

May 11, 2023^(Revised)

Tata Steel Long Products Limited: Continues on Rating Watch with Developing Implications

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Commercial Paper Programme	1500.00	1500.00	[ICRA]A1+; Continues on Rating Watch with Developing Implications
Total	1500.00	1500.00	

*Instrument details are provided in Annexure-1

Rationale

The rating of Tata Steel Long Products Limited (TSLPL) continue to remain On Rating Watch with Developing Implications 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 on its implementation timeline.

The rating factors in TSLPL's status as a strategically important entity for Tata Steel Limited, which leads to a high degree of financial flexibility. ICRA expects TSL to be willing to extend financial support to TSLPL, should there be a need, given its strategic importance to the Tata Steel Group, and out of its need to protect its reputation. Earlier, TSL had provided large funding support to TSLPL during the acquisition of the steel business of Usha Martin Limited and thereafter has again supported the acquisition of Neelachal Ispat Nigam Limited (NINL) through long-term funding, which has aided TSLPL in maintaining a strong liquidity profile despite making two large acquisitions. Moreover, given NINL's sizeable growth capex lined up over the next several years, ICRA expects TSL to be willing to extend financial support to TSLPL, going forward, should there be a need. The rating also reflects the vertically integrated nature of TSLPL's acquired steel businesses (Usha Martin and NINL), supported by captive iron ore mines. The rating also factors in the greater visibility towards recovery of invested capital for the Radhikapur (East) coal block following the successful reauctioning of the block to a new bidder for commercial coal mining.

While the broader steel industry had reported a sequential decline in realisations amid the volatile operating environment, TSLPL's blended realisations (standalone business) increased in FY2023, given the pick-up in demand in the commercial vehicle segment, and the company's focus on new product development and product mix enrichment, leading to a high share of value-added products. Notwithstanding the same, a disproportionately steep increase in input prices (mainly coking/ thermal coal, freight, and regulatory charges) severely dented its profit margin in FY2023. On a consolidated basis, TSLPL posted operating losses in FY2023 that can be attributed to the large one-time start-up costs incurred to restart the operations at the recently acquired NINL, which was closed for almost two years prior to the acquisition. ICRA has noted the uptick in earnings reported by TSLPL's standalone business in Q4 FY2023 amid softening of raw material prices and reduction in losses at NINL, having demonstrated ramping up to its rated capacity levels in March 2023, which in ICRA's view will support an improved operating and financial performance in the coming quarters.

TSLPL's credit profile, however, reflects its exposure to sectoral concentration risks, with the automobile sector accounting for around 50% of the overall sales, exposing the company to earnings cyclicality. TSLPL's rating also incorporates the sub-optimal capacity utilisation level of the pellet plant and steel melt shop at Gamharia, and the exposure of the company's earnings to volatility in steel prices/ input costs and exchange rate fluctuations. The rating also factors in the changes in Mines and Minerals (Development and Regulation) Act (MMDR Act), which will lead to additional regulatory charges on TSLPL, thus remaining a structural drag on its profits. Besides, TSLPL has plans to scale up NINL's capacity to around 5 mtpa over the next few years

and further to 10 mtpa by 2030. While funding risks for the future expansion plans will be largely mitigated by the parent's stated intent of financial support, the company would remain exposed to project execution risks, given the large-sized expansion plans.

Key rating drivers and their description

Credit strengths

Status as a subsidiary of TSL with strategic importance as a growth vehicle in the long product segment – TSLPL's status as a 74.91% subsidiary of TSL imparts considerable financial flexibility to the company. TSL has identified TSLPL as the strategic vehicle to focus on the long-products segment, and has provided operational, management and financial support to TSLPL's future growth plans. In line with TSL's stated intent of growing the long products business using TSLPL as the vehicle, TSL has supported NINL's acquisition by TSLPL through long-term funding, which has aided TSLPL in maintaining a strong liquidity profile despite making large acquisitions.

