January 05, 2024 (Revised)

Mukand Sumi Special Steel Limited: Rating upgraded; 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	90.00	200.00	[ICRA]A(Stable); assigned/upgraded from [ICRA]A-(Stable)
Long Term - Fund Based Term loan	262.00	312.00	[ICRA]A(Stable); assigned/upgraded from [ICRA]A-(Stable)
Total	**352.00**	**512.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating upgrade factors in the improvement in the credit profile of Mukand Sumi Special Steel Limited (MSSSL), which is expected to sustain, going forward, on the back of a healthy uptick in the operating profit margin (OPM), led by elevated sales realisations amid strong demand from the end-user industries, an increase in the share of value-added products (leading to higher contribution), lower conversion costs (owing to ramp-up of production at technologically efficient new rolling mill in Hospet), among others.

While the company's revenues remained largely flat at Rs. 1,918 crore in 8M FY2024, the OPM increased sharply to 17.0% from 9.3% in FY2023. With a significant improvement in the operating profits/cash flows and in the absence of any major capital expenditure (capex) in the current fiscal, the company reduced its debt sharply, leading to improved credit metrics, as reflected in total debt-to-operating profit ratio (TD/OPBITDA) of 0.8 times as on November 30, 2023 (compared to 2.7 times as on March 31, 2023) and an interest cover of 8.0 times in 8M FY2024 (compared to 3.2 times in FY2023). ICRA expects MSSSL's OPM to sustain at healthy levels, going forward, led by continued healthy demand momentum from the auto industry, a further increase in share of value-added products and higher savings in conversion costs (aided by further ramp-up of the new rolling mill at Hospet). Besides, the company has entered into power purchase agreement (PPA) under the group captive model to source power at cheaper rates. This will meet a significant portion of the company's power requirements and lead to savings in power costs from Q4 FY2024. Despite the capex plans, a healthy OPM is likely to translate into continued comfortable financial profile for the company with TD/OPBITDA expected to remain under 1.5 times over the near-to-medium term.

The rating continues to derive comfort from the strong parentage of MSSSL, which is a 51:49 joint venture (JV) between *Bajaj Group*[1] and Sumitomo Corporation (SC; rated Baa1/Stable by Moody's). ICRA also expects JSPL to be willing to extend financial support to MSSSL, should there be a need. The rating favourably factors in the extensive track record of the promoter groups in the automotive industry, through which the company enjoys a healthy market share in products of critical application in the said industry and has a reputed customer base with a proven track record of repeat business.

The rating takes into account the limited availability of billets, the key raw material, which constrains the overall capacity utilisation levels of the company, thereby impacting its return on capital employed (RoCE). ICRA notes the company's partly debt-funded capex plan of Rs. 300-400 crore in FY2024 and FY2025 towards setting up facilities for value added products to improve the contribution levels. Besides, the rating factors in MSSSL's exposure to the cyclicality inherent in the automotive industry (which accounts for 80-85% of the total sales) and to volatility in raw material prices (which account for ~80% of its total operating expenses).

[1] *Bajaj Group holding in MSSSL comprises JSPL - 44.20%, Mukand Limited (ML) - 5.51% & Baroda Industries Private Limited (BIPL) - 1.29%*

The Stable outlook on the [ICRA]A rating reflects ICRA's opinion that the credit profile of MSSSL is expected to remain supported by healthy automotive demand, its established customer base as well as sustained improvement in profitability, led by savings in conversion costs and an increase in the share of value-added products.

Key rating drivers and their description

Credit strengths

Healthy financial flexibility for being a part of Bajaj and Sumitomo Groups – MSSSL was incorporated in FY2018 as a 51:49 JV between ML and SC. In FY2021, ML sold its 51% stake to JSPL, which is the principal holding company of the Bajaj Group. Subsequently in FY2023, ML acquired 5.51% stake in MSSSL post merger of Mukand Sumi Metal Processing Limited's (MSMPL) alloy steel business into MSSSL. MSMPL is 100% owned subsidiary of ML. Even after this merger, shareholding between Bajaj and Sumitomo group is maintained at 51:49. MSSSL enjoys healthy financial flexibility, along with operational and financial support for being a part of the Bajaj and Sumitomo Groups. ICRA also expects JSPL to be willing to extend financial support to MSSSL, should there be a need.

