Electrosteel Castings Limited

Novemebr 20, 2018

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long term Bank Facilities	1487.51 (reduced from 1553.69)	**CARE BBB+; Stable (Triple B Plus; Outlook: Stable)**	**Rating Reaffirmed; Outlook revised from Negative**
Long/Short-term Bank Facilities	877.50 (reduced from 909.00)	**CARE BBB+; Stable/CARE A2 (Triple B Plus; Outlook: Stable /A Two)**	**Rating Reaffirmed; Outlook revised from Negative**
Total	**2,365.01 (Rupees Two Thousand Three Hundred Sixty Five crore and One lakh)**		
Non-convertible debenture (Series IV)	**-**	**-**	**Withdrawn^**

Details of instruments/facilities in Annexure-1

(^) The company has repaid the NCD (series IV) and there is no amount outstanding under the said issue.

Detailed Rationale & Key Rating Drivers

The revision in outlook from negative to stable takes into account order of court for verification of claim raised in respect of funds blocked in de-allocation of coal block within given time frame, infusion of funds by promoters, prepayment of part of debt and improved performance in H1FY19. Further, Electrosteel Steels Ltd, ceased to be an associate, post implementation of resolution plan approved by National Company Law Tribunal, and Electrosteel Castings Ltd (ECL) has substantially written down the exposure at its the fair value.

The ratings assigned to the bank facilities of ECL continues to take into account the experienced promoters with a long track record of operations and established position in the domestic & international ductile iron pipe segment, satisfactory capacity utilisation and satisfactory order-book position. However, the ratings are tempered by volatility in prices of inputs, weak debt coverage indicators, funds blocked in coal blocks and iron ore lease, working capital intensive nature of operations and exposure of the company to foreign exchange fluctuations.

Going forward, its ability to manage liquidity to repay its debt in light of the weak debt coverage indicators, adequate and timely receipt of the funds from the de-allocated captive coal block are the key rating sensitivities.

CARE has withdrawn the rating assigned to the non-convertible debentures (series IV) with immediate effect, as the company has repaid the aforementioned instrument rated by us and there is no amount outstanding under the instrument as on date. The rating has been withdrawn post receipt of No dues certificate from the subscriber of the instrument.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters with a long track record of operations

Electrosteel group, a leading industrial house of Eastern India, is engaged in production of DI pipes and providing techno-economic solutions for water transportation & sewerage management. ECL, the flagship company of the group has a track record of more than five decades with the company having first commenced its operations in May, 1959 with the manufacturing of CI pipes and gradually diversifying into production of Ductile Iron (DI) pipes over the years.

Established position of the group in the DI pipe segment

ECL along with its associate Srikalahasthi Pipes Ltd (SPL; CARE AA-;Stable/CARE A1+) has an established position in the domestic and international DI pipe market with an aggregate DI pipe production capacity of 5,80,000 mtpa *(ECL – 2,80,000 mtpa and SPL – 3,00,000 mtpa)*. While ECL with its manufacturing facilities caters to the Eastern and Northern market, SPL (CARE AA-;Stable/CARE A1+)with its manufacturing facilities in Andhra Pradesh focuses on the Southern and Western region.

ECL's fund based exposure to subsidiary/associate companies in the form of investments, receivables and loans & advances (including security deposits) as on March 31, 2018 was ~36% of the net worth. However, out of the above Rs.455.29 crore was investment in group company Srikalahasthi Pipes Ltd (CARE AA-;Stable/CARE A1+). The net advances and receivables in the fund based exposure majorly included receivables from foreign subsidiaries. ECL makes it export sales through the subsidiaries wherein the receivables period is very high.

Strong order book position providing revenue visibility

As on July 30, 2018, ECL had an order book of around Rs.1135 crore, which is to be executed over the next six to seven months thereby providing revenue visibility. ECL's clientele includes water & sewerage divisions of various State

Governments, local municipal bodies and construction companies. A portion of the Govt. orders have inbuilt 'price escalation clause' for movement in prices of pig iron (the major constituent of the final product) which provides shield against the rise in the prices of the inputs.