Vertically integrated nature of the acquired steel business, supported by captive iron ore mine – TSLPL's around 1-million-tonne-per-annum (mtpa) acquired steel business of Usha Martin comprises integrated upstream and downstream facilities such as sinter, pellet, sponge iron kiln, blast furnace, electric arc furnace, wire rod/ bar/bloom mills, captive power plants, and a captive iron ore mine (which meets a significant portion of the iron ore requirements at Gamharia). The recently acquired NINL unit comprises upstream and downstream facilities such as blast furnace, sinter, coke oven, steel melting shop, power plant and a captive iron ore mine having reserves of around 100 million tonnes.

Increasing share of value-added products supported higher realisations – Following the takeover of the around 1-mtpa alloy steel plant of Usha Martin, TSLPL has focused on new product development and product mix enrichment with the aim of increasing margins and partly insulating the company's profits from the cyclicity associated with commoditised steel grades. In the last fiscal, while the broader steel industry had reported a sequential decline in realisations amid the volatile operating environment, TSLPL's blended realisations (standalone business) had increased, given the rising share of value-added products in its sales mix.

Limited external borrowings and strong parentage increase the company's resilience to withstand a prolonged downcycle – Strong free cash flows generated in FY2021 and FY2022 helped the company deleverage aggressively, leading to a significant reduction in external debt levels, which declined by around 72% between March 31, 2020 and March 31, 2023. Modest external borrowing along with no repayment commitments until FY2030 and its strong parentage increase the company's resilience to withstand periods of downcycle, besides supporting its liquidity.

Greater visibility towards recovery of invested capital for the Radhikapur (East) coal block following successful reauctioning of the block to a new bidder for commercial coal mining – TSLPL has invested towards land and surface infrastructure for the 5-mtpa Radhikapur (East) coal block, which was deallocated by the Supreme Court in September 2014. In November 2020, the Ministry of Coal has reaucted the said coal block, and the same was won by EMIL Mines and Mineral Resources Ltd. TSLPL will be receiving a compensation of ~Rs. 179 crore along with interest on the amount invested towards land acquisition. This mitigates the risk associated with the recoverability of TSLPL's investment in the Radhikapur (East) coal block.

Credit challenges

Exposure to sectoral concentration risks – Historically, around 50% of TSLPL's deliveries has been directed to the automobile sector, which exposes the company to the sectoral concentration risks. High exposure to the automobile sector became apparent as the company faced demand headwinds in FY2020, leading to TSLPL reporting a large net loss during the period. ICRA notes that within the automobile sector, TSLPL earlier had high dependence on the commercial vehicle (CV) segment.

However, new customer additions in the 2W and passenger vehicle (PV) sectors in the last two years aided in partly diversifying its exposure to the highly cyclical CV sector.

Steep increase in input costs and large losses at NINL severely dented earnings in the last fiscal; earnings exposed to volatility in steel prices/ input costs and exchange rate fluctuations – While the broader steel industry had reported a sequential decline in realisations amid the volatile operating environment, TSLPL's blended realisations (standalone business) increased in FY2023, given the pick-up in demand in the commercial vehicle segment, and the company's focus on new product development and product mix enrichment, leading to a high share of value-added products. Notwithstanding the same, a disproportionately steep increase in input prices (mainly coking/ thermal coal, freight, and regulatory charges) severely dented its profit margin in FY2023. On a consolidated basis, TSLPL posted operating losses in FY2023 that can be attributed to the large one-time start-up costs incurred to restart the operations at the recently acquired NINL, which was closed for almost two years prior to the acquisition. TSLPL's profitability and cash flows are also exposed to the cyclicity associated with the steel industry, which keeps margins of all players volatile. TSLPL imports bulk of the coking and non-coking coal requirements from the seaborne market. ICRA notes that high reliance on imported coal exposes TSLPL's profitability to fluctuations in international coal prices as well as fluctuations in the USD-INR exchange rate. ICRA has noted the uptick in earnings reported by TSLPL's standalone business in Q4 FY2023 amid softening of raw material prices and reduction in losses at NINL, having demonstrated ramping up to its rated capacity levels in March 2023, which in ICRA's view will support an improved operating and financial performance in the coming quarters.

