

## RATING RATIONALE

24 Jan 2020

### Aarti Sponge and Power Pvt. Ltd.

### Brickwork Ratings assigns ratings for the Bank Loan Facilities of Rs.137.33 Crs. of Aarti Sponge and Power Pvt. Ltd. (ASPL or 'The Company')

#### Particulars

Facilities**	Amount (Rs. Crs.)	Tenure	Rating*
<b>Fund Based</b> Cash Credit/WCDL	<b>55.50</b>	<b>Long Term</b>	<b>BWR BBB, Stable</b>
<b>Term Loan</b>	<b>64.83***</b>		
<b>Non Fund Based</b> Letter of Credit/ Bank Guarantee	<b>5.00</b>	<b>Short Term</b>	<b>BWR A3+</b>
<b>ILC/FLC</b>	<b>12.00</b>		
<b>Total</b>	<b>137.33</b>	<b>Rs.One Hundred Thirty Seven Crores and Thirty Three Lakhs Only</b>	

\*Please refer to BWR website [www.brickworkratings.com/](http://www.brickworkratings.com/) for definition of the ratings

\*\* Details of Bank Loan facilities are provided in Annexures I & II

\*\*\*Term Loan outstandings as on November 30, 2019

#### RATING ACTION / OUTLOOK

Brickwork Ratings has assigned long term and short term ratings of BWR BBB, Stable /BWR A3+ to the bank loans of Rs.137.33Crs of Aarti Sponge and Power Pvt. Ltd as given above. The ratings assigned are based on the close to the four-decade business experience of the promoters, including their two-decade experience in the Iron and Steel Industry, ASPL's integrated operations with a sponge iron unit and a captive power plant, planned forward integration through the wire rod plant which is to become operational in FY21, increase in scale of operations in FY19 with revenue increase by 60% y-o-y, financial performance in the first eight months of FY2020 which was in line with first eight months of FY2019 on sustained sales realisations, and near to optimum 94% utilisation of sponge iron installed production capacities. An efficient working capital management as reflected in the operating cycle of two and a half months in FY19 and an acceptable credit profile with an acceptable interest coverage ratio, further bodes well for the Company. The financial performance of the Company is expected to be sustained in the second half of the financial year with the uptick in finished goods prices, helping it to achieve its projected topline and profitability and to sustain its present debt metrics, in FY20.



The ratings however, are constrained by ASPL's vulnerability to the volatility in the raw material and finished goods prices. Prices of Iron ore and coal, which are primarily used as inputs for producing Sponge Iron, have witnessed considerable volatility in the past, thus impacting the profitability and cash flows of the industry players. However, the Company has managed the price volatility by ramping up sales volumes. Besides, ASPL has a mining license and expects mining operations to commence in FY21, which is likely to reduce the input costs volatility. Also, the Company faces competition due to the fragmented nature of the iron and steel industry with a large number of organised and unorganised players in the industry.

The "Stable" outlook has been assigned since Brickwork Ratings believes that the business profile of Aarti Sponge and Power Ltd. will be maintained over the medium term. The outlook factors in the increase in scale of operations and better cash accruals going forward, in the backdrop of improved capacity utilisation. The rating outlook may be revised to Positive in case the revenues and profitability surpass the projected levels meaningfully with total gearing of 2.0x. The rating outlook may be revised to Negative if the revenues go down, and margins show lower than expected figures leading to liquidity stress, or if there is a deterioration in the total gearing to beyond 2.0x.

#### **KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED: Not Available**

#### **KEY RATING DRIVERS**

##### **Credit Strengths:**

- **Business Profile and Experience of the Promoters:** ASPL is an integrated Billet manufacturer operating a sponge iron plant of 90,000 MTPA, a Billet manufacturing facility with an installed capacity of 102600 MTPA and a captive power plant of 8MW in Raipur, Chattisgarh. The Company benefits from integration with the sponge iron unit and the captive power plant. As of November 2019, Sponge iron installed capacities are operated at over 90% utilisation. The Promoters have over two decades of experience in the Iron and Steel industry. Before the incorporation of ASPL, the Promoters were engaged in trading of Iron and Steel products. The increase in scale of operations and profitability in FY19 reflects the ability of the management to efficiently plan its product mix and use its resources optimally.
- **CAPEX:** ASPL is integrating forward with a wire rod plant in Chattisgarh with an installed capacity of 1,50,000 MTPA, at a total cost of Rs.48.50Cr funded by around 30% promoter contribution and the remaining amount through Term loans from Banks. The facility is expected to start operations in 1HFY21 and is likely to scale up ASPL's revenue and profitability.
- **FY19 and 1HFY20 Performance:** In FY19, ASPL's revenues grew 60% y-o-y to Rs.315 Crs (FY18: Rs.196 Crs), EBIDTA of Rs. 25.16 Crs (FY18: Rs.10.89 Crs) and net profits of Rs.7.60 Crs (FY18: Rs.2.64Crs). The growth in revenue was driven by a 54% y-o-y increase in total sales volumes, coupled with a 17% y-o-y rise in sales realisation per ton of Billets. Cost synergies from

