

March 28, 2023

Mahindra Steel Service Centre Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based Cash Credit	25.00	25.00	[ICRA]AA- (Stable); reaffirmed
Long-term Fund-based Term Loan	25.00	12.50	[ICRA]AA- (Stable); reaffirmed
Short-term Non-fund Based Limits	140.00	140.00	[ICRA]A1+; reaffirmed
Long-term Interchangeable [^]	(25.00)	(25.00)	[ICRA]AA- (Stable); reaffirmed
Long-term/Short-term Unallocated	10.50	60.00	[ICRA]AA- (Stable)/ [ICRA]A1+; reaffirmed and assigned to enhanced limits
Total	200.50	237.50	

Note: Instrument details are provided in Annexure-I

[^]Cash credit facility is sublimit of non-fund-based facility

Rationale

The rating reaffirmation continues to take into account the strong financial flexibility enjoyed by Mahindra Steel Service Centre Limited (MSSCL) as a part of the Mahindra Group, its strong operational and financial linkages with the parent company, Mahindra Accelo Limited (MAL; rated [ICRA]AA+(Stable)/[ICRA]A1+), and the location specific advantage from the proximity of its plants to its key customers. The ratings also draw comfort from MSSCL's collaboration with Nippon Steel, one of the leading global suppliers of electrical and automotive steel, which reduces procurement related risks.

The rating, however, remains constrained by MSSCL's exposure to cyclical end-markets (automotive and electrical segments), as reflected in volatility in its return indicators and the stiff competition in the steel processing business. This was visible in its operating performance over the recent past, wherein the pandemic period saw a period of revenue and margin contraction, followed by steep recovery in FY2022 and the current fiscal, buoyed by healthy volume offtake as well as firm steel prices. The company is also exposed to competition from other steel processing players, which limits its pricing power to an extent. However, its established market position in the electrical steel segment as well as strong relationships with key customers mitigate this risk to an extent. ICRA, however, will continue to monitor the sustenance of MSSCL's growth momentum as well as its ability to maintain or improve its margins further. The ratings also consider MSSCL's exposure to forex risks since a large part of its raw material is imported, while its entire sales goes into the domestic market. Nevertheless, the company follows a formal hedging policy, which partly mitigates such risks. The ratings also remain constrained to some extent by customer concentration risks, because of its limited customer base, most of whom are transformer manufacturers. However, its efforts to diversify through the new plant set up in Chennai to cater to automotive customers in South India offers comfort.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company will continue to benefit from the support from its promoter group and the established track record of its operations, while maintaining its comfortable financial risk profile over the medium term.

Key rating drivers and their description

Credit strengths

Strong parentage – MAL, the parent company of MSSCL, holds a 61% stake in the company. MAL is involved in a similar business sector as MSSCL and has operational linkages by undertaking steel processing job-works for MAL. A large part of

MSSCL's automotive steel processing is carried out on a job-work basis for MAL, which reduces the inventory requirement and, hence, the price risk for the company. MSSCL also has additional source of liquidity in the form of support from MAL, in case of any temporary cash flow mismatches.

Comfortable capital structure and healthy debt-protection metrics – MSSCL's capital structure has remained comfortable over the years, given the healthy net worth base and stable operations. Its gearing stood at 0.9 time as on March 31, 2022, and debt-protection metrics remain robust with Total debt/OPBITDA of 2.4 times and interest coverage ratio of 8.8 times in FY2022. Despite some expected addition in debt levels for increase in working capital borrowings to support the increased scale of operations, MSSCL is expected to continue to report healthy credit metrics supported by its stable performance.

Collaboration with Nippon Steel – The company sources cold rolled grain oriented (CRGO) and cold rolled non-grain oriented (CRNO) steel through imports. Nippon Steel, one of the leading manufacturers of CRGO and CRNO steel, supplies the same to MSSCL through Metal One Corporation, which is its global distributor. MSSCL's collaboration with Nippon Steel reduces risks related to material availability and procurement.

Location-specific advantage and non-M&M customer base – MSSCL's Bhopal facility primarily caters to CRGO steel used in transformer cores and is located in proximity to key customers of electrical steel, resulting in lower freight cost that supports its profitability. Over the years, MSSCL has mainly catered to the electrical steel segment, limiting its dependence on M&M for revenues. This has been further strengthened over the recent past, with ramp up at its Chennai plant, which caters to non-M&M customers in the automotive space.

Credit challenges

Susceptibility of business growth to cyclicity in end-user industry – MSSCL is exposed to cyclical end-markets (automotive and electrical segments), as reflected by the volatility in its return indicators. This was evident in its performance over the past couple of fiscals, wherein revenues declined by 19% and 29% in FY2021 and FY2020, respectively, followed by robust growth of 84% in FY2022, in line with increased demand from end-user industries and increase in steel prices, which has continued into the current fiscal as well.

High customer concentration risk – MSSCL's customer base includes transformer core manufacturers (for electrical steel) and auto OEMs (for automotive steel). The customer concentration remained high with the top five customers accounting for 50% of operating income in FY2022. Nevertheless, ICRA notes that the customer base of MSSCL comprises large, reputed transformer manufacturers and its Group companies have a strong credit profile, which reduces its exposure to counterparty credit risks. Additionally, in a bid to diversify its customer base, the company has set up a steel blanking and lamination (CR as well as CRGO) facility in Chennai to cater to the OEMs in South India. Ramp up from the same would help mitigate this risk over the medium term.