Sub-optimal capacity utilisation level at the pellet plant and steel melting shop at Gamharia – ICRA notes that TSLPL has not been able to ramp up to the full rated capacity at the 1.2-mtpa pellet plant and the 1-mtpa crude steel making capacity at Gamharia. It has been observed that the peak demonstrated capacity utilisation of the pellet plant is around 60-65%, and that for the crude steel making capacity is around 70%. ICRA has noted increased steel production in FY2022 and FY2023, which has been achieved through debottlenecking at the steel melting shop and arcing, however, it is yet to reach the rated capacity levels. Therefore, TSLPL's ability to debottleneck the pellet plant capacity and achieve higher steel production from the EAF unit at Gamharia would remain key performance drivers, especially in a year when steel spreads have contracted significantly from the FY2022 highs.

Changes in MMDR Act and additional regulatory charges lead to a structural drag on profits – TSLPL procures a part of its iron ore requirements from the captive mines of TSL. Consequent to the amendment in the MMDR Act effective March 28, 2021, TSL recovers an additional amount of 150% of the royalty paid on iron ore fines and 250% on iron ore lumps sourced by TSLPL. Going forward, this additional regulatory charge will remain a structural drag on the profits of TSLPL.

Large-sized expansion plan in pipeline; will remain exposed to project execution risks – After stabilising the acquired steel business of Usha Martin, TSLPL has embarked upon the next phase of expansion with the acquisition of NINL. With NINL ramping up to its rated capacity level in March 2023, the company has plans to scale up NINL's capacity to around 5 mtpa over the next few years and further to 10 mtpa by 2030. While funding risks for the future expansion plans will be largely mitigated by the parent's stated intent of financial support, the company would remain exposed to project execution risks, given the large-sized expansion plans. However, ICRA takes comfort from TSL's established track record of successfully commissioning large greenfield/brownfield steel capacities.

Environmental and Social Risks

Environmental considerations – Steel manufacturing is an energy intensive process and requires substantial use of fossil fuels, which results in greenhouse gas emissions, industrial waste generation, and environmental pollution. Increasing regulatory requirements to reduce greenhouse gas emissions and stricter air pollution standards may lead to higher costs for steel manufacturers in the medium term. This in turn leads to a greater focus on reducing the carbon footprint through various technological interventions, like increasing the share of renewables in the energy mix, increasing the share of steelmaking

through the electrical route, transition to green hydrogen technologies, decrease in fuel rate in furnaces, and setting up carbon capture utilisation and storage units, to name a few. With many of these emerging low-carbon technologies yet to achieve commercial viability, this transition could entail a significant investment for metal manufacturers. Further, TSLPL faces the risk of physical climate change from floods and drought in the form of disruption in raw material availability due to extreme weather events and impact on water availability due to drought.

Social considerations – Social risks for steel manufacturers manifest from health and safety aspects of employees involved in the manufacturing activities. Casualties/ accidents at the operating units due to gaps in safety practices could lead to production outages for steel manufacturers like TSLPL and invite penal actions from regulatory bodies. The sector is exposed to labour related risks and risks of protests/social issues with local communities, which might impact expansion/modernisation plans. Also, the adverse impact of environmental pollution in nearby localities could trigger local criticism.

Liquidity position: Strong

TSLPL's liquidity has been assessed as **Strong**, supported by its free cash and liquid investment balance of around Rs.1,240 crore on a consolidated basis as on March 31, 2023. Besides, the company had large undrawn fund-based working capital lines of around Rs. 1,400 crore as of February end, 2023 which also supports its liquidity profile. The external debt levels remain at modest levels with no repayment obligations until FY2030. In addition, TSLPL's liquidity profile derives strength from the financial flexibility that it enjoys for being a strategically important entity of the Tata Steel Group.

