April 24, 2020

Maharashtra Seamless Limited: Ratings reaffirmed; outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund based (Cash Credit)	15.0	15.0	[ICRA]AA- (Negative); reaffirmed, outlook revised from Stable
Long-term fund based (Term Loan)	66.0	66.0	[ICRA]AA- (Negative); reaffirmed, outlook revised from Stable
Short-term fund based (Short-term Loan/ Bill Discounting Facilities)	45.0	45.0	[ICRA]A1+; reaffirmed
Long-term/ Short-term Non-fund Based (Letter of Credit/ Buyer's Credit/ Bank Guarantee)	974.0	974.0	[ICRA]AA- (Negative)/ [ICRA]A1+; reaffirmed, outlook revised from Stable
Issuer Rating	-	-	[ICRA]AA- (Negative); reaffirmed, outlook revised from Stable
Total	**1,100.00**	**1,100.00**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in outlook to Negative on the long-term and issuer ratings of Maharashtra Seamless Limited (MSL or the company) follows heightened operating risks for the company owing to a steep drop in crude oil prices in recent months and an increasingly uncertain outlook for upstream capital spending. The pressure is accentuated by the current lockdown due to the COVID-19 pandemic, which is disrupting operations across sectors and could result in demand-side pressures. While the company caters to other sectors as well, including fertilisers, power and automotive, it faces significant dependence on the oil and gas sector by its presence in the seamless pipes business and exposure to offshore drilling rigs business. The exposure has increased with MSL's recent acquisition of an oil drilling rig from one of its associate companies (Star Drilling Pte. Ltd. or SDPL). With limited remaining tenure of the rig's lease charter (valid till March 2021) and sizeable debt assumed by the company for the acquisition, its inability to re-deploy the rig in a timely manner and at favourable terms, could potentially affect its debt coverage indicators after the expiry of the existing charter in March 2021. ICRA notes that the acquisition has not resulted in an increase in the company's leverage, as reflected by (consolidated net debt + guaranteed debt)/ OPBIDTA, given that the debt taken over was already guaranteed by MSL. However, dependence on MSL's cash flows to service the associated debt stands increased vis-à-vis the previously stated stance of need-based and limited support to rig entities in the Group. While ICRA has taken a note of the company's comfortable pending order book position in the pipes segment, a prolonged weakness in oil prices which affects capital spending by oil exploration and production companies, besides a slowdown in demand from the other consuming sectors could potentially affect MSL's revenues, profitability and debt coverage metrics.

Nevertheless, despite moderation likely from FY2021 onwards amid increased repayment obligations, ICRA expects MSL's debt coverage metrics to remain healthy with an adequate liquidity position. Further, the ratings continue to draw strength from MSL's leadership position in the domestic seamless pipes sector, supported by its sizeable capacity, presence in the high value-added, large-diameter pipe segment, which faces relatively low competition, and its status as

a registered vendor for major domestic oil producers and refiners. The ratings also continue to reflect MSL's strong financial profile underpinned by low financial leverage at a consolidated level (estimated Total Debt/Tangible Net Worth of 0.4 time and Net Debt/Operating Profit of 1.4 times in FY2020). This is despite an increase in debt outstanding in the books of the company to fund acquisition of a Telangana-based entity, United Seamless Tubular Private Limited (USTPL), under the Corporate Insolvency Resolution Process (CIRP) during FY2019 and the off-shore jack-up rig from SDPL in March 2020. Further, the ratings factor in the sizeable credit support extended by the company to its overseas associates in the form of corporate guarantees and stand-by letters of credit (SBLCs), adjusting for which the leverage ((net debt + guaranteed debt)/ operating profit) stands higher (estimated at ~2.0 times as on March 31, 2020). In this context, ICRA draws comfort from a gradual reduction in guaranteed obligations over the years (estimated at Rs. 320 crore[1] as on March 31,2020 over Rs. 770.9 crore as on March 31, 2019 and Rs. 1,059.1 crore as on March 31, 2018), besides improved earnings visibility from the underlying assets following lease charter renewals over the past one-and-a-half years, which is expected to keep the reliance of these entities for incremental funding support from MSL low in the near to medium term, unlike the recent years.

