

Press Release

Diffusion Engineers Limited

July 29, 2022



Rating Assigned and Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	0.50	ACUITE A- Stable Assigned	-
Bank Loan Ratings	12.50	-	ACUITE A2+ Reaffirmed
Bank Loan Ratings	47.50	ACUITE A- Stable Reaffirmed	-
Bank Loan Ratings	5.00	-	ACUITE A2+ Assigned
Total Outstanding Quantum (Rs. Cr)	65.50	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

Rating Rationale

Acuite has reaffirmed the long-term rating of '**ACUITE A-**' (read as **ACUITE A minus**) and short-term rating at '**ACUITE A2+**' (read as **ACUITE A two plus**) on the Rs.60.00 crore bank facilities of Diffusion Engineers Limited. (DEL). The outlook is '**Stable.**'

Acuite has assigned the long-term rating of '**ACUITE A-**' (read as **ACUITE A minus**) and short-term rating of '**ACUITE A2+**' (read as **ACUITE A two plus**) on the Rs.5.50 crore bank facilities of Diffusion Engineers Limited. (DEL). The outlook is '**Stable.**'

About the Company

Established in 1982, DEL is engaged in welding maintenance and repair solution services for industries like cement, power and steel, among others. The Nagpur-based company manufactures welding consumables like electrodes, flux cored wire, etc. and also offers solutions for reconditioning/repair. The company was promoted by Mr. N. K. Garg. However, after his demise in 2020, Mr. Prashant Garg was appointed as a managing director.

Analytical Approach

Acuite has considered the standalone financial and business risk profiles of DEL to arrive at the rating.

Key Rating Drivers

Strengths

Long track record of operations supported by experienced management

DEL has been in the business of welding consumables since past more than 3 decades.

Besides manufacturing welding consumables like electrodes, flux cored wires, etc., the company also offers solutions for reconditioning/repair of critical equipment used in manufacturing plants of cement, power and steel, among others. Mr. N. K. Garg, promoter of the company, was a managing director of the company. However, after his demise in 2020, Mr. Prashant Garg was appointed as a managing director. Mr. N. K. Garg was having around 4 decades of industry experience, which has enabled DEL not only to maintain good relation with customers and suppliers, but also to diversify the product/service offerings. In addition to welding consumables, DEL also manufactures wear plates and some heavy machineries like plasma cutting machines, etc. The current managing director, Mr. Prashant, has around 14 years of experience and has shown his strong capability by developing a state-of-the-art production facility for DEL to manufacture sophisticated cement, power and steel plant equipment. Acuite believes that DEL's established track record and experienced management would continue to support its growth going ahead.

Healthy financial risk profile

The financial risk profile of the company is healthy marked by strong net worth, comfortable gearing and strong coverage indicators. Total tangible net worth of the company stood at Rs. 116.96 Cr as on 31st March 2022 as against Rs. 104.69 Cr in the previous year. Debt to Equity ratio stood comfortable at 0.21 times in FY 2022 as against 0.18 times in FY 2021. Total debt of Rs. 24.11 Cr consists of Rs. 3.32 Cr of long-term debt, Rs. 19.13 Cr of working capital borrowings and Rs. 1.67 Cr of CPLTD. Interest coverage Ratio remained strong at 18.59 times in FY 2022 as against 10.97 times in FY 2021 while DSCR has improved to 4.27 times in FY 2022 as against 2.96 times in FY 2021. NCA/TD improved from 0.38 times in FY 2020 to 0.74 times in FY 2021 and stood at 0.73 times in FY 2022. Going forward the team believes that the financial risk profile will remain strong in the coming times.

Improving business scale along with sustainable operating margin

The company has achieved revenue of Rs. 196.79 Cr in FY 2022 (Provisional) while in FY 2021 (Audited), the company has earned revenue of Rs. 153.12 Cr as against Rs. 147.04 Cr in FY 2020. Despite the disruptions created by covid pandemic, the company was able to sustain growth in revenue on the back of strong order book position. In the current year the order book position stands at Rs. 81.43 Cr.

Company's EBITDA margin has jumped to 12.99 % in FY 2021 (Audited) as against 11.46 % in FY 2020 and moderated to 11.88 % in FY 2022 (Provisional). PAT margin has increased year on year from 6.16% in FY 2020 to 6.83% in FY 2021 (Audited) and further increased to 6.97% in FY 2022 (Provisional). EBITDA margin has declined in FY 2022 because of sharp increase in raw material cost because of the ongoing Russia-Ukraine Crisis. Major raw material for the company includes steel which amount to around 65-70% of total raw material cost while other raw materials include tungsten, nickel, ferro manganese etc. the prices of which have increased drastically in the current year. PAT margin has seen improvement because of low interest cost.

Weaknesses

Moderately intensive working capital operations, albeit improving

The company's operations are working capital intensive marked by GCA days of 181 in FY 2022. GCA days have moderated in FY 2022 which in FY 2021 stood at 183 days. Inventory holding period has declined from 125 days in FY 2020 to 74 days in FY 2021 and increased to 87 days in FY 2022. Inventory period dipped in FY 2021 due to better sales in other segments but the major reason behind high inventory days is the manufacturing of heavy engineering products which have high lead time hence in the coming times the team expects the inventory holding period to remain at the same level. The debtor realization period has fluctuated from 91 days in FY 2020 to 100 days in FY 2021 and then stood at 90 days in FY 2022. Creditor days have gone up from 74 days in FY 2021 to 84 days in FY 2022. The company has credit terms of around 60-90 days with different suppliers while some customers like Jindal and Tata Steels do not give credit period and in this scenario the payment is either LC backed or the company pays these suppliers on advance.

