Kalyani Steels Limited

December 06, 2022

Ratings

Sr. No.	Instrument/ Bank Facilities*	Amount (Rs crore)	Rating	Rating action
1	Long Term Bank Facilities	331.99	CARE AA; Stable (Double A; Outlook: Stable)	**Reaffirmed**
2	Short Term Bank Facilities	500.00	CARE A1+ (A One Plus)	**Reaffirmed**
	Total Bank Facilities	**831.99 (₹ Eight Hundred Thirty-One Crore and Ninety-Nine Lakhs Only)**		
3	Commercial Paper-Proposed	75.00	CARE A1+	**Reaffirmed**
	Total Short term instruments	**75.00 (Rs. seventy five crore only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings of Kalyani Steels Limited (KSL) continues to factor in its strong promoter group (Pune-based Kalyani group), with long and established track record of over four decades in the manufacturing of forging and engineering quality carbon and specialty steel. The ratings derive strength from its robust capital structure, comfortable debt coverage metrics, stable profitability margins with increasing revenues in H1FY23. The company benefits from established selling arrangements with approved vendor status from major original equipment manufacturers (OEMs) and arrangement with suppliers for procurement of raw material albeit absence of long-term contracts. The ratings also derive comfort from the backward integration project of 200,000 TPA coke oven plant and 17 MW waste heat power plant project set up by the company to reduce dependence on external coke. The above rating strengths are, however, tempered by the company's presence in the cyclical steel industry; the end-users being automobile, oil and natural gas, energy, railway, defense, bearing industry, etc, susceptibility to significant volatility in raw material prices & foreign exchange rates, competition in the steel industry and lack of any backward integration in the form of captive iron ore and coal mines.

Rating Sensitivities

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

- ✓ Significant and sustained improvement in the scale of operations on the back of improvement in the credit profile of the group companies with which KSL shares substantial trade linkages.

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

- × Decline in the total operating income and/or profitability leading to net cash accruals below Rs.100 crore on a sustained basis
- × Deterioration in the credit profile of the group companies with which KSL shares substantial trade linkages.
- × Delayed realization of debtors from the group companies
- × Increased financial leverage indicated by overall gearing ratio of 0.65x or more

Detailed description of the key rating drivers

Key Rating Strengths

Strong promoter group coupled with long track record in iron & steel industry

KSL is a part of the Kalyani group and is spearheaded by Mr B.N Kalyani in the strength of Chairman. He is also the Chairman and Managing Director (CMD) of Bharat Forge Limited. The Kalyani group, established in mid 1960s, has wide capabilities across varied industries including Engineering, Automotive, Industrial, Renewable Energy, Urban Infrastructure and Specialty Chemicals. In a span of more than four decades, KSL has grown from being a primary iron and steel manufacturer to a preferred steel supplier for engineering, auto, seamless tubes, etc., companies mainly catering to forging industry. serving the auto and allied sectors. The promoters are supported by a team of professionals including, Mr RK Goyal (MD) and Mr Balmukand Maheshwari (CFO) who are associated with KSL since more than eight years

Established selling arrangements
KSL was promoted as backward integration unit of the Kalyani group from which majority of the requirements for the group companies is met through KSL. Moreover, long-standing relationship with major OEMs along with approved vendor status continues to garner KSL with repeat orders. The Kalyani group companies accounted for around 53.33% of the total revenue in FY22 (refers to the period April 1 to March 31) and 59.22% of the total revenue in H1FY23 (refers to the period April 1 to September 30).

Arrangement with suppliers for procurement of raw material albeit absence of long-term contracts continues
KSL has diversified raw material procurement source wherein raw materials are procured both from the domestic and overseas market. The key raw materials used by KSL include coke/coke fines, iron ore/iron ore fines and ferro alloys. However, majority of the raw materials have been sourced from few suppliers representing concentration risk; but the risk is partially mitigated as the company takes quotes from various suppliers before placing orders. Furthermore, KSL has not entered into any long-term contracts with the suppliers. Further, due to increase in prices of coal/ coke/ coke fines in H1FY23, the cost of raw material was approximately 64 % of the total revenue from operations. However, KSL has been able to pass on the increase in raw material prices to its customers, albeit with a lag effect which might have some effect on the profitability.