Satisfactory Capacity Utilisation and improvement in performance in H1FY19:

The capacity utilization of the company has consistently remained at about 100% in the last few years on the back of the high inflow of the orders for DI pipe. Further, efficient management of resources led to an achievement of higher production levels over the years. The sales of DI and CI Pipes contributed about 77% to the total net sales of the company in FY18. Apart from selling DI and CI Pipes, the company is also involved in selling DI fittings and in engineering, procurement and construction (EPC) projects on a turnkey basis, selling of molten metal/pig iron over and above its captive requirement, trading of coal & other products.

Total operating income of ECL increased y-o-y by 7.38% in FY18 on account of increase of revenue from turnkey contracts, DI Fittings, trading sales and sale of pig iron. Despite increase in realizations, revenue from the pipe segment remained in line to that in FY17 due to relative decrease in sales volume.

The PBILDT margin deteriorated in FY18 due to increase in cost of main raw materials- coal and iron ore, which the company was not able to fully pass on to its customers. Continued interest burden with increase in more rupee term loans to repay the ECB loan resulted in increase in interest cost, despite decrease in long term debt. This weighed down PAT and PAT margin also deteriorated in FY18. The interest coverage mirrored the trend, deteriorating from 1.43x in FY17 to 1.23x in FY18.

In H1FY19, the company reported a PBILDT of Rs.164.66 crore against operating income of Rs.1,052.74 crore. Although the cost of raw materials coal and iron ore increased, increase in realization of DI pipes helped improve PBILDT margins.

Key Rating Weaknesses

Volatility in input price

Raw material consumption forms the single largest cost component for ECL. Upon de-allocation of the coal mines and further delay in the receipt of the environmental clearance for the iron ore mines, the company has to resort to the open market for meeting its requirement of the key inputs (*iron ore and coal*) at the prevailing market prices. Hence, any adverse movement in raw material price without any corresponding movement in finished good price might affect the profitability of the company. The prices of finished goods generally move in tandem with that of raw materials, however, due to order based nature of the business there exists a time lag. This exposes the company to risk arising on account of volatility in the raw material prices.

Weak debt coverage indicators

Although the capital structure remained comfortable due to the high net worth with overall gearing at 0.88x as on March 31, 2018, the company's debt coverage indicators remained weak due to high debt repayment obligations vis-à-vis its accruals. Gross Cash Accruals (GCA) fell by around 19% in FY18 followed by increase of 27% during H1FY19 over the corresponding period.

The total debt/GCA of the company remained high and deteriorated to 18.58x as on March 31, 2018 and then improved to 15.11x as on Sep 30, 2018.

The company has availed external term debt in June 2018 to meet its debt obligations. The company also issued shares of Rs.140 crore on a preferential basis in August 2018. Out of the above, Rs.40 crore has been infused by the promoters. In last 12 months ended June 2018, ECL's average utilization of cash credit facilities stood at 59.03%. The company has prepaid a part of its debt in October 2018.

Funds blocked in coal block

The Company had a captive coal block at Parbatpur, Jharkhand which was under advanced stage of implementation. However, as per the Supreme Court such coal block was de-allocated with effect from April 1, 2015 and the company has filed its claims for compensation for Rs.1531.76 crore. Against the said expenditure, the company has received interim payment of Rs.84.20 crore. Further, in September 2018, the Delhi High court has directed the nominated authority to complete the valuation process to ascertain/validate the claim of Rs.1531.76 crore and forward it to Ministry of Coal for further action w.r.t disbursal within a given time frame. Going forward, the timely recovery of the same would be key a rating sensitivity.

Working capital intensive nature of operations

The business of the company is working capital intensive in nature on account of higher collection period and higher inventory days. The high collection period is on account of the customer's profile mainly being Government bodies, where the payment terms remains stretched. The company has to extend higher credit terms to the export customer and as the company derives major portion of the sales through exports, the collection period also remains stretched. Further, export sales also involves higher collection period (as there is considerable time gap between despatch and final acceptance). The operating cycle improved from 170 days in FY17 to 139 days in FY18.

Exposure towards foreign exchange risk
ECL has forex exposure in the form of forex payable (for import of coking coal), foreign currency borrowings (in the form of External Commercial borrowings, mainly for capex programme) and forex receivable (for export of DI Pipes and Fittings). The company hedges its entire foreign currency loan repayable over the next one year through forward and option. Although the exports of the final goods and import of the raw materials provide a natural hedge to the company and mitigate the foreign exchange fluctuation risk to a certain extent, the timing difference of the exports and imports exposes the company towards volatile foreign currency movement.

