

December 29, 2023

ISMT Limited: Long-term rating upgraded; short-term rating reaffirmed

Summary of rating action

| Instrument* | Previous Rated Amount (Rs. Crore) | Current Rated Amount (Rs. Crore) | Rating Action |
|---|--------------------------------------|-------------------------------------|--|
| Long-term – Fund-based Limits | 145.00 | 145.00 | [ICRA]A+(Stable); upgraded from [ICRA]A(Stable) |
| Long-term – Fund-based Term Loan | 150.00 | 150.00 | [ICRA]A+(Stable); upgraded from [ICRA]A(Stable) |
| Short-term – Non-fund-based Limits | 385.00 | 385.00 | [ICRA]A1; reaffirmed |
| Long-term/Short-term – Unallocated Limits | 70.00 | 70.00 | [ICRA]A+(Stable); upgraded from [ICRA]A(Stable) and [ICRA]A1; reaffirmed |
| Total | 750.00 | 750.00 | |

*Instrument details are provided in Annexure-I

Rationale

The upgrade in the long-term rating of ISMT Limited (ISMT) factors in the healthy improvement in the operating profit margin (OPM) witnessed in H1 FY2024, which is likely to sustain going forward, thereby strengthening its overall financial profile. In H1 FY2024, ISMT's OPM increased to 14.4% from 8.6% in FY2023, led by improved gross margins, focus on value-added/high-margin products, various cost savings and efficiency improvement measures, among others. ICRA expects the OPM to further improve, going forward, once the solar power plant (phase I) becomes operational by the end of FY2024. This would keep the credit metrics comfortable in the near-to-medium term despite the large capital expenditure (capex) plans of the company of Rs. 350-400 crore in FY2024 and around Rs. 400 crore in FY2025 towards debottlenecking activities, efficiency improvement initiatives and cost-saving projects (including setting up a solar power plant in two phases to reduce power cost). ICRA notes that the proposed merger of ISMT into KFIL (which is subject to regulatory and other approvals) is likely to benefit the combined entity in terms of increased scale of operations, vertical integration, expanded reach and product diversification, among others.

The ratings continue to factor in ISMT's status as one of the leading integrated and specialised seamless tube manufacturers in India and its diversified customer base. ISMT benefits from its strong parentage and reputation of Pune-based Kirloskar Group and its proven management track record. ISMT also enjoys healthy financial flexibility for being a subsidiary of KFIL and the latter's stated intent to provide need-based funding support to ISMT.

The ratings are, however, constrained by ISMT's exposure to the inherent cyclicity in the steel industry, which may lead to volatility in its profits and cash flows. Besides, the company's profits are exposed to volatility in the prices of key raw materials such as pig iron, sponge iron, scrap, among others. The company's operations also remain vulnerable to any adverse changes in the demand-supply dynamics in the end-user industries such as automobile, bearing, oil and gas, among others.

ICRA notes the Serious Fraud Investigation Office's (SFIO) ongoing case against the erstwhile promoters of ISMT. As confirmed by the management, ISMT is only a proforma respondent here and the same is unlikely to have any adverse impact on the company. ICRA will continue to monitor developments in this regard.

The Stable outlook on the [ICRA]A+ rating reflects ICRA's expectations that despite large capex plans, ISMT's credit profile will remain adequately supported by healthy order inflows and steady improvement in margins, supported by its focus on better product mix and various cost efficiency measures that the company is undertaking.

Key rating drivers and their description

Credit strengths

Benefits from its strong parentage – KFIL took over the management control of ISMT by acquiring a 51.25% stake in March 2022. KFIL is a part of the reputed Pune-based Kirloskar Group and is one of the leading players in pig iron and ferrous casting segment. ISMT benefits from the strong reputation and financial flexibility of KFIL, besides the extensive experience of its management team. ISMT also enjoys healthy financial flexibility for being a subsidiary of KFIL and its stated intent to provide need-based funding support to ISMT. In November 2022, the Board of Directors of KFIL and ISMT approved the scheme of arrangement and merger of ISMT into KFIL. The merger (subject to regulatory and other approvals) is likely to benefit the combined entity in terms of increased scale of operations, vertical integration, expanded reach, and product diversification among others.

