RATING RATIONALE

19 August 2021

Lloyds Metals and Energy Limited

Brickwork Ratings revises the long term rating for the existing bank limits of Rs. 100.00 crores of Lloyds Metals and Energy Limited ("LMEL" or "the Company") and simultaneously withdraws the short term rating.

Particulars:

Facility**	Amount (₹ Cr)		Tenure	Rating*	
	Previous	Present		Previous (May, 2020)^	Present
Fund based	95.00	**100.00**	**Long Term**	BWR BBB-/Stable [Assigned]	**BWR BBB/Stable [Upgraded]**
Non Fund based	5.00	-	**Short Term**	BWR A3 [Assigned]	**BWR A3 [Withdrawn]**
Total	100.00	**100.00**	**INR One hundred Crores Only**		

*Please refer to BWR website www.brickworkratings.com/ for definition of the ratings
** Details of Bank facilities are provided in Annexure-I.
^Rating was moved to rating not reviewed category in May, 2021

Rating: Long term rating upgraded, and the short term rating withdrawn.

RATING ACTION / OUTLOOK

BWR has withdrawn its rating on the short term facility at the company's request and the withdrawal is in line with BWR's withdrawal policy on withdrawal of bank loan ratings. Further, BWR has upgraded the long term rating and the rating revision reflects the improvement expected in the operating efficiency following the commencement of the mining operations in June, 2021 at the Surajgarh Iron ore mines, allotted on lease to the company. The captive sourcing of the iron ore is expected to ensure continuous availability resulting in improved capacity utilisation levels and reduction in the cost of iron ore procurement by nearly 50 percent leading to significant improvement in profitability of the company. Also, the surplus iron ore produced over the requirement is available for sale and hence contributes to the revenue of the company. The company is also planning to set up a steel plant with capacity 250000 MTPA over the medium term, which will further enhance its business risk profile with forward integration. The rating revision also considers the significant infusion in the capital of the company during the current year leading to significant reduction in overall debt and interest outgo for the company. The capital infusion will also support the ongoing & future capital expenditure plan of the company.

The rating continues to draw comfort from the established market presence of the Company supported by the extensive experience of the promoters in the iron & steel industry. The rating also derives comfort from the partially integrated nature of operations wherein the Company is engaged in manufacturing of sponge iron and also has 30MW captive power generation capacity. Further, the rating also derives comfort from the unsecured loans provided by the promoters as and when needed along with infusion in the capital.
However, the rating is constrained on susceptibility of the operations & profitability to the volatility in the sponge iron & iron ore prices along with cyclicality in the steel industry.The rating is also constrained by the presence in the highly competitive and fragmented sponge iron manufacturing industry.

Outlook: Stable
BWR believes that LMEL's business risk profile will be healthy considering the favourable demand outlook for the steel industry and the company's captive iron ore sourcing arrangement. The business risk profile is also supported by the company's established market presence, experienced promoters alongwith long standing relation with the customers. The "Stable" outlook indicates a low likelihood of rating change over the medium term.

KEY RATING DRIVERS

Credit Strengths-:

- **Established presence in the market supported by the extensive experience of promoters**
  The Company has an established presence in the steel industry with an operational track record of more than four decades. LMEL mainly caters to the steel producers located in Maharashtra. Apart from sponge iron, the company also sells power generated from waste heat gases produced in sponge kilns to power trading companies.
  The Company also benefits from the extensive experience of its promoter i.e. Mr. Babulal Agarwal who possesses more than five decades of experience in the steel industry, supported by a team of well qualified and experienced professionals as the second line of management.