Analytical approach: Standalone Approach.

Applicable Criteria
[Criteria on assigning Outlook to Credit Ratings]
[CARE's Policy on Default Recognition]
[Criteria for Short Term Instruments]
[Rating Methodology-Manufacturing Companies]
[Policy on Withdrawal of ratings]

About the Company
Incorporated in November 1955 and under the management of Umang Kejriwal & family of Kolkata, the current promoters, since 1965, Electrosteel Castings Limited (ECL) commenced its manufacturing activity in May, 1959 with the commissioning of Cast Iron (CI) pipes manufacturing unit. Currently, the company is operating DI Pipe facility with an installed capacity of 2,80,000 tonnes per annum; Pig Iron facility of 2,50,000 tonnes per annum and LAMC facility of 2,95,000 tonnes per annum with the manufacturing facilities spread across four locations in India.

Brief Financials (Rs. crore)- Standalone	FY17 (A)	FY18 (A)
Total operating income	1,805.36	1,938.66
PBILDT	287.99	248.45
PAT	77.28	46.99
Overall gearing (times)	1.06	0.88
Interest coverage (times)	1.43	1.23

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

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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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
Term Loan-Long Term	-	-	June 2025	947.51	CARE BBB+; Stable
Fund-based - LT-Cash Credit	-	-	-	540.00	CARE BBB+; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	789.00	CARE BBB+; Stable / CARE A2
Non-fund-based - LT/ ST-BG/LC	-	-	-	88.50	CARE BBB+; Stable / CARE A2
Debentures-Non Convertible Debentures	July 05, 2013	11%	July 5, 2018	0.00	Withdrawn

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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Term Loan-Long Term	LT	947.51	CARE BBB+; Stable	-	1)CARE BBB+; Negative (06-Oct-17)	1)CARE BBB+ (28-Oct-16) 2)CARE A (15-Apr-16)	1)CARE A (09-Oct-15)
2.	Commercial Paper-Commercial Paper (Carved out)	ST	-	-	-	1)Withdrawn (06-Oct-17)	1)CARE A2 (28-Oct-16)	1)CARE A1 (09-Oct-15)
3.	Fund-based - LT-Cash Credit	LT	540.00	CARE BBB+; Stable	-	1)CARE BBB+; Negative (06-Oct-17)	1)CARE BBB+ (28-Oct-16) 2)CARE A (15-Apr-16)	1)CARE A (09-Oct-15)
4.	Non-fund-based - LT/ ST-BG/LC	LT/ST	789.00	CARE BBB+; Stable / CARE A2	-	1)CARE BBB+; Negative / CARE A2 (06-Oct-17)	1)CARE BBB+ / CARE A2 (28-Oct-16) 2)CARE A / CARE A1 (15-Apr-16)	1)CARE A / CARE A1 (09-Oct-15)
5.	Non-fund-based - LT/ ST-BG/LC	LT/ST	88.50	CARE BBB+; Stable / CARE A2	-	1)CARE BBB+; Negative / CARE A2 (06-Oct-17)	1)CARE BBB+ / CARE A2 (28-Oct-16) 2)CARE A / CARE A1 (15-Apr-16)	1)CARE A / CARE A1 (09-Oct-15)
6.	Debentures-Non Convertible Debentures	LT	-	-	-	-	1)Withdrawn (28-Oct-16)	1)CARE A (09-Oct-15)
7.	Commercial Paper-Commercial Paper (Standalone)	ST	-	-	-	1)Withdrawn (06-Oct-17)	1)CARE A3+ (28-Oct-16)	1)CARE A2+ (09-Oct-15)
8.	Debentures-Non Convertible Debentures	LT	-	-	-	1)CARE BBB+; Negative (06-Oct-17)	1)CARE BBB+ (28-Oct-16)	1)CARE A (09-Oct-15)
9.	Commercial Paper-Commercial Paper (Carved out)	ST	-	-	-	1)Withdrawn (06-Oct-17)	1)CARE A2 (28-Oct-16)	1)CARE A1 (09-Oct-15)

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