

February 11, 2020

T S Alloys Limited: [ICRA]A+ &/A1+ & assigned to enhanced limits

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Non-fund based BG		260.0	[ICRA]A+ &/ A1+ & assigned
Fund Based – Working Capital Facilities	18.0	18.0	[ICRA]A+ & outstanding
Non-fund Based – Working Capital Facilities	2.0	2.0	[ICRA]A1+& outstanding
Total	20.0	280.0	

*Instrument details are provided in Annexure-1

Rationale

The rating action continue to consider TSAL's status as a 100% subsidiary of Tata Steel Limited (TSL), the strategic importance of the company in TSL's ferro-alloys and mineral division and the high degree of integration of operations and management with TSL. TSL's job-work nature of operations, at present, which almost insulates the company from the volatility in both raw materials and finished goods prices and limits the extent of the company's business risks. The backward integration in the form of a captive power plant under a fellow subsidiary ensures a steady supply of power for its power-intensive nature of operations. While assigning the rating, ICRA has taken note of the company's recent acquisition of two chrome ore mines at the recently concluded auctions in Odisha. This is in-line with TSL's stated strategy of pursuing mining operations – for ferro chrome and iron ore under TSAL going forward. TSAL has received the Letter of Intent from the State Government and have paid the upfront fees for the Saruabil and Kamarda chrome ore mines. These two mines have total reserves of 12.8 million tonnes. At present, Tata Steel Limited (TSL) supplies chrome ore for conversion to ferro chrome to TSAL from its Sukinda mines, the mining lease of which is set to expire in March 2020, post which the conversion arrangement is likely to change. While the new mines are expected to take some time to ramp-up production, sufficient stock of almost a year already available at TSAL's plant is expected to support the company's cashflows under the current conversion agreement. While the long-term rating continues to be supported by the financial flexibility of TSAL, its conservative gearing with nil debt as of end-FY2019, a comfortable liquidity position with a cash and bank balance of Rs. 18.1 crore as of end-FY2019 and unutilised working capital limits, the company's exposure to the cyclical nature inherent in the steel industry is a credit negative. The ratings continue to remain under watch with developing implications since the exact timelines for mine development and funding pattern of the acquisition are yet to be finalised. ICRA however understands that support from TSL, as evident from the Letter of Comfort given by for the bank guarantee facilities, to be forthcoming as and when required. ICRA will continue to monitor the developments in this regard and will review the situation when more clarity emerges.

Key rating drivers and their description

Credit strengths

Status as a wholly-owned subsidiary of TSL; high strategic importance to parent - TSAL is a wholly-owned subsidiary of TSL and acts as a conversion agent for manufacturing high-carbon ferro chrome from chrome ore supplied by the parent company. TSAL's manufacturing facilities consist of two 16.5 MVA blast furnaces, located in Cuttack, Odisha. It has a production capacity of 60,000 tonnes per annum. The company also receives a high degree of management support from TSL as its senior executives are present on the board of TSAL.

Job-work nature of business limits exposure to volatility in ferro-alloy prices – At present, TSAL’s revenue primarily consists of conversion income from TSL for production of high carbon ferro chrome. As per the annual conversion agreement between TSL and TSAL, TSL provides raw materials like chrome ore, coke and coal. The company earns a fixed conversion rate per tonne of ferro-chrome produced as per the annual agreement, insulating it from volatility in raw material and end-product prices.

Conservative capital structure and comfortable liquidity position - TSAL has a conservative capital structure, as reflected by a nil gearing as of end-FY2019. Moreover, the absence of any long-term debt in its books provides the company with considerable financial flexibility. TSAL has a comfortable liquidity profile with a cash and bank balance of Rs. 18.1 crore as of end-FY2019 and sufficient headroom in working capital limits.

