February 20, 2020

Kanishk Steel Industries Limited: Update on Material Event; ratings reaffirmed at [ICRA]BB+ and [ICRA]A4+; outlook revised to Stable from Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term -Cash Credit	22.50	22.50	[ICRA]BB+; reaffirmed; outlook revised to Stable from Positive
Short term - Non-fund based	48.00	48.00	[ICRA]A4+; reaffirmed
Short term - Unallocated	21.00	21.00	[ICRA]A4+; reaffirmed
Total	**91.50**	**91.50**	

**- Instrument details are provided in Annexure-1*

Material event

Kanishk Steel Industries Limited has announced its quarterly results on February 11, 2020. The company reported an operating income of Rs. 205.31 crore with a profit after tax (PAT) of Rs. 0.65 crore in 9M FY2020 against an operating income of Rs. 230.70 crore with a profit after tax (PAT) of Rs. 3.56 crore in 9M FY2019.

Impact of the material event

ICRA has reaffirmed KSIL's ratings at [ICRA]BB+/[ICRA]A4+. The outlook has been changed to Stable from Positive due to weaker-than-expected performance in 9M FY2020.

Rationale

The revision in outlook factors in the weaker-than-expected performance of KSIL in 9M FY2020, as reflected by a decline in its profit margins to 0.32% in 9M FY2020 against 1.54% in 9M FY2019 and a moderation in debt coverage indicators. The company's profitability declined on a YoY basis due to sustained pressure on sales realisation in 9M FY2020.

The ratings, however, continue to factor in Kanishk Steel Industries Limited's (KSIL) established presence and operational profile, going forward, on account of its increased focus on long products and ongoing capacity addition. ICRA also consider the company's established customer base that ensures repeat orders over the years. The ratings derive comfort from its healthy capital structure, backed by relatively low debt levels. Besides, the company has a moderate working capital intensity. Further, the ratings continue to draw comfort from the considerable experience of KSIL's promoters in the steel industry for more than two decades.

The ratings, nonetheless, continue to factor in KSIL's moderate scale of operations, with its existing capacity partially backward integrated. Further, the highly commoditised and fragmented steel industry witnesses intense competition, which restricts the company's pricing flexibility, resulting in subdued profitability and limited scope for revenue growth. Besides, KSIL's business is vulnerable to the inherent cyclicality in the industry and forex fluctuation risk, which resulted in volatile operating margin in the past.

The Stable outlook reflects ICRA's expectation that KSIL will continue to benefit from its established presence, experienced promoters and the ongoing expansion of induction furnace capacity that are likely to support better value addition and consequently margins in the medium term.

Key rating drivers

Credit strengths

Established presence and extensive experience of the promoter – KSIL is a part of the OPG Group, which has an established presence in steel manufacturing and power generation businesses. The company trades in scrap, iron and steel products, the contribution from which has been reducing during the recent fiscals. Established presence of more than two decades, coupled with a relatively stable customer base, which includes large public sector entities like Bharat Heavy Electricals Limited (BHEL) lend some stability to its operations.

Established customer base with repeat orders over the years – The company has over 80 clients, with the top five customers accounting for 46% of the total revenues and the top ten customers contributing about 57% to the revenues in FY2019. It is one of the major suppliers of BHEL.

Moderate working capital capital intensity – The working capital intensity remained moderate at 12% in H1 FY2020 on account of lower debtor and inventory days. The receivables position fluctuates based on the sales mix, where the company extends a credit of 60 days to traders and 90 days to its large customers.

Moderate capital structure – KSIL's capital structure remains healthy, as illustrated by a gearing of 0.27 times and total outside liabilities to net worth (TOL/TNW) of 1.41 times as on September 30, 2019.

Credit challenges

Decline in profitability and debt protection metrics in 9M FY2020 – The company's OPITDA margins have declined to 0.78% in 9M FY2020 from 3.21% in FY2019 due to decline in steel prices realisation and inventory losses. The decline in company's profitability in 9M FY2020 resulted in weakening of its debt protection metrics, as illustrated by an interest coverage of 1.1 times in 9M FY2020 from 2.38 times in FY2019.