ICRA also notes that the operating environment for the domestic seamless pipe manufacturers in recent years has been supported by imposition of definitive anti-dumping duty (ADD) on imports of seamless pipes and tubes into India from China for five years starting May 2016. Together with a favourable movement in crude oil prices and preference given by Indian PSUs to domestic manufacturers for procurements, this supported the demand that drove a strong improvement in the company's core operations in recent years. While the slowdown in Government contracts is expected to have affected the revenue growth in FY2020, ICRA expects its profitability to have remained healthy. Nevertheless, with ADD scheduled to be over in May 2021, which exposes the sector to the risk of surge in imports thereafter, as well as an uncertain oil price environment that could affect demand from the upstream sector, company stands exposed to growth and profitability risks. Besides, the company's profitability remains susceptible to volatility in input prices.

Key rating drivers and their description

Credit strengths

Leadership position in the domestic seamless pipes sector – MSL is the leading domestic manufacturer of seamless pipes with an installed production capacity of 550,000 tonne per annum (tpa) with a strong presence in the high value-added, large-diameter seamless pipes segment (outer diameter or OD >10 inch), which faces relatively low competition. In the seamless pipes segment, MSL primarily caters to companies in the oil and gas sector, where it is a registered vendor for major domestic oil producers and refiners. In addition, it also caters to other segments, including power plants, boilers, automobile engineering, etc. MSL is also present in the electric resistance welded (ERW) pipes segment with an installed manufacturing capacity of 200,000 tpa of pipes of larger sizes (OD between 8–21 inches) that find use in the oil industry, irrigation and water supply sectors. Although it provides diversification benefits, the revenue share of the ERW pipes segment in the company's consolidated revenues and operating profits has remained marginal (13% and 7%, respectively, in FY2019) over the years.

Strong financial profile underpinned by low financial leverage – MSL's established market position in the seamless pipes business has over the years supported healthy revenues, cash accruals and accumulation of sizeable net worth. After the

[1] *Approximately Rs. 350 crore of guaranteed debt was transferred to MSL's own balance sheet in March 2020, with the acquisition of rig from SDPL*

imposition of ADD in May 2016, its revenues and profitability grew at a robust rate in the past three years. Further, its credit profile has remained strong, supported by its strong balance sheet, corroborated by an estimated Consolidated Total Debt/Tangible Net Worth of 0.4 time and Net Debt/Operating Profit of 1.4 times in FY2020. This is despite a significant increase in MSL's indebtedness over the past few years with an estimated consolidated net debt of ~Rs. 800 crore as on March 31, 2020 compared to a cash surplus position of Rs. 560 crore as on March 31, 2014. Further, the company's liquidity position remains adequate, which further improved in FY2020 with total estimated cash and liquid investments of ~Rs. 400-500 crore as on March 31, 2020 as compared to Rs. 153.2 crore as on March 31, 2019. Besides, the company's working capital borrowings remain low vis-à-vis its net current assets, which provides it financial flexibility to avail enhancements when required.

Operational support from ADD and preference given by PSUs to domestic seamless pipe manufacturers – Despite MSL's leadership position in the domestic seamless pipes industry, its production levels remained under pressure during the three-year period ending March 2016 as it witnessed intense competition due to imports from China, particularly after the US and European Union imposed anti-dumping duties on imports of seamless pipes from China in FY2011. To address this, a 20% ad-valorem duty was imposed by India on imports from China in August 2014 for one year, followed by a 10% duty in the second year. In May 2016, a provisional anti-dumping duty was imposed, which was subsequently made definitive in February 2017 for five years starting May 2016. Together with the preference given by PSUs to domestic manufacturers for their procurements, this has kept operating environment for domestic seamless pipe manufacturers favourable, supporting their performance in recent years. With anti-dumping duty scheduled to be over in May 2021, the sector remains exposed to the risk of surge in imports thereafter.

Healthy financial flexibility underpinned by parentage of D. P. Jindal Group– MSL is the flagship company of the D. P. Jindal Group, which also includes Jindal Pipes Limited (JPL[2]) and JDIL among the other key companies in its fold. Besides the presence in steel pipes and tubes segment, the Group also owns six rigs through various Group companies. The drilling/rig management business is now undertaken by JDIL (which manages five rigs) and another Group company, Dev Drilling Pte. Ltd. (which manages one rig).