- **Partially Integrated nature of operations**
  The Company benefits from partially integrated nature of operations with the presence of sponge kilns with installed capacity of 1000 TPD and captive power generation capacity of 30 MW. Also, LMEL has been allotted a mining lease at Surajgarh Iron Ore Mine (Wooria Hills) over an area of 348.09 Ha situated at village Surajgarh in the Gadchiroli district, Maharashtra for a period of 20 years starting from 2007 with environmental clearance for production of 3 million MTPA and total deposits of more than 91 million tonnes. LMEL has also entered into a Mine Development & Operator (MDO) MOU with Thriveni Earthmovers Private Limited (TEMPL), which is one of the largest mining operators in the country. The company has already commenced mining operations in June 2021. The procurement of iron ore directly from its own mines will ensure continuous availability of iron ore leading to improvement in capacity utilisation levels and reduction

in iron ore cost from Rs. 7000 per tonne to Rs. 3000~Rs. 3500 per tonne leading to healthy profitability of the company. Also, the iron ore requirement for the company is around 0.50 million tonnes per annum hence any surplus iron ore production will be available for sale to third parties.

- **Significant capital infusion in the company**
  LMEL has raised equity share capital of Rs. 19.98 crores by alloting Optionally Fully Convertible Debentures (OFCDs) issued to "Clover Media Private Limited" into equity shares during FY2021. The company had issued 2,40,00,000 convertible warrants at issue price of Rs. 7.50 per warrant to the existing promoters during FY2021 and the same was converted to equity shares in the year 2021. The Board of Directors have also approved to issue 9,00,00,000 equity shares at an issue price of Rs. 20 per share to TEMPL on preferential basis during FY2022. TEMPL has also made an open offer to the shareholders of the company and on completion of the open offer TEMPL will be acquiring joint control in the company and will be classified as promoter of the company along with the existing members of the promoter and promoter group of the company. The Board of Directors have also given consent for issue of 1,00,00,000 3% OFCDs at face value of Rs. 20.00 each to TEMPL and the same shall be converted into equity shares within a period of 18 months from the date of allotment. The company has also allotted 6,60,00,000 convertible warrants at a price of Rs. 9.47 per warrant to the existing promoters upon receipt of initial warrant subscription amount of Rs. 15.63 crores and these convertible warrants are expected to be completely converted into equity shares by FY2023.The infusion in the capital of the company during FY2022 and FY2023 is expected to be used for the repayment of the long term debt and also fund the ongoing capacity expansion plan of the company.

Credit Risks-:

- **Subdued performance during FY2021**
  The Company's operations and profitability were adversely impacted by the outbreak of COVID-19 pandemic-related lockdown implemented in Q4 FY2020. The company reported a significant decline in its operating income and losses during Q1 FY2021 due to lockdown restrictions, limited availability and drastic increase in prices of iron ore. Although with easing of the lockdown restrictions and improved demand from steel sector & better realisation for sponge iron, the company reported improvement in revenue and profitability from Q2FY2021 onwards, the overall revenue and profitability margins of the company were lower than FY2020. The company has reported significant improvement in revenue for Q1FY2022 as the same stood at Rs. 95.69 crores as compared to Rs. 10.61 crores during the same period in the previous year.
  BWR believes that the demand outlook and sponge iron prices is likely to remain favourable in the current fiscal, which will support the company's revenue and profitability growth in FY2022.

- **Susceptibility of the profitability to volatility in raw material and finished product prices along with the cyclicality in the steel industry**
  The raw materials are the main cost drivers for LMEL and raw material consumption constituted around 88 percent of the total cost of goods sold for FY2021. The main raw materials of the company i.e. iron ore and/or pellets and non-coking coal are procured locally. However, the prices of these raw materials are volatile in nature and therefore the profitability of the company is susceptible to fluctuation in raw material prices and finished goods. Nonetheless, the company's dependence on the market for iron ore will decrease drastically in the near future with the company's captive sourcing arrangements and hence the profitability shall be protected to that extent.
  Further, the performance of the sponge iron industry is directly dependent on the performance of the nation's steel sector. The steel industry is cyclical in nature and strongly related to the economic cycles with its key end user industries i.e. construction, infrastructure, automobiles and capital goods are hugely dependent on the state of the economy. Hence, slowdown in demand of any of these sectors directly impacts the demand for steel products. The outbreak of the COVID-19 pandemic has severely impacted the demand in major steel-consuming sectors and thereby resulted in lower steel production globally.