Moderate scale of operations – Despite a strong revenue growth in FY2019, KSIL's scale of operation declined to Rs. 205.31 crore in 9M FY2020 against Rs. 230.70 crore in 9M FY2019 due to a decline in sales realisation and lower income from traded goods. The company's further revenue growth would depend on an improvement in its realisations, given the high capacity utilisation of the rolling mill. The existing capacity is only partially backward integrated and KSIL is relying on external vendors for 70-75% of its billet requirement. KSIL purchased an induction furnace from a Hyderabad-based entity in FY2018 for expanding its billet manufacturing unit to 55,000 MTPA from 25,000 MTPA. The additional furnace is expected to commence operations in FY2021 and is expected to improve its operational profile.

Intense competition and limited pricing flexibility in steel industry – The long steel product segment is highly fragmented and commoditised, leading to intense competition, which restricts KSIL's pricing flexibility. Further, the domestic steel industry is cyclical in nature, which is likely to impact the cash flows of the long product manufacturers including KSIL.The company's contribution margin remained thin as it was dependent on the price of raw materials (scrap and sponge iron) and operating costs. KSIL's competitive position is supported by its diversified product profile, with presence across various ranges and dimensions. It enjoys lower freight costs as it is located closer to customers, which allows price advantage against its larger peers.

Liquidity position – Adequate

KSIL's liquidity position remains adequate, supported by cash flow from operations of Rs. 3.62 crore in H1 FY2020 against Rs. 3.17 crore in FY2019 owing to a drop in its working capital requirements. The company's working capital intensity remained moderate at 12% in H1 FY2020 compared to 11% in FY2019 on account of lower debtor days. Further, its moderate working capital utilisation at 39% on an average with adequate buffer available in its working capital limits in the past 13-month period ended January 2020, no debt repayment scheduled and limited capex plans will enable its liquidity to remain adequate. However, timely recovery of advances extended remains a key rating factor.

Rating sensitivities

Positive triggers – ICRA may upgrade KSIL's rating if it improves its profitability and debt coverage metrics on a sustained basis. Specific credit metrics that may lead to an upgrade of KSIL's rating is interest coverage improving above 3.0 times on a sustained basis.

Negative triggers –Pressure on KSIL's rating may arise if its profitability metrics continue to remain subdued. Further, KSIL's ratings could also be downgraded if its liquidity position weakens on account of any increase in working capital intensity or an increase in non-current assets. Specific credit metrics that may lead to a downgrade of KSIL's ratings is TD/OPITDA increasing above 4.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Entities in the Ferrous Metals Industry
Parent/Group Support	Not Applicable
Consolidation / Standalone	The ratings are based on the standalone financial profile of the entity

About the company

Incorporated in 1989, KSIL manufactures TMT bars and structural steel products. It has an installed rolling mill capacity of 70,000 tonnes per annum (TPA). The company is backward integrated with facilities to manufacture MS ingots (viz. induction furnaces with an installed capacity of 25,000 TPA). It is also involved in the trading of steel scrap. KSIL is a part of the OPG Group, which is involved in steel and power businesses. The inputs to the induction furnaces are met through a mix of imports (mainly in the UK and Dubai) and local purchases. The company utilises ingots produced in-house as its raw material requirement for its rolling mill and procures a considerable portion of the ingots/billets requirement from other companies.

Key financial indicators (Audited)

	FY2018	FY 2019
Operating Income (Rs. Crore)	234.78	330.29
PAT (Rs. Crore)	1.58	4.28
OPBDITA/ OI (%)	3.13%	3.21%
RoCE (%)	13.31%	22.49%
Total Debt/ TNW (times)	0.22	0.41
Total Debt/ OPBDIT (times)	1.25	1.76
Interest Coverage (times)	1.62	2.38

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Type	Current Rating (FY2020)				Chronology of Rating History for the past 3 years		
			Amount Rated (Rs. crore)	Amount Outstanding as on May 2019 (Rs. crore)	Date & Rating 20 February 2020	Date & Rating 06 June 2019	Date & Rating in FY2019 02 July 2018	Date & Rating in FY2018 05 July 2017	Date & Rating in FY2017 27 June 2016
1	Cash Credit	Long Term	22.50	-	[ICRA]BB+ (Stable)	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)
2	Non Fund based limits	Short Term	48.00	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+
3	Unallocated Limits	Short Term	21.00	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+

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 No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	March 2019	NA	NA	22.50	[ICRA]BB+ (Stable)
NA	Letter of Credit	March 2019	NA	NA	48.00	[ICRA]A4+
NA	Unallocated limits	NA	NA	NA	21.00	[ICRA]A4+

Source: KSIL

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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.

For more information, visit www.icra.in

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