Press Release

Electrosteel Castings Limited

April 20, 2018

Ratings

Instrument / Facility	Amount (Rs. Crore)	Ratings	Rating Action
Non-Convertible Debentures (Series VI)	125	IVR A /Stable Outlook (IVR Single A with Stable Outlook)	Reaffirmed
Non-Convertible Debentures (Series VII)	75	IVR A /Stable Outlook (IVR Single A with Stable Outlook)	Reaffirmed
Total	**200**		

Details of Facilities are in Annexure 1

Detailed Rationale

The aforesaid ratings continue to derive comfort from Electrosteel Castings Limited's (ECL) long track record of operation with leadership position in the domestic Ductile Iron (D.I) pipe segment, operating efficiency due to its fully integrated production facilities with full capacity utilisation, healthy order book position indicating a near term revenue visibility along with the favourable outlook for domestic D.I pipe market. However, the ratings are tempered by volatility in input prices, fluctuation in operating profit margin and uncertainty associated with the receipt of compensation against de-allocation of coal mine. The ratings also consider ECL's moderately leveraged capital structure having a bearing on debt protection parameters, long receivable collection period and sizeable exposure to one of its associate company, Electrosteel Steels Limited (ESL), which is under National Company Law Tribunal (NCLT). Earning modest level of profit, receipt of compensation against the de-allocated coal mine and impact of the outcome of NCLT's order in respect of ESL on ECL are the key rating sensitivities.

List of Key Rating Drivers

- Long track record of operation.
- Leadership position in the domestic D.I pipe segment.
- Operating efficiency due to fully integrated production facilities.
- Full capacity utilisation of the D.I. Pipe plant.
- Healthy order book indicating a near term revenue visibility.

- Favourable outlook for domestic D.I pipe market.
- Volatile input prices.
- Fluctuation in operating profit margin.
- Uncertainty associated with receipt of compensation against de-allocation of coal mine.
- Moderately leveraged capital structure having a bearing on debt protection parameters.
- Long receivable collection period.
- Sizeable exposure to one of its associate company, Electrosteel Steels Limited (ESL) which is under NCLT.

Detailed Description of Key Rating Drivers

Key Rating Strengths

Long track record of operations

ECL, incorporated in 1955 has been managed by the Kejriwal family of Kolkata for over five decades signifying its long & established track record. The company is first to set up a D.I Pipe plant in India.

Leadership position in the domestic D.I pipe segment

ECL is amongst the largest player in the D.I pipe segment of the country. D.I pipe is the major product of the company having contributed ~73% of gross sales in FY17 (FY refer to the period from April 01 to March 31). However, other players, though late entrants in the market, are gaining prominence gradually.

Operating efficiency due to fully integrated production facilities

ECL has fully integrated production facilities comprising Sinter Plant, Coke Oven Plant for production of LAMC for meeting captive requirements, Blast Furnace, Pig Iron Plant, Sponge Iron Plant, Fittings Plant and Captive Power Plant. Integrated production facilities ensure assured supply of inputs and insulate the company from fluctuation in input prices to an extent. The Company has been allotted an iron ore mine in the state of Jharkhand which is pending for execution of mining lease. The Company has already filed a writ petition before the Hon'ble High Court of Jharkhand, praying inter-alia for direction for grant of the said lease in favour of the Company. In September, 2017, the CBI had filled an FIR against the promoter of ECL in connection with the company's receipt of clearance from the Govt. Of India for use of forest land for iron ore mining. Subsequent to the FIR, the CBI conducted search at the offices of ECL and other locations of the promoter. As of now, there has been no further development in the matter.

Full capacity utilisation

The D.I plant of ECL is running at full capacity in FY17 and 9MFY18 (refers to the period from April 01 to December 31) demonstrating good demand of its products.

Healthy order book indicating a near term revenue visibility

ECL has a strong order book position aggregating about Rs.900 crore as on March 23, 2018 which is about 0.5 times of its FY17 standalone revenue (i.e.~Rs.1808.58 crore). The orders are expected to be completed within next 7-8 months, indicating a satisfactory near term revenue visibility.

