

Infomerics Valuation And Rating Pvt. Ltd.

Press Release

MB Sponge and Power Limited

September 3, 2019

Rating

Instrument / Facility	Amount (Rs. crore)	Rating	Rating Action
Long Term Bank Facilities	11.20	IVR BB+ /Positive (IVR Double B Plus with Positive Outlook)	Assigned
Short Term Bank Facilities	6.10	IVR A4+ (IVR A Four Plus)	Assigned
Total	17.30		

Details of Facilities are in Annexure 1

Detailed Rationale

The rating assigned to the bank facilities of MB Sponge & Power Limited (MBSPL) derive comfort from its experienced promoters, strategic location of the plant, healthy capacity utilization with sustained growth in scale of operation and stable earning. Further, the ratings also consider its comfortable gearing and debt protection parameters with low near-term debt repayment obligations. However, the rating strengths are partially offset by its small scale of operations, high exposure to group companies, lack of adequate backward integration vis-à-vis volatility in prices, working capital intensive nature of operations, highly competitive & fragmented nature of industry and cyclical nature in the steel industry. The outlook is positive as the company is expected to expand its scale of operations and improvement in margins. Growth in operations with improvement in profit margin, sustenance of capital structure outlook of the steel industry effective working capital management are the key rating sensitivities.

List of Key Rating Drivers with detailed description

Key Rating Strengths

Experienced promoters

The promoters have long-standing experience in production and selling of Iron & Steel products such as Sponge Iron, Pig Iron, M.S. Ingot, M.S. Billet, Silico Manganese, Ferro Alloys, Heavy Structural Item, Light Structural Item, TMT Bar etc. through various companies. Currently, the day to day affairs of the company is managed by Mr. Rohit Agarwal, CEO, second generation entrepreneur having an experience of more than 10 years.

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Strategic location of the plant

MBSPL's manufacturing facility is located at Durgapur industrial belt in Burdwan district of West Bengal, which is in close proximity to coal mine of Eastern Coalfield Ltd, Raniganj (W.B.); from where MBSPL procures coal. Further, iron-ore (the main raw material for the company) rich states of Jharkhand and Orissa are also located nearby. Besides, Durgapur being an industrial belt has end market for its sponge iron. Moreover, the plant is well connected through road and rail transport which facilitates easy transportation of raw materials and finished goods. Hence, the plant enjoys competitive advantages in terms of containment of transportation costs and ready market.

Healthy capacity utilisation

MBSPL was operated at a healthy capacity of ~86% in FY19 improved from ~70% capacity utilisation in FY18 driven by improvement in steel products.

Sustained growth in scale of operation with stable earning

The total operating income of the company grew at a CAGR of ~39% during FY17-FY19 with a y-o-y growth of ~54%. The growth is fuelled by enhanced capacity utilization and better sales realisations driven by improvement in the steel sector. However, the operating margin of the company remained range-bound over the past years (FY17-FY19) in the range of 5-6% whereas the absolute EBIDTA has increased from Rs.3.73 crore in FY17 to Rs.6.22 crore in FY19. Improvement in absolute EBIDTA coupled with decline in interest outgo led to improvement in the PAT margin from 1.70% in FY17 and 3.63% in FY19.

Comfortable gearing and debt protection matrices with low near-term debt repayment obligations

The company has a comfortable capital structure over the years. The long-term debt equity ratio and overall gearing remained comfortable at 0.15x and 0.59x as on March 31, 2019 (0.12x and 0.62x in March 31, 2018). However, the company has a comfortable debt protection metrics and its debt protection parameters marked by the interest coverage remained comfortable at 3.63x and Total debt/GCA remained moderate at 4.79x respectively in FY19. Further, the total indebtedness of the company as reflected by the Total Outside Liabilities/Tangible Net worth remained satisfactory at 1.34x s on March 31,2019.

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Key Rating Weaknesses

Small scale of operation

The scale of operation of the company though improved considerably continued to remain small with a PAT of Rs.4.06 crore on a total operating income of Rs.110.27 crore in FY19. Small scale of operations restricts the financial flexibility of the company.

High exposure to a group company

The company has more than six months outstanding debtors aggregating to Rs.16.10 crore to be receive from its group companies. Adjusting the same from the net worth, the long-term debt equity ratio and overall gearing remained moderate at 0.32x and 1.29x as on March 31, 2019. Further, the TOL/ Adjusted TNW of the company also stood moderate at 4.10x as on March 31, 2019 after adjusting its exposure to group companies.

