Arfin India Limited

July 02, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	2.61 (reduced from Rs.7.75 crore)	CARE BBB; Stable (Triple B; Outlook: Stable)	Reaffirmed
Long-term/ Short-term Bank Facilities	120.00 (enhanced from Rs.84.00 crore)	CARE BBB; Stable/ CARE A3+ (Triple B; Outlook: Stable/ A Three Plus)	Reaffirmed
Total Facilities	122.61 (Rupees One Hundred Twenty Two crore and Sixty One lakh only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Arfin India Limited (AIL) continue to derive strength from experience of its promoters in the business of manufacturing ferrous and non-ferrous metals, established relationship with reputed clients being an organized player in the fragmented aluminium recycling industry, gradual diversification in its product portfolio to cater varied requirements across multiple industries and its moderate capital structure which, however, deteriorated to some extent as on end-FY19 due to increased debt levels on account of higher working capital intensity.

The ratings, however, remain constrained on account of vulnerability of AIL's profitability to volatility in raw material prices, fluctuation in foreign exchange rates, customer concentration risk and its presence in a fragmented and competitive aluminium recycling industry. The ratings are further tempered by the decline in AIL's total operating income (TOI) during FY19 on account of lower sales volume which coupled with increase in operating overheads translated into decline in operating profitability and consequent weakening of its debt coverage indicators. The ratings also factors in the increase in AIL's debt levels on account of higher working capital intensity and sizeable capex undertaken by the company during FY19, which also resulted in moderation in its liquidity.

AIL's ability to improve its operating profitability on a sustained basis in a competitive aluminium recycling industry, diversify its customer base and end user industry application along with efficient management of its working capital requirements and improvement in its debt coverage indicators shall be the key rating sensitivities. Any large sized capex and its funding pattern shall also be a key credit monitorable.

Detailed description of the key rating drivers

Key Rating Strengths

Vast experience of the promoters in the manufacturing of ferrous and non-ferrous metals: AIL's promoter, Mr. Mahendra R. Shah (Chairman), has more than two decades of experience in the manufacturing of aluminium products, ferrous and non-ferrous metals. He presently looks after the entire operations of the company and is assisted by his son Mr. Jatin M. Shah (Managing Director) along with qualified and experienced second tier management personnel. The promoters are also associated with other sister concerns namely Krish Ferro Industries Private Limited and Mahendra Corporation which are engaged in similar line of business.

Gradual diversification in product portfolio to cater to requirements of multiple sectors: AIL has presence in multiple product-segment of aluminium industry. The two main products of the company i.e. aluminium wire rod and aluminium deox together contributed nearly 49% of its sales in FY19, which reduced from 66% in FY18. Over the last two years, the company has gradually diversified its product portfolio with addition of products including master & ferro alloys and aluminium conductors & cables. With a diversified product portfolio, AIL caters to the demand of steel, automobile, power and foundry industries. The company majorly operates in domestic market with pan-India presence and it also exports its products to Japan, Middle-East and African countries.

Moderate capital structure: AIL's overall gearing deteriorated from 1.24x as on end FY18 to 1.45x as March 31, 2019, which however, still continued to remain moderate. The deterioration was driven by higher bank borrowings availed to meet its increased working capital requirements.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Key Rating Weaknesses

Decline in operating profitability (PBILDT) during FY19: AIL's total operating income (TOI) declined by 11% y-o-y in FY19, primarily on account of lower sales volume during the year, including that to one of its key customer, Essar Steel Ltd. (ESL). This along with increase in overheads, including demurrage charges paid on account of delay in lifting of imported raw material (which was ordered expecting growth in sales volumes), which were not fully absorbed due to reduced scale of operations led to decline in AIL's PBILDT margin by 399 bps to 5.82% during the year. The delay in lifting of raw material was largely due to restricted availability of funds for working capital requirements. Also, AIL undertook a sizeable capex of around Rs.16.30 crore in FY19, which was funded largely through cash flow from its operations, thereby restricting the funds available to meet its payment commitments for raw material purchase. Increase in employee costs and other fixed expenses amidst decline in its TOI also contributed to the lower operating profitability. The decline in operating profitability also translated into lower PAT margin for the company which was accentuated during Q4FY19 when AIL posted a net loss of Rs.1.21 crore (cash loss of Rs.0.76 crore).

Deterioration in debt coverage indicators: AIL's debt coverage indicators deteriorated in FY19 marked by TD/GCA of 13.56x in FY19 (compared with 4.36x in FY18) and interest coverage of 2.07x in FY19 (compared with 4.93x in FY18). This was driven by decline in AIL's operating profitability and cash accruals coupled with increase in outstanding debt (with higher working capital borrowings) and interest costs.

