

Infomerics Valuation And Rating Pvt. Ltd.

Press Release

VRKP Steel Industries Pvt Ltd

December 23, 2019

Rating

Instrument / Facility	Amount	Rating	Rating Action
Issuer Rating	NA	IVR BBB-[Is] / Stable (IVR Triple B minus [Is] with Stable Outlook)	Revised from IVR BB+ [Is] /Stable (IVR Double B Plus [Is] with Stable Outlook)

Detailed Rationale

The revision in the issuer rating of VRKP Steel Industries Pvt Ltd (VRKP) takes into account the improvement in its scale of operation, profitability, comfortable capital structure and debt protection metrics during FY19, coupled with improvement in H1FY20 working results. Moreover, the aforesaid rating continue to derive comfort from its experienced promoter with long track record, established brand, strategic location of plant with backward integration initiatives, improvement in financial performance in FY19, satisfactory gearing and debt protection metrics and satisfactory working capital management. However, rating strengths are constrained by its thin profitability, volatility in the prices of raw materials and finished goods, geographical concentration risk, high competition and cyclical in the steel industry.

Key Rating Sensitivities

Upward factors

- Significant growth in scale of business with improvement in profitability metrics thereby leading to overall improvement in cash accruals
- Significant improvement in debt protection metrics

Downward Factors

- Dip in operating income or profitability impacting the debt coverage indicators, subdued industry scenario, deterioration in working capital management and moderation in overall gearing to more than 1.5 times could lead to a negative rating action.

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List of Key Rating Drivers with Detailed Description

Key Rating Strengths

Experienced promoter with long track record

VRKP was promoted by one Mr. Vinod Kumar Agarwal in the year 2001. Mr. Agarwal has more than three decades of experience in the iron and steel industry. Over the years of its operation, the company has established its presence in Thermo Mechanically Treated (TMT) bars manufacturing segment in the state of Karnataka. Currently, Mr. Agarwal (Managing Director) is at the helm of affairs of the company.

Established Brand

The company markets its TMT bars under the brand name “VRKP TMT”. VRKP has been able to establish its brand over the course of more than one and a half decade with a focussed advertising campaign to raise brand awareness and recall. VRKP has a direct sales team to penetrate in the market.

Strategic location of plant with backward integration initiatives

The manufacturing facility of VRKP is located within a distance of 10 km from Bangalore city which is its major catchment area. Further, the plant is very well connected with other nearby places through roadways. Agarwal Induction Furnace Pvt Ltd and VRKP Sponge and Power Plant LLP are its group companies and both are mainly part of VRKP group’s backward integration initiative. VSPL is at the lowest end of the value chain. It manufactures sponge iron and then sells the same to AIFPL which is the middle of the value chain and manufacture billets and supply the same to VRKP. AIFPL meets almost 80% of VRKP’s requirement and the balance is procured from other suppliers.

Improvement in financial performance in FY19

The company achieved a y-o-y growth of ~33% in FY19 driven by improved demand from Bangalore real estate market leading to increase in sales volume and realisations. Improvement in sales realisations coupled with higher absorption of fixed overheads driven by improvement in capacity utilisations (from ~73% in FY18 to ~87% in FY19) led to improvement in absolute EBITDA (from Rs.2.50 crore in FY18 to Rs.8.89 crore in FY19) and EBITDA margin (1.16% in FY18 to 3.04% in FY19) in FY19. Driven by improvement in absolute EBITDA, PAT level and PAT margin also improved during the fiscal and the

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company has earned a cash accrual of Rs.5.67 crore in FY19 as compared to Rs.1.84 crore in FY18.

Satisfactory gearing and debt protection metrics

The capital structure of the company is comfortable, marked by its below unity debt-equity ratio and overall gearing ratio. Total indebtedness of the company as reflected by the TOL/TNW remained comfortable at 2.36x as on March 31, 2019 (2.05x as on March 31, 2018). The debt protection metrics for the company also remained comfortable in FY19, with improvement in the interest coverage ratio from 3.04x in FY18 to 6.30x in FY19 and Total Debt to Gross Cash Accruals from 5.9 years in FY18 to 1.98 years in FY19.

Satisfactory working capital management

The company has prudently managed its working capital requirements and maintained its working capital cycle around 30 days over the past periods. Further, the average utilisation of its working capital also remained satisfactory at about ~65% during the past 12 months ended November, 2019.

Key Rating Weaknesses

Thin profitability

The profit margins of the company though improved in FY19 continues to remain thin. Thin profitability is attributable to commoditized nature of its products with minimal product differentiation and intense competition in the operating spectrum. However, in FY19, the company witnessed a steady improvement in its cash accruals.