the Captive power plant which started operations in the 2HFY18, were fully visible in FY19 when power and fuel cost declined ~15% y-o-y, and was well reflected in FY19 EBIDTA. ASPL strategically sold sponge iron and billets produced at its own facility to maximise revenues and profits, which helped sustain sales realisations per ton of sponge iron and Billets during FY19 and 1HFY20 - despite softening product finished goods in the industry. Sales realisations are expected to improve in the 2HFY20 as finished goods prices starts to pick up. About 59% of the projected FY20 revenues have already been achieved until November 2019 and the Company is on course to achieve its projections for the full year FY20.

- **Credit Profile:** ASPL has an acceptable credit profile with total gearing of 1.18x, ISCR of 2.68x and DSCR of 1.48x in FY19. Total gearing will increase in FY20 on account of the debt led CAPEX, but is likely to remain at an acceptable level as the promoters have infused funds in the form of Equity and unsecured loans to strengthen the net worth of the company. ISCR and DSCR are expected to improve going forward, with an improvement in EBIDTA and PAT.
- **Raw Material:** The Company has a long term supply agreement with NMDC for iron ore, the key raw material, and has linkages with South Eastern Coalfields Ltd. for coal. These arrangements ensure uninterrupted supply of input to the facilities. The Company is likely to source iron ore from its own mines in FY21.

#### **Credit Risks:**

- **Volatile Finished Goods and Raw Material Prices:** ASPL is vulnerable to the volatility in the raw material and finished goods prices. However, the Company has been managing such volatility in finished goods prices by increasing its sales volumes. The expected start of mining activities in FY21 will reduce raw material cost volatility to an extent.
- **Competition:** The Company faces competition from the various organised and unorganised players in the Iron and Steel industry - given the fragmented nature of the industry.

#### **ANALYTICAL APPROACH AND APPLICABLE RATING CRITERIA**

For arriving at its ratings, BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

#### **RATING SENSITIVITIES**

**Positive:** Increase in scale of operations, as projected, with increase in sales volumes and gearing of below 2.0x and maintenance of liquidity in the system may trigger a positive rating action going forward.

**Negative:** Deterioration in total gearing to above 2.0x and stretched liquidity, may trigger a Negative rating action going forward.

### LIQUIDITY INDICATORS: Adequate

ASPL has adequate liquidity supported by cash accruals of Rs.11.74 Crs against repayments of Rs.7.47 Crs in FY19. Cash and Cash balance of Rs.2.47 Crs as on March 2019. Although ASPL has availed additional loans for funding the CAPEX, it expects cash accruals to increase by ~24% to match repayments, with improved scale of operations and profitability. The Company is using on an average 90% of its working capital limits. However, have received support from promoters with infusion of unsecured loans and equity that provides cushion to meet future liquidity requirements with the CAPEX becoming operational in FY21.

### COMPANY'S PROFILE

Aarti Sponge and Power Ltd. (ASPL) was incorporated on 14th May, 2004 with its registered office in Raipur, Chattisgarh. Shri Rajeev Agrawal, Shri Prakash Mandal, Shri Rajeev Mundra and Dr Manish Mandal are the Directors of ASPL and have over four decades of business experience. ASPL is into manufacturing Sponge Iron (90,000 MTPA), Billets (102600 MTPA) and has a captive power plant (8MW) in Siltara, Chhattisgarh. The Company acquired iron ore mines in 2013-14 in Dantewada, South Bastar, Chhattisgarh, ~300 kms from the plant. Mining operations are expected to start from FY21 as the transportation route which is adjacent to the mine is still under construction. The Company captively consumes ~ 65% to 70% of the sponge iron produced for making Billets. Approximately 5% of the sales comes from trading of Sponge iron. ASPL has also set up a wire rod plant in Chattisgarh with an installed capacity of 1,50,000 MTPA, along with an induction furnace of 45,000 MTPA.