Reputed clientele and extensive track record of promoter groups in the auto industry – MSSSL's product portfolio comprises round cornered square (RCS), round (RND), wire rod (WRD) and straightened wire rod (STW). These products find application in the automotive industry. MSSSL's top customers are reputed auto ancillary manufacturers. MSSSL is the sole supplier of products in critical applications like engine parts, transmission, suspension spring, bearings etc. for 30-40% of its customers and enjoys a healthy market share in this segment. The rating also derives comfort from the extensive track record of its promoter groups in the auto industry. While the Bajaj Group, through Bajaj Auto Limited, enjoys a healthy market share in the domestic two-wheeler and three-wheeler segments, the Sumitomo Group has presence in the automotive design and development segment.

Location-specific advantages – MSSSL's new rolling mill at Hospet (Karnataka) is well connected to the auto OEM cluster in Chennai by NH48. Besides, its proximity to ML's billet manufacturing facility at Hospet, which is its sole supplier, would also reduce its transportation costs.

Healthy increase in OPM in YTD FY2024 resulted in an improvement in the credit metrics; improved financial profile to sustain, going forward – In 8M FY2024, while the company's revenues remained largely flat at Rs. 1,918 crore, its OPM increased sharply to 17.0% from 9.3% in FY2023. The healthy uptick in OPM was supported by elevated sales realisations amid strong demand from the end-user industries, an increase in the share of value-added products (leading to higher contribution), lower conversion costs (owing to ramp-up of production at technologically efficient new rolling mill in Hospet), among others. With significant improvement in operating profits/cash flows and in the absence of any major capex in the current fiscal, the company reduced its debt and the credit metrics improved, as reflected in TD/OPBITDA of 0.8 times as on November 30, 2023 (against 2.7 times as on March 31, 2023) and interest cover of 8.0 times in 8M FY2024 (against 3.2 times in FY2023). ICRA expects the company's OPM to sustain at healthy levels, going forward, led by continued healthy demand momentum from the auto industry, a further increase in share of value-added products and higher savings in conversion costs (aided by further ramp up of new rolling mill at Hospet). Besides, the company has entered into power purchase agreement (PPA) under the group captive model to source power at cheaper rates. This will meet a significant portion of the company's power requirements and lead to savings in power costs from Q4 FY2024. Despite the capex plans, a healthy OPM is likely to translate into continued comfortable financial profile for the company with TD/OPBITDA expected to remain under 1.5 times over the near-to-medium term.

Credit challenges

Limited availability of billets constrains the capacity utilisation levels and thereby RoCE; debt-funded capex plans – Given the limited availability of billets, the key raw material, MSSSL's overall capacity utilisation level remains constrained, impacting its RoCE. Over the medium-to-long term, the company plans to set up a billet making facility to address the raw material shortage issue. ICRA also notes the company's partly debt-funded capex plan of Rs. 300-400 crore in FY2024 and FY2025 towards setting up facilities for value-added products to improve the contribution levels. Timely commencement and ramp-up of the said facility would be crucial for further improvement in the company's profitability.

Exposure to cyclicality associated with auto industry – The automotive sector accounts for 80-85% of MSSSL's total sales every year. Dependence on the automotive sector exposes the company to the cyclical nature of the industry. Muted demand from the auto sector had led to a 31% revenue fall and a sharp decline in OPM in FY2020. While the savings in conversion costs from the new plant would shield the profit margins to some extent, a prolonged lull in demand conditions in the auto industry could impact MSSSL's operational and financial risk profiles.

Exposure to volatility in raw material prices – The key raw material for MSSSL is alloy steel billet. The prices of billet depend on iron ore and coke prices, which in turn have exhibited sharp volatility in the past. While any major fluctuation in prices can be passed on to the customers with a lag of one to two months, the company would remain exposed to volatility in raw material prices in case of weak demand.

Liquidity position: Adequate

MSSSL's liquidity position is **adequate**, supported by its healthy cash flow from operations. Given the healthy demand momentum and significant increase in the company's profitability in FY2024, the cash generation improved significantly which was deployed towards working capital and capex, thereby minimising dependance on debt. Going forward, given the expectation of continued strong demand from end-user industries and elevated OPM, the cash flow from operations are likely to remain comfortable above Rs. 400 crore per annum to meet debt repayments and a major portion of capex requirements. The company's term loan repayment obligations in FY2024 and FY2025 stand at Rs. 156 crore and Rs. 132 crore, respectively while capex for both years combined is estimated at Rs. 300-400 crore. The company's average utilisation of fund-based working capital limits stood at 71% during October 2022 to September 2023, reflecting average liquidity cushion of around Rs. 130 crore. Given the healthy cash generation in the business in H1 FY2024, the average working capital limit utilisation reduced to 50%, leading to higher liquidity buffer of over Rs. 200 crore for the company. Besides, the company maintains average unencumbered liquid balances of Rs. 20-30 crore. ICRA also expects JSPL to be willing to extend financial support to MSSSL, should there be a need.