Rating sensitivities

Positive factors – Not applicable

Negative factors – Pressure on TSLPL's rating could arise if there is a deterioration in the credit profile of TSL. The rating could also come under pressure if TSLPL witnesses a sustained period of weak earnings and/ or makes a large debt-funded capex/ investment, leading to a significant deterioration in its liquidity profile.

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 (TSL) ICRA expects TSL to be willing to extend financial support to TSLPL, should there be a need, given its strategic importance to the Tata Steel Group, and out of its need to protect its reputation. Both TSLPL and TSL share the common Tata Steel name, which in ICRA's opinion, would persuade TSL to provide financial support to TSLPL to protect its reputation from the consequences of a Group entity's distress.
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of TSLPL. As on March 31, 2023, the company had one subsidiary - Neelachal Ispat Nigam Limited (NINL).

About the company

Tata Steel Long Products Limited (TSLPL) was originally set up as a joint venture between Tata Steel Limited (TSL) and Industrial Promotion & Investment Corporation of Orissa Limited in 1982. At present, TSLPL is a 74.91% subsidiary of TSL. The company is one of the early entrants in the domestic sponge iron industry, with a plant in Keonjhar district of Odisha having an installed capacity of 4,65,000 mtpa. In April 2019, through a slump sale by Usha Martin Limited, TSLPL acquired the former's 1-mtpa integrated alloy steel plant in Jamshedpur which manufactures alloy/ high carbon steel sold to the automotive, tractors and other agriculture equipment, lifting and excavation, general engineering, railways, construction (reinforcement), and power

(transmission and distribution) sectors. On January 31, 2022, TSLPL was declared as the winning bidder for the acquisition of NINL's 1-mpa steel plant located at Kalinganagar, in Jajpur, Odisha. The acquisition was completed officially on July 4, 2022.

Key financial indicators (Audited)

TSLPL	FY2021	FY2022	FY2023^
Operating Income (Rs. crore)	4749.9	6801.6	8,991.8
PAT (Rs. crore)	572.0	629.9	-2,303.9
OPBDIT/OI (%)	23.7%	17.7%	-8.2%
PAT/OI (%)	12.0%	9.3%	-25.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	5.2	15.0
Total Debt/OPBDIT (times)	1.3	11.2	-20.0
Total External Debt/OPBDIT (times)	1.3	0.6	-1.1
Interest Coverage (times)	4.8	10.9	-0.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ^FY2023 financials are consolidated which includes NINL which was acquired on July 4, 2022

Status of non-cooperation with previous CRA – Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Type	Current Rating (FY2024)			Chronology of Rating History for the past 3 years				
			Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31, 2023 (Rs. crore)	Date & Rating on	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021	
					May 11, 2023	Oct 4, 2022	Feb 14, 2022	Feb 9, 2022	Feb 26, 2021	Nov 24, 2020
1	Fund Based Facilities	Long Term	-	-	-	-	-	-	-	-
2	Non-Fund Based Facilities	Short Term	-	-	-	-	-	-	-	-
3	Commercial paper programme	Short Term	1500.00	0.00	[ICRA]A1+; On Rating watch with developing implications	[ICRA]A1+; On Rating watch with developing implications	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Fund Based – Proposed Term Loan	Long Term	-	-	-	-	-	-	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Commercial Paper	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-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (RS Crore)	Current Rating and Outlook
Not placed	Commercial Paper	-	-	-	1500.00	[ICRA]A1+; Rating Watch with Developing Implications

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Neelachal Ispat Nigam Limited	92.68%	Full consolidation

Source: Company

Corrigendum

Rationale dated May 11, 2023 has been revised with changes as below:

Page 1: The first sentence of the second paragraph has been revised as “*The rating factors in TSLPL’s status as a strategically important entity for Tata Steel Limited, which leads to a high degree of financial flexibility*” from “*The rating reaffirmation factors in TSLPL’s status as a strategically important entity for Tata Steel Limited, which leads to a high degree of financial flexibility*”.

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