# Sarda Energy and Minerals Limited

March 27, 2019

**Ratings**

| **Facilities** | **Amount (Rs. crore)** | **Rating[1]** | **Rating Action** |
|---|---|---|---|
| Long Term Bank Facilities | 328.94 (enhanced from 318.92) | **CARE A; Positive (Single A; Outlook: Positive)** | **Rating reaffirmed; Outlook revised to Positive from Stable** |
| Short term Bank Facilities | 419.90 (reduced from 442.08) | **CARE A1 (A One)** | **Reaffirmed** |
| **Total** | **748.84 (Rupees Seven Hundred Forty Eight Crore and Eighty Four Lakh only)** | | |
| **Commercial Paper** (Carved Out) | **50.00** | **CARE A1 (A One)** | **Reaffirmed** |

*Details of instruments/facilities in Annexure-1*

**Detailed Rationale & Key Rating Drivers**

*The reaffirmation of the ratings assigned to bank facilities and instrument of Sarda Energy & Minerals Limited (SEML) derives strength from the improvement in operational and financial performance during FY18 and 9MFY19. The ratings continue to derive comfort from the experience of SEML's promoters in the steel and ferro industry, captive source of power and iron ore mines, improved working capital cycle as well as comfortable liquidity profile and debt coverage indicators. The ratings favourably factor in most of the promoters committed equity already being infused in the project stage companies. Additional comfort can be drawn from liquid investments available in promoter entities, Chhattisgarh Investment Ltd (CIL) and CSP Investment, which would be made available to SEML in case of shortfall in meeting any obligation.*

*The ratings are, however, constrained by project risk associated with time and cost over run in the hydro power project under Madhya Bharat Power Corporation limited [MBPCL, rate CARE BB; Stable/CARE BBB (SO); Stable/CARE A3 (SO)] as well as inherent cyclical nature of the steel and ferro alloys industry.*

*The ability of SEML to further improve its revenue and profitability in the wake of cyclicality associated with steel industry, maintain the capital structure while successfully completing the on-going hydro projects within the revised cost structure and timelines as well as successful execution of long- term power off-take arrangement will remain the key rating sensitivities.*

***Outlook: Positive***

*The outlook has been revised to 'Positive' from 'Stable' on account of further improvement expected in its financial risk profile on account of improved demand conditions in the domestic market as well as expected supportive price trends in the steel and ferro alloys segment thereby resulting in further growth in cash accruals.*

**Detailed description of the key rating drivers**

**Key Rating Strengths**

**Experienced promoters in the steel and ferro industry with financial support expected from promoter companies to meet shortfall in any obligation:** SEML is currently managed by Mr. K. K. Sarda (Chairman & Managing Director) who has over four decades of experience in steel industry. He is assisted by his son Mr. Pankaj Sarda (Joint Managing Director) who has over twelve years of experience in the industry. The promoters are also supported by qualified & experienced management with more than two decades of experience in the industry.

During current year FY19, SEML has already infused required funds in the form of equity and unsecured loan of Rs.89.59 crore in Madhya Bharat Power Corporation Limited (MBPCL). SEML also has current investments having market value of Rs. 150.07 crore as on December 31, 2018 which are available for meeting future obligations. However, CARE has also taken comfort from the liquid investments (equity shares) held by the promoter group entities (Chhattisgarh Investment Limited and CSP Investment), having market value of Rs. 499.85 crore as on March 18, 2019, which are expected to be liquidated to finance future support if required by SEML towards any shortfall in meeting its obligations.

