Suraj Products Limited

February 28, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loans	2.00	2.00	[ICRA]BB+ (Stable); Upgraded from [ICRA]BB (Stable)
Fund Based – Cash Credit	17.50	17.50	[ICRA]BB+ (Stable); Upgraded from [ICRA]BB (Stable)
Non-Fund Based Limits	1.50	1.50	[ICRA]A4+; Upgraded from [ICRA]A4
Unallocated Limits	3.00	3.00	[ICRA]BB+ (Stable) /[ICRA]A4+; Upgraded from[ICRA]BB (Stable)/ [ICRA]A4
Total	**24.00**	**24.00**	

**Instrument details are provided in Annexure-1*

Rationale

The upgrade in the ratings of SPL considers improved vertical integration due to commissioning of the steel melting facility and addition of a captive power plant in FY2018, which positively impacted the company's cost structure. The enhanced operational integration and improved realisations resulted in a significant turnover growth in FY2018, which continued in 9M FY2019, positively impacting its net profits and cash accruals. ICRA also notes SPL's further expansion in steel melting capacity and captive power plant, which is likely to positively impact the company's turnover and cost structure in the short to medium term. ICRA also notes the company's coal linkages, which enhance raw material security and reduce the cost of production to some extent.

The company's ratings are constrained by the increase in debt service obligation arising from debt-funded capex in the recent past and the high working capital intensity of operations, which exert pressure on the company's liquidity. Further, SPL remains vulnerable to the cyclicality inherent in the steel industry, which is likely to keep the company's profitability and cash flows volatile.

Outlook: Stable

ICRA believes that SPL will continue to benefit from the integrated nature of operations and the long experience of its promoters in the steel industry. ICRA believes that SPL's financial profile will remain comfortable, going forward, aided by improved turnover, profit and net cash accrual. The outlook may be revised to Positive if further growth in revenue and profits strengthens the financial risk profile. The outlook may be revised to Negative if revenue and profit are adversely impacted by deterioration in demand, and cash accrual is lower than expected, or if any significant debt-funded capital expenditure leads to deterioration in the company's capital structure and debt coverage metrics.

Key rating drivers

Credit strengths

Significant growth in turnover and profits aided by improved operational integration and increased realisations- The company commissioned its induction furnace (with a capacity of 25,000 tonne per annum) in November 2017 for producing ingots, which is a relatively value-added product. This along with increase in realisation led to an increase in SPL's operating income by 17% in FY2018 to Rs. 69.96 crore from Rs. 59.90 crore in FY2017. SPL's operating margin increased significantly in FY2018 to 16.45% from 8.66% in FY2017 due to an increase in realisation and improved operational integration. The company's average realisation of various products increased further in 9M FY2019 and its operating income stood at Rs. 78.97 crore in 9M FY2019 compared to Rs. 68.91 crore in FY2018. As a result, the company's net profits at an absolute level and net cash accrual in 9M FY2019 surpassed the same reported in the full year FY2018, notwithstanding a decline in operating margin to 13.72% in 9M FY2019 from 16.48% in FY2018. The company's net margin stood at 6.56% in 9M FY2019 compared to 5.12% in FY2018, primarily due to improved operating profits at an absolute level and an increase in the non-operating income.

Presence of captive power plant ensures availability of power at a cheap rate- The company has a captive power plant (CPP) of 6 megawatt (MW), out of which 3 MW is based on waste-heat-recovery (WHR) technology and the balance 3 MW is based on atmospheric fluidised bed combustion (AFBC) process. 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 cheap rate.

Coal linkages secured through auctions at favourable price to enhance raw material security and reduce production cost to some extent- The company has secured coal linkages totalling 25,600 tonne per annum from Mahanadi Coal Fields (MCL) for manufacturing of sponge iron as well as power generation, which is likely to meet a portion of the company's total coal requirement and enhances its raw material security. Moreover, a lower average price of the linkage coal compared to the current market prices is likely to reduce SPL's overall production cost to some extent.

Recent expansion in steel melting capacity and captive power plant likely to positively impact turnover and cost structure- SPL has doubled its steel melting capacity by 25,000 TPA to 50,000 TPA with the installation of an induction furnace in December 2018. It has also installed another CPP of 3 MW capacity (AFBC), which will be utilised to generate power by using coal and dolochar (a by-product obtained from sponge iron production) as inputs. This is likely to positively impact the company's turnover and cost structure.

