March 05, 2014

RATIONALE-CUM-BRIEF RATIONALE

CARE REVISES THE RATINGS ASSIGNED TO VARIOUS DEB FACILITIES/INSTRUMENTS OF BHUSHAN STEEL LTD

<table>
<thead>
<tr>
<th>Facilities/Instruments</th>
<th>Amount (Rs. crore)</th>
<th>Ratings</th>
<th>Remarks</th>
</tr>
</thead>
<tbody>
<tr>
<td><strong>Instruments</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Non-Convertible Debenture (NCD) Programme-I</td>
<td>1,500</td>
<td>CARE BB [Double B]</td>
<td>Revised from CARE A [Single A]</td>
</tr>
<tr>
<td>Non-Convertible Debenture (NCD) Programme-II</td>
<td>800</td>
<td>CARE BB [Double B]</td>
<td>Revised from CARE A [Single A]</td>
</tr>
<tr>
<td>Cumulative Redeemable Preference Shares-I (CRPS-I)</td>
<td>88.50</td>
<td>CARE BB [Double B]</td>
<td>Revised from CARE A- [Single A Minus]</td>
</tr>
<tr>
<td>Cumulative Redeemable Preference Shares-II (CRPS-II)</td>
<td>100</td>
<td>CARE BB/CARE A4 [Double B/A Four]</td>
<td>Revised from CARE A-/CARE A2+ [Single A Minus/A Two Plus]</td>
</tr>
<tr>
<td>Commercial Paper/Short-term Debt Programme*</td>
<td>1,300</td>
<td>CARE A4 [A Four]</td>
<td>Revised from CARE A1 [A One]</td>
</tr>
<tr>
<td>Pass Through Certificates (PTCs)^</td>
<td>100</td>
<td>CARE A4 (SO) [A Four (Structured Obligation)]</td>
<td>Revised from CARE A2+ (SO) [A Two Plus (Structured Obligation)]</td>
</tr>
<tr>
<td><strong>Bank facilities</strong></td>
<td></td>
<td></td>
<td></td>
</tr>
<tr>
<td>Long-term Bank Facilities</td>
<td>29,676.02</td>
<td>CARE BB [Double B]</td>
<td>Revised from CARE A [Single A]</td>
</tr>
<tr>
<td>Short-term Bank Facilities (Short-term Loans)</td>
<td>1,000</td>
<td>CARE A4 [A Four]</td>
<td>Revised from CARE A2+ [A Two Plus]</td>
</tr>
<tr>
<td>Subordinate Debt</td>
<td>100</td>
<td>CARE BB [Double B]</td>
<td>Revised from CARE A- [Single A Minus]</td>
</tr>
<tr>
<td><strong>Total Bank Facilities</strong></td>
<td>35,960.02</td>
<td></td>
<td></td>
</tr>
</tbody>
</table>

*Careved out of fund based working capital limits

^based on credit enhancement in the form of put option provided by BSL for timely payment of PTCs issued by ‘BSL CRPS Mar 2011’ Trust backed by CRPS-II issued by BSL.

**Rating Rationale**

The revision in the ratings takes into account the deterioration in the company’s credit risk profile characterized by decline in its profitability and cash accruals during 9MFY14 (refers to the period April 1 to December 31) aggravated by delay in ramping-up of operations of Orissa phase-III expansion project. The revision in ratings also factor in the weakening of BSL’s liquidity profile in view of the lower than envisaged cash accruals and committed debt repayment obligations.

The ratings are constrained by BSL’s leveraged credit profile attributable to the large debt-funded expansion projects undertaken by the company, the residual risks associated with the projects under execution and effective ramping-up of operations and cyclicality inherent in the steel

1Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.
industry. The ratings take note of the company’s long track record in the steel industry and its healthy operating margins over the years. The ratings also consider BSL’s diversified customer base, the company’s dominant position in the domestic market and its diversified product portfolio with a strong export presence in GP/GC sheets and other value-added products. Going forward, the company’s ability to improve its liquidity and leverage profile, timely and effective ramping-up of the operations of Orissa phase-III and the completion of various projects under execution within the time and cost estimates would be the key rating sensitivities.

Background
Bhushan Steel Ltd (formerly known as Bhushan Steel & Strips Ltd), incorporated in 1993, is one of the large players in the steel industry with a steel making capacity of 4.7 Million Tonnes Per Annum (MTPA) (including Phase-III expansion of 2.5 MTPA). The company has HR steel capacity of 4.4 MTPA, billet manufacturing capacity of 0.3 MTPA and captive power generation capacity of 158 MW (including 110 MW waste heat recovery based capacity in Orissa). The company’s manufacturing facilities are situated in Sahibabad (UP), Khopoli (Maharashtra) and Dhenkanal (Orissa). The company supplies a variety of finished products such as hot rolled coil/sheet, cold rolled coil/sheet, galvanised coil/sheet, high tensile steel strapping, colour coated coil/sheet, galume coils/sheets, hardened & tempered steel strips, precision tubes etc. Its products primarily cater to the demand of automobiles and consumer durable industries.

Credit risk assessment
Significant delay in ramping-up of Orissa Phase-III operations
The company had completed its Orissa phase III project in March 2013 resulting in expansion in HR capacity to 4.4 Million Tonnes Per Annum from 1.9 MTPA. However, in November 2013, there was an explosion near the Blast Furnace No 2 (part of Phase-III expansion) after which phase III operations were stalled as per the direction of State Pollution Control Board (SPCB). The said incident led to loss of production thereby impacting the aggregate sales volumes. BSL took-up the matter with SPCB and the company received “Consent to Operate” from SPCB in January 2014 to restart the Phase III operations. The inordinate delay in ramping-up of the operations of Orissa phase-III has adversely impacting BSL’s revenue, profitability and cash flows. Furthermore, there have been reported cost overruns on Phase III project with the company spending an amount of Rs.7,515 crore (including exchange fluctuation of Rs.777 crore) on the project upto December 31, 2013 as against the estimated project cost of Rs.6,583 crore.

Subdued financial performance with net losses during Q3FY14
BSL has reported dismal financial performance during Q3FY14 and 9MFY14 with a sharp decline in total income, operating margins and losses at the net level during Q3FY14. BSL’s operating margins declined 592 bps during Q3FY14 was largely on account of higher costs and lower sales volumes due to delay in ramping-up of Orissa phase III operations. The lower operational profitability coupled with higher interest cost resulted in net losses during Q3FY14 and decline in net profit during 9MFY14. The company’s total operating income and PBILDT declined by 9.58% and 14.85% during 9MFY14 on y-o-y basis whereas its PAT declined by 87.03%. During 9MFY14, the company reported a PBILDT and net loss of Rs.2,038 crore and Rs.82 crore, respectively on a total operating income of Rs.7,166 crore as against a PBILDT and PAT of Rs.2,393 crore and Rs.629 crore, respectively, on a total operating income of Rs.7,925 crore during 9MFY13. The dip in operating performance along-with with high financial leverage (BSL’s overall gearing (excluding acceptances) at 3.33x as on December 31, 2013 as compared with 2.75x as on March 31, 2013) and higher commitments related to the ongoing capex and debt repayments has impacted the liquidity position of the company. Going forward, the ability of BSL to deleverage its balance sheet and improve its liquidity profile would be important to its prospects.
Brief Rationale

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