Backward integration in the form of a captive power plant set up under a Group company - TSAL and TSL together hold 100% in Bhubaneshwar Power Private Limited (BPPL). TSL holds a 93.58% stake in BPPL, while TSAL holds a 6.42% stake. As per the guaranteed annual offtake clause in the power-purchase agreement, out of the total power offtake of 120 MW, TSAL would procure 20 MW and the balance would be purchased by TSL. In FY2019, the average power tariff was high on account of lower power offtake because of lower levels of production. However, going forward, with stabilisation of TSAL’s production levels, the power cost is expected to reduce to some extent.

Credit challenges

Pricing policy limits scope of margin expansion - Given the job work nature of operations, TSAL has limited scope for margin expansion. TSAL receives a fixed conversion fee from TSL, which is based on standard consumption norms and standard prices for each material, decided on a quarterly basis.

Exposure to cyclical nature inherent in steel industry - While the job-work nature of TSAL’s operations mitigates the exposure to price volatility to some extent, demand is exposed to the cyclical nature inherent in the steel industry, which is the end user of TSAL’s products. This in turn is likely to keep the profitability and cash flows volatile.

Potential raw material disruption in FY2021; however sufficient raw material stock would act as a mitigant – At present, TSAL receives the chrome ore from TSL’s Sukinda mines, whose mining lease is set to expire in March 2020. In addition, the chrome ore availability from the recently acquired mines might get delayed. However, TSL has built chrome ore inventory stock, which will be enough to meet its requirements for the next 9-12 months. This will ensure uninterrupted raw material supply and continue to support TSAL’s cashflows.

Liquidity position: Strong

TSAL’s liquidity position is **Strong** with healthy free cash balances, no long-term debt and unutilised working capital limits. In addition, the company has healthy financial flexibility to be able to raise debt at a short notice for being a wholly-owned subsidiary of Tata Steel Limited, having significant operational and managerial linkages between the two.

Rating sensitivities

The key rating sensitivities include the quantum of investments required to develop new mines, funding pattern of the same and any change in business model from the current conversion nature of business, going forward.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Ferrous Metals Industry
Parent/Group Support	Parent Company: Tata Steel Limited
Consolidation/Standalone	Standalone financials were considered while assigning the ratings

About the company

TSAL is a wholly-owned subsidiary of TSL, involved in the production of high-carbon ferro chrome under a conversion agreement for TSL in its manufacturing facility in Cuttack, Odisha.

In FY2019, the company reported a net loss of Rs. 3.9 crore on an operating income of Rs. 175.0 crore compared to a net profit of Rs. 12.2 crore on an operating income of Rs. 192.2 crore in the previous year.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	192.2	175.0
PAT (Rs. crore)	12.2	-3.9
OPBDIT/OI (%)	10.3%	-0.8%
RoCE (%)	11.6%	-5.9%
Total Outside Liabilities/Tangible Net Worth (times)	0.3	0.3
Total Debt/OPBDIT (times)	0.0	-0.4
Interest Coverage (times)	113.7	-110.0
DSCR	93.8	35.5

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Current Rating (FY2020)				Rating History for the Past 3 Years		
			Amount Rated	Amount Outstanding	Rating		FY2019	FY2018	FY2017
					11-Feb-2020	15-Nov-2019			
1	Cash Credit	Long Term	18.0	-	[ICRA]A+ &	[ICRA]A+ &	[ICRA]A+ (Stable)		[ICRA]A+ (Stable)
2	Letter of Credit & Bank Guarantee	Short Term	2.0	-	[ICRA]A1+ &	[ICRA]A1+ &	[ICRA]A1+		[ICRA]A1+
3	Non- fund based - BG	Long term/short-term	260.0	-	[ICRA]A+ &/ A1+ &				

Note: & denotes Rating Watch with developing implications
Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long term - Cash Credit	NA	NA	NA	18.00	[ICRA]A+ &
NA	Short term - Non fund based	NA	NA	-	2.00	[ICRA]A1+ &
NA	Long term/Short term - Non fund based BG	NA	NA	-	260.00	[ICRA]A+ &/ A1+ &

& denotes Rating watch with developing implications

Source: T S Alloys Limited

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