Favourable outlook for domestic D.I pipe market

Rapid increase in population, urbanisation and industrialisation has led to a significant increase in water requirement, leading to demand overtaking the supply. Increased central government grants under Jawaharlal Nehru National Urban Renewal Mission(JNNURM) scheme, funding from developmental agencies and current Central Government's additional impetus to this sector through the AMRUT (Atal Mission for Rejuvenation and Urban Transformation) scheme are matters for significant comfort for the D.I pipe segment, as the investment in urban water supply and sanitation has increased manifold during the first decade of the 21st century.

Key Rating Weaknesses

Volatile input prices

The costs of raw materials (i.e., coal, iron ore) are the largest component of total cost of sales (accounting for ~49% in FY17).Due to de-allocation of coal mines and delay in clearance of iron ore mine, ECL has to procure raw materials from the open market. It procures coking coal mainly from Australia and iron ore from the domestic market. The prices of these raw materials are volatile in nature and hence, ECL's profitability is susceptible to fluctuation in raw-material prices.

Fluctuation in operating profit margin

Operating margin (as expressed as EBIDTA margin) of ECL has been volatile majorly due to fluctuation in input cost and time lag in passing on input price variation to customers. ECL posted an improvement in EBIDTA margin from 13.8% in FY16 to 16.1% in FY17 despite decline in its total operating income during FY17. The improvement in EBIDTA margin was due to decline in overall input cost (mainly driven by lower iron ore prices). Higher EBIDTA led to increase in PAT level and margin in FY17. In 9MFY18, ECL reported PAT of Rs.24.33 crore on Total Operating Income of Rs.1425.99 crore. During 9MFY18, the bottomline of the company got hit due to subdued performance in the first two quarters on account of sudden spurt in coal prices and fall in export realisation. In the third quarter of FY18, the situation improved significantly enabling the company to earn a modest overall EBIDTA margin of about 12.3% in 9MFY18. Infomerics believes that the improved situation is expected to continue in Q4FY18.

Uncertainty associated with receipt of compensation against de-allocation of coal mine

The Hon’ble Supreme Court had de-allocated many coal blocks in September 2014, including the Parbatpur coal mine which was hitherto allocated to ECL, challenging the reasonableness of the allocation. In terms of the Ordinance, the Company was allowed to continue the operations in the said block till March 31, 2015. Accordingly, the same was handed over to Bharat Coking Coal Limited (BCCL) as per the direction from Coal India Ltd. (CIL) with effect from April 01, 2015 and the same was subsequently allotted to Steel Authority of India Limited (SAIL).All the beneficiaries (including ECL) filed a writ petition in Hon’ble Delhi High Court, for compensation from Government of India. After several hearings, the Hon’ble Delhi High Court pronounced its judgement in March, 2017 in favour of the petitioners (including ECL). Accordingly, based on the said judgement, the Company has claimed Rs.1531.76 crore towards compensation against the said coal block. ECL has already received Rs.83.12 crore till February, 2018 out of its total claim. Based on the subsequent developments including realisation of Rs.83.12 crore, the company strongly believes that it will receive the claim amount; however, there might be some delays.

Long receivable collection period

ECL's average receivable collection period has generally been on the higher side mainly due to supply to government parties (average realisation period is about three months) and export debtors (average realisation period is about five months). However, the credit profile of debtors is generally good and there has not been any issue in collection in the last three years. The average fund based working capital limit utilisation remained satisfactory at about 55% during the past 12 months ended January, 2018 indicating availability of adequate liquidity buffer for the company.

Moderately leveraged capital structure having a bearing on debt protection parameters

The long term debt-equity ratio and overall gearing ratio of the company, on a standalone basis, remained moderate at 0.63x and 1.01x respectively as on March 31, 2017. The debt protection parameters of the company remained moderate with the interest coverage ratio of 1.45x and the long-term debt to GCA of 9.47x in FY17 on a standalone basis in view of high level of interest expenses. However, the company has demonstrated a satisfactory debt servicing track record over the years.

