Welspun Pipes Inc

December 26, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Rating1**	**Rating Action**
Fund Based Facilities (Long term)^	358.63 (USD 50 Million)^	**CARE A+; Positive (Single A Plus; Outlook: Positive)**	**Reaffirmed; Outlook revised from Stable to Positive**
Total Facilities	**358.63 (Rupees Three Hundred & Fifty Eight Crores and Sixty Three Lakhs only)**		

Details of instruments/facilities in Annexure-1

^USD 50 Million @ Rs. 71.72/USD

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of Welspun Pipes Inc (WPI) continues to derive strength from the vast experience of promoters (Welspun Corp Limited, WCL, rated CARE AA-; Positive/ CARE A1+) and long track record of the group in executing complex pipeline projects, dominant position in the global large diameter welded pipe industry.

Further, the rating also reflects WPI's improved operational and financial performance in FY19 and H1FY20 on the back of healthy order book position and significant improvement in the profitability of the company. The rating also factors in management's focus towards debt reduction, resulting into improvement in its capital structure and comfortable debt coverage indicators. The rating strengths are, however, constrained by inherent cyclicality of the steel pipe industry, regulatory risk in the geography wherein it operates.

Any significant change in the liquidity maintained by the company and WPI's ability to sustain the improvement in its operational and financial performance in the medium term, remain the key rating sensitivities.

Rating Sensitivities

Positive Factors

- WPI's ability to maintain its current operating profitability margin on a sustained basis
- Maintenance of its low-leveraged capital structure with overall gearing (including acceptances) not more than 0.60x
- Sustenance of ROCE above 13% and interest coverage ratio above 5x

Negative Factors

- Decline in operating profitability margins below 8% in FY20 and 9% in FY21
- Any significant increase in working capital requirement or any unforeseen debt funded capex/acquisition

Outlook: Positive

The positive outlook reflects expected sustenance in the operating and financial performance of the company on the back of its strong order book position. Moreover, it reflects further expected strengthening of its capital structure and debt coverage indicators on account of further de-leveraging. The outlook may be revised to stable if the operating profitability margin declines from its current level.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters with dominant position in steel pipe segment

Welspun Pipes Inc. (WPI) is a wholly-owned subsidiary of Welspun Corp Ltd. (WCL, rated CARE AA-, Outlook: Positive /A1+, reaffirmed in Oct 2019). WCL is the flagship company of the USD 2.7 billion Welspun group, a diversified conglomerate with dominant position in line pipes and home textiles business and with presence in Steel, Energy and Infrastructure. WCL was set up in 1995 with technical expertise from Intertec GmbH, Germany and equity participation from Intertec GmbH and Gujarat Industrial Investment Corporation Ltd. WCL is engaged in manufacturing of LSAW (Longitudinal Submerged Arc Welded), HSAW (Helically Submerged Arc Welded) and ERW (Electric Resistance Welded Pipe) pipes ranging from half inch to 140 inches, along with specialized coating, double jointing and bending; from its various facilities with domestic pipe capacity of 1.655 Million Tonnes Per Annum (MTPA) in India and a global capacity of 2.555 MTPA as on September 30, 2019.

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

Improvement in operational and financial performance in FY19 and H1FY20

Particulars	FY18	FY19	H1FY20
Installed capacity (KMT pa)	525	525	525
Production (KMT)	214	436	260
Capacity utilization (%)	40.76	83.05	99.05*
Sales Volume (KMT)	222	413	211
EBITDA/Tonne (USD/Tonne)	94	205	346
PBIDT Margin (%)	4.06	12.42	17.06

*Annualized

During FY19, the profitability in US operations improved significantly mainly on account of restrictions on import of steel pipes into the US in the form of tariffs and quotas, which helped the local US plants to command better volumes and profit margins. As a result, EBITDA/ Tonne doubled to ~USD 200 in FY19 and PBILDT margin improved to 12.42% in FY19. The GCA more than doubled to USD 64.67 million in FY19.

Further, in H1FY20 execution of high margin orders also led to an increase in PBILDT margin to 17.06%. Moreover, WPI also repatriated appx USD 29 mn (~Rs. 203 crore) to its Indian holding company, WCL in the form of dividend (net of taxes) in H1FY20.

WPI is a recognized player in the industry and has been certified as preferred supplier by the major Oil and Gas majors. Its customers include players like Kinder Morgan, TransCanada, and Energy Transfer. The company anticipates to see spurt in large size orders in the medium term.

Focus on debt reduction

WPI made a prepayment of half of its outstanding term debt of USD 100 million ie USD 50 million during March-April 2019. Moreover, healthy generation of cash accruals also led to NIL utilisation of fund-based & non-fund based facility in the last 12 months ending November, 2019. Resultantly, the overall gearing significantly improved from 0.76x as on March 31, 2018 to 0.49x as on March 31, 2019 and further to 0.31x as on Sept 30, 2019. Similarly, Total debt/GCA improved from 3.91x in FY18 to 1.24x in FY19 and to 0.52x (annualized) in H1FY20. Moreover, as discussed with the management, the company does not have any significant debt-funded capex plans in the near future.

