

**Rating Rationale**

**AGARWAL FOUNDRIES**

**Brickwork Ratings reaffirms the ratings for the bank loan facilities of Rs. 19.00 crs of Agarwal Foundries (‘AF’ or ‘the proprietorship concern’)**

**Particulars**

| Facilities   | Amount<br>(Rs. Crs) |              | Tenure                             | Ratings*              |                       |
|--|---------------------|--------------|------------------------------------|-----------------------|-----------------------|
|  | Previous            | Present      |                                    | Previous              | Present               |
| <b>Fund Based<br/>Cash Credit</b>                  | <b>15.00</b>        | <b>15.00</b> | <b>Long<br/>Term</b>               | <b>BWR BBB/Stable</b> | <b>BWR BBB/Stable</b> |
| <b>Non Fund<br/>Based<br/>Letter of<br/>Credit</b> | <b>4.00</b>         | <b>4.00</b>  | <b>Short<br/>Term</b>              | <b>BWR A3+</b>        | <b>BWR A3+</b>        |
| <b>Total</b>                                       | <b>19.00</b>        | <b>19.00</b> | <b>Rupees Nineteen Crores only</b> |                       |                       |

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

Note: Details of Bank facilities are provided in Annexure I

**Ratings Action/Outlook**

The ratings continue to reflect industry experience of the proprietor, established operational track record, long standing relationships with customers and suppliers, overall group synergies derived from the operations of the proprietorship concern being aligned to and integrated with the flagship company i.e., MS Agarwal Foundries Private Limited of Hyderabad based MS group and the average financial risk profile. However, the ratings remain constrained by the thin profitability margins, susceptibility of profitability to volatility in raw material prices, moderate scale of operations, stiff competition from both organized and unorganized players in a fragmented industry, inherent risks associated with the cyclical iron & steel industry and working capital intensive nature of operations. BWR notes the impact of Covid-19 on the general business conditions reflected in the drop in steel consumption in India as demand from all the user industries - Construction & Infrastructure, automobiles industry and consumer durables industry is expected to drop substantially in FY21. However, considering the government plans of increased thrust to infrastructure and construction, the demand is likely to see a revival in the long term with key segments being highways, railways, ports, urban infrastructure and airports.

BWR takes cognisance of the Covid-19 RBI moratorium package and the guidance provided by SEBI vide its circular dated 30 March 2020 in this regard. BWR notes that AF has not availed any reliefs under the aforementioned package from its lenders. BWR will continue to monitor the developments in case of a prolonged lockdown and analyse the impact, if any, on the AF's credit profile.

The 'Stable' outlook indicates a low likelihood of rating change over the medium term. BWR expects that **Agarwal Foundries'** business risk profile will be maintained over the medium term. The outlook may be revised to 'Positive' if the proprietorship concern records significantly better-than-expected revenue and profitability, increased scale of operations and improved working capital management, resulting in better debt coverage metrics and liquidity profile. The outlook may be revised to 'Negative' if the proprietorship concern reports significantly lower than expected performance, resulting in lower than estimated coverage indicators and a weaker liquidity position. Further, any major debt-funded expenditure resulting in deterioration in capital structure and debt coverage indicators and/or a sharp reversal in industry operating conditions may exert a downward pressure on the ratings.

## Key Rating Drivers

### Credit Strengths:

- **Experienced management and established track record:** The proprietor has over three decades of experience in the Iron & Steel industry, which has helped in establishing strong relationships with its suppliers and customers. AF has an operational track record of nearly 3 decades.
- **Group support and integrated operations:** AF is part of the Hyderabad based MS Agarwal Group (group). The group forayed into the steel industry through Agarwal Foundries, incorporated in 1991, engaged in the manufacturing of ingots and billets. The Group as a whole is an integrated steel unit operating across the value chain – i.e. from manufacturing of Sponge Iron to Billets, Ingots, TMT bars and steel structures. MS Agarwal Foundries Private Limited [*BWR BBB+/Stable/ A2+*] is the flagship company of the Hyderabad based 'MS Agarwal Group' of Companies. of the Hyderabad based MS group. Another Group company , Maruti Ispat & Energy Private Limited [*BWR BBB+/ Stable/A2*] is engaged in manufacturing of Sponge Iron. The group entities are managed by common promoters and there are strong managerial and operational synergies.