Robust capital structure and comfortable debt coverage metrics
Capital structure of KSL remained robust with 0.14 (0.02) debt to equity and overall gearing (including LC backed creditors) of 0.46x (0.22x) as on March 31, 2022 (2021). The overall gearing increased on account of increase in foreign currency term loan availed by the company during FY22 to fund the projected capital expenditure of Rs.211 crore. As on March 31, 2022, the company has long term debt of Rs.189.52 crore. The debt is projected to increase further, however the overall gearing is expected to remain comfortable. The fund based working capital utilization is also minimal. The net worth of the company stood at Rs.1367.04 crore as on March 31, 2022, as against Rs.1153.42 crore as on March 31, 2021. Further, KSL continues to have healthy debt coverage indicators with PBILDT interest coverage and total debt/Gross Cash Accrual of 28.42x and 2.22x in FY22 as against 43.24x and 1.11x in FY21.

Scale of operations
In FY22, the company earned revenue from operations of Rs. 1,743.09 crore with a growth of 43% compared to FY21 on account of increasing demand from revival in automotive sector, government push in infrastructure sector and improvement in the bearing & engineering segment. KSL is primarily a captive unit of the Kalyani Group. For the FY22 and H1FY23, the top 10 customers of KSL generated 72.22% and 72.06% of the total income from operations, respectively. Further, Bharat Forge Limited and Kalyani Technoforge Limited contribute to approximately 50% of the revenue of KSL. KSL is predominantly producing rolled products which are utilized in the automotive and industrial segments. For the past several years, more than 90% of KSL's revenue is generated from sale of rolled products. Further, there was an increase in cost of production on account of increase in the prices of Hard Coking Coal (HCC Peak Down) to 4.6 times during FY22 which ranged from average USD 127/tonne in April, 2021 to USD 590/tonne in March 2022. The coke prices were ranging from USD 370/tonne to USD 692/tonne during the same mentioned period. This led to deterioration of the PBILDT margin of KSL from 24.04% in FY21 to 21.53% in FY22. Further, the company's PBILDT (PAT) margin has remained in between 14-25% (8-16%) over the past 5 fiscal years through FY22.

Key Rating Weakness
Cyclicality of the steel industry:
Steel is a highly capital-intensive industry which is cyclical in nature. Its growth is intertwined with the growth of the economy at large and, in particular, the steel-user industries such as automobile, housing, infrastructure, and others. KSL generates about 80% of revenue from auto segment which is also affected by economic cycles. Also, the customers of KSL remain vulnerable to pricing pressures from large OEMs which in turn may have adverse impact on profitability margins. Furthermore, competition plays a role in the profitability of steel manufacturer mainly arising out of unorganized players and Chinese imports. However, KSL, being in niche segment providing specialty steel, remain immune to competition from unorganised players.

Competition of steel industry
The producers of steel products are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility of the steel industry. The steel industry is highly competitive with presence of various organized and unorganized players and expanding applications of steel products. Margins continue to remain under pressure due to fragmented nature of industry. Also, the steel industry is sensitive to the shifting business cycles, including changes in the general economy, interest rates and seasonal changes in the demand and supply.

Susceptibility to volatility in raw material prices and forex risk
Raw material consumption is the single-largest cost component for KSL. KSL's cost of production was approximately 79.29% of its total revenue from operations in H1FY23 as compared to 70.82% in FY22 and 66.93% in FY21. The key raw materials used by the company are iron ore/iron ore fines; coking coal/ coke fines, fluxes like limestone and dolomite, ferro alloys and solid charge. Coking coal and iron ore prices fluctuate globally on a demand-supply basis which generally impact the profitability margins. Though the company has pass-through arrangements with the customers, on occasions there is a risk of lag in the mechanism. Furthermore, part of the raw material requirements is imported, thus exposing to foreign currency exchange risk since the company does not hedge its imports. However, the risk is partially mitigated as the same is factored in pricing while placing orders.

Liquidity: Strong
KSL is expected to generate healthy gross cash accruals against nil repayment obligations for next 2 years. Furthermore, KSL had free cash and bank balance of Rs. 1128.05 crore as on September 30, 2022. Additional liquidity cushion is available in the form of largely unutilized lines of credit. The company has availed a short-term loan of Rs.150 crore during FY22. The average fund based working capital utilization for the last 12 months through October 2022 was NIL. This was majorly on account of managing working capital requirements through internal accruals and creditors' support backed by letter of credit.

Analytical approach: Standalone, However, linkages with group companies, which are integral and strategically important to the operations of KSL, have been considered.

