

March 31, 2023

The Indian Steel & Wire Products Limited: continues on Rating Watch with developing implication

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based facilities	30.00	30.00	[ICRA]A; continues on Rating Watch with developing implication
Non-fund based facilities	7.00	7.00	[ICRA]A1; continues on Rating Watch with developing implication
Total	37.00	37.00	

*Instrument details are provided in Annexure-I

Rationale

The ratings of The Indian Steel and Wire Products Limited (ISWPL) continue to remain on Rating Watch with Developing Implication owing to the ongoing merger with Tata Steel Limited (TSL, rated at [ICRA]A1+ and Ba1 (Positive) by Moody's Investors Service), subject to receipt of requisite statutory and regulatory approvals. ICRA will continue to monitor the developments of the merger process and take appropriate action, as may be required, following greater clarity of the merger plan fine print and its implementation timeline.

The ratings continue to factor in ISWPL's debt-free status, which translated into strong debt protection metrics for the company. ICRA notes that the company's debt-free status and strong parentage imparts a high degree of financial flexibility to the company. However, ICRA notes that the operating performance for the company got adversely impacted in the current fiscal due to slower than anticipated ramp up in the new rod mill capacity, in addition to the steel price volatility which led to inventory loss in the direct sales business. These two factors have driven down the operating margins to 1.2% in 9M FY2023 (6.9% in FY2022). Notwithstanding the earnings moderation, the company's credit metrics remained healthy on an absolute basis, as reflected in an interest coverage of 42.8 times in the 9M FY2023. ICRA understands that ISWPL will be able to achieve the required production levels in due course. This, along with a planned phasing down of operations of loss-making businesses like JEMCO¹, is expected to support a recovery in profit margins next fiscal. Additionally, the ratings continue to factor in the status of ISWPL as a 95.01% subsidiary of TSL with more than 60% of the company's revenues generated from the conversion business it carries out for TSL. The conversion business is carried out primarily on a cost-plus basis, partly insulating ISWPL's business from the volatility in steel prices.

While the company remains exposed to sales concentration risks, given that major part of its business comes from its parent, the counterparty risks remain limited. Besides, the company is strategically important for the overall long steel products business of TSL, accounting for 15-20% of TSL's domestic rod and wire manufacturing businesses. The ratings are also constrained by the modest scale of ISWPL's operations, susceptibility of the company's profitability to TSL's pricing policy for the conversion business, and its exposure to the inherent cyclicity in the iron and steel industry.

¹ Jamshedpur Engineering & Machine Manufacturing Company

Key rating drivers and their description

Credit strengths

Strong parentage as a subsidiary of TSL; strategic importance in TSL's long steel products business – ISWPL is a 95.01% subsidiary of TSL and has a high degree of integration with TSL in terms of operations and management, with many key executives of ISWPL being ex-employees of TSL. Moreover, ISWPL's businesses are carried out in two verticals – VAP Business (value added products), which constitutes rod mill and wire mill, and direct business (JEMCO and others). The wire/rod division, which undertakes conversion for TSL, generates above 60% of the company's revenues and is the main profit driver for the company. Through this division, the company has a high share in TSL's domestic rod (over 20% share by ISWPL) and wire manufacturing business (15-20% share by ISWPL). Thus, ISWPL remains strategically important for the overall long steel products business of TSL. ICRA also draws comfort from the demonstrated financial support extended by TSL in turning around the company in the past.

Debt free status – ISWPL has remained debt free since December 2018, a credit positive for a company that operates in an industry with cyclical trends. ISWPL's conservative capital structure has translated into strong debt protection metrics for the company, which is reflected in an interest coverage of 42.8 times in 9M FY2023. ICRA notes that the current debt-free status and strong parentage imparts a high degree of financial flexibility to the company. Additionally, the liquidity profile is characterised by a healthy free cash reserve of Rs. 10.75 crore and undrawn bank lines of Rs. 30 crore as on December 31, 2022.

Sensitivity to steel price volatility partly mitigated from the cost-plus-based conversion business carried out for TSL – For the wire/rod divisions, which is entirely dependent on conversion of products for TSL, and accounts for ~60% of the revenues, ISWPL receives a fixed income per metric tonne of production, which partly insulates the company from volatility in both raw materials and finished goods prices. While the major raw materials are supplied by TSL, the cost of power, another major component in the production of wires and wire rods, is passed on to TSL. This strengthens the business risk profile of the company and provides it with a relatively stable earnings stream. However, the division's profitability is determined by TSL's pricing policies.

Credit challenges

Overall profitability in first nine months of FY2023 remains subdued – The wire/rod division remains the main profit driver for the company. The overall operating profit margins moderated to 1.2% in 9M FY2023 from 6.9% in FY2022 largely because of slower than anticipated ramp up of newly commissioned (October 2022) capacity of 50,000 metric tonne per annum (MTPA) in rod division. This led to significant loss of production in H2 FY2023. In addition, the company's current year performance has also been impacted due to volatility in steel prices resulting in inventory loss in its direct business (nails and weldings) along with continued losses from JEMCO. However, ICRA notes that ISWPL will be able to achieve the required production levels in due course. This, along with a planned phasing down of operations of loss-making businesses like JEMCO², is expected to support a recovery in profit margins next fiscal.