Healthy order book position providing medium-term revenue visibility

A dramatic change in the US pipe market has turned the odds in favor of the company. US, being now the world's largest oil producer (as a result of Shale revolution) and facing pipeline constraints for evacuation of oil & gas is driving the demand for pipelines. Moreover, in 2018, the US Government imposed anti-dumping duty on imports of large diameter welded pipes into the country, thus benefitting the local US plants to command better volumes and higher margins.

As on September 30, 2019, WPI had an order book comprising 197 KMT of pipes translating to approx. USD 377 mn (Rs.2,641 crore) to be executed in 9 months. Further as per their public announcement on Dec 10, 2019, WPI received an additional order of 161 KMT worth appx USD 300 mn to be executed over next 9-12 months. So the total order book now stands at 358 KMT worth appx USD 677 mn (~Rs. 4,740 crores).

Also, the premiums have increased in the USA market with government focus on local manufacturing. The new orders are expected to yield an EBITDA margin of 14-16%.

The order book across geographies has aided WCL to diversify its revenue profile. Before submitting its bid/quote for pipes, the group obtains a quote from its suppliers (for supply valid for 1-1.5 months), keeping adequate margin so as to safely cover estimated volatility in the steel prices. Wherever necessary, the group hedges its exposure to steel prices through forwards. However, the order book position is susceptible to the cycle of the end user industry and regulatory risk in the geography where it is operating.

Strong Liquidity Profile

The liquidity profile of WPI is comfortable with Cash and Cash Equivalents of USD 27 million as on Sep 30, 2019, NIL utilization of working capital lines during last 12 months, adequate cash flows against debt repayment obligations, current ratio of 1.46x as on March 31, 2019; thereby providing cushion to meet contingencies.

Key Rating Weaknesses

Cyclicality of steel pipe industry

Volatility in steel prices affects the profitability of steel pipe manufacturers. Further, majority of steel pipe demand comes from exploration and production activities in the oil & gas sector which is cyclical in nature and depends on the oil prices.

Liquidity: Strong
The liquidity profile of WPI is strong marked by healthy cash flows to meet debt repayment obligations and Cash and Cash Equivalents to the tune of USD 27 million as on Sep 30, 2019. Its unutilized bank lines are more than adequate to meet incremental working capital needs over the next one year, also providing cushion to meet contingencies.

Industry outlook and prospects
The outlook in the American region is positive, with key initiatives such as Make and Melt in America, increase in production from shale gas and procurement of steel from the local steel producers in the US. Owing to significant increase in output of oil and gas in US, there has been an increase in the demand for steel pipes. This is likely to benefit players like WPI, further improving the visibility of the order book position during the short to medium term period.

Analytical approach: Consolidated
Welspun Pipes Inc (WPI) - Consolidated comprises its wholly owned subsidiaries - Welspun Global Trade, LLC (WGTL) and Welspun Tubular, LLC (WTL).
Also, operational and financial linkages with its parent Welspun Corp Limited (WCL) have been considered. WCL is engaged in manufacturing of HSAW, LSAW and ERW pipes in India since 1995.

Applicable Criteria
Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology-Manufacturing Companies
Financial ratios – Non-Financial Sector
Rating methodology- Factoring Linkages

About the Company
Registered in the State of Delaware (USA) in August 2006, Welspun Pipes Inc. (WPI) is a wholly-owned subsidiary of Welspun Corp Ltd. (WCL, rated CARE AA-, Outlook: Positive /A1+, reaffirmed in Oct 2019). WCL is the flagship company of the USD 2.7 billion Welspun group, a diversified conglomerate with dominant position in line pipes and home textiles business and with presence in Steel, Energy and Infrastructure. WCL was set up in 1995 with technical expertise from Intertec GmbH, Germany and equity participation from Intertec GmbH and Gujarat Industrial Investment Corporation Ltd. WCL is engaged in manufacturing of LSAW (Longitudinal Submerged Arc Welded), HSAW (Helically Submerged Arc Welded) and ERW (Electric Resistance Welded Pipe) pipes ranging from half inch to 140 inches, along with specialized coating, double jointing and bending; from its various facilities with domestic pipe capacity of 1.655 Million Tonnes Per Annum (MTPA) in India and a global capacity of 2.555 MTPA as on September 30, 2019. Following table shows the brief financials of Welspun Pipes Inc (Consolidated):

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	513.38	682.53
PBILDT	20.84	84.76
PAT	7.32	45.67
Overall gearing (times)	27.08	64.67
Interest coverage (times)	3.86	10.87

A: Audited; The financials are adjusted 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

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/Non-fund-based-Long Term	-	-	-	358.63	CARE A+; Positive

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.	Fund-based - LT-Term Loan	LT	-	-	-	-	1)Withdrawn (05-Oct-17)	1)CARE A+ (06-Sep-16) 2)CARE A+ (20-Apr-16)
2.	Fund-based/Non-fund-based-Long Term	LT	358.63	CARE A+; Positive	-	1)CARE A+; Stable (19-Dec-18)	1)CARE A+; Stable (05-Oct-17)	1)CARE A+ (06-Sep-16) 2)CARE A+ (20-Apr-16)
3.	Non-fund-based - ST-BG/LC	ST	-	-	-	-	-	1)Withdrawn (20-Apr-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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