September 29, 2022

Neo Metaliks Limited: Ratings reaffirmed; [ICRA]A-(Stable) assigned for the enhanced amount

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based limits	78.50	78.50	[ICRA]A-(Stable); reaffirmed
Non-fund based facilities	158.20	114.20	[ICRA]A2+; reaffirmed
Term Loans	13.00	189.24	[ICRA]A-(Stable); reaffirmed/assigned
Total	**249.70**	**381.94**	

**Instrument details are provided in Annexure-1;*

Rationale

The reaffirmation of the ratings factors in the experience, of over a decade, of the promoters of Neo Metaliks Limited (NML) in the pig iron (mainly steel grade) manufacturing business, which has helped the company establish a strong customer base over the years. The ratings also consider the financial flexibility enjoyed by NML for being a part of the Rupa Group. The Group has a strong market position in the knitwear segment with a pan-India presence through Rupa & Company Limited (flagship company of the Rupa Group). The ratings also consider the semi-integrated nature of operations which strengthens the operating profile of the company. Over the years, NML has taken various cost improvement initiatives viz. setting up of a 4.5-MW power plant in FY2010, which operates on gas generated from the mini blast furnace, and commissioning of a sinter plant in FY2012. In April 2021, the company had commissioned a pulverised coal injection (PCI) facility to partially replace costlier coke with cheaper pulverised coal. The operationalisation and stabilisation of the PCI facility have led to significant cost savings for the company given the cost differences between met coke and pulverised coal. Post expansion of the capacity of the blast furnace, the company would be able to inject higher volumes of pulverised coal, leading to greater efficiencies which will cushion its profits during periods when pig iron prices remain less buoyant.

The ratings, however, remain constrained by the large debt-funded capex, which is expected to weaken the leverage ratios. The debt-funded nature of the capex would keep the overall debt levels elevated leading to a weakening of the leverage indicators (Net Debt/OPBDITA) over the near term. While funding risks remain mitigated with the project debt being already tied-up and equity funding to be done from the existing internal resources, NML would remain exposed to project execution risks given the company's limited track record in commissioning greenfield/brownfield projects. Moreover, ICRA notes that the project execution risks remain heightened given that the scope of the project involves dismantling of the existing smaller blast furnace and replacing it with a larger sized and more efficient blast furnace, leading to the company having no cash flows for two to three months during the final stages of execution. The ability to stick to the targeted timelines once the project enters the critical last-leg, when the existing furnace is shut down, remains a key monitorable. The ratings also remain constrained by the company's exposure to the cyclicality inherent in the pig-iron business as margins fluctuate due to temporary mismatches in the prices of raw materials and pig iron, causing volatility in profitability and cash flows. However, the semi-integrated nature of business, with the presence of sinter plant, captive power plant and PCI facility, enhances the cost-competitiveness and reduces the vulnerability to an extent.

The Stable outlook on the company's long-term rating reflects ICRA's belief that NML's cash flows would remain comfortable relative to its current debt service obligations. Notwithstanding the large debt-funded capex plans which will lead to increased debt levels, the 18-month moratorium on debt servicing for the project debt should support the liquidity profile over the near term.

Key rating drivers and their description

Credit strengths

Extensive experience of promoters; financial flexibility arising from being a part of Rupa Group – NML benefits from the experience of its promoters in the pig-iron manufacturing industry, spanning over a decade. The long experience of the promoters has helped the company establish a strong customer base over the years. ICRA also notes the company's established trade relationships with clients, which enabled it to get repeat business over the years. NML's status as being part of the Rupa Group imparts considerable financial flexibility to the company. The Group has a strong market position in the economy, medium and premium segments of the innerwear market with a pan-India presence through Rupa & Company Limited (flagship company of the Rupa Group). In the past, the Group has supported NML through infusion of funds. ICRA expects support from the Group to be forthcoming, if required.

Semi-integrated nature of operations strengthens operating profile – Over the years, NML has taken various cost-improvement initiatives viz. setting up of a 4.5-MW power plant in FY2010, which operates on gas generated from the mini blast furnace, and commissioning of a sinter plant in FY2012. In April 2021, the company had commissioned a pulverised coal injection (PCI) facility to partially replace costlier coke with cheaper pulverised coal, which led to significant cost savings for the company.

Stabilisation of operations at PCI facility has led to structural cost savings – The operationalisation and stabilisation of the PCI facility in April 2021 has led to significant cost savings for the company given the cost differential between met coke and pulverised coal. Post expansion of the capacity of the blast furnace, the company would be able to inject higher volumes of pulverised coal, leading to greater efficiencies which will cushion its profits during periods when pig iron prices remain less buoyant. Moreover, ICRA understands that the company is looking to increase the PCI injection rate from the existing 80 kg/MT hot metal to ~120-150 kg/MT hot metal following the commissioning of the enhanced capacity in H1 FY2024, which is expected to further increase the quantum of structural cost-savings.

Credit challenges

Large debt funded capex expected to lead to weakening of leverage ratios as well as exposes the company to project execution risks – The company has announced a large-sized capex programme of Rs.250 crore towards almost doubling the pig-iron capacity, and other ancillary expansion such as more-than-doubling the sinter capacity and installation of a new 10-MW captive power plant. The project is expected to be commissioned in H1 FY2024. While the size of the capex is relatively larger compared with the existing balance sheet size and will be funded in a debt: equity ratio of 74:26, the capital cost remains quite competitive, which, coupled with the efficiency gains from operating larger blast furnace based on the more advanced bell-less-top technology, is expected to strengthen the company's cost position.

