December 12, 2023

Shyam Century Ferrous Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term-Fund Based-Working Capital	28.00	26.00	[ICRA]BBB+ (Stable); reaffirmed
Short Term Non-Fund Based – Letter of Credit	6.00	8.00	[ICRA]A2+; reaffirmed
Total	**34.00**	**34.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation for Shyam Century Ferrous Limited (SCFL) favourably considers its comfortable financial risk profile characterised by SCFL's net debt negative status as on September 30, 2023. Additionally, SCFL's liquidity profile remains strong, supported by a significant headroom available in the form of undrawn limits of working capital and sizeable cash and liquid investments, which generates significant non-operating income. The ratings also factor in the financial flexibility enjoyed by SCFL, backed by a strong liquidity, and this has helped the company to raise funds at competitive interest rates. Further, the favourable demand outlook for the steel industry supports the ratings of SCFL.

ICRA notes that SCFL's operating performance was weaker than expected in H1 FY2024 as operating margins of the company declined to negative 1.6% in H1 FY2024 from 18.3% in FY2023 and 35.7% in FY2022. This was primarily due to disruption in power supply which led to escalation of power cost which is a significant portion of SCFL's cost structure. Weaker monsoon in Meghalaya in the current fiscal led to low hydro-generation which translated to power outages for upto 16-18 hours per day. As the 14-MW captive power plant remains idle from FY2020 due to bottlenecks in coal availability in Meghalaya, this has significantly increased the power cost incurred by SCFL due to procurement of power from alternative sources like IEX[1] at significantly higher tariffs. ICRA however believes that earnings are expected to witness some recovery in the second half of the current fiscal as the power supply from the discom has witnessed improvement in the recent months with outages reducing to 8-10 hours per day now. ICRA understands that in the unlikely event of a prolonged period of constrained power availability from the discom, SCFL is also evaluating alternative cost-competitive renewable energy sourcing arrangements with developers based on wind-solar hybrids.

The rating is also constrained due to SCFL's small scale of operations, which makes the company vulnerable to a period of sustained industry downturn. The company is exposed to significant volatility in earnings, given the cyclical nature of steel industry, the key end-user for ferrosilicon. The ratings are further tempered by steadily deteriorating coke quality and suboptimal capacity utilisation levels (in the range of 50-70%) over the years. ICRA also notes that many industries based out of Meghalaya, including SCFL, remain exposed to regulatory risks as any unfavourable change in the Government policy may impact its raw material availability, especially coke and coal.

The Stable outlook on the long-term rating is supported by the healthy domestic steel demand, prudent working capital management, and the comfortable liquidity profile of the company.

[1] Indian Energy Exchange

Key rating drivers and their description

Credit strengths

Comfortable capital structure – SCFL has comfortable financial risk profile, characterised by healthy TOL/TNW of 0.10 times as on September 30, 2023 and 0.13 times as on March 31, 2023. The company is net debt negative since FY2021.

Strong liquidity profile and high financial flexibility – The company's liquidity is strong, supported by significant headroom in undrawn working capital limits and sizeable cash and liquid investments. As on September 30, 2023, the company has undrawn working capital facilities of ~Rs. 23 crore as well as cash and liquid investments worth ~Rs. 108.13 crore. A strong liquidity also imparts financial flexibility to SCFL, as demonstrated by its ability to raise funds at competitive interest rates.

Favourable demand outlook for the steel industry – The Government's infrastructure capex plans are expected to support the domestic demand outlook of the steel industry and support the adequate capacity levels of domestic steel mills, going forward, thus, positively impacting the demand outlook for ferro silicon industry.

Credit challenges

Significant volatility in earnings, given the cyclical nature of steel industry, the key end-user for ferrosilicon; operations to remain loss making in H1 FY2024 due to power cost escalations and subdued ferro-alloy realisations – The company's operating income declined by 13% year on year (YoY) in FY2023 and the operating profit before interest depreciation tax and amortisation (OPBIDTA) declined by 55% YoY in FY2023 on the back of decline in ferro silicon realisations. In H1 FY2024, the company has recorded a negative OPBIDTA due to further deterioration in ferro silicon prices and rising power cost due to constraints in the availability of power in Meghalaya. Low hydropower generation in the state has led to power cuts for upto 16-18 hours/day in H1 FY2024 and has significantly increased SCFL's power cost (which comprises an estimated 45-50% of the overall cost of manufacturing in FY2024) due to procurement of power from alternative sources like IEX at higher tariff rates. ICRA however believes that earnings are expected to witness some recovery in the second half of the current fiscal as the power supply from the discom has witnessed improvement in the recent months with outages reducing to 8-10 hours per day now.

Exposure to regulatory risks associated with raw material availability and steadily deteriorating coke quality – ICRA notes that many Meghalaya-based industries, including SCFL are exposed to regulatory risks as any unfavorable change in the Government policy may impact their raw material availability, especially coke and coal. In the past, ICRA notes that coal/ coke consumers in Meghalaya have encountered operational challenges associated with the banning of coal mining and restrictions on coal movement in the state. Moreover, SCFL's specific consumption of coke has been steadily increasing in the last few years, which indicates deteriorating quality. With coke accounting for ~30% of the overall cost of producing ferrosilicon, this deterioration in coke quality has led to an overall escalation in input costs for SCFL.

