October 12, 2023

Dhanlaxmi Iron Industries Pvt. Ltd.: Ratings Reaffirmed

Summary of rating action

Instrument*	Previous rated amount (Rs. Crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term Fund Based -Cash Credit	23.00	23.00	[ICRA]BBB+ (Stable); reaffirmed
Short Term Non-Fund Based - Letter of Credit	8.00	8.00	[ICRA]A2; reaffirmed
Short Term Interchangeable - Bank Guarantee	(8.00)	(8.00)	[ICRA]A2; reaffirmed
Long Term - Unallocated	14.00	14.00	[ICRA]BBB+ (Stable); reaffirmed
Total	**45.00**	**45.00**	

**Instrument details are provided in Annexure-I*

Rationale

ICRA has taken a consolidated view of Jeevaka Industries Pvt. Ltd. (JIPL) and Dhanlaxmi Iron Industries Pvt. Ltd. (DIIPL) (referred to as the Group hereafter), while arriving at the credit ratings, given the common management, significant operational and financial linkages and fungibility of funds between the companies. The operations of both the companies are highly integrated because of supply of billets from JIPL to DIIPL. These entities have common management persons, who belong to the same family, and centrally source raw materials.

The ratings reaffirmation factors in the Group's healthy year-on-year (YoY) revenue growth of ~23% in FY2023 and the expected good earnings growth in FY2024 due to relief from moderation in input costs (especially thermal coal) in H2 FY2024. Despite input cost pressure from elevated coal and scrap prices, the Group posted an operating profit of Rs. 39.44 crore (as per provisional figures) in FY2023 mainly due to savings in fixed costs amid greater asset sweating along with healthy sales realisations. The ratings also factor in the promoter's long experience of more than two decades in the secondary long steel manufacturing industry along with an established customer and supplier base. The ratings also factor in the semi-integrated operational profile with a capacity to manufacture sponge iron, MS billets and value-added downstream products such as structural steel and TMT bars. ICRA expects favourable domestic steel demand from end-user industries (like construction, infrastructure among others) and moderation in iron ore and coal costs to support the Group's revenue and profitability in FY2024.

Over the years, the Group has followed a calibrated approach to fund growth through a judicious mix of internal accruals/promoter funds and external borrowings. Around 35% of the outstanding debt of the Group as on March 31, 2023, comprised unsecured loan from promoters having flexibility in repayment of principal and interest, which supports the liquidity profile. ICRA notes that the Group has capex plans for setting up a greenfield site, to be executed in phases with setting up of a sponge iron plant planned initially, followed by installation of an induction furnace and a rolling mill in the subsequent phases. Also, the Group is planning to set up a 6-MW waste heat recovery boiler (WHRB)-based captive power plant to improve its cost competitiveness. While these expansion plans could constrain its free cash flows in the medium term, but at the same time increase the scale of operations and generate healthy annual savings post commissioning. At present, the projects are in the nascent stage of development and capital deployment plan is yet to be finalised. Consequently, the impact of this expansion on the Group's financial profile will be a key credit monitorable. The Group's current debt profile and credit metrics remain comfortable, characterised by healthy cash accruals and a low gearing of 0.63 times as on March 31, 2023.

The ratings, however, remain constrained by the Group's moderate operating profitability owing to high dependence on costlier power from the grid, and inbound freight costs for input materials, especially iron ore. The ratings are also tempered by the elevated working capital blockage due to increasing receivables. However, ~95% of the receivables as on March 31, 2023 was outstanding for less than 90 days and are considered recoverable. The ratings are further constrained by intense competition in the fragmented and commoditised steel industry, which limits its pricing flexibility, and the inherent cyclicality in the steel industry, exposing the Group to volatile cash flows. However, the Group has been able to report net profits across the business cycles, reflecting its resilience to cyclical downturns. In addition, the competitive capital cost of the steel making assets and associated low capital charges favourably support the net profit margin. The ratings are also constrained by the Group's exposure to geographical concentration risk, given its high dependence on the southern region. Nevertheless, its established and reputed customer base mitigates such risk to an extent.

The Stable outlook on the [ICRA]BBB+ rating reflects ICRA's opinion that the Group's earnings are expected to remain healthy in FY2024, supported by alleviation of input-cost pressure and strong domestic steel demand growth. ICRA also believes that the financial risk profile would remain comfortable in the near term, supported by low external borrowings and healthy capital structure.

