Both these industries are inherently cyclical in nature, with the demand for CVs being impacted by industrial, agricultural production and freight dynamics, while tractor demand remains closely linked to monsoon performance and agricultural income. Despite the management's focus on expanding its customer and product portfolios (across other segments), the company's dependence on these segments is expected to remain high over the medium term. HFL's established relationships and strong SOB with various customers, however, provide comfort.

Ongoing capacity expansion plans and foray into relatively new product categories – The company has recently concluded its capex programme, wherein the company has increased its forging and machining capacities to ~1,20,000 TPA and 51,000 TPA levels, respectively, as on December 31, 2023. The company recently commissioned a 14,000T mechanical forge press line for heavy precision forging and has established its position as one of the key players in forging heavy components. At present, it is only the second company in India to have a 14,000T or higher forging press and is among the four companies in India that possess an 8,000T or higher presses. The new press line is expected to help the company cater to relatively new product categories, thereby leading to diversification of its revenue profile. The company has plans to further enhance its manufacturing capabilities/capacity, with capex outlay of ~Rs. 200-250 crore/annum planned over the next 2-3 years. While a predominant share of its capex is likely to be funded through internal accruals and IPO proceeds, timely completion of the same and HFL's ability to achieve healthy capacity utilisation levels for the enhanced capacity would remain key rating sensitivities.

Liquidity position: Adequate

HFL's liquidity position remains adequate, supported by healthy cash and liquid investments (~Rs. 250 crore as on December 31, 2023), moderate utilisation of the working capital facilities (average buffer of ~Rs. 55- 60 crore over the last 12 months) and expectation of strong cash accruals (~Rs. 200-250 crore per annum). The entity repaid around Rs. 153 crore of debt from its total debt of Rs. 259 crore as on September 30, 2023 and the entity has no term loans outstanding as on December 31, 2023. The entity is expected to maintain more than sufficient liquidity to meet its ongoing capex programme (~Rs. 200-250 crore/annum) for enhancing its forging and machining capabilities.

Rating sensitivities

Positive factors – A material revenue diversification with sustained scale-up in supplies to the export market, coupled with substantial improvement in scale of operations while maintaining healthy credit metrics, would be favourably considered for an upgrade.

Negative factors – ICRA could downgrade HFL's ratings if a weakness in demand in the segments catered and a consequent inability to achieve healthy capacity utilisation post-capacity expansion, materially impacts the company's return and debt coverage indicators. A specific credit metric that could trigger a downgrade is if Total debt/OPBDITA is greater than 1.0 times, on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Auto Components
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of HFL. As on March 31, 2023, the company had one subsidiary, from which HFL exited on March 31, 2023, which is enlisted in Annexure-II.

About the company

Happy Forgings Limited (HFL), incorporated in 1979, manufactures forged and machined transmission along with engine components that are supplied mainly to the automotive sector. Its product range includes automotive crankshafts, steering knuckles, transmission gears, pinions, shafts, and forged/machined components for the Indian Railways. It has a total forging capacity of 1,20,000 MT (hammer and press forging combined) and a machining capacity of 51,000 MT. The company supplies to leading OEMs in India directly and through tier-1 component suppliers as well.

HFL was incorporated in 1979 by Mr. Paritosh Kumar Garg as a private limited company, which was converted into a public limited company in 1988. The company has about four decades of experience in catering to the automotive, tractor, railway, earth moving and pipe fitting industries. Its day-to-day operations are overseen by Mr. Ashish Garg (Managing Director, son of Mr. Paritosh K. Garg), who has been instrumental in enhancing HFL's share of business with various OEMs. MOPE Investment Advisors Private Limited, a private equity player, invested Rs. 200.0 crore as equity in HFL in FY2019 (shareholding held under

Vistra ITCL (India) Limited), acquiring a stake of 11.76% in the process. The company subsequently came out with an initial public offer in December 2023.

Key financial indicators (audited)

HFL Standalone	FY2022	FY2023	H1 FY2024*	9M FY2024*
Operating income	860.0	1,196.8	672.9	1,014.9
PAT	142.3	208.7	119.3	177.2
OPBDIT/OI	26.8%	28.9%	29.0%	29.2%
PAT/OI	16.5%	17.4%	17.7%	17.5%
Total outside liabilities/Tangible net worth (times)	0.4	0.3	0.4	-
Total debt/OPBDIT (times)	1.0	0.6	0.7	-
Interest coverage (times)	32.3	27.7	27.4	-

*Source: Company, ICRA Research; * Limited audit; All ratios as per ICRA's calculations; Amounts in Rs. crore*