The debt-funded nature of the capex would keep the overall debt levels elevated, leading to a weakening of the leverage indicators (Net Debt/OPBDITA) over the near term. However, ICRA expects the leverage metrics, after weakening temporarily in FY2023 and FY2024, to gradually improve from FY2025 as the benefits of the expansion starts to fully flow in the income statement following a production ramp-up. While funding risks remain mitigated with the project debt of Rs.185 crore being already tied-up and equity funding to be done from internal resources, NML would remain exposed to project execution risks given the company's limited track record in commissioning greenfield/brownfield projects. Moreover, ICRA notes that the project execution risks remain heightened given that the scope of the project involves dismantling of the existing smaller blast furnace and replacing it with a larger sized and more efficient blast furnace, leading to the company having no cash flows for two to three months during the final stages of execution. The ability to stick to the targeted timelines once the project enters the critical last-leg, when the existing furnace is shut down, remains a key monitorable.

Profit and cash flows exposed to cyclical nature of pig-iron business – Raw materials account for the major portion of the operational cost for pig-iron players, including NML, and are thus important determinants of profitability. As the pig-iron business is cyclical in nature (for being exposed to the cyclicality of the steel industry), NML's cash flows and profitability would remain volatile because of vulnerability to mismatches in prices of raw materials and pig iron. However, the semi-integrated nature of business, with the presence of sinter plant, captive power plant and PCI facility enhances the cost-competitiveness and reduces the vulnerability to an extent.

Liquidity position: Adequate

NML's liquidity profile remains **adequate**, reflected in the large cash/bank/liquid investment portfolio of ~Rs. 50 crore as on March 31, 2022, and healthy cash flow from operations (~Rs. 50-60 crore annually in FY2023 and FY2024) expected in the near term. Against these sources of cash, the company has debt repayment obligations of ~Rs. 4-5 crore in FY2023 and FY2024. Although much of the cash/bank/ liquid investment portfolio will be used up in the current fiscal to fund the equity portion of the capex, the remaining portion will be funded by a project debt of Rs.185 crore, which has already been tied-up, thus supporting the liquidity profile.

Rating sensitivities

Positive factors – ICRA may upgrade NML's ratings if it commissions its ongoing expansion project within the budgeted time and costs leading to an increase in scale, healthy growth in earnings and improvement in profitability. A specific credit metric for an upgrade is if RoCE is above 17.5%, on a sustained basis.

Negative factors – Pressure on NML's ratings could arise if the company encounters unexpected challenges during the execution phase of the capex leading to time and cost overruns as well as a deterioration of the liquidity position. Also, any significant contraction in the pig-iron spreads from the prevailing levels could also exert pressure on the ratings. The ratings could also come under pressure if, following the commissioning of the project the Net Debt/OPBDITA exceeds 2.25 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Ferrous Metals Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the standalone financial profile of the company.

About the company

Neo Metaliks Limited (NML) was set up in FY2003 and was jointly promoted by the Madhogaria and Agarwal families of Kolkata. In FY2005, the Madhogaria family exited the business and the Agarwal family took complete control of the company. NML manufactures pig iron at its plant in Durgapur, West Bengal (since FY2007) with the present installed capacity of 1,88,000 TPA. As a part of its backward integration initiative, the company has set up a waste heat recovery-based captive power plant of 4.5 MW and a sinter plant with a capacity of 3,00,000 TPA. At present, the company is undertaking a Rs. 250-crore expansion project, which would double the installed pig-iron capacity to around 3,90,000 TPA. The project is expected to be commissioned in H1 FY2024.

Key financial indicators (Audited)

NML Standalone	FY2021	FY2022^
Operating Income (Rs. crore)	588.5	835.0
PAT (Rs. crore)	27.6	31.2
OPBDIT/OI (%)	9.8%	6.4%
PAT/OI (%)	4.7%	3.7%
Total Outside Liabilities/Tangible Net Worth (times)	0.6	0.8
Total Debt/OPBDIT (times)	0.5	1.7
Interest Coverage (times)	11.6	11.0

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ^Provisional

Status of non-cooperation with previous CRA:

CRA	Status	Date of Release
CRISIL	CRISIL BB+/Stable/A4+; ISSUER NOT COOPERATING	August 25, 2022

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)					Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2022 (Rs. crore)	Date & Rating		Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					Sep 29, 2022	Jul 14, 2022	Jul 8, 2021	Mar 15, 2021	Dec 27, 2019
1	Fund-based limits	Long Term	78.50	--	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
2	Term Loans	Long Term	189.24	4.25	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)
3	Non-fund based facilities	Short Term	114.20	--	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based limits	Simple
Non-fund based facilities	Very simple
Term Loans	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: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (RS Crore)	Current Rating and Outlook
NA	Fund-based limits	NA	NA	NA	78.50	[ICRA]A-(Stable)
NA	Non-fund based facilities	NA	NA	NA	114.20	[ICRA]A2+
NA	Term Loans	FY2020	NA	FY2030	189.24	[ICRA]A-(Stable)

Source: *Company;*

Please click here to view details of lender-wise facilities rated by ICRA

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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About ICRA Limited:

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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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