ICRA

September 19, 2017

# APL Apollo Tubes Limited Revised

**Summary of rated instruments**

| Instrument* | Rated Amount (in Rs. crore) | Rating Action |
|---|---|---|
| Cash Credit Limits | 445.0 | [ICRA]AA- (Stable)/[ICRA]A1+ *Upgraded from [ICRA]A+ (Stable)/[ICRA]A1+* |
| Term Loans | 121.0 | [ICRA]AA- (Stable) *Upgraded from [ICRA]A+ (Stable)* |
| Non-fund Based Limits | 130.0 | [ICRA]A1+ *reaffirmed* |
| Unallocated Limits | 65.0 | [ICRA]AA- (Stable)/[ICRA]A1+ *Upgraded from [ICRA]A+ (Stable)/[ICRA]A1+* |
| Non-convertible Debenture | 125.0 | [ICRA]AA- (Stable) *Upgraded from [ICRA]A+ (Stable)* |
| Commercial Paper | 200.0 | [ICRA]A1+(SO) *reaffirmed* |

*Instrument details are provided in Annexure-1

**Rating action**

ICRA has upgraded the long-term rating from [ICRA]A+ (pronounced ICRA A plus) to [ICRA]AA- (pronounced ICRA double A minus) and reaffirmed the short term rating of [ICRA]A1+ (pronounced ICRA A one plus) for Rs. 761.0-crore [1] bank limits of APL Apollo Tubes Limited (AATL). ICRA has also upgraded the rating from [ICRA]A+ (pronounced ICRA A plus) to [ICRA]AA- (pronounced ICRA double A minus) for Rs. 125.0-crore Non-convertible Debentures (NCD) and reaffirmed the rating of [ICRA]A1+ (SO) (pronounced ICRA A one plus {Structured Obligation}) for Rs. 200.0-crore Commercial Paper (CP) programme of AATL. The outlook on the long term rating is ‘Stable’.

**Rationale**

The SO rating is credit enhanced by a Standby Letter of Credit (SBLC) from Union Bank of India. The rated instrument does not involve a structured payment mechanism.

AATL and its three wholly-owned subsidiaries, namely Shri Lakshmi Metal Udyog Limited, Lloyds Line Pipes Limited and Apollo Metalex Private Limited, are in similar lines of businesses and have significant operational and financial linkages. Thus, ICRA has taken a consolidated view for credit risk assessment of the Group, referred to as the ‘APL Group’ or ‘the Group’.

The revision in rating factors in healthy YoY growth of 20% in manufacturing income during Q1FY2018 on the back of 11% YoY growth in volume sales. The Group has been entailing capex to enhance its manufacturing capacities, which are ramping up steadily. This is anticipated to result in healthy volume growth going forward, as exhibited in the Q1FY2018 performance. It is expected that the growth in volumes would be sustained and drive the uptick in operating income for FY2018. Growth in revenue generation is also expected to be driven by geographical expansion in the Eastern India markets by virtue of the Green-field manufacturing facility in Raipur, addition of new products, growing application of pipes, and the efforts made by the Group to improve its brand. While sustenance and growth in operating profitability remains to be seen in FY2018, given the pressures faced in the first quarter, the cashflow generation is expected to be strong on account of control on interest expenses, as well as working capital requirements.

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[1] *100 lakh = 1 crore = 10 million*

The ratings continue to factor in the Group's strong liquidity position following marked by sizeable cushion in the working capital limits against the drawing power; and healthy debt coverage indicators (interest coverage of 4.75 times, Debt/OPBDITA of 1.84 times, DSCR of 2.20 times and NCA/Debt of 33% as on March 31, 2017). While the company has bullet NCD repayments in FY2020, these are expected to be comfortably covered as the liquidity of the company is expected to remain strong keeping in view the capex plans and the estimated cash flow generation.

Moreover, the rating continues to take into account the Group's leadership position in the electric resistance welded (ERW) pipes segment, and its strong manufacturing base with plants in North (Sikandarabad, UP), West (Murbad, Maharashtra) and South (Bengaluru and Hosur) and one in East (Raipur). Further, the Group is constantly making efforts to improve the product mix in favour of higher-margin products like hollow sections, pre-galvanised (GP) and galvanised iron (GI) pipes, which are expected to aid in improvement in EBITDA per tonne. The rating also captures the fact that the Group has always focussed on introducing new products (like colour-coated pipes, door and window frames, etc.) and adoption of efficient technologies (like direct forming technology, inline galvanising, etc.).