Credit challenges

Increased debt service obligation arising from debt-funded capex in recent past- SPL's capacity expansion with the installation of an induction furnace and another CPP led to an increased long-term borrowing by the company. The cost of expansion (including steel melting shop with CCM and 3 MW CPP) stood at Rs. 19 crore, funded by a term loan of Rs. 11 crore from bank and the balance from internal accruals and unsecured loan from promoters. This led to an increase in debt service obligation of the company.

Exposure to volatility in steel prices - The steel industry is characterised by its inherent cyclicality. This is likely to keep the profitability and cash flows of all the players in the industry, including SPL, volatile going forward.

High working capital intensity of operations exert pressure on liquidity- The company has high working capital intensity due to significant inventory holding requirement that exerts pressure on its liquidity. SPL's net working capital relative to operating income (NWC/OI) declined marginally to 50% in FY2018 compared to 54% in the previous year, though the same still remained very high. As a result, the company's working capital utilisation remains high, as reflected by an average fund-based working capital utilisation of 82% during June 2017 to January 2019.

Liquidity position

SPL's high working capital intensity of operations exerted pressure on its liquidity. Its debt-service obligation has also increased due to fresh long-term loan availed for recent capital expenditure. Nevertheless, SPL's improved net cash accruals are likely to keep its liquidity position comfortable.

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 rating is based on the standalone financial statements of Suraj Products Limited

About the company

Established in 1991, Champion Cement Industries Limited was involved in production of cement. The company changed its name 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 3-MW waste heat recovery based captive power plant (CPP) and an induction furnace of 25,000 tonne per annum capacity in 2018. In the current fiscal, the company has installed another CPP of 3 MW (AFBC based) and also doubled the steel melting capacity. The company has also installed a continuous casting machine (CCM) for production of billets, instead of ingots. At present, the company has an installed capacity to produce 36,000 metric tonnes per annum (MTPA) of sponge iron, 24,000 MTPA of pig iron and 50,000 MTPA of billets.

Key financial indicators

Standalone	FY2017 (audited)	FY2018 (audited)	9M FY2018 (provisional)
Operating Income (Rs. crore)	59.90	69.96	78.97
PAT (Rs. crore)	0.96	3.58	5.18
OPBDIT/ OI (%)	8.66%	16.45%	13.72%
RoCE (%)	5.48%	10.49%	-
Total Debt/ TNW (times)	1.45	1.51	-
Total Debt/ OPBDIT (times)	8.52	4.44	-
Interest Coverage (times)	1.95	2.45	3.87
NWC/ OI (%)	54%	50%	-

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2019) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating February 2019	Chronology of Rating History for the past 3 years Date & Rating in FY2018 August 2017	Date & Rating in FY2017 July 2016	Date & Rating in FY2016 Mar 2016	August 2015
1	Fund-based –Term Loans	Long Term	2.00	NA	[ICRA]BB+ (Stable)	[ICRA]BB (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Stable)
2	Fund-based –Cash Credit	Long Term	17.50	NA	[ICRA]BB+ (Stable)	[ICRA]BB (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Stable)
3	Non-fund based Limits	Short Term	1.50	NA	[ICRA]A4+	[ICRA]A4	[ICRA]A4+	[ICRA]A4+	[ICRA]A3
4	Unallocated	Long Term/ Short Term	3.00	NA	[ICRA]BB+ (Stable)/ [ICRA]A4+	[ICRA]BB (Stable)/ [ICRA]A4	[ICRA]BB+ (Stable)/ [ICRA]A4+	[ICRA]BB+ (Stable)/ [ICRA]A4+	[ICRA]BBB- (Stable)/ [ICRA]A3

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	Term Loans	August, 2016	NA	February, 2024	2.00	[ICRA]BB+ (Stable)
NA	Cash Credit	NA	NA	NA	17.50	[ICRA]BB+ (Stable)
NA	Non Fund Based	NA	NA	NA	1.50	[ICRA]A4+
NA	Unallocated	NA	NA	NA	3.00	[ICRA]BB+ (Stable)/ [ICRA]A4+

Source: Suraj Products Limited

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About ICRA Limited:

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