

## Kalyani Steels Limited

January 17, 2022

### Ratings

Facilities/Instruments	Amount (Rs. crore)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	331.99	CARE AA; Stable (Double A; Outlook: Stable)	Reaffirmed
Short Term Bank Facilities	500.00	CARE A1+ (A One Plus)	Reaffirmed
<b>Total Bank Facilities</b>	<b>831.99</b> <b>(Rs. Eight Hundred Thirty-One Crore and Ninety-Nine Lakhs Only)</b>		

Details of instruments/facilities in Annexure-1

### Other rated facilities

Facilities/Instruments	Amount (Rs. crore)	Rating <sup>2</sup>
Commercial Paper	75.00	CARE A1+ (A One Plus)

### Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings of the bank facilities 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 H1FY22. 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 being undertaken by the company to reduce dependence on coke.

The above rating strengths are, however, tempered by the company's modest scale of operations, presence in the cyclical steel industry; the end-users being automobile, oil and natural gas, energy, railway, defence, bearing industry, etc, susceptibility to significant volatility in raw material prices & foreign exchange rates, exposure to the group companies in the form of investments and lack of any backward integration in the form of captive iron ore and coal mines.

### Key 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% of the total revenue in FY21 (refers to the period April 1 to March 31).

<sup>1</sup>Complete definition of the ratings assigned are available at [www.careedge.in](http://www.careedge.in) and other CARE Ratings Ltd.'s publications

### **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.

### **Robust capital structure and comfortable debt coverage metrics**

Capital structure of KSL remained robust with 0.02 (nil) debt to equity and overall gearing (including LC backed creditors) of 0.22x (0.19x) as on March 31, 2021 (2020). The overall gearing marginally increased on account of ECB taken by the company during FY21 to fund the projected capital expenditure of Rs.211 crore. As on March 31, 2021, the company has long-term debt of Rs.18.37 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.1,153.42 crore as on March 31, 2021, as against Rs.962.71 crore as on March 31, 2020. The gearing when adjusted to investments in group companies also stayed strong (adjusted overall gearing of 0.25x) as on March 31, 2021.

PBILDT interest coverage and total debt/gross cash accrual remained comfortable at 43.24x and 1.11x in FY21 from 10.08x and 1.12x in FY20, respectively.

### **Modest scale of operations albeit stable revenue and profitability**

KSL has modest scale of operations with total operating income (TOI) witnessing marginal growth in FY21 (refers to the period April 1 to March 31) of 0.57% year-on-year (Y-o-Y) to Rs.1,217.73 crore on account of increasing demand from the automotive segment from H2FY21.

KSL improved its profitability margin majorly on account of improvement in gross margins. The company's PBILDT (PAT) margins have remained in between 14.90% and 24.04% (8.2% and 15.59%) over the past five fiscal years through FY21. KSL's PBILDT margin improved to 24.04% in FY21 from 18.93% in FY20 majorly on account of lower raw material and consumable costs. The company is undertaking a backward integration project amounting to Rs.211 crore, to set up a new 200,000 TPA coke oven plant and 17-MW waste heat power plant. The project is expected to be commissioned by September 2022 which shall lead to reduction in cost of production with further improvement in profitability.

The company's profitability is partially constrained by its lack of backward integration in the form of any captive operational iron ore and coking coal mine or any long-term supply contracts with miners/ suppliers. Majority of the company's revenue is generated through group companies (around 53%), with Bharat Forge Limited and Kalyani Technoforge Limited being the largest customers having significant presence in auto sector. Furthermore, during H1FY22, the company earned a PAT of Rs.132 crore on a total revenue of Rs.875 crore.

### **Key Rating Weaknesses**

#### **Cyclicality inherent in the steel and end-user industries coupled with competition from unorganized players**

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.

#### **Susceptibility to volatility in raw material prices and forex risk**

Raw material consumption is the single-largest cost component for KSL (constituting about 45.23% of the total sales in FY21 as against 48.09% of total sales in FY20). 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.

#### **Exposure to the group companies in the form of investments**

KSL has invested in various group companies in the form of investments in equity shares, preference shares and debentures. The exposure to group companies was at Rs.144.21 crore as on March 31, 2021 (12.50% of the net worth as on March 31, 2021).