Key rating drivers and their description

Credit strengths

Semi-integrated operations with capacity to manufacture sponge iron, MS billets, structural steels, and TMT bars – JIPL has manufacturing facilities for sponge iron, which along with MS scrap serves as a feedstock for manufacturing MS billets. Backward integration into captive sponge iron making gives the Group a cost advantage over other secondary steel producers, which are dependent on sourcing costlier sponge iron from the market. The manufactured MS billets are used to produce structural steel products in JIPL and TMT bars in DIIPL. Besides internal consumption of billets, the company sells them to other steel manufacturers, including DIIPL. JIPL has a capacity to manufacture 90,000 metric tonnes per annum (MTPA) of sponge iron, 1,80,000 MTPA of billets and 90,000 MTPA of structural steels. DIIPL has a manufacturing capacity of 1,44,000 MTPA TMT bars. These products are sold by DIIPL and JIPL under DIIL brand.

Extensive experience of promoters; established customer base – The promoters of the Group have more than four decades of experience in the iron and steel industries. Given the vast experience of the promoters in the industry and the established operational track record, the company has been able to develop a wide network of customers. The counterparty risk for the Group is low due to its established and reputed customer base.

Comfortable financial risk profile – The Group's debt levels remain under check, mainly comprising unsecured loans from promoters and working capital borrowings. The Group has taken a Guaranteed Emergency Credit Loan (GECL) in March 2022 to meets its working capital requirement and will repay it by FY2028. Apart from this there is hardly any dependence on external long-term borrowings. This led to a comfortable financial risk profile, characterised by a healthy gearing of 0.63 times and Total Outside Liability (TOL)/ Tangible Net Worth (TNW) of 1.02 times as on March 31, 2023. ICRA notes that the Group has capex plans for setting up a greenfield site, to be executed in phases with setting up of a sponge iron plant planned initially, followed by installation of an induction furnace and a rolling mill in the subsequent phases. Also, the Group is planning to set up a 6-MW WHRB-based captive power plant to improve its cost competitiveness. At present, the projects are in the nascent stage of development and the impact of this expansion on the Group's financial profile will be a key credit monitorable.

Ability to remain profitable across business cycles – The Group has been able to report net profits across all business cycles, reflecting its resilience to cyclical downturns. In addition, the competitive capital cost of the steel making assets and associated low capital charges favourably support the net profit margin.

Favourable domestic steel demand outlook – An accelerated pace of infrastructure spending ahead of the 2024 elections by the Central Government has ensured strong demand momentum for the domestic steel industry in the current fiscal as witnessed by steel consumption growth of 14.1% between April and August of FY2024 on a YoY basis and an upward revision in the steel demand growth to 9-10% in FY2024 full year (from 7-8% made earlier). Large-scale planned investments towards construction of new lines, dedicated freight corridors, high speed trains, track electrification, road overbridges / underpasses at level crossings, modernisation/ capacity augmentation of rolling stock/ locomotives, and station redevelopment projects to support steel demand.

Credit challenges

Moderate operating profit margin owing to structural inefficiencies associated with high power tariff and elevated inbound freight cost for input materials – Being a secondary steel manufacturer, JIPL's major costs are raw material and power contributing ~90% to the operating income (OI) in FY2023. The company is dependent on power supply from the grid, which increases the power cost owing to high tariffs. The consolidated operating margins of the Group stood at a moderate level of 3.39% in FY2023, declining from 4.74% in FY2022 due to a steep increase in raw material costs, which is not commensurate with the rise in steel prices. High fixed employee expenses also make the margins susceptible to a decline in turnover.

Increasing receivables leading to blockage of working capital – The total outstanding receivables increased to Rs. 217.39 crore as on March 31, 2023 from Rs. 143.05 crore as on March 31, 2022. ICRA notes that the debtor days increased to 68 in FY2023 from 49 in FY2020, exhibiting a growth of 39% during the said period, leading to increased blockage of funds available for working capital purposes. The increase is mainly driven by the higher credit period extended to the customers operating in the construction and real estate industry due to the long gestation period of the projects. However, ~95% of the receivables as on March 31, 2023 was outstanding for less than 90 days and are considered recoverable.