Susceptibility to fluctuation in raw material prices

DEL's profitability is susceptible to fluctuations in prices of key raw material, i.e. steel (~65-70

per cent of total raw material cost). DEL's inability to pass on sudden rise in steel prices to its consumers could impact the company's overall operating performance.

Rating Sensitivities

- Inability to sustain operating margin
- Elongation of working capital cycle

Material covenants

None.

Liquidity Position

Strong

Company's liquidity is strong marked by its net cash accruals vs its maturing debt obligations. The company has generated cash accrual of Rs. 17.56 Cr in FY 2022 against CPLTD of Rs. 1.67 Cr in the same period. Going forward the company is expected to generate net cash accruals of Rs. 20.55 Cr and Rs. 23.47 Cr against CPLTD of Rs. 1.67 Cr and Rs. 3.60 Cr in each respective years. The cash and bank position for FY 2022 stood at Rs. 2.49 Cr while current ratio for the period stood at 1.69 times.

Outlook: Stable

Acuité believes that DEL would maintain 'Stable' outlook on the back of established presence in the welding consumables segment and experienced management and improving scale of business while maintaining healthy operating margin. The outlook may be revised to 'Positive' in case the company reports higher than expected growth in revenue and improvement in profitability. Conversely, the outlook may be revised to 'Negative' in case of lower-than-expected revenue and inability to sustain operating margin, thereby hurting operating performance and resulting in deterioration in financial risk profile.

Key Financials

Particulars	Unit	FY 22 (Provisional)	FY 21 (Actual)
Operating Income	Rs. Cr.	196.79	153.12
PAT	Rs. Cr.	13.72	10.46
PAT Margin	(%)	6.97	6.83
Total Debt/Tangible Net Worth	Times	0.21	0.18
PBDIT/Interest	Times	18.59	10.97

Status of non-cooperation with previous CRA (if applicable)

Not Applicable.

Any other information

None.

Applicable Criteria

- Default Recognition - <https://www.acuite.in/view-rating-criteria-52.htm>
- Entities In Manufacturing Sector - <https://www.acuite.in/view-rating-criteria-59.htm>
- Application Of Financial Ratios And Adjustments: <https://www.acuite.in/view-rating-criteria-53.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/view-rating-criteria-55.htm>

Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
	Proposed Bank Facility	Long Term	14.54	ACUITE A- Stable (Assigned)
	Bank Guarantee	Short Term	2.50	ACUITE A2+ (Assigned)

10 May 2021	Term Loan	Long Term	4.91	ACUITE A- Stable (Assigned)
	Cash Credit	Long Term	5.00	ACUITE A- Stable (Assigned)
	Bank Guarantee	Short Term	10.00	ACUITE A2+ (Assigned)
	Term Loan	Long Term	3.05	ACUITE A- Stable (Assigned)
	Cash Credit	Long Term	20.00	ACUITE A- Stable (Assigned)

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Quantum (Rs. Cr.)	Rating
HDFC Bank Ltd	Not Applicable	Bank Guarantee (BLR)	Not Applicable	Not Applicable	Not Applicable	10.00	ACUITE A2+ Reaffirmed
Yes Bank Ltd	Not Applicable	Bank Guarantee (BLR)	Not Applicable	Not Applicable	Not Applicable	2.50	ACUITE A2+ Reaffirmed
DBS Bank Ltd	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	14.50	ACUITE A- Stable Reaffirmed
HDFC Bank Ltd	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	20.00	ACUITE A- Stable Reaffirmed
Yes Bank Ltd	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	5.00	ACUITE A- Stable Reaffirmed
DBS Bank Ltd	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	0.50	ACUITE A- Stable Assigned
HDFC Bank Ltd	Not Applicable	Letter of Credit	Not Applicable	Not Applicable	Not Applicable	5.00	ACUITE A2+ Assigned
Not Applicable	Not Applicable	Proposed Long Term Bank Facility	Not Applicable	Not Applicable	Not Applicable	0.04	ACUITE A- Stable Reaffirmed
HDFC Bank Ltd	Not Applicable	Term Loan	29-11-2019	7.75	29-03-2024	4.91	ACUITE A- Stable Reaffirmed
HDFC Bank Ltd	Not Applicable	Term Loan	29-02-2020	7.75	29-11-2024	3.05	ACUITE A- Stable Reaffirmed

Contacts

Analytical	Rating Desk
Aditya Gupta Vice President-Rating Operations Tel: 022-49294041 aditya.gupta@acuite.in Shreyansh Singh Analyst-Rating Operations Tel: 022-49294065 shreyansh.singh@acuite.in	Varsha Bist Senior Manager-Rating Operations Tel: 022-49294011 rating.desk@acuite.in

About Acuité Ratings & Research

Acuité is a full-service Credit Rating Agency registered with the Securities & Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI) for Bank Loan Ratings under BASEL-II norms in the year 2012. Acuité has assigned ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.

Disclaimer: An Acuité rating does not constitute an audit of the rated entity and should not be treated as a recommendation or opinion that is intended to substitute for a financial adviser's or investor's independent assessment of whether to buy, sell or hold any security. Ratings assigned by Acuité are based on the data and information provided by the issuer and obtained from other reliable sources. Although reasonable care has been taken to ensure that the data and information is true, Acuité, in particular, makes no representation or warranty, expressed or implied with respect to the adequacy, accuracy or completeness of the information relied upon. Acuité is not responsible for any errors or omissions and especially states that it has no financial liability whatsoever for any direct, indirect or consequential loss of any kind, arising from the use of its ratings. Ratings assigned by Acuité are subject to a process of surveillance which may lead to a revision in ratings as and when the circumstances so warrant. Please visit our website (www.acuite.in) for the latest information on any instrument rated by Acuité.