The rating, however, is tempered by the highly competitive nature of the pipes and tubes industry with presence of both organised and unorganised players as well as moderate value-addition resulting in moderate pricing power and range-bound profitability. The ratings also take into account the susceptibility of margins to movement in steel HRC prices given the high raw material intensity and levels of inventory required to be maintained, as was reflected in Q1FY2018. The company has undertaken sizeable expansion of capacities, and utilisation of the same would be critical to maintaining return on capital. While assigning the ratings, ICRA took cognisance of the fact that the promoter holding in AATL has declined in the past one year and stood at a relatively lower level of 37.5% as of June 30, 2017.

ICRA notes that the Group has plans to increase its installed capacity to 2 million TPA by FY2019; and establish new capacities for inline galvinising through a joint venture.  However, the funding for these would be largely met from internal accruals, which would result in an improvement in the capital structure going forward. This apart, steady ramping up of capacities leading to growth in volumes and thus growth in turnover and EBITDA per tonne would be the key rating sensitivities for the Group.

**Key rating drivers**

**Credit strengths**

- **Extensive experience of the promoters in the pipes industry**: Incorporated in 1986, the company has over three-decade-long track record of operations in the pipes industry. The Group manufactures ERW black pipes, hollow sections and GI/GP pipes with the hollow sections contributing to most of the revenues.
- **Market leadership in the ERW pipes segment with consistent enhancement in capacities:** The APL Group has a well-established position in the ERW segment and controls a significant market share in this same. Moreover, the group has consistently expanded its manufacturing capacities to keep pace with the market growth.
- **Expansive manufacturing base with extensive distribution network:** The Group has a pan-India presence with manufacturing units in North, West and South India. The unit in eastern India is under implementation. This apart, the Group has 26 warehouses and around 600 dealers across the country.
- **Diversified product profile**: The Group manufactures MS black pipes, GI pipes, GP pipes and hollow sections with constant focus on value-added products. This has resulted in an increase in the proportion of such products in the product portfolio.

- **Reduction in debt levels and considerable improvement in liquidity position:** With strong accrual generation, the debt levels of the Group have witnessed a decline and the trend is expected to continue. Further, the working capital limits are sufficiently cushioned, which along with healthy cash flow position reflect improvement in the Group's liquidity position.
- **Consistent growth in OI and manufacturing profitability margins:** With a consistent increase in sales volumes backed by higher production capacities, the company's OI has grown at a CAGR of 27% over the last five years. In FY2017, the OI grew by 8% to Rs. 4,545 crore, while the operating margins improved to 7.1% in FY2017 on the back of economies of scale and increase in the proportion of value-added products, resulting in improvement in EBITDA per tonne.
- **Focus on process efficiencies, innovation and new technologies:** The Group has been focussing on process improvements, introduction of new products and adoption of new technologies. Products like colour-coated pipes, door and window frames and new technologies like the DFT and proposed inline galvanising technology not only provide cost savings but also yield superior products.
- **Consistent reduction in working capital intensity with improvement in receivables period:** Over the years, there has been a consistent improvement in the receivables period, which resulted in improvement in working capital intensity of operations as reflected by NWC/OI of 11% as of March 31, 2017 as against 14% as of March 31, 2016.

**Credit weaknesses**

- **Vulnerability of operating profitability to raw material price movement:** The margins are susceptible to movement in steel prices as was witnessed in FY2015 and FY2016, when the Group incurred inventory losses.
- **Intense competition from large as well as unorganised players:** The ERW pipes market is inherently competitive with the presence of large established players like Surya Roshni, Jindal Pipes, Welspun Corp. etc., in addition to large number of unorganised and regional players.
- **Relatively low promoter holding**: Reduction in promoter shareholding over the last one year to 37.5% as of June 30, 2017

**Analytical approach:** For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

**Links to applicable criteria**

Corporate Credit Rating Methodology
Rating Methodology for Entities in the Ferrous Metals Industry
ICRA's Approach for Rating Commercial Papers
Approach for rating debt instruments backed by third-party explicit support

**About the company**

AATL is a public limited company involved in manufacturing steel pipes and tubes. Its product range includes GI pipes, GP pipes and Black pipes in both round and hollow pipes (rectangular and square cross section) within the ERW pipe segment. The company has steadily enhanced its capacities and widened its presence across geographies by way of acquisition – Lloyd Line Pipes Limited (LLPL, acquired in FY2011) in Murbad (Maharashtra), Shree Lakshmi Metal Udyog Limited (SLMUL, acquired in FY2008) in Bangalore (Karnataka) and Apollo Metalex Private Limited (AMPL, acquired in FY2007) in Sikandarabad (Uttar Pradesh). In addition, AATL established a new unit in Hosur (Tamil Nadu) in 2011 and is in the process of setting up a new facility in Raipur (Chhattisgarh). LLPL, SLMUL, and AMPL are 100% subsidiaries of AATL. At present, the Group has an aggregate capacity of 1,300,000 MTPA on a consolidated basis.