Small scale of operations; captive power plant remains unutilised from FY2020 due to bottlenecks in coal availability in Meghalaya – The small scale of operations makes SCFL vulnerable to a period of sustained industry downturn. SCFL's modest scale is also a function of its moderate capacity utilisation over the last five years, which stood in the range of 50-70%. The company is unable to utilise its 14-MW captive power plant under Meghalaya Power Limited (MPL) due to constraints faced in respect of availability of coal in the Meghalaya region after the ban of coal movement in Meghalaya from FY2020. However, if adequate coal at a competitive rate is made available, then the company would be able to operate the plant and will become largely self sufficient in its power requirements at the current capacity utilisation level.

Environment and Social Risks

Environmental considerations – Ferro-alloy manufacturing is an energy-intensive process and requires a substantial use of fossil fuels (scope 1 emissions) and power (scope 2 emissions), which results in greenhouse gas emissions, industrial waste generation, and environmental pollution. Increasing regulatory requirements to reduce greenhouse gas emissions and stricter air pollution standards may lead to higher costs for ferro-alloy manufacturers in the medium term. SCFL has progressively taken steps towards conservation of energy and technical absorption like carrying out of cooling tower hot basin modification work to arrest water leakage. These measures partly mitigate the risk of non-compliance to applicable environmental laws and ensures business continuity. Further, SCFL faces risk of physical climate change from rainfall in the form of disruption in the availability of raw material like coke and coal.

Social considerations – Social risks for ferro-alloy manufacturers manifest from health and safety of employees involved in the manufacturing activity. In this regard, SCFL has taken proactive measures for its employees, which includes managing the crisis and ensuring the safety and wellbeing of its employees. SCFL has engaged in getting more and more people vaccinated and organised free vaccinations camps for employees across locations. In the area of safety, casualties/ accidents at operating units due to gaps in safety practices could not only lead to production outages for ferro alloy manufacturers, but also invite penal actions from regulatory bodies. The sector is exposed to labour related risks and risks of protests/social issues with local communities, which might impact expansion/modernisation plans. Also, the adverse impact of environmental pollution in nearby localities could trigger local criticism. SCFL is engaged in Corporate Social Responsibility (CSR) activities in the areas of eradication of hunger and malnutrition, promoting education, art and culture, healthcare, destitute care and rehabilitation, environment sustainability, disaster relief and rural developments projects.

Liquidity position: Strong

SCFL's liquidity position is strong with sufficient undrawn limits and comfortable liquidity position. The average monthly utilisation of the fund-based working capital limits stood negative from May 2022 to September 2023 due to credit balances outstanding in most of the months. The company has no long-term debt service obligations, which further strengthen its liquidity profile. In addition, free cash and liquid investments balance stood at Rs. 108.13 crore as on September 30, 2023, thus supporting the on-balance sheet liquidity position of the company.

Rating sensitivities

Positive factors – SCFL's ratings could be upgraded if there is a significant improvement in the profitability while maintaining its comfortable liquidity profile.

Negative factors – A sustained period of loss-making operations could lead to ratings downgrade. Moreover, a significant debt-funded capex, leading to a deterioration in the debt protection metrics, or material deterioration in the liquidity position will also exert negative rating pressure.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Corporate Credit Rating Methodology]
Parent/Group support	Not Applicable
Consolidation/Standalone	The rating is based on the standalone financials of SCFL. The company does not have any subsidiary, associate or joint venture as on March 31, 2023.

About the company

Shyam Century Ferrous Limited (SCFL) was incorporated in 2011. It was a dormant company till April 1, 2014 before the transfer of the ferro alloy business, including a 48.8% shareholding in Meghalaya Power Ltd. (MPL, operating a 43-MW thermal power plant) from Star Ferro and Cement Limited (which earlier used to house ferro alloy, power, and cement businesses), as per the scheme of demerger approved by the High Court of Meghalaya in Shillong on March 31, 2015, effective from April 01, 2014. SCFL manufactures ferrosilicon with a total capacity of 21,600 MTPA and has a captive power plant of 14 MW (currently non-operational) in Meghalaya.

Key financial indicators (audited)

SCFL Standalone	FY2022	FY2023	H1 FY2024*
Operating income	207.4	181.0	65.5
PAT	56.9	26.6	1.2
OPBDIT/OI	35.7%	18.3%	-1.6%
PAT/OI	27.4%	14.7%	1.9%
Total outside liabilities/Tangible net worth (times)	0.1	0.1	0.1
Total debt/OPBDIT (times)	0.0	0.1	-2.1
Interest coverage (times)	117.1	95.9	-13.1

*PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; *Un-audited financials*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on March 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Dec 12, 2023	Oct 31, 2022	Jul 08, 2021	-
1	Fund Based – Working Capital	Long-term	26.00	-	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	-
2	Non-Fund Based – Letter of Credit	Short-term	8.00	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term-Fund Based-Working Capital	Simple
Short Term Non-Fund Based- Letter of Credit	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Working capital**	NA	NA	NA	26.00	[ICRA]BBB+ (Stable)
NA	**Letter of Credit**	NA	NA	NA	8.00	[ICRA]A2+

Source: Company

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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