Credit challenges

Sizeable contingent liabilities and increased leveraging following acquisitions; reduction in guaranteed amounts and deployment of rigs in international subsidiaries, however, provides comfort - Over the years, MSL has extended sizeable credit support to its overseas associates in the form of corporate guarantees and SBLCs (aggregating Rs. 770.9 crore as on March 31, 2019). Most of these guarantees were towards two associate concerns, Dev Drilling Pte. Ltd. (DDPL) and SDPL, which have developed two off-shore jack-up rigs. With recent acquisition of rig owned by SDPL in FY2020, the guaranteed amount is estimated to have reduced to Rs. 320 crore as on March 31, 2020, with the falling off of guarantee provided by MSL for SDPL's debt. However, correspondingly, debt outstanding in the books of MSL stands increased by ~Rs. 375 crore, with the debt availed to partly fund the acquisition consideration. ICRA notes that the company intends to claim accelerated depreciation on the acquired rig to reduce its tax outflows over the next few years. This apart, MSL also raised a debt of Rs. 375 crore during FY2019 to partly fund the acquisition consideration of USTPL. Together with larger working capital requirements accompanying the growth and continued financial support extended to group companies, this has resulted in a significant increase in MSL's indebtedness over the past few years with an estimated consolidated net debt of ~Rs. 800 crore as on March 31, 2020 compared to a cash surplus position of

[2] *ICRA has [ICRA]A+ (Stable)/ MA+ (Stable)/ [ICRA]A1+ ratings outstanding for bank facilities of Jindal Pipes Limited. The rating for its fixed deposit programme has been placed on notice of withdrawal. For detailed rating rationale on the company, please refer to ICRA's website: www.icra.in.*

Rs. 560 crore as on March 31, 2014. This has been despite external funding requirements in the core operations remaining low. As a result, leverage as reflected by (consolidated net debt + guaranteed debt)/ OPBDITA stands higher at ~2.0 times as on March 31, 2020(E), vis-à-vis consolidated net debt / OPBDITA of 1.4 times as on March 31, 2020(E). In this context, deployment of all rigs owned by the group (including the ones with guaranteed debt), debt-free status achieved by some rigs and management's stated stance to provide only limited and need-based support to the rig entities in the group provided comfort. However, with the charter for the acquired rig set to expire in March 2021, MSL's acquisition has exposed it to a lease renewal risk. The company's inability to re-deploy the rig in a timely manner and at favourable terms could potentially affect its debt coverage indicators after the expiry of the existing charter in March 2021. The risk is heightened by the increasingly uncertain oil price environment.

Sizeable investment portfolio - MSL has a sizeable investment portfolio (including amount extended as loans and advances), which stood at ~Rs. 1,600 crore as on March 31, 2019, equivalent to ~37% of its capital employed. Besides the Rs. 477 crore invested in USTPL, these mainly comprise investments made in international group entities owning offshore drilling rigs and mining assets. With most of these investments yet to generate any returns (investment in an international mining asset was partially impaired in FY2019) for MSL, its return metrics remain moderate, as reflected in a return on capital employed (ROCE) of ~11% in FY2019. In comparison, MSL's ROCE from its core operations was healthy at 28.3% in FY2019.

Vulnerability to cyclicality associated with the oil and gas industry, besides its exposure to volatility in input prices – MSL's profitability remains exposed to volatility in input prices due to the fixed-price nature of its contracts and lack of backward integration; although the company takes orders with short tenure and stocks raw material inventory to mitigate the risk. Further, most of the demand for seamless pipes comes from exploration and production (E&P) activities in the oil and gas sector, which is cyclical in nature and depends on oil prices. The company's exposure to cyclicality in the oil and gas sector stands increased with its recent acquisition of an oil drilling rig from SDPL. With limited remaining tenure of the rig's lease charter (valid till March 2021) and sizeable debt assumed by the company for the acquisition, the company's inability to re-deploy the rig in a timely manner and at favourable terms if the weakness in oil prices is prolonged, could potentially moderate its debt coverage indicators after the expiry of the existing charter in March 2021.

