Welspun Specialty Solutions Limited

June 16, 2022

Ratings

Facilities	Amount (₹ crore)	Rating[1]	Rating Action
Long-term/short-term bank facilities	27.36	CARE AA (CE); Stable/CARE A1+ (CE) [Double A (Credit Enhancement); Outlook: Stable/A One Plus (Credit Enhancement)]	Reaffirmed
Long-term/short-term bank facilities	125.00 (Enhanced from 72.64)	CARE AA (CE); Stable/CARE A1+ (CE) [Double A (Credit Enhancement); Outlook: Stable/A One Plus (Credit Enhancement)]	Revised from CARE BBB- (Triple B Minus) and removed from 'Credit Watch with Developing Implications'
Short-term bank facilities	20.00	CARE A1+ (CE) [A One Plus (Credit Enhancement)]	Assigned
Total facilities	172.36 (₹ One hundred seventy-two crore and thirty-six lakh only)		

Details of instruments/facilities in Annexure-1.
#The rating is backed by credit enhancement in the form of unconditional and irrevocable corporate guarantee provided by Welspun Corp Limited.

Unsupported Rating As stipulated vide SEBI circular dated June 13, 2019
CARE BBB-/CARE A3 [Revised from CARE BBB- (Triple B Minus) and removed from 'Credit Watch with Developing Implications]

Note: Unsupported Rating does not factor in the explicit credit enhancement.

Detailed rationale and key rating drivers for the credit enhanced debt of Welspun Specialty Solutions Limited (WSSL)

The ratings assigned to the bank facilities of WSSL factor in the credit enhancement (CE) in the form of an unconditional and irrevocable corporate guarantee (CG) extended by Welspun Corp Limited (WCL) towards the timely servicing of debt obligations. The above rating is solely based on CARE Ratings Limited's (CARE Ratings') view of the guarantor's (WCL's) credit profile, and accordingly, the rating rationale highlights the credit risk assessment parameters for the guarantor.

Detailed rationale and key rating drivers of WCL (the guarantor)

The rating reaffirmation of the bank facilities/instruments of WCL continues to factor in the strong business risk profile, supported by its dominant position in the steel pipe business with a diverse geographical presence in India, the US, and Saudi Arabia. The ratings also consider the strong financial risk profile, supported by a comfortable capital structure and liquidity position.

CARE Ratings notes the debt-funded (70%) greenfield expansion undertaken by WCL in terms of setting up pig iron (PI) and ductile iron (DI) manufacturing plants at Anjar, Gujarat, has moderated its capital structure in FY22. The project cost has undergone revision because of changes in the project plan and the rising input cost, which is primarily funded through debt (70%) and the balance through equity. The project is expected to be commissioned in H2FY23 and with balance debt being drawn in FY23, the leverage is expected to moderate further, though will remain comfortable.

The liquidity position of the company remains strong, with sale consideration received for the PCMD division in H1FY22. Furthermore, in Q4FY22, WCL received US$ 40.49 million as a dividend from Welspun Mauritius Holdings Limited with its stake dilution in the JV company – East Pipe Integrated Company – during its IPO.

WCL encountered challenges due to the COVID-19 pandemic in FY21, which led to a moderation in its revenue profile and a slow pace of order book execution. In FY22, although the company achieved a total income of ₹6,505 crore, profitability was impacted due to the product mix and rising commodity prices. Furthermore, there were minimal operations in the US in H2FY22 on account of the change in the government and the slowdown due to the pandemic. However, considering the increase in oil and gas pipeline requirements, in the US, the company has received a large order with distribution to the exports markets. This

[1]Complete definitions of the ratings assigned are available at www.careedge.in and in other CARE Ratings Ltd.'s publications.
As stipulated vide SEBI circular no SEBI/ HO/ MIRSD/ DOS3/ CIR/ P/ 2019/ 70 dated June 13, 2019. As per this circular, the suffix 'CE' (Credit Enhancement) is assigned to the ratings with explicit external credit enhancement, against the earlier used suffix 'SO' (Structured Obligation).

project will be executed from September 2022 onwards. As on March 31, 2022, the company has a healthy order book position to supply 925 KMT, valued at ₹12,250 crore, providing revenue visibility for the next two years. Moreover, in the US, the company is already executing orders worth US$ 110 million, with delivery in Q4FY23, which is over and above the large order mentioned above.