One of the largest seamless tube manufacturers in India; diversified customer base – ISMT is among the largest seamless tubes manufacturers in India. It has tube manufacturing facilities in Ahmednagar and Baramati (Maharashtra) with a combined capacity of 3,71,000 metric tonnes per annum (MTPA) and steel-making facility in Jejuri (Maharashtra) with a capacity of 3,50,000 MTPA. Its operations are integrated so that the company manufactures steel required for production of seamless tubes. Besides, it procures steel from external sources. All the manufacturing facilities are in the vicinity to each other, which leads to savings in transportation costs for the company.

ISMT's product profile is diversified as it produces seamless tubes in the range of 6 to 273 mm diameter. ISMT has customers in the automobile, bearing, power, oil and gas, boiler, general engineering, and hydraulic segments among others. ISMT's top-10 customers account for only 20-30% of the total sales each fiscal, reflecting a diversified customer base. ISMT also has a presence in the export markets, which accounted for 9-10% of its revenues in FY2023.

Turnaround in company's performance in FY2023; healthy and sustainable improvement in margins witnessed in H1 FY2024 – Post management takeover by KFIL and one-time settlement with the lenders in March 2022, ISMT's operating and financial performance recovered, supported by availability of bank lines (which facilitated smooth trade and led to improved order inflows). This also enabled the company to reduce its cost of procurement. Besides, the company undertook several efficiency improvement and cost-saving initiatives, which along with the benefit of the operating leverage helped it in margin expansion. In FY2023, ISMT reported revenues of Rs. 2,585 crore, reflecting a 19% YoY growth (aided by higher volumes and sales realisations) and its OPM increased to 8.6% from 3.5% in FY2022. In H1 FY2024, while the company reported 6% YoY revenue growth, its OPM increased to 14.4% owing to improved gross margins, focus on value-added/high margin/remunerative products, various cost efficiency measures, debottlenecking, among others. Its credit metrics strengthened, as reflected in its total debt-to-operating profit ratio of 0.1 times as on September 30, 2023, compared to 0.4 times as on March 31, 2023. Its interest cover stood at 31.9 times in H1 FY2024 compared to 10.2 times in FY2023. ICRA expects ISMT's credit metrics to remain robust in the near-to-medium term despite large capex towards solar power and other cost saving/upgradation projects. ISMT's OPM would further improve once the solar power plant phase I becomes operational by the end of FY2024.

Credit challenges

Large capex plans – While ISMT does not have debt repayment obligations at present, there are large capex plans of ~Rs. 350-400 crore in FY2024 (partly debt-funded) towards setting up a solar power plant, cost saving and efficiency improvement projects, debottlenecking activities and around Rs. 400 crore in FY2025 (partly debt-funded) towards capacity expansion and cost saving projects, which would keep its free cash flows under check. The company's ability to achieve the desired benefits and improve its overall operating performance from the above-mentioned capex plans over the medium term would be monitored.

Vulnerable to cyclicalities associated with the end-user industries – The company’s operations are vulnerable to any adverse change in the demand-supply dynamics in the end-user industries such as automobile, bearing, oil and gas, among others. The cyclicalities inherent in these sectors may lead to volatility in the company’s profits and cash flows. Nevertheless, ICRA notes that ISMT’s revenue mix is well diversified across sectors such that dependence on a particular sector is limited.

Exposure to volatility in raw material prices – The company’s profitability remains exposed to volatility in the prices of key raw materials like pig iron, sponge iron, scrap etc. ICRA notes that ISMT is focusing to increase the share of value-added and high-margin products in its portfolio, which will aid in margin expansion, going forward.