Risk appetite for inorganic growth opportunities – MSL has a track record of inorganic growth, through acquisitions in the pipes as well as other segments, such as mines and oil rigs. The most recent investments by the company was towards the acquisition of USTPL, previously a joint venture between the Hyderabad-based Kamineni Group and the Malaysian UMW Group, under CIRP, and an oil rig from its associate company, SDPL. While the acquisition cost of ~Rs. 477 crore for USTPL's installed seamless pipe capacity of 350,000 tonne per annum appears prudent, MSL's consolidated indebtedness increased as it availed a long-term debt of Rs. 375 crore for part funding the acquisition during FY2019, besides using its internal accruals. Although the clarity on purchase consideration has emerged with the announcement of the Supreme Court's verdict, turnaround of USTPL's operations remains to be seen. Further, the debt of ~Rs. 370 crore availed for rig acquisition has also increased the debt outstanding on MSL's books, while resulting in a corresponding decline in the guaranteed debt.

Liquidity position: Adequate

MSL has an **adequate** liquidity profile. Although the liquidity position moderated during FY2019 (free cash and liquid investments declined to Rs. 153.2 crore as on March 31, 2019 from Rs. 194.2 crore as on March 31, 2018) due to part funding of USTPL's acquisition cost and extension of funding support to group entities from internal accruals, it improved subsequently supported by surplus cash flow generation, improvement in working capital cycle and tax benefit availed on depreciation on acquired rig (free cash and liquid investments stood at ~Rs. 500-550 crore as on March 31, 2020).

ICRA expects the company's liquidity position to remain comfortable, supported by its portfolio of liquid investments, healthy surplus cash flow generation from the core businesses as well as expected reduction in incremental financial support to group companies.

Rating sensitivities

Positive triggers – Given the negative outlook, a rating upgrade in the near term looks less likely. However, there could be a revision in outlook or a revision in the long-term rating if the company sustains a healthy growth in its scale of operations while maintaining robust profitability and diversifying across segments, hence strengthening its business risk profile; and achieves a material and healthy improvement in its return metrics.

Negative triggers – The ratings could be downgraded if MSL's operating performance weakens materially, or there is a delay in commencement/ stabilisation of USTPL's operations or inability to re-deploy the acquired rig in a timely manner and at favourable rates because of, reasons including but not limited to, a prolonged weakness in the oil and gas sector's operating environment and lockdown because of COVID-19, which affects company's coverage metrics. Additionally, negative triggers for the ratings would include aggressive investments/ acquisitions (debt-funded or otherwise) or a significant stretch in the working capital cycle, which weakens the company's liquidity profile and/or results in an increase in its leverage. Specific metric that could trigger a downgrade include the company's inability to improve (consol. net debt + guaranteed debt)/ OPBIDTA to less than 2.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	The ratings factor in the financial flexibility as part of the established D. P. Jindal Group
Consolidation/Standalone	The ratings are based on the consolidated operational and financial profile of the company. In addition, the ratings factor in the explicit credit support extended by MSL to some group companies in the form of Corporate Guarantees and stand-by letter of credits (SBLCs).

About the company

Incorporated in 1988, MSL is part of the D. P. Jindal Group, which also includes Jindal Pipes Limited[3] and Jindal Drilling & Industries Limited. The company primarily manufactures seamless pipes with an installed production capacity of 550,000 TPA and ERW pipes with an installed capacity of 200,000 TPA across its manufacturing facilities at Raigad in Maharashtra. It enjoys market leadership in the domestic seamless pipes market and has the capacity to manufacture seamless pipes with outside diameter (OD) of up to 20 inches.

Apart from the seamless and ERW pipes business, MSL has developed a renewable power portfolio aggregating to 47 MW capacity across Maharashtra and Rajasthan and is in the process of installing a 21-MW solar power plant for its captive consumption in Maharashtra. It has also floated subsidiaries and invested in associate companies with business interests in developing jack-up rigs and iron ore mines.