However, any slowdown on account of uncertainties around the fourth wave of the pandemic and any other material developments impacting the sales volume and incremental orders in the key markets remain key rating monitorable. However, the demand for pipelines is expected to increase, with the rising demand from European markets due to the curtailment of oil and gas distribution from Russia and Ukraine.

The above rating strengths are offset by the volatility associated with crude oil and gas and steel prices impacting the demand for pipelines, and the order book in the line pipe segment, and the regulatory risk in the geographies in which it operates.

In June 2021, WCL had announced the scheme of demerger, to acquire the steel business of Welspun Steel Limited (WSL; rated CARE A-/CARE A2; under Credit Watch with Developing Implications), directly and indirectly carried out through investments held in Welspun Specialty Solutions Limited (WSSL; 50.03%), Anjar TMT Steel Private Limited (ATSPL; 100%) and Welspun Captive Power Generation Limited (WCPGL, rated CARE A+; Stable/CARE A1+; 2.95%), cumulatively referred to as 'demerged company'. The scheme has been approved by the Ahmedabad Bench of the National Company Law Tribunal (NCLT) on March 16, 2022, and WCL is now the holding company of the steel assets of the group. WCL has paid ₹11 crore as cash and issued ₹350 crore of redeemable preference shares (RPS) to the shareholders of the 'demerged company', redeemable at the option of the holder, upon the expiry of 18 months from the date of issue. Upon the effectiveness of the scheme, WCL has consolidated the steel business under it and is likely to benefit from being an integrated manufacturer now.

CARE Ratings notes that with the acquisition of Sintex BAPL by WCL, the company plans to foray into the plastic or polymer pipes segment. CARE Ratings will continue to monitor the developments in this regard.

Key rating drivers of WSSL for the Unsupported rating

CARE Ratings has removed the ratings of WSSL from 'Credit Watch with Developing Implications'. The above action comes on the back of the completion of the scheme of arrangement announced by WCL, wherein, it had proposed to acquire the division of WSL's steel operating business, which manufactures BIS-certified steel billets and direct reduced iron (DRI), specialty steel and thermo mechanical treatment (TMT) bars and the businesses directly or indirectly carried out through the investments held in WSSL, ATSPL and WCPGL. The scheme has been approved by the Ahmedabad Bench of the NCLT, and March 16, 2022 onwards, WCL is the holding company of WSSL.

The reaffirmation of the ratings assigned to the bank facilities of WSSL considers the strong operational and financial linkages with the Welspun group entities, viz, WCL and WSL. The ratings derive strength from the redefined product mix, with the management discontinuing its alloy steel business and focusing on the production of stainless steel, pipe, and tube products. The modernisation capex undertaken by WSSL over FY18-FY20 has been completed and benefits from the same, coupled with the new product mix, is expected to accrue from FY23. Furthermore, with the completion of the demerger scheme, WSSL will have a stronger presence across the market segments, access to new markets and product offerings, while also having access to WCL's marketing capabilities. This can translate into better earnings and improved operational cash flows.

That said, the above rating strengths are offset by the sub-par operational performance of WSSL, with the company reporting a negative operating profit in the last few years, including FY22. This has resulted in a weak financial risk profile and stretched liquidity position and has led to dependence on the group companies for repayment obligations as well as to avail financing from lenders. The ratings also remain constrained by the inherent cyclicality in the steel industry.

Rating sensitivities of WSSL

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

- Improvement in the credit metrics, with breakeven and sustained growth visible at the PBILDT level.
- Improvement in the sales volume for stainless steel and pipes, leading to growth and sustenance of the revenue beyond ₹500 crore.

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

- Any further deterioration in the credit metrics and withdrawal of support from group entities, particularly from WSL and WCL.
- Delay in the stabilisation of new capacities for stainless steel and seamless pipes, resulting in lower-than-expected revenues and margin.

Rating sensitivities of WCL

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

- WCL's ability to improve its consolidated operating profitability margin to more than 16% on a sustained basis.
- Low leveraged capital structure, with overall gearing (including CG) not more than 0.30x.
- Sustenance in the return on capital employed (ROCE) above 25% and improvement in the interest coverage ratio above 8.00x.

