Kalyani Steels Limited

September 30, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Ratings[1]**	**Rating Action**
Long Term Bank Facilities	158.99 (reduced from 192.41)	**CARE AA; Stable (Double A; Outlook : Stable)**	**Reaffirmed**
Short Term Bank Facilities	500.00	**CARE A1+ (A One Plus)**	**Reaffirmed**
Long term/ short term bank facilities*	33.00	**CARE AA; Stable/CARE A1+ (Double A; Outlook : Stable/A One Plus)**	**Reaffirmed**
Total	**691.99 (Rs. Six hundred ninety one crore and ninety nine lakh only)**		
Commercial Paper-Proposed#	**75.00** (**Rs. Seventy Five Crore Only**)	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1
** Change in nature of facilities*
 # carved out of sanctioned working capital limits of the company.

Detailed Rationale & Key Rating Drivers

The reaffirmation of ratings to 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 & alloy steel. The ratings also derive strength from the comfortable financial risk profile marked by stable revenues and profitability during FY19 (refers to April 01 to March 31) and Q1FY20 (UA, refers to April 01 to June 30), comfortable capital structure and debt coverage indicators coupled with strong liquidity position.
The ratings also takes cognizance of established selling arrangements with approved vendor status from major OEMs and arrangement with suppliers for procurement of raw material albeit absence of long term contracts continues.
The above rating strengths are, however, tempered by company's presence in highly cyclical steel industry, lack of any backward integration in the form of captive iron ore and coal mines, susceptibility to volatility in raw material prices & foreign exchange rates, exposure to the group companies in the form of investments, modest scale of operations and susceptibility to slowdown in the end user industries.

Going forward, any large incremental debt funded capital expenditure by KSL deteriorating its capital structure and debt coverage indicators from current levels would be key rating sensitivity. The ability of the company to increase its scale of operations as envisaged while sustaining its profitability on the back of headwinds faced by end user industries such as automobile would remain a key rating sensitivity.
In addition, any further exposure to group companies shall remain key rating monitorable.

Detaild 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 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 six years.

Modest scale of operations albeit marginal increase revenue and stable profitability margins during FY19 and Q1FY20

KSL registered a marginal growth in total operating income to Rs.1411.99 crore in FY19 from Rs.1401.84 crore in FY18 aided by better realizations for the end products. However, scale of operations remains to be modest. PBILDT margin increased

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

marginally from 14.90% in FY18 to 15.39% in FY19. PAT margin for FY19 stood at 13.63% as against 12.45% in FY18 backed by lower interest costs and extraordinary income of Rs.11.92 crore. KSL registered a y-o-y growth of ~7% in TOI to Rs.348.26 crore in Q1FY20 as against Rs.325.98 crore in Q1FY19. The company registered a PBILDT margin of ~19% in Q1FY20 as against ~16% in Q1FY19. KSL reported a PAT margin of 10.51% in Q1FY20 as against 8.60% in Q1FY19.

Comfortable capital structure and debt coverage metrics
Capital structure of KSL has remained comfortable with debt to equity and overall gearing below unity as on March 31, 2019. While the debt to equity has improved to 0.02x as on March 31, 2019 (0.08x as on March 31, 2018); overall gearing (including acceptances on LC) improved to 0.27x as on March 31, 2019 as against 0.43x as on March 31, 2018. Capital structure of the company improved on account of scheduled repayment of foreign currency term loans coupled with accretion of profits to reserves. Further, KSL continues to have comfortable debt coverage indicators with TDGCA at 1.42x as at March 31, 2019 as against 2.24x as at March 31, 2018 and Total Debt/ PBILDT at 1.09x as at March 31, 2019 as against 1.62x as at March 31, 2018. Interest coverage stood comfortable at 32.81x in FY19 as against 24.19x in FY18. Going forward, any large incremental debt funded capital expenditure by KSL deteriorating its capital structure and debt coverage indicators from current levels would be key rating sensitivity.

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 top five clients contribute 65-75% of the total sales during FY19. Kalyani Group companies accounted for ~60-65% of total revenue in FY19.

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 and iron ore/iron ore fines. Further, diversified supplier base is also evident from the fact that the single largest supplier constitutes around 18-20% of the total raw-material requirement with top five suppliers supplying 25-30% of the total requirement of KSL during FY19 which is in line with FY18. However, absence of any long term contracts with supplies continues.

Liquidity – Strong
Liquidity of KSL is marked by strong cash accruals against minimal repayment obligation. KSL had free cash and bank balance of Rs.37.86 crore as on March 31, 2019 as against Rs.33.02 crore as on March 31, 2018. Furthermore, KSL had liquid investments (Mutual funds) of Rs.203.57 crore as on March 31, 2019 as against Rs.117.62 crore as on March 31, 2018. Additional liquidity cushion is available in the form of unutilized lines of credit. The average Cash Credit utilization for the last 12 months ended March 31, 2019 stood low at ~2%.

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 80% of revenue from auto segment which is also cyclical in nature. Also, the customers of KSL remain vulnerable to pricing pressures from large OEMs which in turn may have adverse impact on profitability margins. Competition plays a role in the profitability of steel manufacturer's mainly arising out of unorganized players and Chinese imports. Given the scenario of rising Chinese steel dumping, it has become imperative to focus on cost reduction and quality improvement to remain competitive in current market and to maintain margins.