### **Industry outlook**

India is the second-largest crude steel producer in the world. India's crude steel production fell by 5.59% and finished steel production was flat at 95.12 MT in FY21 against 102.62 MT in FY20. Domestic steel demand was impacted by a slowdown in manufacturing activities during H1FY21 due to Covid-19 pandemic. However, post lockdown, the global commodity markets witnessed a sharp rebound with a continuous increase in prices. While the demand recovery, especially in China and other economies, was on the back of substantial government stimulus, the lockdowns and restrictions caused significant supply-side headwinds in terms of difficulty in procurement and movement of key raw materials resulting in reduced production across steel mills. The double whammy effect resulted in one of the sharpest and perhaps the fastest recoveries in the global steel prices, which was considered beyond the market's expectation. CARE Ratings expects the domestic steel demand to grow at a compounded annual growth rate (CAGR) of about 7.5% during the next 2-3 years. CARE Ratings further expects net sales

realization to remain healthy. As far as volumes growth is concerned, demand improvement and the low base effect of FY21 is likely to help improve the volumes of the domestic players. The solvency ratios of steel companies are expected to improve on account of accretion to net worth and healthy cash accruals along with continuous reduction in debt levels.

#### Liquidity: Strong

KSL is expected to generate healthy gross cash accruals against nil repayment obligations for the next two years. Furthermore, KSL had free cash and bank balance of Rs.625.12 crore as on March 31, 2021. 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 FY21. The average fund-based working capital utilization for the last 12 months through August 2021 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

#### Applicable Criteria

[Policy on default recognition](#)

[Financial Ratios – Non financial Sector](#)

[Liquidity Analysis of Non-financial sector entities](#)

[Rating Outlook and Credit Watch](#)

[Short Term Instruments](#)

[Steel](#)

#### 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 (Rs. crore)	FY20 (A)	FY21 (A)	H1FY22(UA)
Total operating income	1210.85	1217.73	874.89
PBILDT	229.21	292.73	205.69
PAT	137.12	190.30	131.73
Overall gearing (times)- Including lease liabilities	0.19	0.22	NA
Interest coverage (times)	10.08	43.24	30.88

<sup>^</sup>Includes acceptances/ Creditors on LC

A: Audited; UA: Unaudited

**Status of non-cooperation with previous CRA: Not Applicable**

**Any other information:** Not Applicable

**Rating History for last three years:** Please refer Annexure-2

**Covenants of rated instrument / facility:** Please refer Annexure-3

#### Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. 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+
Fund-based/Non-fund-based-Short Term		-	-	-	200.00	CARE A1+
Term Loan-Long Term		-	-	March 2026	181.99	CARE AA; Stable

**Annexure-2: Rating History of last three years**

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Fund-based - LT-Cash Credit	LT	150.00	CARE AA; Stable	1)CARE AA; Stable (07-Dec-21)	<b>1)CARE AA; Stable</b> (08-Oct-20)	1)CARE AA; Stable (30-Sep-19)	1)CARE AA; Stable (31-Oct-18)
2	Non-fund-based - ST-BG/LC	ST	300.00	CARE A1+	1)CARE A1+ (07-Dec-21)	1)CARE A1+ (08-Oct-20)	1)CARE A1+ (30-Sep-19)	1)CARE A1+ (31-Oct-18)
3	Fund-based/Non-fund-based-Short Term	ST	200.00	CARE A1+	1)CARE A1+ (07-Dec-21)	1)CARE A1+ (08-Oct-20)	1)CARE A1+ (30-Sep-19)	1)CARE A1+ (31-Oct-18)
4	Commercial Paper-Commercial Paper (Standalone)	ST	75.00	CARE A1+	1)CARE A1+ (07-Dec-21) 2)CARE A1+ (07-Oct-21)	1)CARE A1+ (08-Oct-20)	1)CARE A1+ (30-Sep-19)	1)CARE A1+ (31-Oct-18)
5	Fund-based - LT-External Commercial Borrowings	LT	-	-	-	1)Withdrawn (08-Oct-20)	1)CARE AA; Stable (30-Sep-19)	1)CARE AA; Stable (31-Oct-18)
6	Term Loan-Long Term	LT	181.99	CARE AA; Stable	1)CARE AA; Stable (07-Dec-21)	1)CARE AA; Stable / CARE A1+ (08-Oct-20)	1)CARE AA; Stable / CARE A1+ (30-Sep-19)	-

\* Long Term / Short Term

**Annexure-3: Detailed explanation of covenants of the rated instrument / facilities - NA****Annexure 4: Complexity level of various instruments rated for this company**

Sr. No	Name of instrument	Complexity level
1	Fund-based - LT-Cash Credit	Simple
2	Fund-based/Non-fund-based-Short Term	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 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 CARE Ratings:

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