

September 30, 2024

VRKP Sponge and Power Plant LLP: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term/ Short term – Fund based - Cash credit	40.00	40.00	[ICRA]BBB+ (Stable)/ [ICRA]A2; reaffirmed
Short term – Non fund based - Letter of Credit	25.00	25.00	[ICRA]A2; reaffirmed
Long term – Fund Based - Term Loan	8.36	6.27	[ICRA]BBB+ (Stable); reaffirmed
Total	73.36	71.27	

*Instrument details are provided in Annexure-I

Rationale

To arrive at the rating of VRKP Sponge and Power Plant LLP (VRKP), ICRA has changed the analytical approach from a standalone to a consolidated view with VRKP Integrated Steel Industries Private Limited (VISIPL) along, given the common management and significant operational and financial linkages between them. VRKP has also extended corporate guarantee for the loan taken by VISIPL.

The rating reaffirmation considers an expected improvement in the VRKP Group's operational and financial risk profile in FY2025 owing to sizeable cost savings that is likely to emanate from the new waste heat recovery boiler (WHRB) set up at VISIPL, which has already commenced commercial operation from March 2024. The steam generated from the unit will be supplied to VRKP to run the captive power plant, which is likely to significantly reduce the power expenses at the Group Level. VRKP is also sourcing renewable power through a captive arrangement with renewable power generators, resulting in further cost savings for the Group.

In FY2024, only VRKP was operational, and the performance remained stable with estimated OPBDITA of Rs. 48 crore in FY2024 compared to Rs. 43 crore achieved in FY2023. While the term loans taken for the VISIPL project impacted the Group's leverage and coverage indicators in FY2024, these metrics are likely to improve in the current fiscal. While the TMT and billet realisation continues to be subdued in FY2025, the Group's profits and cash accruals are likely to improve significantly on the back of the power cost savings and the ramp-up of sponge iron production (capacity of 165,000 MT) at VISIPL. The Group is expected to report a revenue of ~Rs. 950-1,000 crore and OPBDITA of ~Rs. 110-120 crore in FY2025. The leverage and coverage metrics are also expected to significantly improve with the full benefits of the cost savings expected to accrue in the current fiscal. ICRA also notes that a significant portion of the project capex at VISIPL was funded through unsecured loan taken from promoters, which are subordinated to the bank loans. Additionally, VISIPL's eligibility for capital subsidy and income tax incentives strengthens its financial position.

The rating also favourably acknowledges the extensive experience of the promoters and the management in the steel industry and also the high capacity utilisation and cost-efficient integrated nature of operations on the back of captive power generation, sponge iron, billet and TMT bar manufacturing capacities.

However, the ratings continue to be constrained by the high degree of geographical concentration of VRKP's operations in the southern region of the country and the intense competition in the fragmented and commoditised long steel market, partly limiting its pricing flexibility. ICRA notes that VRKP's operations are vulnerable to the inherent industry cyclicality, which often results in a volatility in raw material and product prices. The company also imports a part of its scrap requirement, which

further exposes it to fluctuations in exchange rates. Besides, VRKP's status as a limited liability partnership within the VRKP Group exposes it to the risk of capital withdrawals. ICRA understands that the Group is undergoing sizeable expansion plans, which is expected to commence commercial operation shortly and no financial support is further required for the project. However, any large capital withdrawal from VRKP to part-fund the expansion would remain a key rating monitorable.

The Stable outlook on the long-term rating indicates ICRA's expectations that the VRKP Group's profits and accruals are likely to remain healthy, going forward, which would help the company keep its credit metrics comfortable.

Key rating drivers and their description

Credit strengths

Earnings likely to improve in current fiscal on healthy capacity utilisation and power cost savings at Group level - In FY2024, only VRKP was operational, and the performance remained stable with estimated OPBDITA of Rs. 48 crore in FY2024 compared to Rs. 43 crore in FY2023. While the TMT and billet realisation continues to be subdued in FY2025, the Group's profits and cash accruals are likely to improve significantly on the back of the power cost savings and the ramp-up of sponge iron production (capacity of 165,000 MT) at VISIPL. The Group is expected to report a revenue of ~Rs. 950-1,000 crore and OPBDITA of ~Rs. 110-120 crore in FY2025, which would be a significant improvement compared to the previous fiscal.

Comfortable capital structure and improved debt coverage indicators expected in current fiscal - While the term loans taken for the VISIPL project impacted the Group's leverage and coverage indicators in FY2024, these metrics are likely to improve in the current fiscal significantly as the full benefits of the cost savings are expected to accrue in FY2025. ICRA expects the Group's leverage (total debt/OPBDITA) to remain at ~2.0 times and the interest coverage at >4.0 times in the current fiscal. ICRA also notes that a significant portion of the project capex at VISIPL was funded through unsecured loans taken from promoters, which are subordinated to bank loans, which also provides comfort.

Backward integration into manufacturing sponge iron, billets and captive power generation supports cost competitiveness - VRKP has manufacturing facilities for sponge iron, which along with scrap, serves as a feedstock to produce MS billets. It further manufactures TMT bars using mostly the in-house produced MS billets, which gives VRKP a cost advantage over other secondary steel producers, which has to source costlier inputs from the market. In addition, the 47-tonne-per-hour WHRB set up at VISIPL has begun commercial operation from March 2024 and the steam generated from the unit is being supplied to VRKP to run the captive power plant, which is likely to significantly reduce the power expenses at the Group Level. VRKP is also sourcing renewable power through a captive arrangement with renewable power generators, resulting in further cost savings for the Group.