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years				
		Type	Amount rated (Rs. crore)	Amount outstanding as of Dec 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022	Date & rating in FY2021	
					Feb 15, 2024	Dec 21, 2022	May 20, 2022	-	Feb 26, 2021	August 18, 2020 May 11, 2020
1	**Term loans**	Long-term	0.00	0.00	-	**[ICRA]AA- (Stable)**	**[ICRA]A+ (Positive)**	-	**[ICRA]A+ (Stable)**	**[ICRA]A (Stable)**
2	**Long-term/ Short -term – Fund based**	Long-term and short-term	210.00	--	**[ICRA]AA (Stable)/ [ICRA]A1+**	**[ICRA]AA- (Stable)/ [ICRA]A1+**	-	-	-	-
3	**Fund Based Limits**	Long-term	0.00	--	-	-	**[ICRA]A+ (Positive)**	-	**[ICRA]A+ (Stable)**	**[ICRA]A (Stable)**
4	**Unallocated Limits**	Long-term and short-term	0.00	--	-	-	**[ICRA]A+ (Positive)/ [ICRA]A1**	-	**[ICRA]A+ (Stable)/ [ICRA]A1**	**[ICRA]A (Stable)/ [ICRA]A1**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/ Short -term – Fund-based	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Fund Based Limits**	NA	NA	NA	210.00	[ICRA]AA (Stable)/[ICRA]A1+

Source: Company

[*Please click here to view details of lender-wise facilities rated by ICRA*]

Annexure II: List of entities considered for consolidated analysis

Company Name	LTHL Ownership	Consolidation Approach
Happy Forgings Limited	100.00% (rated entity)	Full Consolidation
Linchpin Technologies Private Limited	100.00%	Full Consolidation

Source: HFL annual report FY2023; Note: During the year ended 31st March 2022, the Company entered into a Joint Venture agreement with 'VVDN Technologies Private Limited' and acquired Linchpin Technologies Private Limited. On 31st March 2023, these shares are sold to VVDN Technologies Private Limited

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About ICRA Limited:

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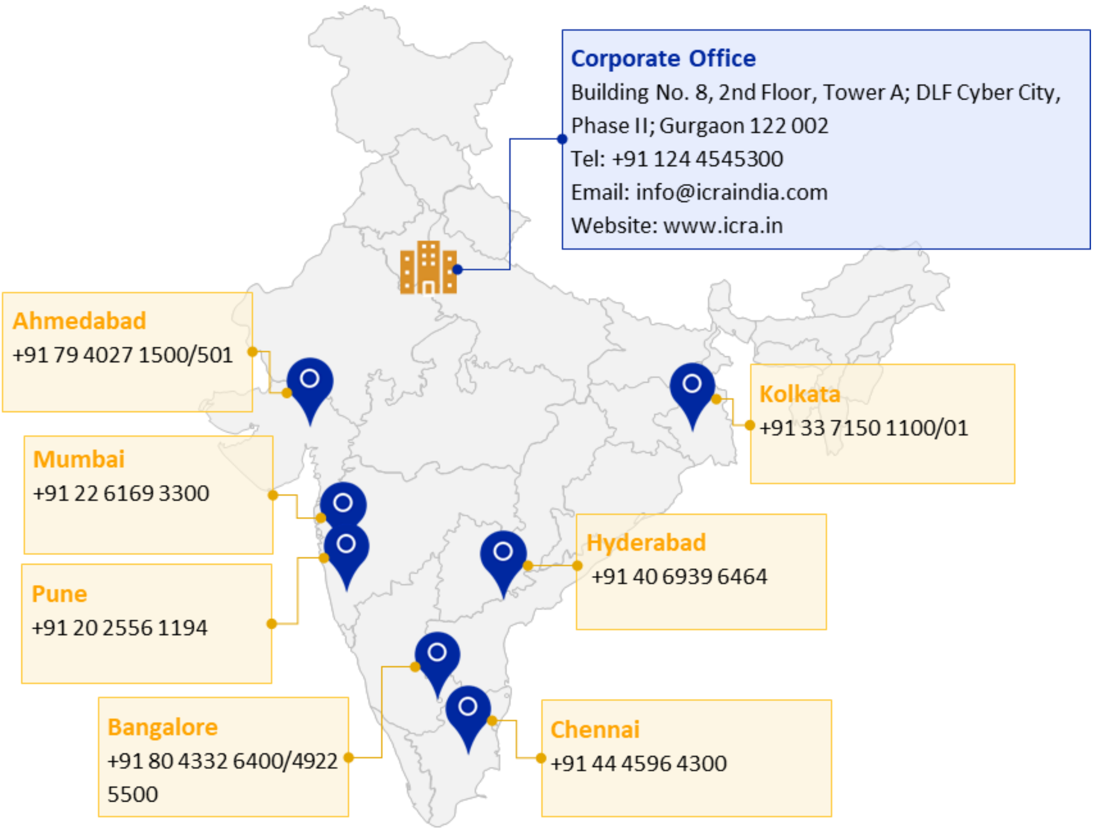

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