

May 29, 2008

CARE ASSIGNS 'PR1' & 'A-' RATING TO BANK LOAN RATING TO MUKAND LTD.

CARE has assigned ratings to long-term and short-term bank facilities of Mukand Ltd (Mukand) aggregating Rs 1271.90 crore (including sanctioned but not yet availed term loan) as at Mar. 31, 2008. The ratings assigned are 'CARE A-' (Single A Minus) to the long-term bank facilities having a tenure of over one year and 'PR1' (PR One) to the short-term bank facilities having tenure up to one year.

Instruments with 'CARE A-' (Single A Minus) rating are considered to offer adequate safety for timely servicing of debt obligations. Such instruments carry low credit risk. Instruments with 'PR1' (PR One) rating would have strong capacity for timely payment of short-term debt obligations and carry lowest credit risk. Within this category, instruments with relatively better credit characteristics are assigned PR1+ rating.

The ratings derive their strength from the strong group support that Mukand enjoys, its strong current ratio and adequate interest coverage, management capability, long-term relationships with well-known clients, large variety of customized products, cost advantages and growth potential of the speciality steel sector in domestic and export markets. The key constraints are Mukand's exposure to a single industry viz. auto component, high gearing, low profitability and the fact that it is under the purview of a debt restructuring programme. Stable demand from the automobile and auto component sector, ability to pass on raw material costs to customers, export growth and increase in value-added products 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, CMD, who is ably supported by a team of experienced and qualified personnel.

The company underwent a corporate debt restructuring (CDR) programme in FY03, necessitated by the steel downturn in 2001. The company has been repaying its debts as scheduled by the CDR.

Mukand's manufacturing facilities are located at Kalwe (Maharashtra) and Hospet (Karnataka). The Kalwe plant has extensive rolling and downstream facilities which are being expanded to take advantage of higher margins in value-added products. Mukand has its own captive power plant at Kalwe and has captive sources of iron ore at Hospet. It is in the process of building another captive power plant and a coke-oven power plant to utilize the fume gases emitted by the mini-blast furnace and coke-oven plant.

Mukand has initiated a capex programme of Rs 380 crore with facilities expected to come online by FY09. The expansion will result in capacity expanding to 623,000 tpa from 400,000 tpa in FY07.

Mukand's total income grew at a CAGR of 10% during FY05-07 on the back of strong steel demand. Although PBILDT margin was healthy at 15.46% in FY07, PAT margin was negatively impacted by increased interest costs and remained low in the past three years. Although overall gearing has reduced over the years as the company progressively paid off its CDR dues, still, Mukand's high overall gearing of 1.85x in FY07 and relatively high total debt / net cash accruals (5.50x in FY07) reflect the debt that it has yet to pay under the CDR terms. Mukand's current ratio is healthy at 1.78x as at March 31, 2007.

During the nine month period ended Dec.31, 2007, Mukand's sales grew a modest 3.8% y-o-y to Rs 1,385 crore. PAT dipped y-o-y by 19% to Rs 46 crore during the given period. The PBILDT margin in the steel division were under pressure due to increased costs of major inputs like metallurgical coke, furnace oil, melting scrap, ferro-alloys, etc. and a time lag before costs could be passed on to customers. Revenue growth and profits for the road construction division continue to be negative due to time and cost overruns. PAT margin was also adversely affected in the nine month period due to higher interest on account of increase in working capital borrowings and higher tax outgo. The decline in PAT was stemmed to an extent by a write-back of previous provision towards diminution of investment in Mukand Engineers in view of improved market price of Mukand Engineers' shares. Interest coverage dipped to 1.6x for the nine months period, due to fall in PBIT and moderate rise in interest cost.

Mukand invested Rs 330 crore either in the form of equity or by way of loans, advances or credit in companies whose net worth has eroded or whose ability to repay is otherwise unclear. Around 97% of this investment is in associates/subsidiaries. After netting off the value of these companies as at Mar.31, 2007, recovery of an amount of Rs 227 crore is unclear. Had the company provided for the doubtful amount of Rs.227 crore, the company's overall gearing would have been 3.0x at end FY07 instead of the current 1.85x.

Post considering the latest valuation of these companies and the recovery of Rs.25 crore in FY08, recovery of Rs.92 crore is unclear as of date. The management is confident that it will recover all the dues based on the improving operating performance of some of these companies and has estimated the timelines for recovery of the same based on current performance of these companies.

Analyst Contact D R Dogra
Tel # (022) 6754 3434
Mobile # 982 0416 002
Email: dr.dogra@careratings.com

Disclaimer

CARE's ratings are opinions on credit quality and are not recommendations to buy, sell or hold any security. CARE has based its ratings on information obtained from sources believed by it to be accurate and reliable. CARE does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most issuers of securities rated by CARE have paid a credit rating fee, based on the amount and type of securities issued.