Kalyani Steels Limited

December 05, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	331.99	CARE AA; Stable	Reaffirmed
Short-term bank facilities	500.00	CARE A1+	Reaffirmed
Commercial paper	75.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The reaffirmation of the ratings assigned to the bank facilities and instruments of Kalyani Steels Limited (KSL) continues to derive strength from the experience and resourcefulness of its promoters, the Pune-based Kalyani Group, and the four-decade-long and established track record of KSL in the manufacturing of quality engineering grade carbon and specialty steel products. The ratings further consider KSL's strong financial and operational risk profiles marked by the robust capital structure, comfortable debt coverage metrics and close to optimum levels of the plant capacity utilisation over the past few fiscals.

The total operating income (TOI) has grown by 12% in FY23 (refers to the period April 1 to March 31) with the revival in demand from auto original equipment manufacturers (OEMs). However, the margins have declined due to volatility in raw material prices, especially coking coal and other ferro alloy products during most part of FY23. However, in absolute terms, KSL has consistently earned a minimum profit before interest, lease rentals, depreciation and taxation (PBILDT) above ₹200 crore over the past several fiscals.

The company benefits from established selling arrangements with approved vendor status from OEMs and arrangements with suppliers for procurement of raw material albeit absence of long-term contracts. The sales to group companies constituted 58% of net sales in FY23. The ratings also positively consider the successful commissioning of the backward integration project of 200,000 TPA coke oven plant and 17-MW waste heat recovery-based power plant which will further contribute to KSL's cost optimisation initiatives. The liquidity continues to be strong supported by cash and liquid investments of ₹590.70 crore as on September 30, 2023, and moderately utilised bank lines providing sufficient cushion in terms of funding requirements. Net debt has been consistently negative over the past few fiscals.

The above rating strengths are, however, tempered by the company's presence in the cyclical steel industry, susceptibility to significant volatility in raw material prices and 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: Factors likely to lead to rating actions

Positive factors - Factors likely to lead to positive rating action

- 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 likely to lead to negative rating action

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

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

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

Outlook: Stable
Stable outlook reflects that the rating entity is likely to sustain stable operating performance owing to continued strong demand from group companies and external customers as well. The company is expected to sustain its strong financial risk and liquidity profile amidst healthy cash flow generation from the operations.

Detailed description of the key rating drivers:

Key strengths

Strong promoter group coupled with long track record in iron and steel industry
KSL is a part of the Kalyani group and is spearheaded by 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 RK Goyal (MD) and Balmukand Maheshwari (CFO) who are associated with KSL since more than eight years.

Established selling arrangements
KSL is promoted as backward integration unit of the Kalyani group from which majority of the steel requirements for the group companies is met through. Moreover, long-standing relationship with major OEMs along with approved vendor status continues to garner KSL with repeat orders. The Kalyani group companies together accounted for around 58% of the net sales in FY23 (refers to the period April 1 to March 31). The customer concentration is high with significant revenues derived from group companies (Bharat Forge Limited and Kalyani Technoforge Limited). However, the company has large customer base and has repeat orders from external customers as well.

Steady performance along-side moderate profitability
The domestic demand for alloy steel has improved on the back of strong demand from auto industry, and resultantly, KSL has seen 13% YoY growth in volumes for rolled products during FY23. The TOI reached ₹1,899 crore in FY23 and ₹998.44 crore in H1FY24. There was correction in the domestic finished steel prices during FY23 after government export duty restrictions were imposed from May 2022 to November 2022. The realisations were, however, maintained by players in this space, as there was significant volatility in the input prices of imported coking coal/coke due to the Russia-Ukraine conflict. Coal, coke and fines (which contribute around 60% of overall raw material cost) witnessed 40% increase in the prices on per tonne basis. While prices of iron ore and fines (which contribute around 17% of the overall raw material cost) declined by 28% in FY23 on per tonne basis. Henceforth, the PBILDT margin of KSL deteriorated from 19.41% in FY22 to 12.87% in FY23. Though the profit after tax (PAT) margins also have reduced, they are still quite comfortable at 8.79% for FY23. Going ahead, CARE Ratings expects the margins to gradually improve, on the back of continued demand and steady-state raw material prices.

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. Although majority of the raw materials have been sourced from few suppliers representing concentration risk, 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. Furthermore, due to fluctuation in the prices of imported coal/ coke/ coke fines during FY23, gross margin for the company declined by 552 bps. However, KSL has been able to pass on the increase in raw material prices to its customers, albeit with a lag effect which had some effect on the profitability.

Robust capital structure and comfortable debt coverage metrics

The capital structure of KSL remained robust with debt to equity ratio and overall gearing (including LC backed creditors) of 0.14x and 0.42x, respectively, as on March 31, 2023 (as against 0.14x and 0.53x for March 31, 2022). The term loan comprises foreign currency loan availed by the company during FY22 to fund the projected capital expenditure of ₹211 crore. The fund-based working capital utilisation is also minimal. The net worth of the company stood at ₹1,489.16 crore as on March 31, 2023, as against ₹1,367.04 crore as on March 31, 2022. Furthermore, KSL continues to have healthy debt coverage indicators with PBILDT interest coverage and total debt/gross cash accrual (TD/GCA) of 8.70x and 2.97x in FY23 as against 24.93x and 2.57x in FY22.