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

- Decline in profitability margins below 11% on a consolidated basis in the projected period.
- Continued contraction in the order book position, leading to lower sales volumes in the projected period.
- Increase in adjusted overall gearing (including CG) above 1.00x during the projected period.
- Any delay in the proposed capex plan, resulting in time and cost overruns.

Detailed description of the key rating drivers of WSSL

Key rating strengths

Strong operational and financial linkages with the Welspun group entities: There are operational and financial linkages between WSSL and the other group entities of the Welspun group, ie, WCL and WSL, which have strengthened over the years, evident with the promoter group increasing its shareholding from 49.81% in FY20 to 53.62% in FY21, upon conversion of share warrants. Furthermore, from March 16, 2022, WCL is the holding company of WSSL.

Change in product mix to help drive volumes and improve sales realization: Prior to FY21, WSSL was into the carbon steel and alloy business, which involved the manufacturing of alloy-based ingots and blooms. Post FY21, WSSL has moved away from the carbon steel business to stainless steel product mix, wherein, the margins and operating cycles are more accretive as compared to the former. Since December 2021, WSSL is manufacturing SS long products and SS seamless pipes and tubes.

Synergistic benefits due to merger with WCL: The Welspun group has relevant experience and an established track record of two decades in selling and marketing steel products. WSSL may leverage on the in-house expertise of the holding company to market its own products. The Welspun groups' strong relations with the suppliers and the timely supply of good raw materials for the smooth running of operations will remain key rating monitorable. Furthermore, WSSL will have access to the marketing capabilities and the customer profile of WCL.

Key rating weaknesses

Weak financial risk profile, leading to dependence on group companies: WSSL's financial risk profile remains weak, marked by underutilization of capacity and reporting operating losses in the last few years, including FY22. The continued losses have resulted in an eroding of the net worth and negative interest coverage for the said period. WSSL has been relying on support from the group companies for repayments and availing finance from lenders.

Inherent cyclicity in the steel industry: The prospects of the steel industry are strongly co-related to economic cycles. The demand for steel is sensitive to trends of particular industries, viz, automotive, construction, infrastructure, and consumer durables, which are the key consumers of steel products. These key user industries, in turn, depend on various macroeconomic factors, such as consumer confidence, employment rates, interest rates, and inflation rates, among others, in the economies in which they sell their products. When downturns occur in these economies or sectors, the steel industry may witness a decline in demand.

Liquidity: Stretched

Liquidity remains stretched, marked by a modest cash balance of ₹5 crore as on March 31, 2022. The average utilisation of the fund-based limits stands at 61% for the last 12 months ending March 31, 2022. WSSL has repayment obligations of ₹8.44 crore in FY23, which is expected to be met through cash generated from operations, with full year of operations post the capex and a healthy order book in hand.

Detailed description of the key rating drivers of the guarantor, WCL

Key rating strengths

Strong business risk profile: WCL is one of the dominant players in the steel line pipe business, with an established track record of over two decades and demonstrated capabilities in the supply of line pipes for complex projects in the oil and gas as well as water segments. WCL has a global pipe production capacity of 2.55 million tonne per annum (MTPA), with an aggregate capacity of 1.65 MTPA at four locations across India, 0.52 MTPA capacity in the US, and 0.375 MTPA capacity through a joint venture (JV) in Saudi Arabia. Over the last three years ending March 31, 2021, the company has consistently sold more than 1,000 kilometre tonne (KMT) of pipes globally (FY22: approximately 800 KMT of sales volume for pipes), which is aided by its established relationships with reputed overseas and domestic customers. Owing to the requirement of sophisticated infrastructure in such business results in high entry barriers for new players, thereby limiting competition, and thus, strengthening WCL's business risk profile.