Significant sales concentration risk – ISWPL remains exposed to significant sales concentration risks as more than 60% of its revenues is generated from the conversion business it undertakes for TSL. However, ICRA notes that the counterparty risk remains limited, given the healthy financial position of TSL. ICRA also notes that ISWPL remains strategically important for the overall long steel products business of TSL. Nonetheless, the financial performance is limited by TSL's pricing policies and its modest scale of operations at present, with the wire rod capacity standing at 3.0 lakh MTPA (increased by 50,000 MTPA in October 2022) and the wire capacity at 1.2 lakh MTPA in FY2023. With the company's plan to phase out some of its loss-making segments going forward, the overall scale of operations is expected to remain modest.

² Jamshedpur Engineering & Machine Manufacturing Company

Exposure to the inherent cyclicality in the iron and steel industry – Although the cost-plus nature of ISWPL’s conversion business cushions it from the volatility in steel prices to some extent, ICRA notes that the overall volumes processed, and hence the overall profits, depend on the demand for long products in the market, which govern the volumes contracted out by TSL to ISWPL. Additionally, the other divisions of the company also remain exposed to the inherent cyclicality in the iron and steel industry.

Liquidity position: Strong

ISWPL’s liquidity position is strong, with healthy fund flow from operations, large free cash balances relative to the size of its balance sheet, nil long-term debt, and unutilised working capital limits. ICRA expects ISWPL to be able to comfortably meet its near-term capex commitments through internal accruals and yet be left with sufficient cash surplus. In addition, the company has healthy financial flexibility in terms of raising debt as well as working capital support, given its status as a 95.01% subsidiary of TSL.

Rating sensitivities

Positive factors – Sustained growth in absolute revenues and profits and improved performance of the direct business, particularly reduction of losses from the JEMCO division, could trigger ratings upgrade.

Negative factors – Any material deterioration of the credit profile of the parent company (TSL) and/or weakening of operational and managerial linkages with the parent company can lead to a ratings downgrade. Additionally, any large debt-funded capex, resulting in a deterioration of the financial risk profile, could also trigger a ratings downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Ferrous Metals Industry Rating Approach - Implicit support from Parent or Group
Parent/Group Support	Parent Company: Tata Steel Limited (TSL) ISWPL’s ratings are supported by the strong parentage of TSL, which holds a 95.01% stake in the company and the presence of top TSL executives on the board of ISWPL. There are considerable operational, financial, and managerial linkages between ISWPL and TSL.
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company.

About the company

The Indian Steel & Wire Products Limited (ISWPL) primarily works as a conversion agent for Tata Steel Limited (TSL) in the wires, TMT rebars and wire rods segments through its wire division. In addition, the company manufactures industrial rolls and engineering castings through its JEMCO division and produces welding products and nails through its direct business division. At present, TSL has a 95.01% stake in the company.

Key financial indicators (audited)

	FY2021	FY2022	9M FY2023*
Operating income	283.2	354.2	262.3
PAT	12.0	19.9	1.0
OPBDIT/OI	6.2%	6.9%	1.2%
PAT/OI	4.2%	5.6%	0.4%
Total outside liabilities/Tangible net worth (times)	0.5	0.5	0.5
Total debt/OPBDIT (times)	0.0	0.0	0.0
Interest coverage (times)	270.7	311.5	42.8

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	Type	Current rating (FY2023)		Chronology of rating history for the past 3 years					
		Amount rated (Rs. crore)	Amount outstanding as of Dec 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022		Date & rating in FY2021		Date & rating in FY2020
				Mar 31, 2023	Oct 4, 2022	Dec 3, 2021	Nov 24, 2020	Oct 16, 2020	Oct 10, 2019
1 Fund Based Facilities	Long-term	30.00	-	[ICRA]A; On Rating watch with developing implications	[ICRA]A; On Rating watch with developing implications	[ICRA]A; On Rating watch with developing implications	[ICRA]A; On Rating watch with developing implications	[ICRA]A (Stable)	[ICRA]A (Stable)
2 Non-fund Based Facilities	Short-term	7.00	-	[ICRA]A1; On Rating watch with developing implications	[ICRA]A1; On Rating watch with developing implications	[ICRA]A1; On Rating watch with developing implications	[ICRA]A1; On Rating watch with developing implications	[ICRA]A1	[ICRA]A1

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund Based Facilities	Simple
Non-fund Based Facilities	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](https://www.icra.in)

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund Based Facilities	NA	NA	NA	30.00	[ICRA]A; Rating watch with developing implication
NA	Non-fund Based Facilities	NA	NA	NA	7.00	[ICRA]A1; Rating watch with developing implication

Source: Company; &: Rating watch with developing implications

Annexure II: List of entities considered for consolidated analysis: Not applicable

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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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