Volatility in the prices of raw materials and finished goods

The price of steel has seen a lot of volatility over the last three years. The price of sponge iron/billets which is one of the main raw materials required for VRKP fell by around 2% in FY17 as compared to FY16, but increased by around 24% in FY18, which has again declined by around 18% during November 2019 vis-à-vis November 2018. Similarly, the price realisation for TMT bars also witnessed a volatility in the recent past. The costs of raw materials and finished goods are volatile in nature and hence, VRKP's profitability is susceptible to fluctuation in the prices of its raw material prices and/or its finished goods.

Geographical concentration risk

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VRKP mainly caters to the state of Karnataka which contributed more than 90% of its sales in FY19. Hence, the company is exposed to geographical concentration risk. However, the company has begun efforts to strengthen its brand presence and grow its sales in nearby markets.

High competition and cyclicity in the steel industry

VRKP mainly operates in the State of Karnataka and faces stiff competition from not only established players, but also from the unorganised sector due to low level of product differentiation. Further, the steel industry is also cyclical in nature and witnessed prolonged periods where it faced a downturn due to excess capacity leading to a downtrend in the prices.

Analytical Approach: Standalone

Applicable Criteria:

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation (Non-financial Sector)

Group Support

Liquidity – Adequate

VRKP has adequate liquidity marked by its healthy cash accruals against negligible repayment obligations along with adequate cushion from unutilised bank limits. The company has projected to earn cash accruals of Rs.7.45 crore as against its repayment obligation of Rs.0.22 crore in FY20. Further, the company has no planned capex or avilment of long-term debt and has sufficient gearing headroom due to its comfortable capital structure. Average cash credit utilisation of the company remained comfortable at ~64% during the past 12 months ended November, 2019 indicating an adequate liquidity cushion.

About the Company

Incorporated in December 12, 2001, Bangalore based VRKP Steel Industries Pvt Ltd (VRKP) was promoted by one Mr. Vinod Kumar Agarwal. VRKP is engaged in manufacturing of Thermo Mechanically Treated (TMT) bars of different sizes (ranging from 8mm to 36mm) and length. The manufacturing facility of the company is located at Bangalore with an

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installed capacity of 84,000 MTPA. The company sells its TMT bars under the brand name, 'VRKP TMT' and mostly operates in the state of Karnataka through its direct sales team. VRKP is the flagship company of VRKP group formed by Mr. Vinod Kumar Agarwal having major interest in the steel industry through its various companies. The other major companies/firms of the promoters are, Agarwal Induction Furnace Pvt Ltd (AIFPL, incorporated in 2008, rated: IVR BBB-; Stable/A3) engaged in manufacturing of Steel Billets and VRKP Sponge and Power Plant LLP (VSPL) engaged in manufacturing of sponge iron, billets, TMT bar with a captive 10MW power plant.

Financials (Standalone): The financials for FY18 & FY19 is furnished below: (Rs. crore)

For the year ended* / As On	31-03-2018	31-03-2019
	Audited	Audited
Total Operating Income	214.45	285.94
EBIDTA	2.50	8.69
PAT	0.23	4.21
Total Debt	11.02	11.21
Tangible Net worth	13.19	17.40
EBIDTA Margin (%)	1.16	3.04
PAT Margin (%)	0.11	1.47
Overall Gearing Ratio (x)	0.84	0.64

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Nil

Rating History for last three years:

Sr. No.	Name of Instrument/Facilities	Current Rating (Year 2019-20)			Rating History for the past 3 years		
		Type	Amount outstanding (Rs. Crore)	Rating	Date(s) & Rating(s) assigned in 2018-19	Date(s) & Rating(s) assigned in 2017-18	Date(s) & Rating(s) assigned in 2016-17
1.	Issuer Rating	Issuer	NA	IVR BBB-[Is] / Stable	IVR BB+ [Is] / Stable	-	-

Note on complexity levels of the rated instrument: Infomerics has classified instruments rated by it on the basis of complexity and a note thereon is available at www.infomerics.com.

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About Infomerics:

Infomerics commenced rating & grading operations in April 2015 after having spent over 25 years in various segments of financial services. Infomerics is registered with the Securities and Exchange Board of India (SEBI) and accredited by Reserve Bank of India. It is gradually gaining prominence in domestic rating and/or grading space. Infomerics is striving for positioning itself as the most trusted & credible rating agency in the country and is gradually widening its product portfolio. Company's long experience in varied spectrum of financial services is helping it to fine tune its product offerings to best suit the market.

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Annexure 1: Details of Facilities

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility (Rs. Crore)	Rating Assigned/ Outlook
Issuer Rating	-	-	-	NA	IVR BBB-[Is] / Stable