Extensive experience of promoters in steel business - Mr. Vinod Agarwal, Chairman of the VRKP Group, has more than three decades of experience in the iron and steel industry and has established the Group as a leading TMT bar manufacturer and supplier in south India, supported by a wide network of distributors.

Credit challenges

High geographical concentration risk - The Group's operations are mainly concentrated in southern India, exposing it to geographical concentration risk. A slowdown in steel demand in its key markets could lead to an overall decline in its revenues and profits in the future.

Susceptibility of margins to raw material price fluctuations and exposure to cyclicity inherent in the steel industry - The VRKP Group's operations are raw material intensive with raw materials and consumables accounting for 80-90% of its operating income over the last two fiscals. VRKP imports a part of its scrap requirement, which further exposes the company to fluctuations in exchange rates. Also, the domestic steel industry is cyclical in nature and is likely to keep the cash flows volatile for steel players, including the VRKP Group. The Group's operations are vulnerable to any adverse change in the demand-supply dynamics in the construction sector, especially in southern India.

Intense competition in highly fragmented and commoditised steel market – The VRKP Group operates in the commoditised structural steel business, characterised by intense competition in the secondary steel sector, which limits the pricing flexibility of the players, including the VRKP Group. As raw material costs are a crucial indicator of profitability, the margins remain susceptible to a large increase in raw material prices, which may not match with a commensurate increase in the realisation of products sold, going forward.

Risk of capital withdrawal by the partners – Given VRKP’s constitution as an LLP, it is exposed to discrete risks, including the possibility of capital withdrawal by the partners (as experienced in the past), which could adversely impact the capital structure and leverage metrics. ICRA notes that the entity had withdrawn a large amount in FY2024 to fund the capex undertaken in other entities at the Group level, including VISIPL. Any large capital withdrawal from VRKP would remain a key rating monitorable.

Liquidity position: Adequate

The VRKP Group’s liquidity position remains adequate, supported by strong cash flow from operations. Major principal repayments will commence from FY2026, when the cash flows are expected to stabilise further. The working capital utilisation, however, remained high at ~96% in August 2024. However, prudent working capital management practices and negligible capital expenditure provides some comfort.

Rating sensitivities

Positive factors – The rating could be upgraded if the Group demonstrates a significant improvement in its scale and a sustained high profitability, resulting in healthy credit metrics and an improved liquidity position.

Negative factors – The rating could be downgraded in case of a significant decline in the Group’s profitability, which will adversely impact its credit metrics and liquidity position. Further, any large debt-funded capex or capital withdrawal/dividend could lead to a downgrade. A specific metric for downgrade includes an interest cover of less than 4.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Iron & Steel
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of VRKP and VISIPL given the close business, financial and managerial linkages among them.

About the company

VRKP Sponge and Power Plant LLP (VRKP), incorporated in 2015 by Bangalore-based Mr. Vinod Kumar Agarwal, manufactures sponge iron, MS billets, TMT bars and generates power primarily for captive consumption, besides trading in various steel products in relatively limited quantity. Its manufacturing facilities are at Bellary, Karnataka. The entity has an installed manufacturing capacity of 120,000 MT-per-annum (MTPA) sponge iron plant, a 150,000-MTPA MS billet plant and a 140,000-MTPA TMT bar plant. The entity has a captive 12-MW power plant as well. The Group has further set up a project in VISIPL, wherein the sponge iron is 165000 MT and 47 TPH WHRB boiler. The steam generated from the boiler is being used for the captive power plant in VRKP, resulting in significant cost savings at the Group level. The project achieved its commercial operations date (COD) on February 28, 2024.

Key financial indicators (audited)

Standalone	Standalone			Consolidated
	FY2022	FY2023	FY2024*	FY2024*
Operating income	609.3	756.0	685.4	700.1
PAT	14.5	18.6	21.1	21.0
OPBDIT/OI	4.9%	5.7%	7.0%	7.1%
PAT/OI	2.4%	2.5%	3.1%	3.0%
Total outside liabilities/Tangible net worth (times)	0.9	0.9	1.7	4.7
Total debt/OPBDIT (times)	1.3	0.7	1.3	5.4
Interest coverage (times)	4.4	6.1	4.7	4.2

Source: Company, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current rating (FY2025)		Chronology of Rating History for the past 3 years				
	Type	Amount rated (Rs. crore)	Date & rating in FY2025	Date & rating in FY2024		Date & rating in FY2023	Date & rating in FY2022
			Sep 30, 2024	15-Nov-23	20-Oct-23	22-Jul-22	-
1 Cash credit	Long Term/Short Term	40.00	[ICRA]BBB+ (Stable)/[ICRA]A2	[ICRA]BBB+ (Stable)/[ICRA]A2	[ICRA]BBB+ (Stable)/[ICRA]A2	[ICRA]BBB (Stable)/[ICRA]A3+	-
2 Term loan	Long Term	6.27	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)			-
3 Letter of credit	Short Term	25.00	[ICRA]A2	[ICRA]A2			-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Cash credit	Simple
Term loan	Simple
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	Cash credit	NA	NA	NA	40.00	[ICRA]BBB+ (Stable)/ [ICRA]A2
NA	Term loan	FY2023	NA	FY2027	6.27	[ICRA]BBB+(Stable)
NA	Letter of credit	NA	NA	NA	25.00	[ICRA]A2

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

Annexure II: List of entities considered for consolidated analysis

Company Name	VRKP Ownership	Consolidation Approach
VRKP Integrated Steel Industries Private Limited	-	Full Consolidation

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Branches



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