May 31, 2024 (Revised)

Mahindra Steel Service Centre Limited: Ratings reaffirmed and assigned for enhanced amount

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-Term Fund-Based Cash Credit	25.0	25.0	[ICRA]AA- (Stable); reaffirmed
Long-Term Fund-Based Term Loan	12.5	2.8	[ICRA]AA- (Stable); reaffirmed
Short-Term Non-Fund-Based Limits	140.0	230.0	[ICRA]A1+; reaffirmed and assigned for enhanced amount
Long-Term Interchangeable^	(25.0)	(85.0)	[ICRA]AA- (Stable); reaffirmed and assigned for enhanced amount
Long-Term/Short-Term Unallocated	60.0	-	-
Total	**237.5**	**257.8**	

**Instrument details are provided in Annexure-I; ^Cash credit facility is sublimit of non-fund based limit*

Rationale

The ratings reaffirmation continues to consider the strong financial flexibility enjoyed by Mahindra Steel Service Centre Limited (MSSCL) for being 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 owing to 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 ratings, however, remain constrained because of MSSCL's exposure to cyclical end-markets (automotive and electrical segments), as reflected in volatility of its return indicators, and stiff competition in the steel processing business. The volatility was visible in its operating performance in the recent past. The company witnessed revenue and margin contraction during the pandemic period, followed by a steep recovery in FY2022, buoyed by healthy volume offtake as well as firm steel prices, and again contraction in demand in the electrical segment in FY2024. The company is also exposed to competition from other steel processing players, which limits its pricing power to an extent. Nonetheless, 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 as a large part of its raw material is imported, while its entire sales is made in 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 risk because of its limited customer base, most of which are transformer manufacturers. However, its efforts to diversify through the new plant set up in Chennai to cater to automotive customers in South India offer comfort.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company will continue to benefit from the promoter group's support and the established track record of its operations and client base, 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 total debt (excluding lease liability) outstanding as on March 31, 2024 stood at Rs. 74.4 crore, comprising largely working capital of Rs. 46.6 crore, ICD from MAL and M&M of Rs. 25.0 crore (of which ICD amount to Rs. 10 crore was paid off in April 2024) and current maturity of long-term debt of Rs. 2.8 crore. MSSCL's gearing stood at 0.8 times as on March 31, 2024. Its Total debt/OPBITDA stood at 3.0 times and the company reported an interest coverage ratio of 3.0 times in FY2024. The ratios moderated from the previous levels due to moderation in OPBDITA and higher debt levels. Despite expected addition in debt levels for the planned capex and rise in working capital borrowing to support the increased scale of operations, MSSCL's credit metrics are likely to improve because of its healthy performance and strong financial support from the holding company, MAL.

Collaboration with Nippon Steel – The company imports cold rolled grain oriented (CRGO) and cold rolled non-grain oriented (CRNO) steel. 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 it is in proximity to the key customers of electrical steel, resulting in lower freight cost, which supports its profitability. Over the years, MSSCL has mainly catered to the electrical steel segment, limiting its dependence on Mahindra & Mahindra (M&M) for revenues. This has been further strengthened in the recent past, with the ramp-up of its Chennai plant, which caters to non-M&M customers in the automotive space.

Credit challenges

Susceptibility to cyclicality in end-user industry – MSSCL is exposed to the cyclical end-markets (automotive and electrical segments), as reflected by the volatility in its return indicators. This was evident in its performance in the last few fiscals, wherein its revenues declined by 19% and 29% in FY2021 and FY2020, respectively, followed by a robust growth of 84% in FY2022, in line with increased demand from the end-user industries and rise in steel prices. MSSCL's revenues moderated to 21% in FY2023 and further to 12% in FY2024 (provisional).

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 60% of the operating income in FY2023. Nevertheless, ICRA notes that the customer base of MSSCL comprises large, reputed transformer manufacturers and its Group companies have a strong credit profile, which reduce its exposure to counterparty credit risks. Additionally, 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 of the Chennai unit would help mitigate the customer concentration risk over the medium term.

Large debt-funded capex would constrict coverage ratios in the near term – The company plans to incur capex of Rs. 80-90 crore in FY2025 largely towards blanking and lamination lines, for which the company will be availing some debt. The increase in debt level is expected to moderate the coverage ratio over the near term. However, the same is expected to continue to remain adequate, supported by its healthy performance and strong financial support from the holding company, MAL.

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 FY2023, 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 provide 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 flow of Rs. 30-50 crore generated from operations annually, and unutilised working capital limits (~Rs. 5 crore as on December 31, 2023). These are expected to remain sufficient in meeting its current debt repayment obligations (existing loans), while planned capex requirements in FY2025 are likely to be met jointly through internal accruals and incremental external borrowings. Additionally, funding support from MAL to meet any cash flow mismatch 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 Auto Components
Parent/Group support	The ratings assigned to MSSCL factor in the high likelihood of its parent, MAL, 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 MAL (holding a 61% stake) 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 2,16,716 MTPA (including Kanhe 1 & 2), 8,400 – 10,000 MTPA (including Slitting) and 1,800 - 2400 MTPA, respectively. In August 2020, MSSCL commissioned a steel blanking and lamination facility in Chennai with a production capacity of 44,000 MTPA to cater to the OEMs in that region.

Key financial indicators (audited)

MSSCL – Standalone	FY2022	FY2023	FY2024*
Operating income	315.1	381.4	428.9
PAT	18.4	16.9	7.0
OPBDIT/OI	14.0%	11.6%	8.4%
PAT/OI	5.9%	4.4%	1.6%
Total outside liabilities/Tangible net worth (times)	1.9	1.7	1.5
Total debt/OPBDIT (times)	2.4	1.9	3.0
Interest coverage (times)	8.8	5.6	3.0

*Source: Company, ICRA Research; All ratios as per ICRA's calculations; Amount in Rs. Crore; PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; *Provisional*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2025)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2024 (Rs. crore)	Date & rating in FY2025	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022
					May 31, 2024	-	Mar 28, 2023	Feb 14, 2022
1	Cash Credit	Long term	25.0	--	[ICRA]AA- (Stable)	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
2	Term Loan	Long term	2.8	2.8	[ICRA]AA- (Stable)	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
3	Non-Fund-Based Limits	Short term	230.0	--	[ICRA]A1+	-	[ICRA]A1+	[ICRA]A1+
4	Interchangeable	Long term	(85.0)	--	[ICRA]AA- (Stable)	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
5	Long-Term/Short-Term Unallocated	Long term and short term	0.00	--	-	-	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [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	Very 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: 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	25.0	**[ICRA]AA- (Stable)**
NA	**Long-Term Fund-Based Term Loan**	FY2019-FY2020	7.30-8.20%	FY2025	2.8	**[ICRA]AA- (Stable)**
NA	**Short-Term Non-Fund-Based Limits**	NA	NA	NA	230.0	**[ICRA]A1+**
NA	**Long-Term Interchangeable**	NA	NA	NA	(85.0)	**[ICRA]AA- (Stable)**

Source: Company

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

Annexure II: List of entities considered for consolidated analysis – Not Applicable

Corrigendum

Rationale dated May 31, 2024 has been revised with following changes as below:

In the rationale, in the about the company section, the capacities have been revised

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