February 26, 2024

Suraj Products Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term – Term Loans	31.00	26.00	[ICRA]BBB (Stable); reaffirmed
Long term – Cash Credit	25.00	30.00	[ICRA]BBB (Stable); reaffirmed
Short term - Non-fund based Facilities	1.50	1.50	[ICRA]A3+; reaffirmed
Total	**57.50**	**57.50**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings reaffirmation reflects the healthy financial performance of Suraj Products Limited (SPL) in FY2023 and 9M FY2024, as reflected in its healthy profitability and debt coverage indicators. The company reported an OPBITDA[1] of Rs. 39.9 crore in 9M FY2024 against Rs. 34.1 crore in 9M FY2023. The healthy performance of the company was primarily driven by the benefits accruing from the coal linkages, which meet almost ~50% of the company's total thermal coal requirements for manufacturing of sponge iron at a discount to the prevailing market price. Besides, the smaller kiln size of the company permits using domestic thermal coal having lower calorific value, thus insulating spreads during periods when international coal prices stay elevated. ICRA expects SPL's financial performance to remain healthy for the remainder of FY2024 with strong steel demand and input costs remaining under check. The ratings also consider the comfortable financial risk profile of the company, which has witnessed a steady improvement over the years. The ratings continue to derive comfort from SPL's vertically integrated nature of operations, characterised by the presence of DRI[2] kiln (used to manufacture sponge iron), mini blast furnace (used to manufacture pig iron), induction furnace and continuous caster to produce billets using captive sponge iron and pig iron. The manufactured billets are then subjected to rolling to produce TMT bars of desired profile. The ratings also derive comfort from the presence of the company's captive power plant (CPP), which has further increased from 6 MW to 9 MW in FY2024, leading to availability of power at a competitive rate. This has positively impacted its cost structure owing to a highly power intensive nature of operation. The ratings also derive strength as SPL's plant in located in proximity to major raw material sources.

The ratings are, however, constrained by the intensely competitive nature of the secondary steel industry, which leads to pricing pressure, keeping margins under check. The ratings also remain constrained because of the company's exposure to the cyclicality inherent in the steel industry and susceptibility of SPL's profitability to the volatility in raw material prices and end-product realisations, although the vertically integrated nature of operations reduces the vulnerability to an extent. The ratings also factor in SPL's small scale of operations relative to other established players in the secondary steel industry, which constrains its ability to benefit from the economies of scale and limits its pricing flexibility. In addition, ICRA notes that smaller steel mills remain more vulnerable during a sustained period of industry downturn.

ICRA notes that during the recently conducted search by the income tax (IT) department, there was no impact on the business operations based on the discussions with the management. ICRA also understands that there have been no restrictions imposed by the IT authorities on the company and no demand notice has been received by SPL. ICRA would continue to monitor closely on any such developments related to the same.

[1] Operating Profit Before Interest, Tax, Depreciation and Amortisation

[2] Direct Reduced Iron

The Stable outlook on the long-term rating reflects ICRA's opinion that the company's credit metrics would continue to remain at comfortable levels, going forward, aided by steady accruals and moderate dependence on debt.

Key rating drivers and their description

Credit strengths

Healthy financial performance in FY2023 and 9M FY2024; expected to sustain for the rest of FY2024 – SPL witnessed a healthy revenue growth of 20% in FY2023 and touched Rs. 285 crore, supported primarily by higher proportion of sales of finished products, leading to healthy blended realisations. The momentum continued in 9M FY2024 with a top line of Rs. 253 crore. However, the improvement in the current fiscal was supported by higher sales volumes and large proportion of sales of finished products, leading to healthy blended realisations. The company reported an OPBITDA of Rs. 39.9 crore in 9M FY2024 against Rs. 34.1 crore in 9M FY2023. The healthy performance of the company was primarily driven by the benefits accruing from the coal linkages, which meet almost ~50% of the company's total thermal coal requirements for manufacturing of sponge iron at a significant discount to the prevailing market price. Besides, the smaller kiln size of the company permits using domestic thermal coal having lower calorific value, thus insulating spreads during periods when international coal prices remain elevated. ICRA expects SPL's financial performance to remain healthy for the remainder of FY2024 as well with healthy steel demand and input costs remaining under check.