Lack of adequate backward integration vis-à-vis volatility in prices

The degree of backward integration defines the ability to minimize price volatility risk and ability to resist cyclical downturns generally witnessed in the steel industry. MBSPL does not have any backward integration for its raw materials and procures the same from outside, exposing the company to price volatility risk. The price of iron ore/pellet and coal are volatile in nature and the same exposes the company to input price fluctuation risk for its entire requirement.

Highly competitive & fragmented nature of industry

The spectrum of the steel industry in which the company operates is highly fragmented and competitive due to presence of numerous players in India owing to relatively low entry barriers. Hence, the players in the industry do not have pricing power and are exposed to the prices fixed by the industry giants. Further, the company derive around 64% of its sales in FY19 from its top ten customers, indicating a moderately concentrated customer base.

Working capital intensive nature of operations

The operations of the MBPL are working capital intensive as the company needs to procure its main raw materials i.e. iron ore and coal mostly on advance basis or with minimum credit period and on the other hand has to extend higher credit period to its customers due to high competition in the industry. Besides, it also needs to maintain raw material inventory (mainly

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iron ore) for uninterrupted production. The average utilisation of its working capital limit of MBSPL remained satisfactory at about 80% during the past 12 months ended on July, 2019.

Cyclicality in the steel industry

The steel industry is sensitive to the business cycles, including changes in the general economy, interest rates and seasonal changes in the demand and supply conditions in the market. Furthermore, the producers of steel & related products are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility of the steel industry.

Analytical Approach: Standalone

Applicable Criteria

Rating Methodology for Manufacturing Companies

Financial Ratios and Interpretation (Non-financial sector)

Liquidity

MBSPL's liquidity profile is expected to remain adequate marked by its healthy cash accruals vis a- vis its debt repayment obligations of Rs.0.41 crore in next three years with no near-term debt funded capex plan. The average cash credit utilisation of the company remained at ~80% during the past 12 months ended July, 2019 indicating a moderate liquidity cushion. However, the company a free cash and bank balance of Rs.3.56 crore as on March 31, 2019.

About the Company

MB Sponge & Power Limited (MBSPL), incorporated in September 2004, is engaged in the manufacturing of Sponge Iron, located at Burdwan, with a current installed capacity of 60,000 metric tonne per annum (MTPA), belongs to the one Agarwal family based out of Bardhaman, West Bengal with Mr. Shankarlal Agarwal being the main promoter. The Agarwal family is actively involved in the steel sector from last 30 years through various companies under its fold. All the Promoters and Directors of MBSPL are fully equipped with the knowledge of Iron & Steel Industry and in the activity since 1993.

Financials (Standalone):

	(Rs. crore)	
For the year ended* / As On	31-03-2018	31-03-2019
	Audited	Audited
Total Operating Income	71.43	110.27
EBITDA	4.03	6.22
PAT	2.91	4.06

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For the year ended* / As On	31-03-2018	31-03-2019
Total Debt	15.71	17.26
Tangible Net worth	25.33	29.40
EBITDA Margin (%)	5.65	5.64
PAT Margin (%)	3.95	3.68
Overall Gearing Ratio (x)	0.62	0.59

*Classification as per Infomerics' standards.

Status of non-cooperation with previous CRA: CARE Ratings has moved the rating of MBSPL into the Issuer Non-Cooperating category as the company did not co-operate in the rating procedure despite repeated follow ups as per the Press Release dated February 27, 2019.

India Ratings has moved the rating of MBSPL into the Issuer Non-Cooperating category as the company did not co-operate in the rating procedure despite repeated follow ups as per the Press Release dated October 24, 2018.

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.	Long Term Bank Facilities –Cash Credit	Long Term	11.20	IVR BB+ / Positive Outlook	-	-	-
2.	Short Term Bank Facilities – Overdraft	Long Term	0.40	IVR A4+			
3.	Short Term Bank Facilities – Foreign LC (DP/DA)	Short Term	3.60	IVR A4+			
4.	Short Term Bank Facilities – Inland LG		2.10	IVR A4+			

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. 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
Cash Credit	-	-	-	11.20	IVR BB+ /Positive
Overdraft	-	-	-	0.40	IVR A4+
Foreign LC (DP/DA)	-	-	-	3.60	IVR A4+
Inland LG	-	-	-	2.10	IVR A4+