Exposure to cyclicality inherent in steel industry despite profitable operations across business cycles – The steel industry is cyclical in nature and is likely to impact the cash flows of the players, including JIPL and DIIPL. The company's operations are vulnerable to any adverse change in the demand-supply dynamics in the end-user industries such as power transmission and real estate sectors, especially in the southern region. Nevertheless, the Group's moderately integrated operations reduce the vulnerability of its profitability to the downturn in the steel industry, as evident from its modest profit even during the peak of the slowdown in the metal industry in FY2016. This demonstrates the resilience of the Group's performance during periods of stress.

Exposure to geographical concentration risks and intense competition in the fragmented long-steel business – The Group's operations are mainly concentrated in the southern region, exposing it to the geographical concentration risk. Moreover, its revenues are concentrated in power transmission, real estate, and construction sectors. Slowdown in these sectors led to an overall decline in its revenue during the past two fiscals. The fragmented long-steel manufacturing businesses is characterised by intense competition due to low product differentiation and entry barriers, which limit the pricing flexibility of the players, including that of JIPL and DIIPL.

Liquidity position: Adequate

The Group's liquidity position is adequate, supported by healthy cash accruals and sufficient undrawn limits. The average monthly utilisation of fund-based working capital limits, on a consolidated level, stood below 50% during March 2022 to June 2023. Though the free cash flows slipped to negative in FY2021 and FY2022 owing to rising steel prices and input costs, it became positive in FY2023. The Group's low scheduled debt repayment obligations and working capital buffer supported the overall liquidity during this period. As raw material prices (especially thermal coal) moderate in FY2024, a release in the working capital and steady earnings are expected to support free cash flows, supporting JIPL's and DIIPL's liquidity position.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings in case of a healthy growth in consolidated revenues and profitability on a sustained basis. Specific credit metric that could lead to ratings upgrade include an interest coverage of more than 5.0 times on a sustained basis.

Negative factors – Pressure on the ratings could arise if there is a decline in revenues or profitability of the Group on a sustained basis. Elevated capex plans or increased working capital cycle, adversely impacting the Group's financial performance and liquidity position, may also put pressure on the ratings. The Group's inability to maintain an interest coverage above 3.50 times on a sustained basis could trigger ratings downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	[Corporate Credit Rating Methodology](#) [Rating methodology for Entities in the Ferrous Metal Industry](#)
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated the financials of JIPL and DIIPL, given the close operational, financial, and managerial linkages among them.

About the company

Dhanlaxmi Iron Industries Private Limited (DIIPL) was incorporated in 1999 and is promoted by Mr. Mohan Agarwal and his family members. The company manufactures TMT bars under the brand name of DIIL. DIIPL has an installed capacity for manufacturing 1,44,000 tonnes of TMT bars per annum at its manufacturing facility in Bonthapally, Telangana. DIIPL procures power from Telangana Southern Power Distribution Company Limited.

Key financial indicators

Consolidated	FY2022	FY2023*
Operating income	946.97	1,163.89
PAT	21.33	16.95
OPBDIT/OI	4.74%	3.39%
PAT/OI	2.25%	1.46%
Total outside liabilities/Tangible net worth (times)	1.03	1.02
Total debt/OPBDIT (times)	3.0	3.4
Interest coverage (times)	4.1	3.4

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

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
					Oct 12, 2023	Sep 12, 2022	Aug 30, 2022	May 10, 2021	April 06, 2020
1	**Fund Based-Cash Credit**	Long Term	23.00	27.66	**[ICRA]BBB+ (Stable)**	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB (Stable)
2	**Unallocated**	Long Term	14.00	-	**[ICRA]BBB+ (Stable)**	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB (Stable)
3	**Interchangeable - Bank Guarantees**	Short Term	(8.00)	-	**[ICRA]A2**	[ICRA]A2	-	-	-
4	**Non Fund Based -Letter of Credit**	Short Term	8.00	-	**[ICRA]A2**	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A3+

5	**Bank Guarantees**	Short Term	-	-	-	-	[ICRA]A2	[ICRA]A2	[ICRA]A3+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term Fund Based - Cash Credit	Simple
Short Term Non-Fund Based - Letter of Credit	Very Simple
Short Term Interchangeable - Bank Guarantee	Very Simple
Long Term – Unallocated	NA

