Srikalahasthi Pipes Limited

May 07, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings1	Rating Action
Long-term Bank Facilities	444.84 (enhanced from 306.57)	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Reaffirmed
Short-term Bank Facilities	320.00	'CARE A1+' (A One Plus)	Reaffirmed
Total	764.84 (Rupees seven hundred and sixty four crore and eight four lakh only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Srikalahasthi Pipes Limited (SPL) continues to take into account long and satisfactory track record of operations, established position of the group in the domestic Ductile Iron (DI) pipe segment with favorable location of the plant and satisfactory capacity utilization, moderate financial risk profile with comfortable capital structure and liquidity position.

The ratings also factor in volatility in input prices, risk of foreign exchange fluctuation and moderate operating cycle.

Going forward, the ability of the company to maintain a net debt around Rs.150 crore over next three financial years, any major debt laden capex, improvement in profitability and prospects of the DI pipe industry are key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Long and satisfactory track record of operations

Initially promoted by LANCO group of Hyderabad, SPL was formed by merging the companies of the LANCO Group, acquired by Kolkata based Electrosteel Castings Limited (ECL) in March 2002. The company is a part of the Electrosteel Castings Ltd, Kolkata, which has interest mainly in the manufacturing of DI pipes and fittings. The Company has a track record of more than six decades of operations and is currently one of the largest producers of DI pipes in India.

Established position of the group in the domestic DI pipe segment with favorable location of the plant

SPL predominantly operates in Southern India with its manufacturing unit located at Srikalahasthi, a small town in Andhra Pradesh. It is in close proximity to raw materials- where it imports coking coal from Vizaag port and iron ore from mines of Tamil Nadu and Karnataka. In addition, due to presence of limited players in the southern region, SPL has a significant advantage over others in terms of freight cost. SPL along with ECL holds dominant position in the domestic DI pipe market with an aggregate DI pipe production capacity of 5,80,000 mtpa (SPL-3,00,000 mtpa and ECL – 2,80,000 mtpa).

Satisfactory capacity utilization:

SPL reported a volume growth in production of ~21% in FY18, on account of full year of operations of its expanded facility. During Q4FY17, the company had expanded its DI Pipe installed capacity from 2,25,000 mtpa to 3,00,000 mtpa in order to cater to the growing demand. The capacity utilization of the DI pipe facility was satisfactory at ~92% in FY18, in line with the utilization in the preceding year. The pig iron facility, majorly a backward integration for the manufacture of DI pipes, saw utilization more than 100% in FY18 for the expanded facility.

In Q1FY19, the production of the DI pipe segment was low due lower capacity utilization of the mini blast furnace (pig iron) facility, which was had issues with refractory lining for which the same had to be shut in Q1FY19. However, post relining, the pig iron division has had production of more than 100% in Q2FY19 and Q3FY19. Consequently, the capacity utilization of the DI pipe segment also improved in Q2FY19 and Q3FY19 with utilization being around 97% in 9MFY19.

Moderate financial risk profile with comfortable capital structure:

The income from operations of SPL grew by 27.22% in FY18, mainly on account of volume growth of its DI pipes from its expanded facility. The PBILDT margin however, saw deterioration from 20.23% in FY17 to 16.19% in FY18. This was mainly due to rise in prices of its raw materials-primarily coking coal, which was not followed by a corresponding increase in sales realization of DI pipes. In absolute terms, the PBILDT level remained in line with that in FY17 due to increased overall contribution.

In 9MFY19, the y-o-y income from continuing operations decreased mainly due to decrease in trading sales. The DI pipe segment however, reported an increase, despite decrease in realizations due to increased sales volume. The PBILDT

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

margin however, was impacted due to Mini Blast furnace issue in Q1FY19 and continued increase in cost of major raw materials, which was not followed with increase in DI pipe realizations due to time lag involved in passing costs in order based nature of contracts.

In December 2017, the company had raised Rs.250 crore through Qualified Institutional Placement. This had led to improvement in its gearing ratio to 0.33x as on March 31, 2018 vis-à-vis 0.70x as on March 31, 2017. Despite increase in term loans in 9MFY19, the capital structure of the company continued to be comfortable with overall gearing of 0.41x as on December 31, 2018, owing to high net worth.

Liquidity Position

The liquidity position of the company was comfortable with company having free cash, bank and liquid investments of around Rs.455 crore as on March 31, 2019. With increase in term debts, the Total Debt/gross cash accruals of the company moderated but continued to be satisfactory as on Dec 31, 2018 at 3.37x. The average utilization of the fund based facilities was comfortable at around 47% for the last 12 months ended Feb 2019. The company also relies on non-fund bases limits mainly for importing coking coal.