***Improvement in operational and financial performance in FY18 as well as in 9MFY19:*** On a consolidated basis, SEML's total operating income grew significantly by 50.06% on a Y-o-Y basis in FY18 to Rs. 2229.79 crore from Rs. 1,485.90 crore in FY17 primarily on account of improvement in sales realizations as well as better capacity utilisation. The capacity

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

utilization of both steel as well as ferro alloys have improved on account of rising demand and improved industry dynamics. The PBILDT margins also improved to 19.80% in FY18 from 18.01% in FY17 on account of increase in sales realisation partially offset by increase in price of raw materials. The PAT margin has also improved to 9.22% in FY18 as compared to 8.55% in FY17. The strong performance is expected to continue in the near term on the back of stable industry outlook.
On a standalone basis, SEML's total operating income grew by 43.65% in FY18 to Rs. 1,527.93 crore from Rs. 1,063.63 crore in FY17. The PBILDT margin has improved to 22.40% in FY18 from 19.19% in FY17 on account of increase in sale realisation and capacity utilization partially offset by increase in raw material price. SEML has reported a net profit of Rs. 187.86 crore in FY18 as against Rs. 131.20 crore in FY17.
During 9MFY19, SEML's consolidated total operating income has improved to Rs. 1820.03 crore from Rs. 1683.95 crore during 9MFY18 owing to further improvement in steel and ferro alloys prices in the market. The PBILDT margins also improved to 21.61% during 9MFY19 from 20.42% during 9MFY18.
During 9MFY19, the company has increased the capacity of billet plant from 2,00,000 mtpa to 3,00,000 mtpa and the production will start post receipt of environmental clearances. Further, capacity expansion plan for pellet plant from 6,00,000 mtpa to 7,50,000 mtpa under SEML is under progress .

***Comfortable capital structure and improved debt coverage indicators:*** At consolidated level, overall gearing of the company remains comfortable at 0.92x as on March 31, 2018 (PY: 1.06x). Due to improved profitability, total debt to Gross cash Accrual (GCA) significantly improved to 5.04x in FY18 from 8.21x in FY17 and Interest coverage ratio also increased to 4.57x in FY18 from 2.85x in FY17. The overall gearing has further improved to 0.84x as on December 31, 2018 from 0.92x as on March 31, 2018 on account of accretion of profits to networth.
The standalone overall gearing of the company continued to be comfortable at 0.32x as on March 31, 2018 as compared to 0.41x as on March 31, 2017. The total debt to GCA improved to 1.72x in FY18 (PY: 2.84x) on account of higher profits generated during the year as well as reduced debt levels. Interest coverage ratio also improved to 9.54x in FY18 from 4.91x in FY17.

***Comfortable liquidity profile and working capital cycle:*** At consolidated level, , the working capital cycle of the company improved to 77 days as on March 31, 2018 as against 88 days as on March 31, 2017 on account of liquidation of inventory due to increase in demand of steel as well as better collection cycle. Debtor days marginally increased from 31 days in FY16 to 33 days in FY17. SEML only accepts orders from the companies which have given advances or letters of credit from their bankers. The average utilisation of fund based working capital limits remained moderate at 56.07% for the last trailing twelve month ended January, 2019. SEML on consolidated basis had cash and bank balance of Rs. 21.02 crore as on March 31, 2018 (PY: Rs. 10.00 crore). Apart from this, SEML also had current investment holding of Rs. 232.54 crore as on March 31, 2018 (PY: Rs. 203.49 crore). Moreover, the liquidity profile of the company is also supported by unutilized working capital limits.

***Captive source of power with partial coal linkages:*** SEML has 81.50 MW captive coal based power plant at Raipur which meets almost entire power requirement of its Raipur facility. The company has coal linkages with South Eastern Coalfields Limited (SECL) and Coal India Limited towards 75% of its requirement and is also planning to participate in further coal auctions to meet its balance requirements which are currently met through open markets. Additionally, the company has also set up 80 MW captive power plant at Vizag in its wholly owned subsidiary – Sarda Metals and Alloys Limited to support its ferro alloys operations. The coal requirement for SMAL is met through external market. During FY18, SEML had replaced its old turbines with new turbines which are expected to benefit the company in near term.

***Commencement of operations at iron ore mine however under-utilised due to social unrest:*** SEML's iron ore mine at Rajnandgaon, Chhattisgarh (which was non-operational since December 2008 due to social unrest) commenced operation in July 2014. Presently, the company is fulfilling only around 50% of its iron ore requirement from this mine as it is not able to utilise it fully due to social unrest in the area and is currently depending on manual labour to extract iron ore. For remaining requirement, the company has to rely on purchase of iron ore from open market. The company procures manganese ore and coal from open market both domestically and internationally.