**Key Financial Indicators**

| Consolidated (Rs. Crore) | FY2016 | FY2017 |
|---|---|---|
| Operating Income (Rs. crore) | 4213.6 | 4545.0 |
| PAT (Rs. crore) | 100.6 | 145.9 |
| OPBDIT/ OI (%) | 6.7% | 7.1% |
| RoCE (%) | 18.9% | 22.7% |
| | | |
| Total Debt/ TNW (times) | 1.15 | 0.83 |
| Total Debt/ OPBDIT (times) | 2.31 | 1.84 |
| Interest coverage (times) | 4.05 | 4.75 |
| NWC/ OI (%) | 14% | 11% |

*OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);*
*NWC: Net Working Capital*

**Status of non-cooperation with previous CRA:** Not applicable

**Any other information:** Not applicable

**Rating history for last three years**

**Table**

| S. No. | Instrument | Current Rating (FY2018) | | | | Chronology of Rating History for the past 3 years | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated (Rs. Crore) | Date &Rating | | Date & Rating in FY2017 | Date & Rating in FY2016 | Date & Rating in FY2015 | |
| | | | | Sep 2017 | Aug 2017 | Oct 2016 | Dec 2015 /Jan 2016 | Mar 2015 | Sep 2014 |
| 1 | Fund-based Limits | Long/ Short Term | 445.0 | [ICRA]AA- (Stable)/ [ICRA]A1+ | [ICRA]A+ (Stable)/ [ICRA]A1 + | [ICRA]A + (Stable)/ [ICRA]A1 | [ICRA]A (Stable)/ [ICRA]A1 | [ICRA]A (Stable) | [ICRA]A- (Stable) |
| 2 | Term loans | Long Term | 121.0 | [ICRA]AA- (Stable) | [ICRA]A+ (Stable) | [ICRA]A + (Stable) | [ICRA]A (Stable) | [ICRA]A (Stable) | [ICRA]A- (Stable) |
| 3 | Non-fund Based Limits | Short Term | 130.0 | [ICRA]A1+ | [ICRA]A1 + | [ICRA]A1 | [ICRA]A1 | [ICRA]A1 | [ICRA]A1 |
| 4 | Unallocated limits | Long/ Short Term | 65.0 | [ICRA]AA- (Stable)/ [ICRA]A1+ | [ICRA]A+ (Stable)/ [ICRA]A1 + | [ICRA]A + (Stable)/ [ICRA]A1 | - | - | |
| 5 | Non Convertible Debenture | Long Term | 125.0 | [ICRA]AA- (Stable) | [ICRA]A+ (Stable) | [ICRA]A + (Stable) | - | - | |
| 6 | Commercial Paper | Short Term | 200.0 | [ICRA]A1+ (SO) | [ICRA]A1 + (SO) | [ICRA]A1 + (SO)/ [ICRA]A1 | [ICRA]A1 + (SO)/ [ICRA]A1 | [ICRA]A1 | [ICRA]A1 |

**Complexity level of the rated instrument**

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website [www.icra.in](http://www.icra.in)

**Annexure-1**
**Instrument Details**

| ISIN No. | Instrument | Date of Issuance / Sanction | Coupon Rate | Maturity | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| | Fund-based Limits | - | - | - | 445.0 | [ICRA]AA- (Stable)/ [ICRA]A1+ |
| | Term loans | FY2015-FY2017 | - | FY2019-FY2023 | 121.0 | [ICRA]AA- (Stable) |
| | Non-fund Based Limits | - | - | - | 130.0 | [ICRA]A1+ |
| | Unallocated limits | - | - | - | 65.0 | [ICRA]AA- (Stable)/ [ICRA]A1+ |
| | | | | | | |
| | Commercial Paper | 26/07/17 | - | 27/09/17 | 50.0 | [ICRA]A1+ (SO) |
| | Commercial Paper* | - | - | - | 150.0 | [ICRA]A1+ (SO) |
| INE702C07024 | Non Convertible Debenture | FY2017 | 8.2% | FY2020 | 50.0 | [ICRA]AA- (Stable) |
| | NCD* | - | - | - | 75.0 | [ICRA]AA- (Stable) |

Source: APL Apollo Tubes Limited
Note - Non fund based limits to be used as Fund based limits also
* - yet to be issued

**Corrigendum**

Document dated September 19, 2017 has been corrected with revision as detailed below

- The month in the rating history table for FY2018 has been revised as Aug 2017 instead of July 2017 as mentioned in earlier version on Page 5 of the document.

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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.

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