Moderation in financial risk profile and profitability indicators: The financial risk profile, marked by overall gearing and total debt to GCA (TD/GCA) at 0.49x and 3.00x, respectively, as on March 31, 2022, moderated from 0.28x and 1.59x, respectively, as on March 31, 2021, with debt availed for the capex being executed for PI and DI by WCL.
The company received the entire consideration from sale of its PCMD division in H1FY22 and further ₹500 crore from the stake dilution in the JV Company – East Pipe Integrated Company – in Q4FY22, resulting in a cash and liquid investment balance of ₹2,195 crore as on March 31, 2022. The profitability margin, viz, PBILDT margin, declined to 7.25% in FY22 from 13.26% in FY21, with more volumes in low-margin products and rising commodity prices and minimal operations in the US in H2FY22. Going forward, the financial risk profile is expected to moderate, with balanced debt to be availed for the capex and working capital borrowings needed for operating the plant from H2FY23. WCL has extended a CG for the debt facilities availed/to be availed for the capex purpose. The overall project cost has been revised to ₹1,900 crore (earlier ₹1,550 crore), which will be 70% funded through debt and the balance through equity. However, the overall gearing is expected to be less than unity in FY23.

Satisfactory order book position, providing medium-term revenue visibility: WCL's globally confirmed order book position stands at 925 KMT, translating into a sales value of around ₹12,250 crore as on March 31, 2022, thus providing medium-term revenue visibility for the company. In addition to the above, the company has an active bid book of around 1,250 KMT, with orders in the oil and gas and water segments. For the Indian market, the demand for large-diameter pipes in the oil and gas segment is mainly driven by gas grid development and oil pipeline network by domestic oil companies, while the demand for small-diameter pipes is driven by city gas distribution projects. The US operations entirely supplies to the oil and gas segment while in Saudi Arabia, the order book is majorly driven by water orders from SWCC. The order book across geographies has aided the group in diversifying its revenue profile over the years.

Impact of COVID-19 on the business profile: In FY22, WCL reported a total operating income (TOI) of ₹6,505 crore, as compared to ₹6,527 crore in FY21. While the top-line was maintained, the profitability was impacted due to the product mix and the rising commodity prices and the minimal operations in the US in H2FY22. In FY21, WCL reported a moderation in revenue and net income by 35% and 4%, respectively, on account of the impact of the COVID-19 pandemic and the decline in oil prices. The uncertainty around the pandemic led to a cautious approach of midstream and exploration and production companies of the US in their large capex programme. Additionally, the major pipeline projects in the US got stalled due to concerns related to environment safety and presidential elections in November 2020. To some extent, WCL was able to offset the loss of orders in the US by securing orders from new markets, viz, Australia and Latin America. The Indian operations was supported to some extent by the intent of the government to double down on the capex to revive the economy, which led to an increased tender activity from public sector companies. The Saudi JV operations were severely impacted due to the prolonged shutdown due to the COVID-19 pandemic from March 2020 until June 2020, which led to a backlog in terms of order execution, resulting in low sales. Additionally, the market was impacted by the decline in oil prices and the sharp increase in steel prices.

Key rating weakness

Susceptible to slowdown in end-user industries and to government policies: WCL derives more than 50% of its revenue from the oil and gas segment. The significant volatility in crude prices can question the viability of new explorations, thereby impacting the demand for line pipes in the oil and gas segment. Furthermore, the recent upward rally in the steel prices may defer the capex plans of large steel customers. Amid the pandemic-induced slowdown in oil prices in March 2020, WCL witnessed deferment and cancellation of a few orders by customers. The revival of new projects in the oil and gas segment in the key markets of the US and the Middle East is critical to sustain improvement in the overall operations. Any major and continued slowdown in end-user industries will weaken the demand for line pipes and impact performance. Furthermore, operations remain exposed to government policies and regulations in the geographies it operates.

Liquidity: Strong

WCL's liquidity position is supported by cash and liquid investments of ₹2,195 crore as on March 31, 2022, and GCA of ₹685 crore for FY22. WCL also has access to fund-based limits of ₹5,000 crore, which remained utilised at a 20% average over the 12 months ended April 30, 2022. The current ratio stood at 1.46x and the operating cycle at 57 days during FY22 (PY: 97 days).

Analytical approach

For CE debt: CARE Ratings' rating on the bank facilities of WSSL factors in the CE in the form of an unconditional and irrevocable CG extended by WCL (rated CARE AA; Stable/CARE A1+) towards the timely servicing of debt obligations.
For Unsupported rating: Standalone approach. Furthermore, the financial and operational linkages with the entities of the Welspun group have been taken into consideration.