Liquidity position: Adequate

ISMT’s liquidity position is **adequate**, supported by free cash and bank balance of Rs. 12.8 crore as on September 30, 2023, and largely undrawn fund-based bank limits (sanctioned lines of Rs. 145 crore with adequate drawing power). Given the continued revenue growth and significant improvement in profitability in the current fiscal, ISMT’s fund flow from operations is expected to improve substantially on a YoY basis to around Rs. 300 crore, which will be mainly deployed towards working capital and capex requirements. Hence the company’s dependence on debt is expected to be limited. The company’s average utilisation of non-fund-based limits of Rs. 385 crore stood at around 64% during the 12-month period ended in October 2023. While ISMT does not have any debt repayment obligation at present, its large capex plan of ~Rs. 350-400 crore each in FY2024 and FY2025 towards solar power plant, cost saving projects and debottlenecking would keep its free cash flows under check.

Environmental & Social Risks

Environmental risks: ISMT, like all other players in the ferrous metals industry, is exposed to environmental risks emanating from its energy intensive process, which requires a substantial use of fossil fuels, resulting in greenhouse gas emissions, industrial waste generation and environmental pollution. ISMT faces pressure to reduce greenhouse gas and carbon emissions, among other sustainability issues. The company is equipped with total environmental control facilities like bag filters, zero liquid discharge system, recycle of solid waste like dust, among others which help reduce emissions. In the steel plant division, the company has reduced raw water intake by reprocessing of wastewater through RO treatment plant at various points. Besides, the company is in the process of setting up captive solar power plants, which would meet the major portion of its power requirements.

Social risks: Social risks for entities engaged in ferrous metal segment emerge from health and safety aspects of employees involved in the manufacturing activity. Casualties/accidents at the operating units due to gaps in safety practices could lead to production outages and invite penal actions from regulatory bodies. The company has institutionalised a safety organisation structure and conducts training programmes and safety audits to measure the efficacy of the training programmes as well as their implementation. ISMT also has a unionised workforce. However, there were no labour union protests/strikes in the last year.

Rating sensitivities

Positive factors – ICRA could upgrade ISMT’s ratings if it demonstrates continued healthy growth in revenues and profitability and improves its liquidity position while maintaining a comfortable capital structure and healthy debt coverage indicators.

Negative factors – Pressure on the ratings could arise if there is a deterioration in the earnings or a stretch in the working capital cycle or a large debt-funded capex adversely impacts ISMT’s financial risk profile and the liquidity position. The total debt-to-operating profit ratio remaining above 1.5 times on a sustained basis would be a negative factor. A deterioration in the credit profile of the parent company, KFIL, or weakening in the linkages with KFIL may also put pressure on the ratings.

Analytical approach

| Analytical Approach | Comments |
|---------------------------------|--|
| Applicable Rating Methodologies | Corporate Credit Rating Methodology Iron & Steel |
| Parent/Group Support | Parent - Kirloskar Ferrous Industries Limited (rated [ICRA]AA(Stable)/[ICRA]A1+) ICRA expects KFIL to provide need-based funding support to ISMT. |
| Consolidation/Standalone | For arriving at the ratings, ICRA has considered the consolidated financials of ISMT, which include 11 subsidiaries (as per annexure 2). |

About the company

Incorporated in 1977, ISMT manufactures seamless tubes, alloy and carbon steel rounds and billets. It is among the largest specialised seamless tube manufacturers in India. It has three manufacturing plants, one each in Jejuri (steelmaking facility), Baramati and Ahmednagar (tube manufacturing). Its current tube manufacturing capacity is 3,71,000 MTPA and steelmaking capacity is 3,50,000 MTPA. The company's products find application in various industries including automobile, bearings, forging, oil and gas, boilers, and hydraulic segments, among others. In March 2022, KFIL acquired a 51.25% stake in ISMT and took over its management control.

