Kamdar and Associates
December 02, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term / Short Term Bank Facilities	65.00	CARE BBB-; Stable / CARE A3 (Triple B Minus ; Outlook: Stable/ A Three)	Reaffirmed
Short Term Bank Facilities	1.30	CARE A3 (A Three)	Reaffirmed
Total Bank Facilities	**66.30 (₹ Sixty-Six Crore and Thirty Lakhs Only)**		

Details of instruments/facilities in Annexure-1.

Detailed rationale and key rating drivers

For arriving at the ratings of Kamdar and Associates (KA), CARE has considered the combined business and financial profiles of three entities, namely, Kamdar and Associates, Panchvati Ship Breakers (PSB; rated 'CARE BBB-; Stable/CARE A3') and Sagar Laxmi Ship Breakers (SLSB; rated 'CARE BBB-; Stable/CARE A3'), collectively known as Kamdar Group (KAG) as they operate in same line of business i.e. ship breaking and are jointly managed by a common set of promoters.

The ratings of KAG continue to derive strength from the extensive experience of the partners in ship-breaking industry, presence of KAG's ship-breaking yards at Alang which is India's largest ship-breaking cluster, certifications regarding environmental and worker safety for its yards, and adequate liquidity. The ratings also factor in its moderate but fluctuating scale of operations and profitability which declined during FY22 (FY refers to the period from April 1 to March 31) over FY21.

The ratings, however, continue to remain constrained on account of moderate capital structure and constitution as partnership firm. The ratings further constrained on account of exposure to adverse movement in steel prices and forex rates, cyclicality industry as well as exposure to regulatory and environmental hazards risk.

Rating sensitivities

Positive factors – Factors that could lead to positive rating action/upgrade:

- Growth in scale of operations along with improvement in PBILDT margin to more than 5% on a sustained basis
- Increase in net worth base leading to overall gearing (based on net debt) below 1.50x on a sustained basis during periods where ship breaking activity is being undertaken
- Improvement in LC coverage ratio above 1.40x on a sustained basis [LC (letter of credit) coverage is defined as the ratio of an entity's outstanding inventory and fixed deposits (including margin money) to its outstanding fund based and non-fund based bank borrowings]

Negative factors – Factors that could lead to negative rating action/downgrade:

- Deterioration in LC coverage ratio below 1.15x on a sustained basis (considering the stipulation of 15% margin by the lender for LCs of KAG)
- Operating loss leading to sizeable erosion of net-worth and reducing the cover for the maturing LCs
- Extension of sizeable loans and advances to external entities engaged in unrelated business activities

Detailed description of the key rating drivers

<u>Key rating strengths</u>

Experienced promoter group in ship breaking industry: Kamdar group is one of the oldest groups in ship-breaking industry at Alang and has been successfully operating its business through various business cycles. Mr. Harshad Padia, key promoter, possesses an experience of over three decades in the ship breaking industry. Due to GMB's policy of allotting only one plot to one legal entity, KAG has set-up three different entities in similar line of business. KAG receives the benefit of economies of scale in the fragmented ship-breaking industry and has relatively better bargaining power vis-à-vis its suppl/iers (mainly the shipping companies/ brokers selling old vessels) as well as its customers viz. the re-rolling mills and the scrap traders. Further, the promoters have, on a need basis, infused funds in the form of unsecured loans/capital to support business operations of various entities of the group.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Location of yard at Alang which has unique geographical features suitable for ship-breaking operations: The group's ship breaking yards are located at Alang-Sosiya belt which is considered to be one of the world's largest ship-breaking yards and caters to nearly 90% of India's ship-breaking activity. The unique geographical features of the area, including a high tidal range, wide continental shelf, 15 degree slope, and a mud free coast, are ideal for even large sized ships to be beached easily during high tide. It accommodates nearly 170 plots spread over around 10 km long stretch along the sea coast of Alang. All the yards of KAG are having frontage of 80 meters.

NK Class and RINA certification: Various agencies such as Nippon Kaiji Kyokai (NK) and RINA certify the operations of the ship-breaking yards from the environmental and worker safety points of view, including secure management of hazardous waste generated from the ship-breaking activities. Some of these certifications are carried after an audit as per the guidelines laid down by the Hong Kong Convention of the International Maritime Organization (IMO) in 2009 and that under European Union regulations. KAG's ship breaking yards also possess these certifications, which gives it an advantage to source ships at marginally better prices compared with market rates. All three yards have RINA certification while yard under PSB and SLSB holds NK class certification.