ASPL belongs to the promoters of the Aarti Group in Chhattisgarh. The Group was started by Shri Rajeev Agarwal and Shri Rajeev Mundra (present promoters of ASPL) along with others, in 1991. The Group has a long presence in the Construction industry in Chhattisgarh and has completed residential, commercial and government projects through Aarti Infrastructure and Buildcon Ltd.

### KEY FINANCIAL INDICATORS

Key Financial Indicators	Units	FY18	FY19
Result Type		Audited	Audited
Operating Revenue	₹ Cr	196.21	314.64
EBITDA	₹ Cr	10.89	25.16
PAT	₹ Cr	2.64	7.60
Tangible Net worth	₹ Cr	74.55	82.15
Total Debt/Tangible Net worth	Times	1.29	1.18
Current Ratio	Times	1.19	1.33

**NON-COOPERATION WITH PREVIOUS CREDIT RATING AGENCY: ACUIE BBB-/A3, Issuer Not Cooperating, vide press release dated November 11, 2019.**

**RATING HISTORY FOR THE PREVIOUS THREE YEARS [including withdrawal and suspended]**

Facilities	Current Rating			Rating History		
	Tenure	Amount (Rs. Crs.)	Rating	2018	2017	2016
Fund Based	Long Term	120.33	BWR BBB, Stable	Not Rated	Not Rated	Not Rated
Non Fund Based	Short Term	17.00	BWR A3+			
<b>Total</b>		<b>137.33</b>	<b>(Rs.One Hundred Thirty Seven Crores and Thirty Three Lakhs Only)</b>			

**COMPLEXITY LEVELS OF THE INSTRUMENTS**

For more information, visit [www.brickworkratings.com/download/ComplexityLevels.pdf](http://www.brickworkratings.com/download/ComplexityLevels.pdf)

**Hyperlink/Reference to applicable Criteria**

- [General Criteria](#)
- [Approach to Financial Ratios](#)
- [Manufacturing Sector](#)
- [Short Term Debt](#)

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**Aarti Sponge and Power Ltd.**

**ANNEXURE I**

**Details of Bank Loan Facilities rated by BWR**

Sl. No.	Name of the Bank	Type of Facilities	Long Term (Rs.Crs.)	Short Term (Rs.Crs.)	Total (Rs.Crs.)
1.	Punjab National Bank	Cash Credit	4.00	0.00	4.00
		Term Loan	26.00	0.00	26.00
2.	HDFC Bank	Cash Credit/WCDL	31.50	0.00	31.50
		Term Loan	24.83	0.00	24.83
		Letter of Credit	0.00	5.00	5.00
3.	IDBI Bank	Cash Credit	10.00	0.00	10.00
		Term Loan	14.00	0.00	14.00
		ILC/FLC	0.00	12.00	12.00
		Bank Guarantee (Sublimit of ILC/FLC)	0.00	(6.00)	(6.00)
4.	Yes Bank	Working Capital Demand Loan	10.00	0.00	10.00
		Cash Credit (Sublimit of WCDL)	(10.00)	0.00	(10.00)
		Bill Discounting (Sublimit of WCDL)	(10.00)	0.00	(10.00)
		Bank Guarantee (Sublimit of WCDL)	0.00	(5.00)	(5.00)
<b>(Total Rs. One Hundred Thirty Seven Crores and Thirty Three Lakhs only)</b>					<b>137.33</b>

\* Term Loan outstanding as on November 30,2019



### **For print and digital media**

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**DISCLAIMER:** Brickwork Ratings Private Limited (BWR) has assigned the rating based on the information obtained from the issuer and other reliable sources, which are deemed to be accurate. BWR has taken considerable steps to avoid any data distortion; however, it does not examine the precision or completeness of the information obtained. And hence, the information in this report is presented “as is” without any express or implied warranty of any kind. BWR does not make any representation in respect to the truth or accuracy of any such information. The rating assigned by BWR should be treated as an opinion rather than a recommendation to buy, sell or hold the rated instrument and BWR shall not be liable for any losses incurred by users from any use of this report or its contents. BWR has the right to change, suspend or withdraw the ratings at any time for any reasons