Key financial indicators (Consolidated, audited)

| | FY2022 | FY2023 | H1 FY2024^ |
|--|---------|---------|------------|
| Operating Income (Rs. Crore) | 2,176.4 | 2,584.5 | 1,406.4 |
| PAT (Rs. Crore) | 2,374.1 | 87.7 | 92.1 |
| OPBDIT/OI | 3.5% | 8.6% | 14.4% |
| PAT/OI | 109.1% | 3.4% | 6.6% |
| Total Outside Liabilities/Tangible Net Worth (times) | 0.5 | 0.4 | 0.3 |
| Total Debt/OPBDIT (times) | 2.8 | 0.4 | 0.1 |
| Interest Coverage (times) | 5.7 | 10.2 | 31.9 |

Source: ISMT; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

All ratios are as per ICRA's calculations; ^based on limited review of auditor

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 (Rs. Crore) | Date & rating in FY2024 | | | Date & rating in FY2023 | Date & rating in FY2022 | Date & rating in FY2021 | |
| | | | | Dec 29, 2023 | Aug 22, 2023 | Jul 20, 2023 | Dec 27, 2022 | Jul 04, 2022 | - | - |
| 1 Fund-based / non-fund-based proposed facilities | LT | - | - | - | - | - | - | [ICRA]A-(Stable)/[ICRA]A2+ | - | - |
| 2 Fund-based limits | LT | 145.00 | - | [ICRA]A+ (Stable) | [ICRA]A (Stable) | [ICRA]A (Stable) | [ICRA]A-(Stable) | - | - | - |

| | | | | | | | | | | |
|--------------------------------|-----------|---------------|---|-----------------------------------|----------------------------------|----------------------------------|------------------------------------|---|---|---|
| 3 Proposed term loan | LT | 150.00 | - | [ICRA]A+ (Stable) | [ICRA]A (Stable) | [ICRA]A (Stable) | - | - | - | - |
| 4 Non-fund-based limits | ST | 385.00 | - | [ICRA]A1 | [ICRA]A1 | [ICRA]A1 | [ICRA]A2+ | - | - | - |
| 5 Unallocated limits | LT/ ST | 70.00 | - | [ICRA]A+ (Stable)/ [ICRA]A1 | [ICRA]A (Stable)/ [ICRA]A1 | [ICRA]A (Stable)/ [ICRA]A1 | [ICRA]A- (Stable)/ [ICRA]A2+ | - | - | - |

LT- Long-term; ST – Short-term

Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|----------------------|
| Long-term - Fund-based Limits | Simple |
| Long-term – Fund-based Term Loan | Simple |
| Short-term - Non-fund-based Limits | Very Simple |
| Long-term/Short-term - Unallocated Limits | 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 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 | 8-9% | NA | 145.00 | [ICRA]A+(Stable) |
| NA | Proposed Term Loan | NA | NA | NA | 150.00 | [ICRA]A+(Stable) |
| NA | Letter of Credit | NA | NA | NA | 385.00 | [ICRA]A1 |
| NA | Unallocated Limits | NA | NA | NA | 70.00 | [ICRA]A+(Stable)/[ICRA]A1 |

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

| Sr. | Entity Name | Consolidation Approach |
|-----|---|------------------------|
| 1 | ISMT Limited | Full consolidation |
| 2 | ISMT Enterprises SA | Full consolidation |
| 3 | Structo Hydraulics AB | Full consolidation |
| 4 | ISMT Europe AB | Full consolidation |
| 5 | Indian Seamless Inc | Full consolidation |
| 6 | Tridem Port and Power Company Private Limited | Full consolidation |
| 7 | Nagapattinam Energy Private Limited | Full consolidation |
| 8 | PT ISMT Resources | Full consolidation |
| 9 | Best Exim Private Limited | Full consolidation |
| 10 | Success Power and Infraprojects Private Limited | Full consolidation |
| 11 | Marshall Microware Infrastructure Development Company Private Limited | Full consolidation |
| 12 | Adicca Energy Solutions Private Limited | Full consolidation |