Margins remain vulnerable to commodity price and forex risks – The basic raw material for the company is steel and the company's revenues and profitability remain exposed to fluctuations in steel prices. Additionally, imports accounted for more than 50% of MSSCL's total procurement in FY2022, while its entire revenue came from the domestic market. In the absence of a natural hedge, the company's operations remain exposed to forex risks. Nevertheless, most of the foreign currency payables of MSSCL are hedged by forward contracts, which provides some comfort. Hedging is based on the sale price closure and the hedging cost is recovered from buyers.

Liquidity position: Adequate

MSSCL's liquidity position is likely to remain adequate, supported by cash flows of Rs. 30-40 crore generated from operations annually, and unutilised working capital limits (~Rs. 25 crore as on December 31, 2022). Against these sources of liquidity, the company has minimal capex plans of Rs. 15-20 crore annually, and limited debt repayments of Rs. 7-10 crore annually, which

would be comfortably met from existing sources of liquidity. Besides, funding support from MAL to meet any cash flow mismatches strengthens its liquidity.

Rating sensitivities

Positive factors – ICRA may upgrade MSSCL’s rating in case of a sustained growth in revenues and/or profitability, leading to an improvement in the financial risk profile.

Negative factors – Any sustained pressure on revenues and profitability, leading to low cash accruals, coupled with an elongation in the working capital cycle, could impact MSSCL’s liquidity profile and in turn, the ratings. Pressure on the ratings could also arise if the interest coverage ratio remains below 5.0 times on a sustained basis. Deterioration in the credit profile of the parent company or weakening of linkages with the parent could also result in a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Auto Component Supplier Impact of Parent or Group support on an Issuer’s Credit Rating
Parent/Group Support	The ratings assigned to MSSCL factor in the high likelihood of its parent, Mahindra Accelo Limited (MAL; rated [ICRA]AA+ (Stable)/A1+), extending financial support to it because of close business linkages between them. ICRA also expects MAL to be willing to extend financial support to MSSCL to protect its reputation from the consequences of a Group entity’s distress.
Consolidation/Standalone	The ratings are based on the standalone financial statements of MSSCL.

About the company

Mahindra Steel Service Centre Limited, a joint venture between Mahindra Accelo Limited (rated [ICRA]AA+/Stable/[ICRA]A1+; holding 61%) and Metal One Corporation (Japan), is involved in the processing of automotive and electrical steel on a job-work as well as stock-and-sale basis. MSSCL’s steel processing facilities are located at Kanhe (near Pune), Bhopal and Noida, with installed production capacities of 114,800 MTPA, 32,200 MTPA and 2,400 MTPA, respectively. In August 2020, MSSCL commissioned a steel blanking and lamination facility in Chennai with a production capacity of 30,000 MTPA to cater to the OEMs in that region.

Key financial indicators (Audited)

MSSCL– Standalone	FY2021	FY2022
Operating income	171.3	315.1
PAT	-6.6	18.4
OPBDIT/OI	3.8%	14.0%
PAT/OI	-3.9%	5.9%
Total outside liabilities/Tangible net worth (times)	1.5	1.9
Total debt/OPBDIT (times)	10.7	2.4
Interest coverage (times)	1.3	8.8

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	Type	Current rating (FY2023)		Chronology of rating history						
		Amount rated (Rs. crore)	Amount outstanding as of Sept 30, 2022 (Rs. crore)	for the past 3 years						
				Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021		Date & rating in FY2020		
				Mar 28, 2023	Feb 14, 2022	Jan 15, 2021	Dec 31, 2020	Sept 27, 2019		
1 Fund-Based Cash Credit	Long-term	25.0	-	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	
2 Fund-Based Term Loan	Long-term	12.5	15.7	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	
3 Non-Fund-Based Facilities	Short-term	140.0	-	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	[ICRA] A1+	
4 Interchangeable	Long-term	(25.0)	-	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	-	-	-	-	
5 Unallocated	Long/Short Term	60.0	-	[ICRA]AA-(Stable)/[ICRA] A1+	[ICRA]AA-(Stable)/[ICRA] A1+	-	[ICRA]AA-(Stable)/[ICRA] A1+	-	-	
6 Fund-Based Facilities	Short-term	-	-	-	-	-	-	-	[ICRA] A1+	
7 Commercial Paper	Short term	-	-	-	-	-	-	-	[ICRA] A1+	

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based Cash credit	Simple
Long-term fund-based Term loan	Simple
Short-term non fund-based limits	Very simple
Long-term Interchangeable	Not applicable
Long-term/Short-term unallocated	Not applicable

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 analyzing 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, is available on ICRA's website: [Click Here](#)

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term fund-based Cash credit	NA	NA	NA	25.0	[ICRA]AA- (Stable)
NA	Long-term fund-based Term loan	FY2019-FY2020	7.30-8.20%	FY2025	12.5	[ICRA]AA- (Stable)
NA	Short-term non fund-based limits	NA	NA	NA	140.0	[ICRA] A1+
NA	Long-term Interchangeable	NA	NA	NA	(25.0)	[ICRA]AA- (Stable)
NA	Long-term/Short-term unallocated	NA	NA	NA	60.0	[ICRA]AA- (Stable)/ [ICRA] A1+

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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