Comfortable financial risk profile – SPL's financial risk profile remains comfortable and has witnessed a steady improvement over the years. SPL's leverage has improved further in FY2023 with scheduled repayment of the term loan obligations, leading to Total debt to OPBDITA improving to 1.1 times from 1.4 times in FY2022. The leverage is likely to continue to improve with the metric expected to reduce to below 1 times in FY2024 and continue to the downward trend subject to any large debt funded capex by the company. In terms of coverage indicators, interest coverage stood healthy at 12 times in FY2023 and 15.3 times in 9M FY2024 and is expected to remain healthy over the medium term, supported by lower interest servicing obligations and healthy earnings profile. SPL is likely to maintain its comfortable financial risk profile, aided by steady accruals and no major growth plans in the near term.

Vertically integrated nature of operations with capacity to manufacture sponge iron, pig iron, billets and TMT bars – The company has a vertically integrated continuous casting steel manufacturing facility with a capacity of 36,000 metric tonnes per annum (MTPA) of sponge iron, 24,000 MTPA of pig iron, 72,000 MTPA of billets and 72,000 MTPA of TMT bars. Billets are manufactured using captive sponge iron and pig iron. The manufactured billets are then rolled to produce TMT bars of desired profile.

Presence of captive power plant, coal linkage and ability to process inferior grade input materials for steel making strengthen the operating profile of the company – The company's steel melting operation is highly power intensive. The company has a captive power plant (CPP) of 9 mega watt (MW), out of which 3 MW is based on waste-heat-recovery (WHR) technology, 3 MW is based on atmospheric fluidised bed combustion (AFBC) process and the balance 3 MW utilises gas from the mini blast furnace (MBF) to produce power. The cost structure of the steel melting operation, which is highly power intensive in nature, is positively impacted by the power available from the CPP at a competitive rate. The input cost for WHR remains very low as it uses waste heat gas obtained from the sponge iron kiln. The input mix for AFBC primarily includes Dolochar (byproduct obtained from sponge iron production) and the turbine utilises process gases from MBF. Power generated through SPL's captive power plant at a competitive rate meets the major part of its overall power requirement, which positively impacts the cost structure. In addition, ~50% of the company's total thermal coal requirements for manufacturing of sponge iron is met from the linkages obtained through auctions, keeping the landed cost of coal competitive and enhancing raw material security. ICRA expects SPL to remain cost competitive, supported by the cost improvement initiatives, which include support infrastructure, enabling the company to process inferior grade of iron ore and the jigging facility, which improves the recovery rate of iron ore.

Credit challenges

Competitive nature of the industry likely to keep margins under check – SPL is a secondary steel producer and derives the major portion of its revenue from semi-urban and rural areas. The fragmented nature of the long product/semis industry and intense competition from other organised as well as unorganised players are likely to keep its margins under check.

Exposed to cyclicality inherent in the steel industry – SPL is exposed to cyclicality inherent in the steel industry, which leads to volatility in revenue and cash flows for the industry players, including SPL. The cash flows and profitability of the company would remain volatile largely because of the fluctuation in steel spreads emanating from the mismatch in price movement of raw materials and end products. However, the vertically integrated nature of SPL's operations reduces the earnings volatility to an extent.

Relatively smaller scale of operations – Notwithstanding the increase in the scale of operations of SPL in the recent years, the same remained small compared to other established players in the secondary steel industry. This constrains its ability to benefit from the economies of scale and limits its pricing flexibility vis-à-vis that of the bigger entities operating in the industry. In addition, ICRA notes that smaller steel mills remain more vulnerable during a sustained period of industry downturn.

