VMS Industries Limited

October 07, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term / Short-term Bank Facilities	110.00	**CARE BB+; Stable / CARE A4+; ISSUER NOT COOPERATING* [Double B Plus; Outlook: Stable / A Four Plus *]**	**Issuer Not Cooperating; Revised from CARE BBB-; Stable/CARE A3 [Triple B Minus; Outlook: Stable / A Three]**
Short Term Bank Facilities	5.50	**CARE A4+; ISSUER NOT COOPERATING* [A Four Plus *]**	**Issuer Not Cooperating; Revised from CARE A3 [A Three]**
Total	**115.50 (Rupees One hundred fifteen crore and fifty lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

CARE has been seeking information from VMS Industries Limited (VIL) to monitor the ratings vide e-mail communications dated August 13, 2020, August 21, 2020, August 26, 2020, August 28, 2020, September 09, 2020, September 10, 2020, September 11, 2020 and numerous phone calls. However, despite our repeated requests, the company has not provided the requisite information for monitoring the ratings. In line with the extant SEBI guidelines, CARE has reviewed the ratings on the basis of the best available information which however, in CARE's opinion is not sufficient to arrive at a fair rating. Further, VIL has not paid the surveillance fees for the rating exercise as agreed to in its Rating Agreement. The rating on VIL's bank facilities will now be denoted as **CARE BB+; Stable/CARE A4+; ISSUER NOT COOPERATING***.

Users of this rating (including investors, lenders and the public at large) are hence requested to exercise caution while using the above rating(s).

Detailed description of the key rating drivers

At the time of last rating on September 24, 2019, the following were the rating weaknesses and strengths (updated for available information):

Key Rating Weaknesses

Moderation in capital structure and debt coverage indicators along with losses reported during FY20

The company reported largely stable total operating income of Rs.181.33 crore during FY20 as against Rs.179.97 crore during FY19. However, it reported net loss of Rs.2.20 crore along with cash losses during FY20 due to decline in its operating profitability, booking of hedging cost of the LC opened for newly procured ship in Feb. 2020 and on account of prior period items of Rs.3.41 crore which included income tax of earlier years of Rs.2.52 crore.

VIL does not have any term loan except few vehicle loans; and its total debt mostly comprised of the outstanding LC obligations against the ships purchased. The capital structure of VIL marked by overall gearing deteriorated to 2.24 times as on March 31, 2020 as compared to 1.66 times as on March 31, 2019 mainly upon procurement of high value ship during February 2020 and LC opened for steel trading purpose leading to higher availment of LC limit at the end of the year. VIL's adjusted overall gearing (i.e. including the corporate guarantees extended for the bank facilities of VMS TMT Pvt. Ltd. & group company and reducing VIL's net-worth for the investments & loans given to its group companies) also moderated and stood at 4.76 times as on March 31, 2020 as against 3.02 times as on March 31, 2019. Debt coverage indicators moderated with interest coverage (PBILDT/interest) and Total debt/PBILDT stood at 1.78x and 36.02x as on March 31, 2020 as compared to 5.37x and 22.31x as on March 31, 2019 respectively.

During Q1FY21, VIL's TOI moderated by 36% on y-o-y basis along with moderation in its PBILDT margin by 103 bps to 3.71% on account of Covid-19 pandemic. The company faced labour issues wherein it was working with lower labour at Alang in Gujarat resulting in moderation in its performance during Q1FY21.

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

**Issuer did not cooperate; Based on best available information*

Susceptibility of its profitability to volatile steel prices

On purchase of ship, VIL is required to immediately pay entire purchase value of the ship by availing LC limit from the bank whereas its sales happen over a period of time. Accordingly, it is exposed to the volatility in steel prices driven by demand and supply conditions in the global as well as local markets. Accordingly, any adverse price movement on the uncut ship inventory as well as unsold inventory of steel scrap held by the company can impact its profitability.

Exposure to adverse movement in forex rates

The business model of VIL largely requires non-fund based facility i.e. Letter of Credit (LC) which is used to purchase the old ships for ship breaking activity. LC is denominated in foreign currency whereas the company's revenue is denominated in Indian Rupee (INR); hence the company is exposed to forex risk. Earlier, VIL used to estimate its approximate sales value for cut ship for every day and then enter in to a forward contract for an equivalent value of USD on a daily basis to reduce its risk on account of exchange rate fluctuations. However, during FY19 for the ship procured in February, 2019, it had hedged ~70% of its exposure by way of a mix of forward contracts & currency options.

Linkage to cyclicality inherent in the industry

Ship breaking industry is cyclical in nature as supply of old ships for recycling is inversely proportional to freight index. The freight index is a function of global demand of seaborne transport and supply of new vessels which in turn depend on global merchandise trade. Accordingly, there would be better availability of old ships for recycling at the time of recession when freight rates are low which makes it economical to dismantle the ship rather than continue to operate it. In past years, sharp fluctuation in freight index had been observed which had resulted in disruption in operations of ship breakers.