Key Rating Weaknesses

Volatility in input price

Raw material consumption is the single largest cost component for SPL. With company having no backward integration for its primary raw materials (such as coking coal, iron-ore), it has to resort to open market purchases at the prevailing market prices. Hence, any adverse movement in raw material price without any corresponding movement in finished good price might affect the performance of the company. Though, the company has a price variability clause in some of the contracts and prices of finished goods generally move in tandem with that of raw materials; however it exposes the company to risk arising on account of volatility in the raw material prices.

Foreign exchange fluctuation risk

SPL sources majority of its raw material requirements (coking coal, coke, etc.) through imports for which it uses buyer's credit facility to minimize interest cost. Thus, it is exposed to the foreign exchange fluctuation risk. Moreover, to part fund its capex programme in the past, the company has availed ECBs. However, since SPL hedges its foreign currency exposure related to buyer's credit for import of coking coal and current portion of repayment obligations of ECB loans; thereby mitigating the foreign exchange fluctuation risk to a large extent.

Moderate working capital cycle

The business of SPL is working capital intensive in nature on account of relatively higher collection period which is on account of the ultimate end user of the product being Government bodies, where the payment terms remains stretched. Average collection period was in the range of 61 to 92 days during the last 3 years. Since the commissioning of the sinter plant, the raw material inventory has come down significantly, as iron ore fines are easily available in the market. The company purchase the same through e-auction from NMDC. However, the company generally stocks its coking coal requirement due to its imported nature which entails a lead time of around one quarter. The operating cycle of the Company ranged from 96 to 120 days in the last three years. As on March 31, 2019, the company's inventory period increased due to stocking of coking coal due to increasing price trend of the material. The company has taken up new orders at higher prices to ease the pressure of rising prices.

Analytical approach*:* Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology-Manufacturing Companies

About the Company

Incorporated in 1991, Srikalahasthi Pipes Limited (SPL; erstwhile known as Lanco Industries Ltd), is engaged in manufacturing of Ductile Iron (DI) spun pipes (installed capacity of 3,00,000 tonnes p.a.), pig iron (installed capacity of 2,25,000 tonnes p.a.) and port-land slag cement (installed capacity of 90,000 tonnes p.a.) with DI pipes as its core product (contributing about 80% to the net sales of the company in FY18) at its manufacturing facility located at Chittor, Andhra Pradesh.

SPL is a leading public utility services company predominantly catering to the needs of water infrastructure development and its clientele include construction companies executing contracts of water & sewerage divisions of various State Governments and local municipal bodies.

Initially promoted by LANCO group of Hyderabad, SPL was formed by merging the companies of the LANCO Group, acquired by Kolkata based Electrosteel Castings Limited (ECL; rated CARE BBB+/Negative/CARE A2) in March 2002. The company is now a part of Electrosteel Castings Ltd of Kolkata, which has interest mainly in the manufacturing of D.I. pipes and fittings.
SPL along with ECL holds the leadership position in the domestic DI pipe market with an aggregate DI pipe production capacity of 5,80,000 tpa (SPL – 3,00,000 tonnes p.a. and ECL – 2,80,000 tonnes p.a.). However, both the companies operate in different regions and have different sets of customers. Further, there are no operational linkages among them.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	1179.53	1500.55
PBILDT	238.59	242.97
PAT	138.66	147.40
Overall gearing (times)	0.70	0.33
Interest coverage (times)	6.07	6.05

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
Non-fund-based - ST-BG/LC	-	-	-	320.00	CARE A1+
Term Loan-Long Term	-	-	Sep 2024	199.84	CARE AA-; Stable
Fund-based - LT-Cash Credit	-	-	-	245.00	CARE AA-; Stable

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.	Non-fund-based - ST-BG/LC	ST	320.00	CARE A1+	-	1)CARE A1+ (06-Jul-18)	1)CARE A1+ (15-Feb-18) 2)CARE A1+ (10-Jul-17)	1)CARE A1+ (31-Dec-16) 2)CARE A1+ (20-Jul-16)
2.	Term Loan-Long Term	LT	199.84	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jul-18)	1)CARE AA-; Stable (15-Feb-18) 2)CARE A+; Stable (10-Jul-17)	1)CARE A+; Stable (31-Dec-16) 2)CARE A+ (20-Jul-16)
3.	Short Term Instruments-CP/STD	ST	75.00	CARE A1+	-	1)CARE A1+ (06-Jul-18)	1)CARE A1+ (15-Feb-18) 2)CARE A1+ (10-Jul-17)	1)CARE A1+ (14-Sep-16) 2)CARE A1+ (20-Jul-16)
4.	Fund-based - LT-Cash Credit	LT	245.00	CARE AA-; Stable	-	1)CARE AA-; Stable (06-Jul-18)	1)CARE AA-; Stable (15-Feb-18) 2)CARE A+; Stable (10-Jul-17)	1)CARE A+; Stable (31-Dec-16) 2)CARE A+ (20-Jul-16)

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