Rating sensitivities

Positive factors – ICRA could upgrade MSSSL's rating if there is a substantial growth in its scale of operations and profits, leading to a sustained improvement in credit metrics and liquidity position.

Negative factors – Pressure on MSSSL's rating could arise if there is any weakening in linkages with the Bajaj and Sumitomo Groups. Any sharp decline in revenues and/or profits or any large unanticipated debt-funded capex/investment, which results in sustained weakening of its credit metrics and/or the liquidity position would also be a negative factor. Specifically, MSSSL's debt-to-operating profit ratio remaining above 2.5 times on a sustained basis, would be a negative trigger.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Iron & Steel
Parent/Group Support	JV partners – Bajaj Group (51%) and SC (49%); MSSSL's rating factors in the high likelihood of its JV partners extending financial support to it, as and when required.
Consolidation/Standalone	Standalone

About the company

MSSSL manufactures alloy steel bars and wire rods, which find applications in automotive and engineering industries. MSSSL was incorporated by amalgamation of alloy steel rolling and finishing business of ML into Mukand Alloy Steels Private Limited (MASPL) in FY2018. Post the amalgamation, SC in FY2019, acquired a 49% stake in MSSSL for Rs. 1,181 crore. In December 2020, the Competition Commission of India (CCI) approved the acquisition of ML's share by JSPL. The acquisition was completed in April 2021. MSSSL was earlier operating from its 5,00,000-MTPA Kalwe unit in Thane (Maharashtra). However, in August 2021, the company shifted its manufacturing activities entirely to Hospet (Karnataka) by commissioning a new 4,00,000-MTPA facility. From August 2022, the alloy steel business of MSMPL was merged into MSSSL.

Key financial indicators

Standalone	FY2022 (Audited)	FY2023 (Audited)	8M FY2024 (Provisional)
Operating Income (Rs. Crore)	2,426.9	2,976.6	1,917.6
PAT (Rs. Crore)	171.2	42.3	163.5
OPBDIT/OI	10.9%	9.3%	17.0%
PAT/OI	7.1%	1.4%	8.5%
Total Outside Liabilities/Tangible Net Worth (times)	0.5	0.4	0.2
Total Debt/OPBDIT (times)	3.5	2.7	0.8
Interest Coverage (times)	3.5	3.2	8.0

Source: MSSSL; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation
All ratios are as per ICRA's calculations

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
					Jan 05, 2024	Oct 20, 2022	Jul 06, 2021	-
1	**Fund-based Cash Credit**	LT	200.00	-	[ICRA]A(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	-
2	**Fund-based Term Loans**	LT	312.00	312.00	[ICRA]A(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	-

LT- Long-term; ST – Short-term

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term - Fund Based Cash Credit	Simple
Long Term - Fund Based Term loan	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	**Cash Credit**	NA	8-9%	NA	200.00	[ICRA]A(Stable)
NA	**Term Loan**	FY2021	8-9%	FY2028	312.00	[ICRA]A(Stable)

Source: Company

<u>*Please click here to view details of lender-wise facilities rated by ICRA*</u>

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

Corrigendum

Rationale dated January 05, 2024 has been corrected with revision as detailed below:

- Changes made in the rationale (Page No.1; 3rd paragraph), credit strength related to "Healthy financial flexibility for being a part of Bajaj and Sumitomo Groups" (Page No. 2) and Analytical approach (Page no. 4 with respect to Group support). These changes relate to detailed break-up of Bajaj Group holding in MSSSL, where JSPL holds 44.20%, Mukand Limited (ML) holds 5.51% and Baroda Industries Private Limited (BIPL) holds 1.29%. The change in shareholding was led by ML acquiring 5.51% stake in MSSSL post-merger of MSMPL's alloy steel business into MSSSL. MSMPL is 100% owned subsidiary of ML. Thus, even after this merger, shareholding between Bajaj and Sumitomo group is maintained at 51:49. Thus ICRA's analytical approach remains same.

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