Regulatory and environmental hazard risks

The ship-breaking industry in the Alang-Sosiya belt of Gujarat is highly regulated with strict working and safety standards to be maintained by the ship-breakers for their labourers and environmental compliance. Furthermore, the industry is prone to risks related to pollution as it involves dismantling of ships which contain various hazardous substances like lead, asbestos, acid, hazardous paints, etc. that have to be properly disposed-off as per the regulatory guidelines. Any breach or non-compliance of environment or safety standards could result in discontinuation of ship breaking activity.

Key Rating Strengths

Extensive experience of the promoter in the ship-breaking industry

The promoter of VIL is one of the oldest in the ship-breaking industry of Alang, Gujarat and has successfully run the business through various business cycles. VIL's promoter Mr. Manoj Kumar Jain (Managing Director) is a qualified chartered accountant with more than two decades of experience in the ship-breaking industry as well as ferrous and nonferrous metal trading business.

Location of yard at Alang having unique geographical features suitable for ship-breaking operations

VIL's ship breaking yard is located at Alang-Sosiya belt which is considered to be one of the largest ship-breaking yards and constitutes almost 90% of India's ship-breaking activity. The unique geographical features of the area including a high tidal range, wide continental shelf, 15 degree slope, and a mud free coast are ideal for any size of ship to be beached easily during high tide. It accommodates nearly 165 plots spread over around 10 km long stretch along the sea coast of Alang. VIL has one plot to carry out its ship recycling business at Alang which is leased out by Gujarat Maritime Board (GMB) under a long-term lease agreement.

NK certification of ship recycling facility leading to lower procurement cost of ships

VIL's ship breaking yard has got 'Green Recycling' certification from Nippon Kaiji Kyokai, Tokyo which certifies that VIL's shipyard is compliant to the safe and environmentally sound ship recycling guidelines adopted by IMO resolution MEPC.210 (63). This compliance is in relation to adopting more environment friendly practices from an environmental and worker safety point of view, including secure management of hazardous waste generated from the ship-breaking activities. This certification gives VIL an advantage to source a ship at a relatively lower price compared to market rates as major shipping players give preference to companies having green recycling certificate.

Analytical approach: Standalone along with factoring corporate guarantees extended to its two group companies.

Applicable Criteria:
[Policy in respect of Non-Cooperation by issuer]
[Criteria on assigning 'Outlook' and 'Credit Watch' to Credit Ratings]
[CARE's Policy on Default Recognition]
[Rating Methodology-Manufacturing Companies]
[Rating Methodology-Trading Companies]
[Financial ratios - Non- Financial Sector]
[Rating Methodology: Consolidation and Factoring Linkages in Ratings]

About the Company
VMS Industries Ltd. (VIL) was originally incorporated as 'Varun Management Services Private Limited' in 1991 and was reconstituted as a limited company with effect from January 2010. VIL came out with an initial public offering in June 2011 and became a listed company. VIL was earlier engaged in providing various consulting & information technology (IT) services and gas supply to the various ship recycling units at Alang, Gujarat. Since May 2009, it is engaged in the ship breaking/recycling activity at Alang, Gujarat which is the leading centre for ship breaking and recycling in Asia. VIL was allotted berth nos. 159 & 160 which was later on merged as berth no. 160-M which has a width of 60 meters with a depth of 45 meters which can handle a vessel with a peak level of 70,000 LDT (Light Displacement Tonnage). VIL is the flagship company of VMS group and it operates along with VMS TMT Pvt Ltd. which is engaged in the trading of steel bars, ingots and billets.

Brief Financials (Rs. Crore)	**FY19 (A)**	**FY20 (A)**
Total operating income (TOI)	179.97	181.33
PBILDT	4.13	3.30
PAT	1.98	(2.20)
Overall gearing (times)	1.66	2.24
Interest coverage (times)	5.37	1.78

A: Audited

As per Q1FY21 published results, VIL reported a TOI of Rs.23.60 crore with PAT of Rs.0.05 crore as against TOI of Rs.36.91 crore with PAT of Rs.0.40 crore during Q1FY20.

Status of non-cooperation with previous CRA: CRISIL has migrated the ratings assigned to the bank facilities of VIL to 'Issue not cooperating' category vide its press release dated August 21, 2020 in the absence of requisite information from the company.

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 - LT/ ST-Letter of credit	-	-	-	110.00	CARE BB+; Stable / CARE A4+; ISSUER NOT COOPERATING*
Non-fund-based - ST-Credit Exposure Limit	-	-	-	5.50	CARE A4+; ISSUER NOT COOPERATING*

**Issuer did not cooperate; Based on best available information*

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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Non-fund-based - LT/ ST-Letter of credit	LT/ST	110.00	CARE BB+; Stable / CARE A4+; ISSUER NOT COOPERATING*	-	1)CARE BBB-; Stable / CARE A3 (24-Sep-19)	1)CARE BBB-; Stable / CARE A3 (23-Jul-18)	-
2.	Non-fund-based - ST-Credit Exposure Limit	ST	5.50	CARE A4+; ISSUER NOT COOPERATING*	-	1)CARE A3 (24-Sep-19)	1)CARE A3 (23-Jul-18)	-

**Issuer did not cooperate; Based on best available information*

Annexure 3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Non-fund-based - LT/ ST-Letter of credit	Simple
2.	Non-fund-based - ST-Credit Exposure Limit	Simple

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.

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