Moderate but fluctuating scale of operations and profitability which declined during FY22: Over the years, scale and profitability of the group on a combined basis has remained volatile depending upon the availability of ship for cutting along with the volatility associated with steel scrap prices. During FY22, KAG's total operating income declined significantly over FY21 with lower ship breaking activity as KAG has purchased lower ships due to volatility in steel prices. KAG had reported TOI of Rs. 131.83 crore as against Rs. 250.92 crore in FY21.
PBILDT margin had also declined to 4.41% in FY22 as against 5.89% during FY21. KAG had forex gain of Rs. 0.15 crore as against gain of Rs.5.31 crore in FY21 (adjusted in cost of RM). Consequently, net profit of Rs.10.14 crore in FY21 moderated to net profit of Rs.5.84 crore in FY22. This further translated into moderated GCA of Rs.6.27 crore in FY22.
The group has purchased small vessels during the year FY22 considering the volatility of prices resulting in lower TOI and profitability. However, in H1FY23, there is a significant increase in scale with large ship purchased in Q4FY22 and H1FY23 resulting in TOI of Rs.218 crore reflecting recovery from FY22 levels but declining trend in prices is expected to put pressure on margins in near term.

Stable outlook for industry: The outlook for domestic shipbreaking industry is expected to be stable backed by increase in demand of steel primarily on account of drop-off in steel exports from China and the rise in infrastructure investment in India. Implementation of the Recycling of Ships Act, 2019, and joining the Hong Kong International Convention (HKC) have strengthened country's leadership position worldwide in ship breaking industry. Further, The Indian Finance Ministry announced that the shipbreaking capacity in Alang will be extended by FY24 to capture 50% of the global ship recycling business. However, with increased trade volumes during the post unlock period and upward freight rates supports profitability of sailing vessels, limiting availability of ships for dismantling in near term. With ship rates declining in H1FY23 and new ship additions, ship availability to increase going forward.

Key rating weaknesses
Moderate capital structure: KAG's total debt is primarily comprised of outstanding LC obligations against the purchase of ship along with some utilization of fund based working capital limit which is used only for paying customs duty, port charges and IGST (on reverse charge basis) prior to beaching of the ship. During year end FY22, the group had 1 outstanding LC in SSB resulting in moderation in capital structure of KAG's, marked by an overall gearing of 1.46x as on March 31, 2022 (1.22x as on March 31, 2021). Furthermore, with moderation in profitability, interest coverage deteriorated from 4.60x in FY21 to 2.23x in FY22.

Constitution as a partnership firm: All the entities of KAG are partnership concerns which restricts its financial flexibility and there is an inherent risk of withdrawal of capital by the partners from the firm. Distribution of profits of the business by way of withdrawal from partners adversely impacting Networth base and capital structure of the firm.

Exposure to adverse movement in steel prices and forex rates: The volatility in steel prices driven by demand and supply conditions in the global as well as local markets exposes NSBC to any adverse price movement on the uncut ship inventory (which depends on the time elapsed since the purchase of the ship and the size/tonnage of the ship) as well as unsold inventory of steel scrap held by the firm (which is generally minimal). The firm uses Letter of Credit (LC) facility to purchase old ships. Since the transactions are denominated in foreign currency, the firm is exposed to forex risk during the LC Usance period, as the firm's revenue is denominated in Indian Rupee (INR). However, firm is doing hedging as per market situation thus mitigating exposure to certain extent.

Cyclical and competitive industry: The ship breaking industry is cyclical in nature as supply of old ships for recycling is inversely proportional to freight rates in the global economy. Better availability of old ships for recycling is ensured at the time of recession and when freight rates are low which makes it economical to dismantle the ship rather than continue to operate it. The Baltic Dry Index, which serves as one of the major freight indices, increased during H1FY23, indicating lesser availability of ships for breaking. Further, Indian ship-recycling yard face intense competition from the neighbouring countries like Bangladesh and Pakistan due to availability of low wage labour, lax occupational health and environment related regulations and larger yards giving better bargaining power to yard owners

Exposure to regulatory and environment hazard risk: The ship-breaking industry is highly regulated with strict working and safety standards to be maintained by the shipbreakers for their labourers and environmental compliance. Further, last year Government of India enacted the Recycling of Ships Act, 2019 ("Act") for the regulation of recycling of ships by setting certain standards and laying down the statutory mechanism for enforcement of such standards and related matters. Thus, if any adverse circumstances or event may affect business operations of entities.