- **Average financial risk profile:** Revenue remained nearly flat over the last three years, with revenue of Rs. 106.23 crs in FY18, ~Rs. 116.27 crs in FY19 and Rs.113.74 crs in FY20 (provisional). Operating margin was 2.57% for FY19 as against 2.25% for FY18 and Net margin was 0.80% for FY19 as against 0.87% for FY18. Proprietor's capital continues to be modest at Rs. 20.68 crs as on 31 Mar 2019 as against Rs. 16.87 crs as on 31 Mar 2018. Capital structure was comfortable with Total debt/Proprietor's capital at 0.68 time as on 31 Mar 2019 and 0.60 time as on 31 Mar 2020 (prov)). Debt protection metrics are considered adequate as reflected by ISCR and DSCR of 1.65 times and 1.65 times respectively as on 31 Mar 2019 and 3.32 times and 3.16 times respectively as on 31 Mar 2020 (Prov).

### **Credit Challenges:**

- **Susceptibility to cyclical and fluctuation in raw material prices:** The profitability is vulnerable to fluctuations in the prices of raw materials as the latter constitutes 75% - 80% of the operating expenses. Further the performance of AF is linked to the steel industry, with cyclical changes in demand and price volatility. As the demand for steel is closely linked to economic activity, the domestic steel industry is susceptible to the cyclicity in the industry. AF's operations are vulnerable to any demand slowdown in the end user industry - real estate / infrastructure etc., thereby impacting the capacity utilisations and margins.
- **Thin profitability margins:** Profitability margins continued to be thin over the last three years, due to the intensely competitive and fragmented nature of industry. Operating profit margin is around 2% - 3% and net profit margin less than 1%. Any further deterioration of profitability margins would be a key rating monitorable.
- **Intense competition in the fragmented industry:** The Iron & Steel industry is characterised by intense competition across the value chain due to low product differentiation and consequent intense competition from unorganised as well as organised players leading to pricing pressures. These in turn affect the profitability margins of the proprietorship concern.
- **Prolonged impact of Covid-19:** AF's operations were partially impacted during the initial stages of lockdown wherein the manufacturing unit was required to be closed from last week of March 2020 till 2nd week of May 2020 in compliance with the COVID-19 related lockdown. Operations resumed during May 2020 and the plant presently is reported to be

operating at ~80% of its capacity. Although it has staff quarters and has not faced any labour related disruption, the impact of COVID-19 at a macro level on the end user industries is expected to result in a subdued FY21. Any greater than expected impact on the business profile is considered as key rating sensitivity.

### **Analytical Approach and Applicable Rating Criteria**

As it is a proprietorship concern, Standalone approach has been adopted and BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale).

### **Rating Sensitivities**

The ability of the proprietorship to increase its scale of operations, revenues, improve its profitability margins, strengthen its credit risk profile and manage its working capital efficiently would remain the key rating sensitivities.

**Positive:** Given the ongoing weakness in the macro-economic environment and the impact on the sector, a rating upgrade in the near term appears unlikely.

### **Negative:**

- Deterioration in key credit metrics on account of weaker than expected business performance.
- Specific credit metrics that could lead to a downgrade of AF's rating include (1) Decline in profitability margins i.e., Operating margin below 2% and net margin below 0.5%, due to lower price realisations, increase in input costs due to changing industry conditions or a rise in capex (2) Total Debt/Proprietor's capital exceeding 1.75 times and weakening in debt protection metrics with DSCR and ISCR declining below 1.5 times
- Prolonged impact of Covid on the revenues and cash flows leading to material deterioration in its financial risk profile and liquidity.

### **Liquidity Position: Adequate**

Cash and cash equivalents were low at Rs.0.12 crs as on 31 March 2020 (Prov). The proprietorship concern does not have any significant debt repayment obligations part from some vehicle loans. The net cash accruals are sufficient to service these minor debt repayments in FY21 and FY22. EBITDA at Rs.2.99 crs for FY19 was sufficient to cover the interest and finance charges of Rs.1.81 crs for FY19. Liquidity is considered adequate as reflected in the average utilisation of WC limits ~90% and a conversion cycle of around 60-70 days. As on 31 Mar 2020 (Prov), the conversion cycle further improved to 59 days. Current ratio continues to remain adequate at 1.43 times as on 31 Mar 2019. Timely recovery of receivables and efficient management of its working capital requirements without any strain on borrowings/cash flows is

a rating sensitivity.

