
February 10, 2009**CARE REVISES THE RATING ASSIGNED TO VARIOUS ISSUES OF MUKAND LTD.**

CARE has revised the rating assigned to the Short-Term Debt (STD) issue of Mukand Limited (Mukand) aggregating Rs.75 crore, for a maturity not exceeding one year, to 'PR3 [PR Three] from the rating of 'PR2+' [PR Two Plus]. The STD issue is not carved out of the sanctioned working capital limits of the company.

Additionally, CARE has revised the rating assigned to the Long-term Bank Facilities of Mukand, aggregating Rs.855.51 crore, to 'CARE BBB-' [CARE Triple B Minus] from the rating of 'CARE BBB+' [CARE Triple B Plus]. This rating is applicable to facilities having tenure of more than one year. Facilities with this rating are considered to offer moderate safety for timely servicing of debt obligations. Such facilities carry moderate credit risk. CARE assigns '+' or '-' signs to be shown after the assigned rating (wherever necessary) to indicate the relative position within the band covered by the rating symbol.

Further, CARE has revised the rating assigned to the Short-term Bank Facilities of Mukand, aggregating Rs.395 crore, to 'PR3' [PR Three] from the rating of 'PR2+' [PR Two Plus]. This rating is applicable to facilities having a tenure upto one year. Instruments/facilities with 'PR3' rating would have moderate capacity for timely payment of short-term debt obligations at the time of rating and carry higher credit risk as compared to facilities rated higher.

The ratings have been revised on account of impaired liquidity due to high reliance on short-term debt, a downturn in both the steel industry as well as Mukand's ultimate end-user industry viz. automobiles, which is expected to result in a drop in cash accruals and dip in operational and financial performance in H1FY09. The ratings continue to be constrained by high gearing and the fact that Mukand is under the purview of a Corporate Debt Restructuring (CDR) programme. The ratings are further constrained by exposure to foreign exchange fluctuations and lack of captive sources of raw material.

The ratings are supported by management capability, long-term relationships with well-known clients, large variety of customised products and captive power plant.

The ability of the company to manage liquidity and working-capital requirements, reduce time lag in passing on raw material costs to customers and maintain adequate interest coverage will be the key rating sensitivities.

Incorporated in 1937, Mukand is part of the Bajaj group. Mukand manufactures specially-engineered long steel products in the alloy and stainless steel categories. It also manufactures industrial machinery and has a road construction business which it is phasing out. Mukand is headed by Mr. Niraj Bajaj, Chairman and Managing Director, who is ably supported by a team of experienced and qualified personnel.

The company underwent a CDR programme in FY03, necessitated by the steel downturn in 2001. Mukand has been repaying its debts as scheduled by the CDR programme.

Mukand's manufacturing facilities are located at Kalwe (Maharashtra) and Hospet (Karnataka). Mukand has its own Captive Power Plant (CPP) at Kalwe. It is in the process of building another CPP and a coke-oven power plant to utilise the fume gases emitted by the mini-blast furnace and coke-oven plant. As of December 3, 2008, Mukand had deferred the project to build a coke-oven plant due to the prevailing industry conditions.

The company has been unable to utilise its captive sources of iron ore at Hospet due to a dispute with the supplier and hence has been unable to avail the potential cost advantages. Another key raw material required by the company is coking coal, which it imports. Due to the reliance on imported raw material, Mukand is subject to the risk of foreign exchange movements. Due to the depreciation of the Indian rupee by 15% against the US Dollar from April 2008 to September 2008, Mukand suffered a foreign exchange loss of Rs.12 crore in H1FY09.

Mukand had initiated a capex programme of Rs.380 crore in FY07. The capex is expected to enhance the capacity to 623,000 tpa from 400,000 tpa in FY07. The cost of the

project had been revised upward to Rs.430 crore in July 2008, an increase of Rs.50 crore due to increase in the capacity planned for both the captive power plants. Of this, Rs.352 crore was spent till December 3, 2008 (Rs.62 crore in FY07, Rs.240 crore in FY08 and Rs.50 crore in the first eight months of FY09). The expansion is being funded primarily by internal accruals. The increase in project cost is being funded through sanctioned term loan from Bank of India. The project has come on-stream in September 2008, except for the coke oven plant and the CPP. The CPP is expected to be commissioned by October 2009.

Mukand registered sales of Rs.1,155 crore in H1FY09, a growth of 27% over H1FY08. In spite of this growth, PBILDT remained more or less flat at Rs.123.44 crore in H1FY09 while PAT dipped sharply by 54% to a modest Rs.12.60 crore in H1FY09 as compared to Rs.27.30 crore in H1FY08. Mukand's financial situation worsened in H1FY09 due to sharp increase in the cost of major inputs such as metallurgical coke, ferro-alloys, fuel etc, which Mukand was not able to fully pass on to its customers in Q1FY09. Steel prices started dipping from August 2008. Prices fell 11% since July 2008 to November 2008 while raw material was acquired by Mukand in 2QFY09 at high costs (contracted in the earlier period). This put further pressure on Mukand's margins and cash accruals in Q2FY09. As such, PBILDT margin in H1FY09 dipped to 9.9% from 13.52% in FY08. The significant short-term debt taken by Mukand to tide over immediate liquidity issues raised interest cost in H1FY09. The company also incurred foreign exchange loss of Rs.12 crore arising out of a depreciating rupee which further pressured its PAT. Consequently, PAT margin in H1FY09 fell to 1.01% compared to 2.76% in H1FY08. Interest coverage in H1FY09 remained in the range of 1.40x. There have been some instances of devolvement of Letters of Credit (LCs) in H1FY09 which further indicate liquidity constraints.

Mukand had invested Rs.326 crore either in the form of equity or by way of loans, advances or credit in few companies as on March 31, 2008. The networth of some of these companies has eroded and hence realising the full value of these investments / advances seems uncertain. The valuation report of some of these companies estimates the realisable value of the Rs.326 crore exposure at Rs.237 crore, based on the realisable value of the fixed assets of these companies. The balance Rs.89 crore is the estimated unrecoverable amount for which no provision has been made. If the expected loss on investment value (after netting off realisable value) is reduced from net worth, the overall gearing would be 2.5x in FY08. The management has maintained that it is confident that it will recover all the dues.

Around 80% of Mukand's sales in FY08 were from the steel segment. Of this, 60% of sales were derived from the automobile-related industry in FY08 as against 84% in FY07. Despite the reduced exposure to the auto industry, the pronounced downturn in the automobile industry in Q2FY09 impacted Mukand's earnings in that period and if the downturn continues, this could impact the automobile players' H2FY09 sales and profit.

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