**Key Rating Weaknesses**

***Project risk with time and cost over run in the hydro power project:*** The 24 MW hydro power plant under Chhattisgarh Hydro Power LLP (CHPLLP) at Gullu has started generating power. The firm has signed long term Power purchase agreement with Chhattisgarh State Power Distribution Co. Ltd for supply of power. CHPLLP has been awarded 5 small hydro power projects under IPP route with a total capacity of 106.80 MW. The second 24 MW Rehar project has obtained first stage forest clearance and various NOCs from CREDA, TEC, Tourism Dept., Gram Panchayat, WRD & Collector. Forest and private land acquisition is under progress. The firm expects to start work on the project during the current year which is expected to achieve COD by FY22.

The 96 MW power plant under MBPCL has been facing time and cost overrun on account of unexpected geographical complexities. The total project cost has been further revised to Rs. 1250.00 crore from Rs. 1,187.45 crore with revised COD in March 31, 2020 due to change in size and scope of the project. As per the LIE report (dated September 30, 2018), overall, percentage of work completed remains at around 60.64%.

**Inherent cyclicality of the steel industry:** Prospects of steel industry are strongly co-related to economic cycles. Demand for steel is sensitive to trends of particular industries, viz. automotive, construction, infrastructure and consumer durables, which are the key consumers of steel products. These key user industries in turn depend on various macroeconomic factors, such as consumer confidence, employment rates, interest rates and inflation rates, etc. in the economies in which they sell their products. Apart from the demand side fluctuations, the highly capital intensive nature of steel projects along-with the inordinate delays in the completion hinders the responsiveness of supply side to demand movements. When downturns occur in these economies or sectors, steel industry may witness decline in demand, thereby impacting volumes, revenue and margins of steel makers. The producers of steel construction materials are essentially price-takers in the market, which directly exposes their cash flows and profitability to volatility in the steel prices.

***Prospects:*** During FY18, steel production in India grew by 3.14% to 105 mn tonnes and consumption grew by 7.98% to 90.70 mn tonnes. During FY18, domestic steel prices remained buoyant as they rose in the range of 18%-21% on a y-o-y basis on account of growth in domestic consumption and international prices. Besides, higher raw material prices also resulted in rise in steel prices. On a cumulative basis, finished steel output grew by 6.6% to 82.4 million tonnes during April-December 2018 while consumption rose at a faster pace of 7.9% to 71.6 million tonnes during the period. CARE expects, the total finished steel production in India is likely to grow by 6%-8% during FY20 backed by a growth in demand from user industries like construction & infrastructure, automobiles, consumer durables among others. Domestic consumption of steel is expected to rise in the range of 5.5%-7.5% during FY20.

**Analytical approach:** CARE has adopted a consolidated approach on account of operational and financial linkages among entities. The list of entities whose financials have been consolidated is mentioned in Annexure 3.

**Applicable Criteria**
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology: Factoring Linkages in Ratings
Rating Methodology-Manufacturing Companies
Rating methodology – Steel Companies
Financial ratios – Non-Financial Sector

**About Sarda Energy and Minerals Limited**
Since its incorporation as Raipur Wires & Steel Limited in 1973, Sarda Energy & Minerals Ltd (SEML) has converted itself from a standalone steel melting shop to an integrated steel, power and ferro alloys producer in a phased manner. Presently, the company is engaged in the manufacturing and selling of pellets, sponge iron, steel billets, wire rods, ferro alloys and power from its plant located at Raipur.
In March 2013, SEML commissioned an 80 MW power plant at its wholly owned subsidiary Sarda Metals & Alloys Ltd while the 1 mtpa ferro alloy plant at the same premises became operational in June 2014. Under Parvatiya Power ltd, 4.8 MW hydro power project is operational. SEML's 24 MW hydro power project executed under Chhattisgarh Hydro Power Ltd. (CHPLLP) was completed in March, 2017 and started generation from July, 2017. The 96 MW hydro power project under MBPCL and 24 MW Rehar project are under project stage. Apart from the above, SEML has invested in several other subsidiaries/Special Purpose Vehicles (SPVs)/Joint Ventures (JVs) with interests in power plants and mining blocks. However, most of these subsidiaries are yet to commence operations.