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	Long Term Fund Based - Cash Credit	NA	NA	NA	23.00	[ICRA]BBB+ (Stable)
NA	Short Term Non-Fund Based - Letter of Credit	NA	NA	NA	8.00	[ICRA]A2
NA	Short Term Interchangeable - Bank Guarantee	NA	NA	NA	(8.00)	[ICRA]A2
NA	Long Term – Unallocated	NA	NA	NA	14.00	[ICRA]BBB+ (Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	Consolidation Approach
Jeevaka Industries Private Limited	Full Consolidation
Dhanlaxmi Iron Industries Private Limited	Full Consolidation

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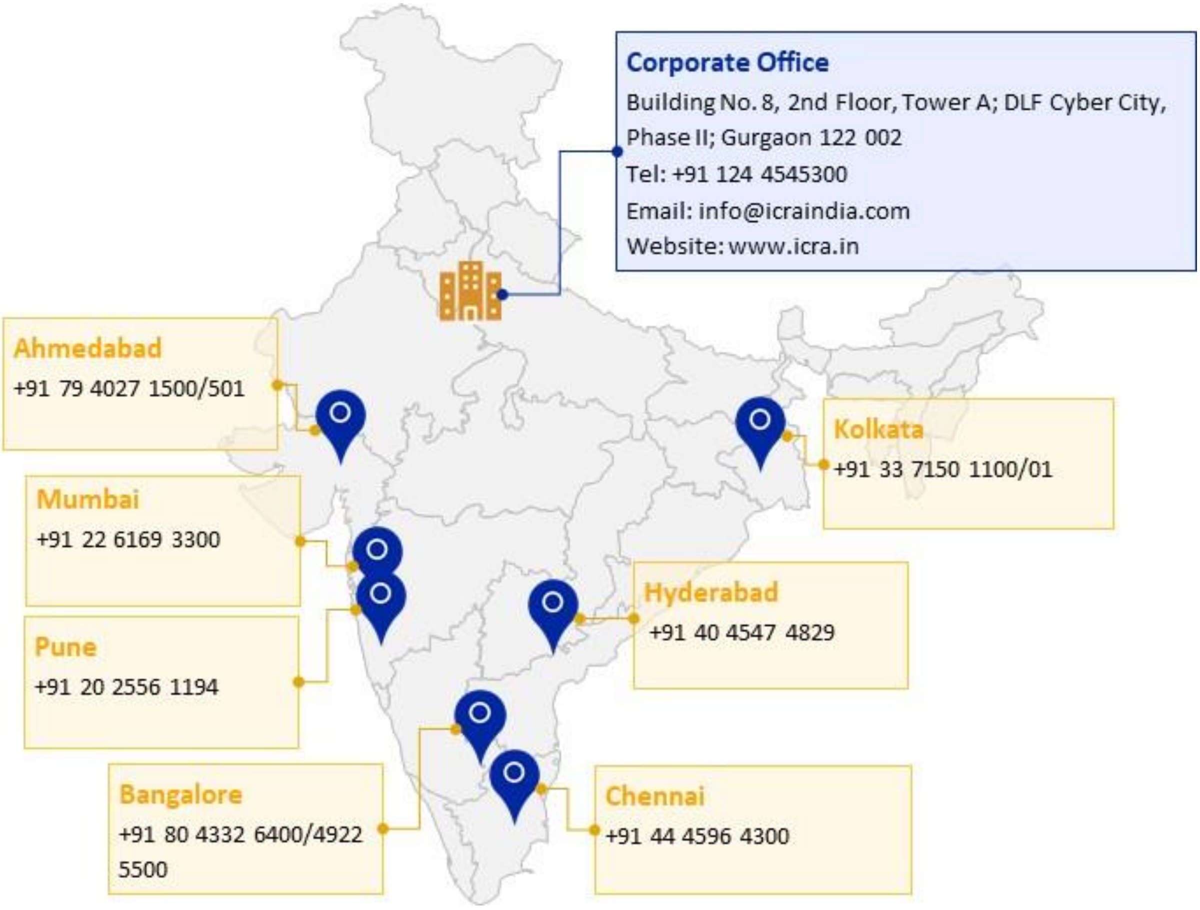

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