Applicable Criteria
- Criteria on assigning 'outlook' and 'credit watch'
- CARE's Policy on Default Recognition
- Criteria for Short Term Instruments
- Financial ratios – Non-Financial Sector
- Rating Methodology - Manufacturing Companies
- Rating Methodology - Steel Sector
- Rating Methodology: Factoring Linkages in Ratings

About the Company
Incorporated in 1973, Kalyani Steels Limited (KSL) is a part of the Pune (Maharashtra)-based Kalyani group. The company is spearheaded by Mr B. N Kalyani, who is the chairman of the Kalyani Group of companies. The manufacturing facility of KSL are located at Ginigera village, dist. Koppal (Karnataka). KSL is a leading manufacturer of forging and engineering quality carbon and alloy steel which caters to the requirement of various segments, viz., automotive, oil & gas, energy, bearings, seamless tubes, railways, etc. The company is a preferred steel supplier for engineering, automotive, seamless tube and primary aluminium industry used in the automobile and engineering industries. KSL has a state-of-the-art integrated manufacturing facility spread across 375 acres located at Hospet. The total installed capacity (Hospet Steels Limited) is around 7 lakh Metric Tonne Per Annum (MTPA). There is a strategic alliance between KSL and Mukand Limited (ML, part of the Bajaj group) where the manufacturing facilities are shared, with KSL holding 41.38% of the assets and ML holding the remaining.

Brief financials of KSL (Standalone):

Brief Financials (Rs. crore)	31-03-2021(A)	31-03-2022 (A)	H1FY23(UA)
Total operating income	1217.85	1743.09	1018.68
PBILDT	292.73	375.35	112.43
PAT	255.04	325.84	58.25
Overall gearing (times)	0.22	0.14	NA
Interest coverage (times)	43.24	28.42	10.31

A: Audited; UA: Unaudited; NA: Not Available

Status of non-cooperation with previous CRA: NA
Any other information: NA
Rating History for last three years: Please refer Annexure-2
Covenants of rated instrument / bank facility: Detailed explanation of covenants of the rated instruments/ bank facilities is given in Annexure-3
Complexity level of various instruments rated for this company: Annexure 4

Annexure-1: Details of Instruments / Bank Facilities

Name of the Instrument/ Bank Facilities	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Cash Credit		-	-	-	150.00	CARE AA; Stable
Non-fund-based - ST-BG/LC		-	-	-	300.00	CARE A1+
Non-fund-based - ST-BG/LC					200.00	CARE A1+
Term Loan-Long Term				March 2026	181.99	CARE AA; Stable
Proposed Commercial Paper-Commercial Paper (Standalone)				7-365 days	75.00	CARE A1+

Annexure-2: Rating History of 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	150.00	CARE AA; Stable	-	1)CARE AA; Stable (17-Jan-22) 2)CARE AA; Stable (07-Dec-21)	CARE AA; Stable (08-Oct-20)	CARE AA; Stable (30-Sep-19)
2	Non-fund-based - ST-BG/LC	ST	300.00	CARE A1+	-	1)CARE A1+ (17-Jan-22) 2)CARE A1+ (07-Dec-21)	CARE A1+ (08-Oct-20)	CARE A1+ (30-Sep-19)
3	Fund-based/Non-fund-based-Short Term	ST	200.00	CARE A1+	-	1)CARE A1+ (17-Jan-22) 2)CARE A1+ (07-Dec-21)	CARE A1+ (08-Oct-20)	CARE A1+ (30-Sep-19)
4	Commercial Paper-Commercial Paper (Standalone)	ST	75.00	CARE A1+	-	1)CARE A1+ (07-Dec-21) 2)CARE A1+ (07-Oct-21)	CARE A1+ (08-Oct-20)	CARE A1+ (30-Sep-19)
5	Fund-based - LT-External Commercial Borrowings	LT	-	-	-	-	Withdrawn (08-Oct-20)	CARE AA; Stable (30-Sep-19)
6	Term Loan-Long Term	LT	181.99	CARE AA; Stable	-	1)CARE AA; Stable (17-Jan-22) 2)CARE AA; Stable (07-Dec-21)	CARE AA; Stable CARE A1+ (08-Oct-20)	CARE AA; Stable / CARE A1+ (30-Sep-19)

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instrument / bank facilities: NA

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

Sr. No.	Name of Instrument/ bank facilities	Complexity Level
1	Commercial Paper-Commercial Paper (Standalone)	Simple
2	Fund-based - LT-Cash Credit	Simple
3	Non-fund-based - ST-BG/LC	Simple
4	Term Loan-Long Term	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 instrument: CARE Ratings Ltd. 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.

Contact us

Media Contact
Name – Mr. Mradul Mishra
Contact no. - +91-22-6754 3596
Email ID - mradul.mishra@careedge.in

Analyst Contact
Group Head Name - Hitesh Avachat
Group Head Contact no.- +91-90048 60007
Group Head Email ID- hitesh.avachat@careedge.in

Relationship Contact
Name – Saikat Roy
Contact no. - +022-67543404/136
Email ID - saikat.roy@careedge.in

About CARE Ratings Limited:
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