- **Exposure to project implementation risk**
  The company has planned expansion into value added products i.e. billets, thermo-mechanically treated (TMT) steel bars, wire rods as well as a power plant with total capex of Rs. 1200.00 crores. The construction period is around 8 years and the same is spread over three phases. The construction for Phase I is expected to commence in November 2021 and the commercial operation shall commence from July, 2023 . The total project outlay is estimated at Rs. 185.00 crores and the same will be funded through internal accruals & promoters funds. The demand risk is expected to be low considering the cost advantage of the company over non-integrated players in the market due to captive iron ore as well as healthy market conditions. Nevertheless, as the project is large relative to the present size of the company and of long tenure, the company remains exposed to project implementation risk.

- **Presence in the highly competitive and fragmented sponge iron manufacturing industry**
  With the presence of around 400 sponge iron units in the country, the Indian sponge iron industry is highly fragmented. The top 20 producers contribute about 60~65% of the total production whereas the rest contribute 35~40% of the production. Hence, the pricing flexibility of the Company is restricted due to this intense competition.

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). BWR has principally relied upon the standalone audited financials up to FY21, publicly available information and clarification/information provided by the Company.

RATING SENSITIVITIES

Positive:

- Significant improvement in the operating income and profitability resulting in substantial improvement in the financial risk profile and debt coverage indicators of the company.
- Efficient working capital management leading to improvement in liquidity profile.

Negative:

- Significant decline in operating income and profitability leading to deterioration in debt coverage indicators
- Stretch in working capital cycle leading to deterioration in liquidity profile of the company.
- Majorly debt funded capacity expenditure plan resulting in high leveraged capital structure.

LIQUIDITY POSITION: ADEQUATE

The company has reported a significant decline in net cash accruals from Rs. 30.65 crores in FY 2020 to Rs. 13.95 crores in FY 2021. The current ratio comfortably stood at 1.63 times as on 31.03.2021. Further, the company's average working capital limit utilisation stood at around 78.04 percent for the period from October, 2020 to June, 2020. The cash and bank balance stood at Rs. 8.04 crores as on 31.03.2021. Further, the repayment of around Rs. 118.63 crores is estimated to be due over the next three years and the same is expected to be met through internal accruals and infusion of capital by the promoters.

The company had availed moratorium period for the interest and principal payments towards the term loan from its lenders during March 2020 to August 2020 under the COVID-19 regulatory package. The principal repayments were extended by six months and the accrued interest was serviced in September 2020. Further, the liquidity of the company was supported by infusion of promoters funds to the tune of Rs. 37.00 crores during FY 2021-22.

Also, the company had raised around Rs. 37.00 crores through issue of new shares and application money for convertible warrants during FY 2021.

The company plans to raise fund to the tune of Rs. 234.00 crores during FY2022 and Rs. 31.24 crores during FY 2023 through issue of equity shares,convertible warrants and Optionally Fully Convertible Debentures (OFCDs) to partially repay its long term debt and support the ongoing capital expenditure plan. The company also plans to avail additional working capital limits to support its working capital requirement.

COMPANY PROFILE

Lloyds Metals and Energy Limited [Erstwhile Lloyds Metals & Engineer Limited] was initially incorporated as a private limited company under the name "Nagarjuna Metals and Engineer Private Limited" in the year 1977. Subsequently, in 1986 the constitution of the entity was converted into a public limited company and listed on the Bombay Stock Exchange in February, 1987 however the name was changed to Lloyds Metals & Engineer Limited in January 1990 and to the latest name in April 2011. The Company is engaged in manufacturing of sponge iron & its by-products and generation/distribution of power. The by-products of the sponge iron include Char, Fly Ash, ESP Dust, Bed Material and Iron Ore Fines. The sponge iron plant is located in Chandrapur district of Maharashtra with an installed capacity of 3,00,000 metric tonnes per annum (MTPA) and also the captive power plant with a 30 MW capacity which runs on the