[3] *ICRA has [ICRA]A+ (Stable)/ MA+ (Stable)/ [ICRA]A1+ ratings outstanding for bank facilities of Jindal Pipes Limited. The rating for its fixed deposit programme has been placed on six-month notice of withdrawal. For detailed rating rationale on the company, please refer to ICRA's website: www.icra.in.*

Further, MSL has also acquired USTPL for a consideration of Rs. 477 crore, under the Insolvency and Bankruptcy Code (IBC) proceedings. The Telangana-based USTPL has a seamless pipe manufacturing capacity of 350,000 TPA.

Key financial indicators (Consolidated- audited)

	FY2018	FY2019
Operating Income (OI) (Rs. crore)	2,149.7	3,072.7
Profit after tax (PAT) (Rs. crore)	166.2	177.4
OPBDIT/OI (%)	14.5%	21.8%
RoCE (%)	8.3%	11.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.6
Total Debt/OPBDIT (times)	2.0	1.6
Interest Coverage (times)	7.5	17.2
DSCR	2.8	4.6

Source: MSL's Annual Reports and ICRA research

Note: OPBDIT: Operating profit before depreciation, interest and tax; ROCE: Return on capital employed; DSCR: Debt service coverage ratio

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019		FY2018
					24-Apr-20	07-Jan-20	29-Mar-2019	24-Sep-2018	3-Jul-2017
1	Cash Credit	Long Term	15.0	-	[ICRA]AA-(Negative)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)
2	Term Loan	Long Term	66.0	66.0	[ICRA]AA-(Negative)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)
3	Short-term Loan/ Bill Discounting Facilities	Short Term	45.0	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-	-
4	Letter of Credit/ Buyer's Credit/ Bank Guarantee	Long Term/ Short Term	974.0	-	[ICRA]AA-(Negative)/ A1+	[ICRA]AA-(Stable)/ A1+	[ICRA]AA-(Stable)/ A1+	[ICRA]AA-(Stable)/ A1+	[ICRA]AA-(Stable)/ A1+
5	Unallocated	Long Term/ Short Term	-	-	-	-	[ICRA]AA-(Stable)/ A1+	[ICRA]AA-(Stable)/ A1+	[ICRA]AA-(Stable)/ A1+
6	Issuer Rating	Long Term	-	-	[ICRA]AA-(Negative)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)^	IrAA-(Stable)

Amounts in Rs. crore

^ With effect from September 1, 2017, ICRA aligned the symbols and the definitions of ratings pertaining to the Issuer Rating Scale with that of the Long-Term Rating Scale. The change in the symbol is not to be construed as a change in the credit rating.

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 click here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance/ Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit	NA	NA	NA	15.0	[ICRA]AA- (Negative)
NA	Term Loan	FY2019	NA	FY2022	66.0	[ICRA]AA- (Negative)
NA	Short-term Loan/ Bill Discounting Facilities	NA	NA	NA	45.0	[ICRA]A1+
NA	Letter of Credit/ Buyer's Credit/ Bank Guarantee	NA	NA	NA	974.0	[ICRA]AA- (Negative)/ [ICRA]A1+
NA	Issuer Rating	NA	NA	NA	-	[ICRA]AA- (Negative)

Source: MSL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Maharashtra Seamless (Singapore) Pte. Ltd.	100% owned by MSL	Full Consolidation
Maharashtra Seamless Finance Ltd.	100% owned by MSL	Full Consolidation
Discovery Oil And Mines Pte. Ltd.	100% owned by MSL	Full Consolidation
Jindal Premium Connections Pvt. Ltd.	100% owned by MSL	Full Consolidation
Internovia Natural Resources FZ LLC	56% owned by MSL	Full Consolidation
Zircon Drilling Supplies And Trading FZE	100% owned by MSL	Full Consolidation
Jindal Pipes (Singapore) Pte. Ltd.	30% owned by MSL and 70% owned by JPL	Equity method
Star Drilling Pte. Ltd.	25% owned by MSL	Equity method
Dev Drilling Pte. Ltd.	25% owned by MSL	Equity method
Gondkhari Coal Mining Ltd.	30.3% owned by MSL	Equity method

Source: MSL's Annual Report, ICRA research

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