### About the concern

Agarwal Foundries is a proprietorship concern of Mr. Pramod Kumar Agarwal incorporated in 1991 at Secunderabad, Telangana. It is engaged in manufacturing of MS Billets at its manufacturing unit at Petbasheerabad, Quthbullapur mandal, Ranga Reddy district, Telangana and has an installed capacity of 50500 TPA. Agarwal Foundries is part of Hyderabad based MS Group. Other operational entities of the group are MS Agarwal Foundries Private Limited [*BWR BBB+/Stable/ A2+*], Maruti Ispat & Energy Private Limited [*BWR BBB+/ Stable/A2*], Rama Spinners Private Limited [*BWR BBB-/ Stable*] and Sitaram Spinners Private Limited [*BWR BBB/Stable/A3+*].

### Key Financial Indicators

| Particulars                     | Units   | 31 Mar 2018<br>Audited | 31 Mar 2019<br>Audited |
|---------------------------------|---------|------------------------|------------------------|
| Operating Revenue               | Rs. Crs | 106.23                 | 116.27                 |
| EBITDA                          | Rs. Crs | 2.39                   | 2.99                   |
| Profit After Tax                | Rs. Crs | 0.92                   | 0.93                   |
| Proprietor's Capital            | Rs. Crs | 16.87                  | 20.68                  |
| Total Debt/Proprietor's Capital | Times   | 0.94                   | 0.68                   |
| Current Ratio                   | Times   | 1.97                   | 1.43                   |

On a provisional basis, the proprietorship concern has achieved a revenue of ~Rs. 114 crs for FY20 and ~Rs.31 crore in 4MFY20.

**Key Covenants of the facility rated:** The terms of sanction include standard covenants normally stipulated for such facilities.

**Status of non-cooperation with previous CRA – Not Applicable**

**Rating History for the last three years(Including withdrawal and suspended):**

| Sl. No       | Facilities       | Current Rating (Aug 2020) |   |                        | Rating History         |                        |                        |
|--------------|------------------|---------------------------|---|------------------------|------------------------|------------------------|------------------------|
|              |                  | Type                      | Amount (Rs. Cr)                                     | Rating                 | 2019 [20 Sep 2019]#    | 2018 [30 May, 2018]^   | 2017 [12 Apr, 2017]#   |
| 1            | Cash credit      | Long Term                 | 15.00   | <b>BWR BBB /Stable</b> | <b>BWR BBB/ Stable</b> | <b>BWR BBB/ Stable</b> | <b>BWR BBB/ Stable</b> |
| 2            | Letter of Credit | Short Term                | 4.00  | <b>BWR A3+</b>         | <b>BWR A3+</b>         | <b>BWR A3+</b>         | <b>BWR A3+</b>         |
| <b>Total</b> |                  |                           | <b>Rs. 19.00 Crore (Rupees Nineteen Crore Only)</b> |                        |                        |                        |                        |

# Rated amount is Rs. 19.00 crs; ^ Rated amount is Rs. 23.50 crs;

Note: An initial rating of BWR BBB/Stable/A3+ was assigned on 08 Apr 2015 and reaffirmed on 25 Apr 2016.

**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**

|  |   |
|--|---|
| <ul style="list-style-type: none"> <li>• <b><u>General Criteria</u></b></li> </ul>             | <ul style="list-style-type: none"> <li>• <b><u>Manufacturing Companies</u></b></li> </ul> |
| <ul style="list-style-type: none"> <li>• <b><u>Approach to Financial Ratios</u></b></li> </ul> | <ul style="list-style-type: none"> <li>• <b><u>Short Term Debt</u></b></li> </ul>         |

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**Agarwal Foundries**  
**Annexure I: Details of Bank Facilities rated**

| Sl. No.                                    | Name of the Bank     | Type of Facilities | Long Term (Rs. Crs) | Short Term (Rs. Crs) | Total (Rs. Crs) |
|--|----------------------|--------------------|---------------------|----------------------|-----------------|
| 1.   | Indian Overseas Bank | Cash Credit        | 15.00               | -                    | 15.00           |
|  |                      | Letter of Credit   | -                   | 4.00                 | 4.00            |
| <b>TOTAL - Rupees Nineteen Crores Only</b> |                      |                    |                     |                      | <b>19.00</b>    |

**Note:**

1. The concern enjoys Working Capital Demand Loan [WC DL] of Rs. 12.00 crore as a sub-limit of Cash credit with tenor of 120 days.
2. The concern also has a sanctioned Forward contract/ derivative limit of Rs.4.00 crs as a sublimit of LC which has not been rated at its request.

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