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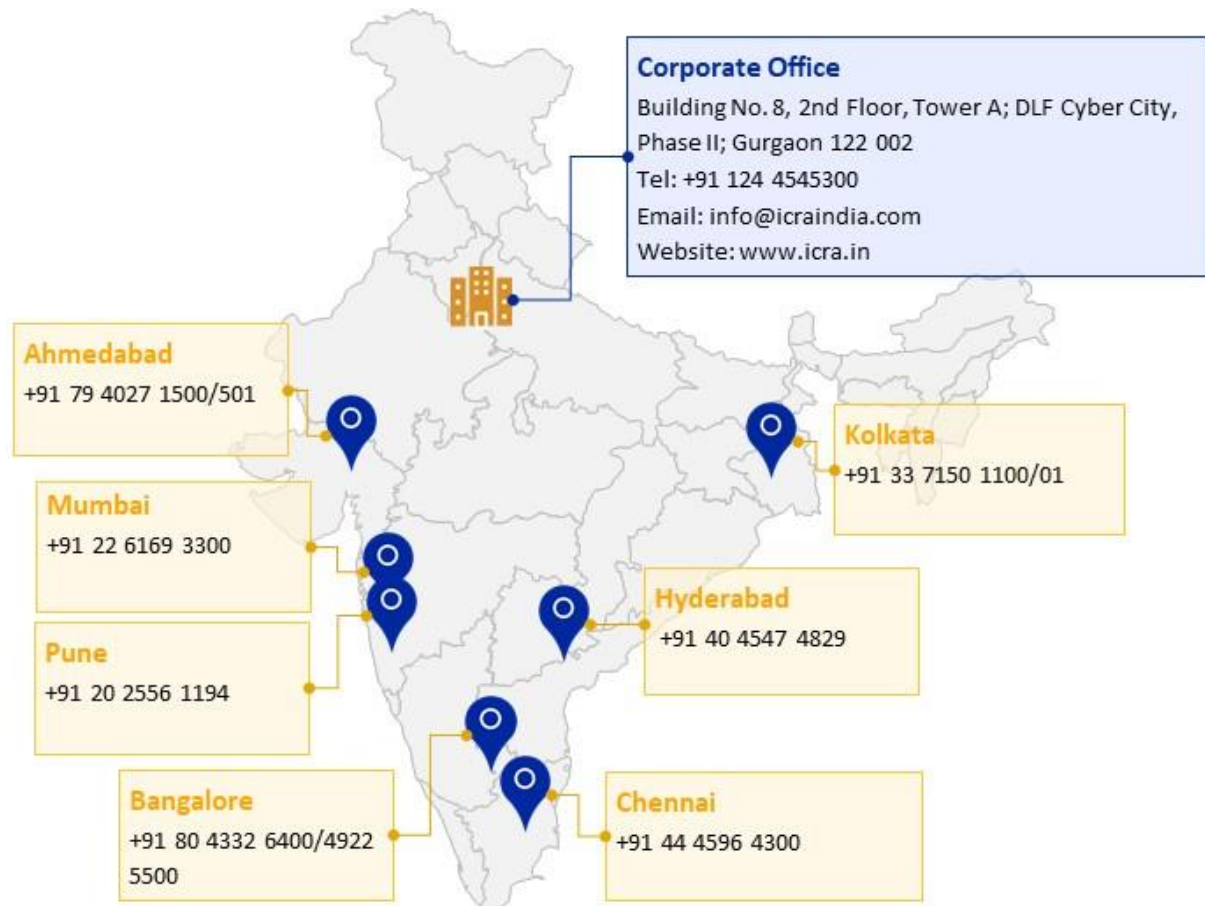
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