Srikalahasthi Pipes Limited (Revised)

July 4, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings1	Rating Action
Long-term Bank Facilities	469.84 (enhanced from 444.84)	**CARE AA-; Stable (Double A Minus; Outlook: Stable)**	**Reaffirmed**
Short-term Bank Facilities	370.00 (enhanced from 320)	**CARE A1+ (A One Plus)**	**Reaffirmed**
Total	**839.84 (Rupees eight hundred and thirty nine crore and eight four lakh only)**		
Commercial Paper^	**75.00 (Rupees Seventy Five crore only)**	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

^ aggregate of commercial paper and other fund based working capital borrowings should be within the assessed fund based working capital limits

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 high capacity utilization, moderate financial risk profile with comfortable capital structure and liquidity position.

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

Going forward, ability of the company to maintain a net debt of around Rs.150 crore over next three financial years, any major debt laden capex, improvement in company's 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, rated CARE BBB+; Stable/ CARE A2) in March 2002. The company is a part of the Electrosteel Group, Kolkata, which has interest mainly in the manufacturing of DI pipes and fittings. The group has a track record of more than six decades of operations.

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).

High capacity utilization

SPL reported a volume growth in production of ~8.53% in FY19. The capacity utilization of the DI pipe facility was almost full in FY19 improving from 92% in the previous year. Despite, refractory lining issues in Q1FY19, the pig iron facility, majorly a backward integration for the manufacture of DI pipes, saw utilization more than 100% in FY19.

Moderate financial risk profile

The income from operations declined marginally from Rs.1,590.38 crore in FY18 to Rs.1,567.79 crore in FY19, mainly due to decrease in trading sales in FY19. However, the DI pipe segment (contributing around 90% of the manufacturing sales in FY19) reported a y-o-y growth of 4.76% in FY19 on account of increase in sales volume. The PBILDT margin witnessed deterioration from 15.46% in FY18 to 12.50% in FY19 mainly due to decrease in spread of the DI pipes on the back of rising costs of raw materials. However, since the company enters into fixed price orders for DI pipes having an average

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

tenure of around 6-8 months, it is unable to pass on the increase in prices immediately. Thus the increase in prices are only reflected in new orders appearing with a time lag. The realizations of DI pipes increased in Q4FY19. The PBILDT margin was also impacted due to Mini Blast Furnace (MBF, pig iron) issue in Q1FY19. For correction of the same, the MBF was shut for 12 days in June 2018. Post resolution of the issue, the capacity utilization of the MBF and the DI pipe facility has been satisfactory.

Comfortable capital structure and debt protection metrics
The overall gearing of the company deteriorated from 0.38x as on March 31, 2018 to 0.48x as on March 31, 2019 but remained comfortable. The company has availed term loans for meeting long term working capital requirements and for capital expenditure in FY19. With increase in term debts, the Total Debt/gross cash accruals of the company moderated but continued to be satisfactory as on March 31, 2019 at 3.69x. As a backward integration, SPL is setting up of ferro alloy plant, and also setting up a new mini blast furnace of higher capacity (pig iron capacity would increase to 350,000 mtpa from 275,000 mtpa). It is also expanding the annealing furnace and finishing line of the DI pipe segment which would lead to an expansion in the DI pipe capacity from 300,000 mtpa to 350,000 mtpa. The above projects are expected to be executed over the next two years, with an aggregate cost of around Rs.285 crore, expected to be mostly funded out of internal accruals. Thus gearing is also expected to remain comfortable going forward. However, maintenance of net debt of Rs.150 crore in the next three financial years is a key rating sensitivity.

Liquidity: Strong
The liquidity position of SPL was comfortable with company having free cash, bank and liquid investments of Rs.457.23 crore as on March 31, 2019 in the form of fixed deposits, in current account and cash. In FY19, the company had gross cash accruals (GCA) of Rs. 163 crore against a term debt obligation of Rs.41 crore. In FY20, SPL has a term debt obligation of Rs.34 crore and the same are expected to be met out of cash accruals in the year. The average utilization of the fund based facilities was comfortable at around 47% for the last 12 months ended April 2019.

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.

Foreign exchange fluctuation risk
SPL sources majority of its raw material requirements (coking coal) through imports, exposing it to 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 for import of coking coal and current portion of repayment obligations of ECB loans; foreign exchange fluctuation risk is mitigated 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. Average collection period was in the range of 64 to 81 days during the last 3 years. In case of raw materials, the company generally stocks its coking coal requirement due to its imported nature which entails a lead time of around one quarter. Moreover, due to rising prices the company had stocked coking coal which resulted in increase in inventory days in FY19. The operating cycle of the Company ranged from 102 to 120 days in the last three years.

Analytical approach*:* Standalone Approach.

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

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 2,75,000 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 86% to the net sales of the company in FY19) at its manufacturing facility located at Chittor, Andhra

Pradesh. SPL also has a sinter plant of 500,000 mtpa, coke oven capacity of 270,000 mtpa and captive power plant of capacity 14.5 MW, as backward integration.
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.

Brief Financials (Rs. crore)	FY18 (Audited)	FY19 (Abridged)
Total operating income	1590.38	1567.79
PBILDT	245.80	195.94
PAT	147.40	117.54
Overall gearing (times)	0.38	0.48
Interest coverage (times)	5.72	4.84

Status of non-cooperation with previous CRA: Not Applicable

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
Non-fund-based - ST-BG/LC	-	-	-	370.00	CARE A1+
Term Loan-Long Term	-	-	Sep 2024	199.84	CARE AA-; Stable
Fund-based - LT-Cash Credit	-	-	-	270.00	CARE AA-; Stable
Commercial Paper	-	-	7-364 days	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.	Non-fund-based - ST-BG/LC	ST	370.00	CARE A1+	1)CARE A1+ (07-May-19)	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 (07-May-19)	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.	Commercial Paper	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	270.00	CARE AA-; Stable	1)CARE AA-; Stable	1)CARE AA-; Stable	1)CARE AA-; Stable	1)CARE A+; Stable

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					(07-May-19)	(06-Jul-18)	(15-Feb-18) 2)CARE A+; Stable (10-Jul-17)	(31-Dec-16) 2)CARE A+ (20-Jul-16)

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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