

January 07, 2020

## Mahadev Ship Breakers Private Limited: Ratings reaffirmed; rated amount enhanced

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Cash Credit	6.00	-	-
Long term interchangeable – Cash Credit <sup>^</sup>	-	(9.00)	[ICRA]BB (Stable); Reaffirmed
Non-fund Based Letter of Credit	39.00	60.00	[ICRA]A4+; Reaffirmed
Non-fund Based Credit Exposure Limit	0.90	1.20	[ICRA]A4+; Reaffirmed
Unallocated Limits	5.10	-	-
<b>Total</b>	<b>51.00</b>	<b>61.20</b>	

\*Instrument details are provided in Annexure-1

<sup>^</sup>Sublimit of Letter of Credit

### Rationale

The reaffirmation of ratings factors in Mahadev Ship Breakers Private Limited's (MSBPL) moderate scale of operations and high dependence on letter of credit (LC) backed purchases. This dependence resulted in moderately high TOL/TNW of 1.89 times as on March 31, 2019. The ratings factor in the vulnerability of its profitability to fluctuations in steel scrap prices and foreign exchange rates, along with the exposure of its revenues to the cyclicity inherent in the ship breaking industry. ICRA notes that the company is exposed to intense competition from players operating in and around Alang, along with international competitors.

The ratings, however, favourably factor in the partners' extensive experience in the ship breaking industry, comfortable coverage indicators and the efficient management of LC maturity funding.

The Stable outlook on the [ICRA]BB rating reflects ICRA's opinion that MSBPL will continue to benefit from the extensive experience of its promoters in the ship breaking industry.

### Key rating drivers and their description

#### Credit strengths

**Extensive experience of promoters in ship breaking industry** – MSBPL has been involved in the ship breaking business since 2006. The key promoter, Mr. Ramesh Mendapara, has more than two decades of experience in the ship breaking industry.

**Comfortable coverage indicators and adequate liquidity** – MSBPL's coverage indicators remain comfortable, as reflected by interest coverage of 3.27 times in FY2019. Further, the liquidity remains adequate with build-up of fixed deposit to service the maturing letter of credit.

#### Credit challenges

**Moderate scale operation; revenue vulnerable to cyclicity inherent in industry** – The company's scale of operation remains moderate with an operating income (OI) of Rs. 52.27 crore in FY2019 versus Rs. 42.17 crore in FY2018. Ship procurement depends on the current trends in the ship breaking industry and the international economic situation, which affect its revenues and thus the profit margins. MSBPL's OI significantly declined in the current fiscal as reflected in sales of ~Rs. 9.46 crore in 8M FY2020 (provisional figures), due to no ship procurement during the period following considerable decline in steel scrap prices (realisations) and adverse fluctuation in forex rates leading to high procurement cost. Further, it is exposed to regulatory risks pertaining to environmental and human right-related issues.

**High reliance on LC-backed purchase** – Ship purchases are entirely backed by letter of credit facilities, resulting in the company’s high dependence on LC-backed purchasing. The TOL/TNW remained moderately high at 1.89 times for FY2019, although it improved from 2.12 times for FY2018.

**Profitability susceptible to fluctuations in foreign currency exchange rate** – The company purchases ships in foreign currency under an LC arrangement, where the usance period is around 90 to 270 days. Since ship breaking entities usually have a long payment period on LC-backed purchases, any depreciation in rupee increases the amount payable to honour the same LC. Thus, the company’s profitability is exposed to adverse movements in the forex currency rates. However, the forex risk is mitigated by parallel hedging of foreign exposure.

**Vulnerability of margins to steel price fluctuations and intense competition** – It takes around five to six months on an average to completely dismantle a ship and generate revenues. Hence, MSBPL faces an inventory risk for ships that are under the process of breaking due to the time lag involved between the ship’s purchase and the sale of scrap, given the high volatility faced in steel prices. However, if steel prices rise, the company is likely to gain from the inventory (vessel) purchased at lower rates. Its revenue and profitability are exposed to intense competition from numerous players operating in Alang, apart from competition from players in Bangladesh and Pakistan.