Susceptibility to volatility in raw material prices and forex risk
Raw material consumption is the single largest cost component for KSL (constituting about 67% of total cost of sales in FY19 as against 58% of total cost of sales in FY18). 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 scrap. Coking coal and iron ore prices fluctuate globally on a demand-supply basis which generally impact the profitability margins of the large and mid/small steel manufacturers. 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 remains to be a challenge.
KSL is exposed to foreign currency risks as the company is a net importer along with ECB repayments in USD. As on March 31, 2019, KSL has foreign currency liabilities of Rs.237.95 crore (including ECB loan and trade payables towards raw material) (PY: Rs.232.81 crore as on March 31, 2018). Further, FOB value of export sales stood at Rs.58.40 crore (Rs.20.12 crore in FY17).

Net exposure to foreign currency risk (liabilities) stood at ~Rs.233 crore as on March 31, 2019 (~Rs.214 crore as on March 31, 2018).

Exposure to the group companies in the form of investments
KSL has invested in various subsidiaries/group companies in the form of investments in equity shares, preference shares and debentures. The exposure to group companies was seen at Rs.162.43 crore as on March 31, 2019 (18.43% of the net worth as on March 31, 2019)

Industry Outlook
India's steel consumption is expected to grow by 5%-6% on the back of government's expenditure towards infrastructure and construction. With the same government coming to power, the focus will continue to remain on infrastructure development in the country. While the international steel prices has seen some softening during the last 6-8 months. However, the global prices may witness an upward trend, if the current trend of higher raw material prices, especially iron ore continues, provided trade war doesn't escalate. Consumption from auto sector will likely to see an upward trend in the latter half of FY20 which will further support the growth of steel industry.

Analytical approach: Standalone
Applicable Criteria
CARE's Criteria on assigning outlook and credit watch to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology - Manufacturing Companies
Rating Methodology - Steel Sector
Financial ratios – Non-Financial Sector
Rating Methodology: Factoring Linkages in Ratings

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 ~7 lakh metric tonne per annum (MTPA). The manufacturing facilities are shared with Mukand Limited (ML, part of Bajaj Group) with KSL holding 41.38% of the assets and ML holding the remaining.

Covenants of rated instrument / facility: NA

Brief Financials (Rs.crore) (Standalone)	FY18 (A)	FY19 (A)	Q1FY19 (UA)	Q1FY20 (UA)
Total operating income	1401.84	1411.99	325.98	348.26
PBILDT	208.89	217.40	52.57	66.59
PAT	114.88	132.05	28.04	36.61
Overall gearing (times)^	0.43	0.27	NA	NA
Interest coverage (times)	24.19	32.81	44.55	32.01

^Including Acceptances / Creditors on LC
A: Audited; UA: Unaudited;

Status of non-cooperation with previous CRA: ICRA has suspended rating assigned to the bank facilities of KSL and the commercial paper on account of ICRA's inability to carry out a rating surveillance in the absence of the requisite information from the company as per press release dated June 23, 2016.

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-Cash Credit	-	-	-	150.00	CARE AA; Stable
Non-fund-based - ST-BG/LC	-	-	-	300.00	CARE A1+
Non-fund-based - ST-BG/LC	-	-	-	200.00	CARE A1+
Fund-based - LT-External Commercial Borrowings	-	-	December 2019	8.99	CARE AA; Stable
LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	-	-	-	33.00	CARE AA; Stable / CARE A1+
Commercial Paper	-	-	Proposed	75.00	CARE A1+

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-Cash Credit	LT	150.00	CARE AA; Stable	-	1)CARE AA; Stable (31-Oct-18)	1)CARE AA; Stable (18-Aug-17)	1)CARE AA (28-Oct-16) 2)CARE AA (13-May-16)
2.	Non-fund-based - ST-BG/LC	ST	300.00	CARE A1+	-	1)CARE A1+ (31-Oct-18)	1)CARE A1+ (18-Aug-17)	1)CARE A1+ (28-Oct-16) 2)CARE A1+ (13-May-16)
3.	Non-fund-based - ST-BG/LC	ST	200.00	CARE A1+	-	1)CARE A1+ (31-Oct-18)	1)CARE A1+ (18-Aug-17)	1)CARE A1+ (28-Oct-16) 2)CARE A1+ (13-May-16)
4.	Commercial Paper	ST	75.00	CARE A1+	-	1)CARE A1+ (31-Oct-18)	1)CARE A1+ (18-Aug-17)	1)CARE A1+ (28-Oct-16) 2)CARE A1+ (13-May-16)
5.	Fund-based - LT-External Commercial Borrowings	LT	8.99	CARE AA; Stable	-	1)CARE AA; Stable (31-Oct-18)	1)CARE AA; Stable (18-Aug-17)	1)CARE AA (28-Oct-16) 2)CARE AA (13-May-16)
6.	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	LT/ST	33.00	CARE AA; Stable / CARE A1+	-	-	-	-

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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About CARE Ratings:
CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

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