Liquidity: Adequate
The group has adequate liquidity marked by low utilization of working capital limit, considerable amount of cash and cash equivalents and moderate LC coverage ratio. The average non fund-based limit utilization for the past twelve months ended October 2022 stood ~32%. As on March 31, 2022, group has current ratio of 1.80x where as quick ratio of 0.80x. Ship-breaking entities need to park their sale proceeds into fixed deposits (FDs) as per the schedule given by banks at the time of opening the LC for ship purchase, which are lien marked against the LC obligation towards purchase of the ship, in addition to the upfront margin kept for opening of the LC in favor of the supplier. This ensures gradual build-up of reserve funds to meet the sizeable LC payment obligations at maturity. KAG is continuously maintaining adequate LC coverage ratio above 1.15 times (considering 15% LC margin) over the period. LC coverage remained healthy at 1.35 times as on March 31, 2022 and 1.48 times as on September 30, 2022.

Analytical approach:- Combined
For arriving at the credit rating, CARE has combined the financial risk profile of KA, PSBC and SLSB [together referred to as Kamdar Group (KAG)]. As all three entities are partnership firms operating in similar business i.e. ship breaking with shareholding being held by the family members and having cashflow fungibility.

Applicable criteria
Policy on default recognition
Consolidation
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Wholesale Trading
Policy on Withdrawal of Ratings

About the Group - KAG
Kamdar Group (KAG) consists of three partnership firm i.e. KA, PSB and SLSB incorporated in year 1984, 2000 & 2002 respectively. KAG, managed by Padia family of Bhavnagar, is engaged in ship-breaking activity at three plots in the Alang – Sosiya belt of Bhavnagar region. All three plots are having frontage of 80 meters, taken on lease from Gujarat Maritime Board (GMB) for a period of one year and on completion of the tenure of agreement, the lease is renewed at prevailing lease rental rates.

About the firm
KA was incorporated in 1984 by Mr. Harshad Padia and Mr. Raju Padia and is one of the oldest ship breaking entities of the ship recycling facilities at Alang-Sosiya belt of Bhavnagar region in Gujarat.

Brief Financials (₹ crore)	KA Standalone			KAG combined		
	FY21 (A)	FY22 (A)	H1FY23 (Prov.)	FY21 (UA)	FY22 (UA)	H1FY23 (UA)
Total operating income	61.05	0.04	43.50	252.42	131.83	218.38
PBILDT	2.51	-0.61	NA	16.27	5.80	NA
PAT	1.86	0.04	NA	11.64	5.84	NA
Overall gearing (times)	0.00	0.00	NA	1.22	1.46	NA
Interest coverage (times)	4.17	-1.72	NA	4.08	2.23	NA

A: Audited; UA: Unaudited as financials are combined by analytical team, Prov :- Provisional

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating history for the last three years: Please refer Annexure-2

Covenants of the rated instruments/facilities: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Non-fund-based - LT/ ST-Letter of credit	-	-	-	-	65.00	CARE BBB-; Stable / CARE A3
Non-fund-based - ST-Credit Exposure Limit	-	-	-	-	1.30	CARE A3

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Cash Credit	LT	-	-	-	1)Withdrawn (24-Nov-21)	1)CARE BBB-; Stable (18-Dec-20) 2)CARE BBB-; Stable (06-Apr-20)	1)CARE BBB-; Stable (27-Nov-19)
2	Non-fund-based - LT/ ST-Letter of credit	LT/ST*	65.00	CARE BBB-; Stable / CARE A3	-	1)CARE BBB-; Stable / CARE A3 (24-Nov-21)	1)CARE BBB-; Stable / CARE A3 (18-Dec-20) 2)CARE BBB-; Stable / CARE A3 (06-Apr-20)	1)CARE A3 (27-Nov-19)
3	Non-fund-based - ST-Credit Exposure Limit	ST	1.30	CARE A3	-	1)CARE A3 (24-Nov-21)	1)CARE A3 (18-Dec-20) 2)CARE A3 (06-Apr-20)	1)CARE A3 (27-Nov-19)

*Long term/Short term.

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

Name of the instrument	Detailed explanation
A. Financial covenant	
Hedging	Hedging is mandatory (in absence of which additional 5% margin require)
B. Non-financial covenant	
Time frame	Ship to be dismantle within 300 days for repayment of LC

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Non-fund-based - LT/ ST-Letter of credit	Simple
2	Non-fund-based - ST-Credit Exposure Limit	Simple

Annexure-5: Bank lender details for this company

To view the lender wise details of bank facilities please click here

Note on complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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