Key weaknesses

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 the 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 unorganised players and Chinese imports. CARE Ratings notes that KSL, being in niche segment providing specialty steel, remains 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 organised and unorganised players and expanding applications of steel products. The margins continue to remain under pressure due to the 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

The raw material consumption is the single-largest cost component for KSL. 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: Superior

KSL is expected to generate healthy GCA against minimal repayment obligations over the next two years. Furthermore, KSL had free cash and bank balance of ₹590.70 crore as on September 30, 2023. Additional liquidity cushion is available in the form of largely unutilised lines of credit. The average fund-based working capital utilisation and non-fund-based limit utilisation for the last 12 months ended October 2023 was around 7% and 28%, respectively. This was majorly on account of managing working capital requirements through internal accruals and creditors' support backed by letter of credit.

Assumptions/Covenants Not applicable

Environment, social, and governance (ESG) risks

	Risk factors
Environmental	**Greenhouse gas emissions: High** The GHG emissions have been 0.59 mn metric tonnes for scope-1 and 21.8k tonnes for scope-2. However, such emissions are common in the steel manufacturing industry. The Company used 5.736 crore units of renewable energy to replace equivalent number of units from Karnataka Power Transmission Corporation Limited (KPTCL) Grid Power. **Energy conservation: Adequate** Energy intensity (total energy consumption by turnover) has been reduced by 7% in FY23 as compared with FY22.
Social	**Safety standards: Adequate** Adequate standards are maintained as indicated by nil fatalities and zero lost-time injury frequency rate over the past two fiscals. **Employee training: Done** All the employees were given training on health and safety measures. While multiple skill upgradation trainings have been conducted for all the workers (non-permanent).
Governance	**Board independence: Adequate** 50% of the board comprises of independent members as on March 31, 2023. **Board attendance: Good** The attendance rate for majority of the members (especially non-promoters) was 100% for the four meetings held during fiscal 2023.

Applicable criteria

Policy on default recognition
Factoring Linkages Parent Sub JV Group
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Manufacturing Companies
Steel
Policy on Withdrawal of Ratings

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Commodities	Metals & Mining	Ferrous metals	Iron & steel

Incorporated in 1973, KSL is a part of the Pune (Maharashtra)-based Kalyani group. The company is spearheaded by 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 (₹ crore)	FY2022 (A)	FY2023 (A)	H1FY2024 (UA)
Total operating income	1,697.05	1,899.30	998.44
PBILDT	329.32	244.50	207.04
PAT	242.92	167.03	119.57
Overall gearing (times)	0.53	0.42	-
Interest coverage (times)	24.93	8.70	13.25

A: Audited UA: Unaudited; Note: 'the above results are latest financial results available'

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

Complexity level of various instruments rated: Annexure-4

Lender details: Annexure-5

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
Commercial paper-Commercial paper (Standalone)	-	Proposed	-	7-365 days	75.00	CARE A1+
Fund-based - LT-Cash credit	-	-	-	-	150.00	CARE AA; Stable
Fund-based/Non-fund-based-Short term	-	-	-	-	200.00	CARE A1+
Non-fund-based - ST-BG/LC	-	-	-	-	300.00	CARE A1+
Term loan-Long term	-	-	-	31-03-2026	181.99	CARE AA; Stable

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 2023-2024	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
1	Fund-based - LT-Cash credit	LT	150.00	CARE AA; Stable	-	1)CARE AA; Stable (06-Dec-22)	1)CARE AA; Stable (17-Jan-22) 2)CARE AA; Stable (07-Dec-21)	1)CARE AA; Stable (08-Oct-20)
2	Non-fund-based - ST-BG/LC	ST	300.00	CARE A1+	-	1)CARE A1+ (06-Dec-22)	1)CARE A1+ (17-Jan-22) 2)CARE A1+ (07-Dec-21)	1)CARE A1+ (08-Oct-20)
3	Fund-based/Non-fund-based-Short term	ST	200.00	CARE A1+	-	1)CARE A1+ (06-Dec-22)	1)CARE A1+ (17-Jan-22) 2)CARE A1+ (07-Dec-21)	1)CARE A1+ (08-Oct-20)
4	Commercial paper-Commercial paper (Standalone)	ST	75.00	CARE A1+	-	1)CARE A1+ (06-Dec-22)	1)CARE A1+ (07-Dec-21) 2)CARE A1+ (07-Oct-21)	1)CARE A1+ (08-Oct-20)
5	Fund-based - LT-External commercial borrowings	LT	-	-	-	-	-	1)Withdrawn (08-Oct-20)
6	Term loan-Long term	LT	181.99	CARE AA; Stable	-	1)CARE AA; Stable (06-Dec-22)	1)CARE AA; Stable (17-Jan-22) 2)CARE AA; Stable	1)CARE AA; Stable / CARE A1+ (08-Oct-20)

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	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
							(07-Dec-21)	

*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

Sr. No.	Name of the Instrument	Complexity Level
1	Commercial paper-Commercial paper (Standalone)	Simple
2	Fund-based – LT-Cash credit	Simple
3	Fund-based/Non-fund-based-Short term	Simple
4	Non-fund-based – ST-BG/LC	Simple
5	Term loan-Long term	Simple

Annexure-5: Lender details

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

Note on the 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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