Liquidity position: Adequate

SPL's liquidity position is adequate with free cash/bank balances of around Rs. 15 crore as on December 31, 2023 and healthy retained cash flow of ~Rs. 22 crore expected in the current fiscal. Against these sources of cash, the company has no major capex commitments and annual debt repayment obligation of ~Rs. 7 crore over the medium term. Overall, ICRA expects SPL to be able to comfortably service its debt obligations through internal sources of cash.

Rating sensitivities

Positive factors – ICRA may upgrade SPL's ratings if there is a sustained increase in its scale of operations while maintaining healthy business returns and credit metrics.

Negative factors – Pressure on SPL's ratings may arise in case of weaker-than-expected financial performance due to adverse demand scenario. Any unfavorable outcome related to the recent IT department search affecting its liquidity could also have a trigger for rating downgrade. A specific trigger for downgrade would be DSCR lower than 1.8 times on a sustained basis. Additionally, any major debt-funded capex, leading to weakening of capital structure would put pressure on SPL's ratings.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodologies for Entities in the Iron & Steel Industry
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of SPL.

About the company

Established in 1991, Champion Cement Industries Limited was involved in production of cement. The company's name was changed to Suraj Products Limited in 2000. Since 2002, the company discontinued the cement manufacturing plant and diversified into manufacturing of sponge iron and pig iron. The manufacturing facility is located in Sundargarh district, Odisha. The company commissioned its captive power plant (CPP) of 3 MW (waste heat recovery) and an induction furnace of 25,000 MT in 2017. In FY2019, SPL installed its second CPP of 3 MW (AFBC based) and doubled the steel melting capacity. The company has also installed a continuous casting machine for production of billets instead of ingots. At present, the company has an installed capacity to produce 36,000 MTPA of sponge iron, 24,000 MTPA of pig iron, 72,000 MTPA of billets, 72,000 MTPA of TMT bars and 9 MW of captive power generation capacity.

Key financial indicators

SPL	FY2022	FY2023	9M FY2024*
Operating income	236.9	285.0	252.6
PAT	23.6	26.0	23.1
OPBDIT/OI	18.4%	17.0%	15.8%
PAT/OI	10.0%	9.1%	9.2%
Total outside liabilities/Tangible net worth (times)	0.9	0.7	-
Total debt/OPBDIT (times)	1.4	1.1	-
Interest coverage (times)	9.7	12.0	15.3

*Source: Company, ICRA Research; * Provisional numbers; Amount in Rs. Crore; PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation*

Status of non-cooperation with previous CRA:

CRA	Status	Date of Release
CRISIL	CRISIL B+/Stable/A4; ISSUER NOT COOPERATING	September 28, 2023

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 of Sep 30, 2023 (Rs. crore)	Date & Rating in FY2024		Date & Rating in FY2023	Date & Rating in FY2022	Date & Rating in FY2021
					Feb 26, 2024	Jan 31, 2024	Nov 30, 2022	Aug 12, 2021	Jun 23, 2020
1	Term Loans	Long-term	26.00	23.77	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)	[ICRA]BB+ (Stable)
2	Cash Credit	Long-term	30.00	--	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB- (Stable)	[ICRA]BB+ (Stable)
3	Non Fund-Based Facilities	Short term	1.50	--	[ICRA]A3+	[ICRA]A3+	[ICRA]A3+	[ICRA]A3	[ICRA]A4+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term Loans	Simple
Cash Credit	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

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs Crore)	Current Rating and Outlook
NA	Term Loans	FY2017	NA	FY2027	26.00	[ICRA]BBB(Stable)
NA	Cash Credit	NA	NA	NA	30.00	[ICRA]BBB(Stable)
NA	Non Fund-Based Facilities	NA	NA	NA	1.50	[ICRA]A3+

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

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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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