| Brief Financials (Rs. crore) | FY17 (A) | FY18 (A) |
|---|---|---|
| Total operating income | 1485.90 | 2229.79 |
| PBILDT | 267.68 | 441.60 |
| PAT | 127.04 | 205.68 |
| Overall gearing (times) | 1.06 | 0.92 |
| Interest coverage (times) | 2.85 | 4.57 |

*A: Audited*
*The financials have been reclassified as per CARE standards.*
**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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**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.



**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 | - | - | - | 191.42 | CARE A; Positive |
| Non-fund-based - ST-BG/LC | - | - | - | 359.90 | CARE A1 |
| Term Loan-Long Term | - | - | July 2025 | 137.52 | CARE A; Positive |
| Fund-based - ST-Term loan | - | - | May 2019 | 60.00 | CARE A1 |
| Commercial Paper | - | - | 7-364 days | 50.00 | 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 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. | Fund-based - LT-Cash Credit | LT | 191.42 | CARE A; Positive | - | 1)CARE A; Stable (22-Mar-18) | 1)CARE A (24-Oct-16) | 1)CARE A (15-Jan-16) |
| 2. | Non-fund-based - ST-BG/LC | ST | 359.90 | CARE A1 | - | 1)CARE A1 (22-Mar-18) | 1)CARE A1 (24-Oct-16) | 1)CARE A1 (15-Jan-16) |
| 3. | Term Loan-Long Term | LT | 137.52 | CARE A; Positive | - | 1)CARE A; Stable (22-Mar-18) | 1)CARE A (24-Oct-16) | 1)CARE A (15-Jan-16) |
| 4. | Debentures-Non Convertible Debentures | LT | - | - | - | 1)Withdrawn (22-Mar-18) | 1)CARE A (24-Oct-16) | 1)CARE A (15-Jan-16) |
| 5. | Fund-based - ST-Term loan | ST | 60.00 | CARE A1 | - | 1)CARE A1 (22-Mar-18) | 1)CARE A1 (24-Oct-16) | 1)CARE A1 (15-Jan-16) |
| 6. | Fund-based - LT-External Commercial Borrowings | - | - | - | - | - | - | 1)Withdrawn (15-Jan-16) |
| 7. | Commercial Paper | ST | 50.00 | CARE A1 | - | 1)CARE A1 (22-Mar-18) | 1)CARE A1 (12-Jan-17) | - |

**Annexure-3: List of subsidiaries, associates and joint ventures of TSL getting consolidated (list as on March 31, 2018)**

| S.no | Name of the Company | % of holding by SEML |
|---|---|---|
| 1 | Sarda Energy & Minerals Hongkong Limited | 100.00% |
| 2 | Sarda Global Venture Pte. Limited | 100.00% |
| 3 | Sarda Global Trading DMCC | 100.00% |
| 4 | Sarda Metals & Alloys Limited | 100.00% |
| 5 | Sarda Energy Limited | 100.00% |
| 6 | Madhya Bharat Power Corporation Limited | 62.41% |
| 7 | Parvatiya Power Limited | 51.00% |
| 8 | Sarda Hydro Power Private Limited | 60.00% |
| 9 | Raipur Fabritech Private Limited | 52.38% |
| 10 | Raipur Industrial Gases Private Limited | 51.00% |
| 11 | Natural Resources Energy Private Limited | 71.55% |
| 12 | Chhatisgarh Hydro Power LLP | 60.00% |
| 13 | Shri Ram Electricity LLP | 51.00% |
| 14 | Raipur Infrastructure Company Limited | 33.33% |
| 15. | Madanpur South Coal Company Limited | 20.63% |

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