Moderation in liquidity: AIL's liquidity moderated in FY19 due to lower cash accruals, delay in realization of receivables from one customer as well as on account of funding the sizeable capex undertaken during the year which was not previously envisaged through cash flow from operations, thereby reducing the funds available to meet the increased working capital requirements. The utilization of working capital limits was high at more than 90% during the trailing 12 months ended May 2019 (compared with 73% during the trailing 12 months ended April 2018), underlining the moderation in its liquidity. Also, its quick ratio deteriorated from 0.73 times as on March 31, 2018 to 0.49 times as on March 31, 2019. While AIL's inventory holding increased as on March 31, 2019 compared to a year ago, it was only partly offset by the reduction in its trade receivables; thereby its working capital cycle elongated from 88 days in FY18 to 121 days in FY19. Receivables outstanding for more than six months stood at Rs.10.72 crore as on March 31, 2019. However, AIL's liquidity eased to some extent with sanction of additional bank limits towards the end of March 2019. Further, AIL has limited principal requirements during the next year, which is expected to provide some cushion to its liquidity.

High customer and end-user industry concentration: Despite gradual diversification in product portfolio and end user industry, AIL's dependency on steel sector remained high. The steel sector contributed nearly 68% of its total operating income during FY19, followed by automobile and power sectors which contributed 20% and 8% respectively. Further, AIL also faces high customer concentration with top five customers contributing around 66% of the total sales during FY19; albeit some of its clientele are reputed players in their respective industries.

Exposure to price volatility in raw materials and foreign exchange fluctuation risk: The main raw material for AIL is aluminium scrap which it imports mainly from European countries, whereas its sales is majorly in the domestic market which exposes AIL's profitability to exchange rate fluctuations. Also, the raw material prices are linked to international commodity indices, which exposes it to inherent volatility associated with aluminium prices, while its sales prices are dictated largely by the demand-supply in the domestic market for various products, exposing the company to adverse movement in prices which it may not be able to pass on to its customers.

Highly fragmented nature of industry characterized by intense competition: The spectrum of the aluminium industry in which the company operates is highly fragmented and competitive marked by presence of numerous small and unorganized players in India. Hence the players in the industry have a limited pricing power and are exposed to competitive pressure on their profitability. This apart, its products, largely being of intermediary usage, are subject to the risks associated with the industry cyclicality and price volatility.

Analytical approach: Standalone

Applicable Criteria

[Criteria on assigning Outlook to Credit Ratings]
[CARE's Policy on Default Recognition]
[Criteria for Short Term Instruments]
[Rating Methodology – Manufacturing Companies]
[Financial ratios – Non Financial Sector]

About the Company

Incorporated in 1992, Gujarat based AIL is promoted by Mr. Mahendra R. Shah. The company is engaged in manufacturing of aluminium products like aluminium wire rod, aluminium deox, cored wire, aluminium alloy ingots, conductors & cables from aluminium scrap. AIL's manufacturing facility is located at Chhatral near Gandhinagar in Gujarat with installed capacity of 58,500 MTPA as on March 31, 2019.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	466.97	413.44
PBILDT	45.81	24.08
PAT	21.70	6.56
Overall gearing (times)	1.24	1.45
Interest coverage (times)	4.93	2.07

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based - LT-Term Loan	-	-	2022	2.61	CARE BBB; Stable
Fund-based - LT/ ST-Cash Credit	-	-	-	117.50	CARE BBB; Stable / CARE A3+
Fund-based - LT/ ST-Cash Credit	-	-	-	2.50	CARE BBB; Stable / CARE A3+

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT/ ST-Cash Credit	LT/ST	117.50	CARE BBB; Stable / CARE A3+	1)CARE BBB; Stable (05-Jun-19)	1)CARE BBB+; Negative (22-Feb-19) 2)CARE BBB+; Stable (22-Jun-18)	1)CARE BBB; Positive (16-Oct-17)	-
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	2.50	CARE BBB; Stable / CARE A3+	1)CARE A3+ (05-Jun-19)	1)CARE A2 (22-Feb-19) 2)CARE A2 (22-Jun-18)	1)CARE A3+ (16-Oct-17)	-
3.	Fund-based - LT-Term Loan	LT	2.61	CARE BBB; Stable	1)CARE BBB; Stable (05-Jun-19)	1)CARE BBB+; Negative (22-Feb-19) 2)CARE BBB+; Stable (22-Jun-18)	-	-

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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