Sizeable exposure to one of its associate companies, Electrosteel Steels Ltd. (ESL) which is under NCLT

ECL has an outstanding financial exposure of Rs.842.03 crore in ESL (as on December 31, 2017) which has been yielding zero return. ESL, one of the major associate companies of ECL, commissioning a large integrated steel and D.I Pipe project and a 120 MW captive power project at Jharkhand, has been facing many challenges from the project implementation stage owing to delays in project commissioning and bearish steel industry scenario. The project is still to be implemented fully, although a significant part of the capacity has already been on stream. Owing to delay in project implementation, the company went into CDR and the lenders had finally invoked the SDR in 2015. ESL is under NCLT and in April 2018, NCLT has approved the terms of the Resolution Plan submitted by Vedanta to acquire ESL, under Insolvency and Bankruptcy Code 2016. Post implementation of NCLT's final decision, ESL will not be a part of the Electrosteel group. While this is likely to adversely affect the net worth of ECL, the Electrosteel group shall have smooth liquidity comfort on the back of ECL's moderate cash accruals and strong cash accruals of its other group company, Srikalahasthi Pipes Ltd.

Analytical Approach & **Applicable Criteria:**

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation (Non-financial Sector)

About the Company

ECL incorporated under the name “Dalmia Iron and Steel Limited” in November, 1955 currently belongs to Shri G. Kejriwal and his family based in Kolkata. ECL commenced its manufacturing activity in May, 1959 with the commissioning of Cast Iron (CI) pipes manufacturing unit. Although, the company started operations with manufacturing of C.I pipes, ECL over the years diversified into production of ductile iron (D.I) pipes and increased the capacity in both the segments through acquisitions and/or setting up greenfield units. Currently, ECL manufactures D.I pipes, C.I pipes and D.I fittings, besides producing pig iron and low ash metallurgical coke (LAMC) majorly for captive consumption with D.I pipes and fittings being the major products. The company has three manufacturing units - two in West Bengal and one in Tamil Nadu. ECL is one of the largest players in the DI Pipe industry with aggregate manufacturing capacity being 2.8 lakh tones, which is being operated at full capacity. The company also has its co-generation power plants at each location.

Financials (Standalone):

(Rs. crore)

For the year ended* / As On	**31-03-2016**	**31-03-2017**
	Audited	**Audited**
Total Operating Income	1984.75	1808.58
EBITDA	273.84	291.20
PAT	55.87	77.28
Total Debt ^	2253.18	2128.43
Tangible Net worth	2022.08	2099.00
EBITDA Margin (%)	13.80	16.10
PAT Margin (%)	2.77	4.09
Overall Gearing Ratio (x)	1.11	1.01

^includes interest bearing advances

*Classification as per Infomerics’ standards.

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 2017-18)			Rating History for the past 3 years		
		Type	Amount outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2016-17	Date(s) & Rating(s) assigned in 2015-16	Date(s) & Rating(s) assigned in 2014-15
1.	Non-Convertible Debentures(Series VI)	Long Term	125	IVR A /Stable Outlook (IVR Single A with Stable Outlook)	March 21, 2017 IVR A /Stable Outlook (IVR Single A with Stable Outlook)	NA	NA
2.	Non-Convertible Debentures(Series VII)	Long Term	75	IVR A /Stable Outlook (IVR Single A with Stable Outlook)	IVR A /Stable Outlook (IVR Single A with Stable Outlook)		

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.

Annexure 1: Details of Facilities

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility (Rs. Crore)	Rating Assigned/ Outlook
Non-Convertible Debentures(Series VI)	March 7, 2017	11.75%	March 06,2023	125	IVR A /Stable Outlook (IVR Single A with Stable Outlook)
Non-Convertible Debentures (Series VII)	March 7, 2017	12%	March 06,2023	75	IVR A /Stable Outlook (IVR Single A with Stable Outlook)