Applicable criteria

CARE Ratings' criteria on rating outlook and credit watch
CARE Ratings' policy on Default Recognition
Criteria for short-term instruments
Financial ratios – Non-financial sector
Liquidity analysis of Non-financial sector entities
Rating methodology – Steel companies
Rating methodology – Credit enhanced debt
Rating methodology – Factoring linkages parent sub-JV group
Manufacturing companies

About the Company – WCL

WCL is a flagship company of the US$ 2.7-billion Welspun group. WCL is a welded pipe manufacturing company engaged in offering solutions in line pipes, with a capacity to manufacture longitudinal submerged arc welded (LSAW; used for onshore and offshore oil, gas transmission), spiral helical submerged arc welded pipes (HSAW; used for onshore oil, gas and water transmission), and electrical resistance welded (ERW; used for downstream distribution of oil, gas and water) pipes. The company also offers coating, bending, and double jointing facilities. WCL has a 2.55-MTPA capacity of steel pipes manufacturing, with plants located in India, the US, and Saudi Arabia.

About the company – WSSL

Incorporated in December 1980, WSSL (earlier known as RMG Alloy Steel Limited) is a part of the Welspun group, with a 50.03% stake held by WCL as on March 31, 2022. WSSL operates an electric arc furnace (for alloy steel) and induction furnace (for stainless steel)-based steel melting shop, a rolling mill, and a seamless pipe manufacturing facility in Bharuch, Gujarat. It has a capacity of 150,000 tonne per annum (TPA) in steel melting shop, 100,000 TPA in rolling mill, along with 18,000 TPA in the pipes division.

Financial performance – WCL

Brief Financials (₹ crore)	FY20 (A)	FY21 (A)	FY22 (Abr)
Income from continuing operations	10,019.98	6,527.47	6,505.11
PBILDT	1,263.96	865.51	471.70
PAT (after discontinued operations)	654.06	630.64	444.17
Overall gearing (including LC acceptances) (times)	0.57	0.28	0.49^
Interest coverage (times)	8.78	12.89	4.63

A: Audited; Abr: Abridged.
^Excluding acceptances.
Note: The financials are adjusted as per CARE Standards

Financial performance – WSSL

Brief Financials (₹ crore)	FY20 (A)	FY21 (A)	FY22 (Abr)
TOI	299.86	94.49	182.41
PBILDT	-66.35	-18.63	0.74
PAT	-81.37	93.18	-30.78
Overall gearing (including LC acceptances) (times)	-3.55	5.82	49.11
Interest coverage (times)	-4.31	-1.62	0.04

A: Audited; Abr: Abridged.
Note: The financials are adjusted as per CARE Standards

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 the various instruments rated for this company: Annexure-4

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
LT/ST Fund-based/Non-fund-based-CC/WCDL/OD/LC/BG		-	-	-	125.00	CARE AA (CE); Stable/CARE A1+ (CE)
Fund-based/Non-fund-based-LT/ST		-	-	-	27.36	CARE AA (CE); Stable/CARE A1+ (CE)
Unsupported Rating-Unsupported Rating (LT/ST)		-	-	-	0.00	CARE BBB-/CARE A3
Non-fund-based - ST-Forward Contract		-	-	-	20.00	CARE A1+ (CE)

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	LT/ST Fund-based/Non-fund-based-CC/WCDL/OD/LC/BG	LT/ST*	125.00	CARE AA (CE); Stable/CARE A1+ (CE)	-	1)CARE BBB- (CWD) (03-Dec-21)	-	-
2	Fund-based/Non-fund-based-LT/ST	LT/ST*	27.36	CARE AA (CE); Stable/CARE A1+ (CE)	-	1)CARE AA (CE); Stable / CARE A1+ (CE) (03-Dec-21)	-	-
3	Unsupported Rating-Unsupported Rating (LT/ST)	LT/ST*	0.00	CARE BBB-/CARE A3	-	1)CARE BBB- (CWD) (03-Dec-21)	-	-
4	Non-fund-based - ST-Forward Contract	ST	20.00	CARE A1+ (CE)				

*Long term/short term

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

Not applicable

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

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based/Non-fund-based-LT/ST	Simple
2	LT/ST Fund-based/Non-fund-based-CC/WCDL/OD/LC/BG	Simple
3	Non-fund-based - ST-Forward Contract	Simple
4	Unsupported Rating-Unsupported Rating (LT/ST)	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:
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