### Liquidity position: Adequate

The company’s liquidity profile remains adequate, characterised by comfortable surplus available in the form of fixed deposit to service maturing letter of credit. Moreover, it derives comfort from absence of fixed repayment obligations and cushion in the working capital limits. The average utilisation of the fund-based working capital limits remained low at ~4% in the 15-month period from September 2018 to November 2019.

### Rating sensitivities

**Positive triggers** – The ratings might be upgraded if a significant scale up of operations, coupled with sustenance of higher margins lead to an improvement in its financial risk profile.

**Negative triggers** – Lower-than-anticipated cash accruals for servicing maturing LC payment may trigger a rating downgrade.

### Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company.

### About the company

Established in 2006, MSBPL is a private limited company involved in the business of ship breaking. It has an office at Bhavnagar, Gujarat, and its ship breaking yard is at Alang, in Gujarat. At present, MSBPL has leased a plot at the Sosiyo ship breaking yard at Bhavnagar.

In FY2019, the company reported a net profit of Rs. 0.63 crore on an OI of Rs. 52.27 crore compared to a net profit of Rs. 0.62 crore on an OI of Rs. 42.17 crore in the previous year.

## Key financial indicators (Audited)

	FY2018	FY2019
Operating Income (Rs. crore)	42.17	52.27
PAT (Rs. crore)	0.62	0.63
OPBDIT/ OI (%)	0.93%	2.09%
RoCE (%)	13.57%	13.09%
Total Outside Liabilities/Tangible Net Worth (times)	2.12	1.89
Total Debt/OPBDIT (times)	0.00	0.00
Interest Coverage (times)	1.20	3.27
DSCR	3.58	3.39

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding as on March 31, 2019	Rating	FY2019	FY2018	FY2017
					07-Jan-2020	18-Feb-2019	20-Dec-2017	10-Oct-2016
1	Cash Credit	Long Term	-	-	-	[ICRA]BB (Stable)	[ICRA]BB (Stable)	[ICRA]BB-(Stable)
2	Interchangeable – Cash Credit <sup>^</sup>	Long Term	(9.00)	-	[ICRA]BB (Stable)	-	-	-
3	Letter of Credit	Short Term	60.00	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4
4	Credit Exposure Limit	Short Term	1.20	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A4
5	Unallocated Limits	Long Term/Short Term	-	-	-	[ICRA]BB (Stable)/ [ICRA]A4+	[ICRA]BB (Stable)/ [ICRA]A4+	[ICRA]BB-(Stable)/ [ICRA]A4

<sup>^</sup>Sublimit of Letter of Credit  
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](http://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	Interchangeable – Cash Credit <sup>^</sup>	NA	NA	NA	(9.00)	[ICRA]BB (Stable)
NA	Letter of Credit	NA	NA	NA	60.00	[ICRA]A4+
NA	Credit Exposure Limit	NA	NA	NA	1.20	[ICRA]A4+

<sup>^</sup>Sublimit of Letter of Credit

Source: Mahadev Ship Breakers Private Limited

## ANALYST CONTACTS

**K. Ravichandran**  
+91 44 4596 4301  
[k.ravichandran@icraindia.com](mailto:k.ravichandran@icraindia.com)

**Suprio Banerjee**  
+91 22 6114 3443  
[supriob@icraindia.com](mailto:supriob@icraindia.com)

**Sanket Thakkar**  
+91 79 4027 1528  
[sanket.thakkar@icraindia.com](mailto:sanket.thakkar@icraindia.com)

**Jaimin Patel**  
+91 79 4027 1550  
[jaimin.patel@icraindia.com](mailto:jaimin.patel@icraindia.com)

## RELATIONSHIP CONTACT

**Jayanta Chatterjee**  
+91 80 4332 6401  
[jayantac@icraindia.com](mailto:jayantac@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**  
Tel: +91 124 4545 860  
[communications@icraindia.com](mailto:communications@icraindia.com)

### Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

[info@icraindia.com](mailto:info@icraindia.com)

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## ICRA Limited

### Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: [info@icraindia.com](mailto:info@icraindia.com)

Website: [www.icra.in](http://www.icra.in)

### Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

### Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 2556 0194/ 6606 9999

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