waste heat gases produced in sponge kiln. The Company possesses certifications including ISO - 9001, 14001, OHSAS 18001 ISO 9001:2008. Sponge iron is an intermediate product; a source of metallics for secondary steel making through EAF or IF route.
The sale of sponge iron contributed around 88%whereas the power contributed around 12% to the total revenue for FY 2021. The main raw material required by the Company is iron ore and non-coking coal. The iron ore is sourced from the iron ore mine located in Surjagarh village, Gadchiroli district Maharashtra which it has leased for a period of 20 years starting from 2007. It also procures iron ore from other suppliers located in Raipur and Odisha. The Company procures coal from Western Coalfields Limited under long-term linkages. The credit period received from the suppliers ranges from 30 to 90 days. LMEL mainly caters to steel manufacturers located in the state of Maharashtra. The day to day operations of the Company are handled by Mr. Babulal Agarwal who possesses more than five decades of experience in the iron & steel industry.

KEY FINANCIAL INDICATORS (in ₹ Cr)

Key Parameters	Units	FY2020	FY2021
Result Type		**Audited**	**Audited**
Operating Revenue	Rs. Crs	371.74	253.41
EBITDA	Rs. Crs	21.13	10.87
PAT	Rs. Crs	31.83	0.13
Tangible Net worth	Rs. Crs	144.41	182.11
Total Debt/Tangible Net worth	Times	0.83	0.95
Current Ratio	Times	1.55	1.63

KEY COVENANTS OF THE INSTRUMENT/FACILITY RATED
The terms of sanction include standard covenants normally stipulated for such facilities.

STATUS OF NON-COOPERATION WITH PREVIOUS RATING AGENCY IF ANY : Not Applicable

ANY OTHER INFORMATION: None

RATING HISTORY FOR THE PREVIOUS THREE YEARS [INCLUDING WITHDRAWAL AND SUSPENDED]

Instrument / Facilities	Current Rating			Rating History		
	Tenure (Long Term/ Short Term)	Amount (₹ Cr)	Rating	26 May 2020	30 January 2019	2018
Fund Based	Long Term	100.00	BWR BBB/ Stable (Upgraded)	BWR BBB- /Stable (Reaffirmed)	BWR BBB- /Stable (Assigned)	-
Non Fund Based	Short Term	-	BWR A3 (Withdrawn)	BWR A3 (Reaffirmed)	BWR A3 (Assigned)	-
Total		**100.00**	**INR One Hundred Crores Only**			

COMPLEXITY LEVELS OF THE INSTRUMENTS: SIMPLE
For more information, visit www.brickworkratings.com/download/ComplexityLevels.pdf

Hyperlink/Reference to applicable Criteria

- General Criteria
- Approach to Financial Ratios
- Rating Criteria for Manufacturing Companies

Analytical Contacts	
Shashikala Hegde **Senior Rating Analyst** **Board: +91 22 2831 1426, +9122 2831 1439** **Ext: 652** **shashikala.h@brickworkratings.com**	**Vidya Shankar** **Principal Director – Ratings** **Board: +91 80 40409999** **vidyashankar@brickworkratings.com**
1-860-425-2742	**media@brickworkratings.com**

Lloyds Metals and Energy Limited

ANNEXURE I
Details of Bank Facilities rated by BWR

Sl. No.	Name of the Bank	Type of Facilities	Long Term (₹ Cr)	Short Term (₹ Cr)	Total (₹ Cr)
1.	Kotak Mahindra Bank	Term Loan I	23.40	-	23.40
2.	Kotak Mahindra Bank	Term Loan II	7.71	-	7.71
3.	Kotak Mahindra Bank	Term Loan III	20.00	-	20.00
4.	CitizenCredit Co-operative Bank Limited	Term Loan	24.38	-	26.90
5.	CitizenCredit Co-operative Bank Limited	Cash Credit	10.00	-	10.00
6.	Proposed Bank	Proposed Cash Credit	11.99	-	11.99
TOTAL					**100.00**

Total Rupees One Hundred Crores only.

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