Rating Report

Brickwork Ratings assigns/reaffirms 'BWR BBB-' for the Bank Credit Facilities of Adhunik Metaliks Ltd.

Brickwork Ratings (BWR) has reaffirmed/assigned the following **Ratings**[1] for Bank Loan Facilities of Adhunik Metaliks Ltd. *('AML' or 'the Company')*.

Facility	Tenure	Existing Facility (₹ Cr)	Previous Rating	Rating Assigned/ Reaffirmed
Term Loan	**Long Term**	**1054.07**	**BWR BBB-** (BWR Triple B Minus) **(Outlook: Stable)**	**BWR BBB-** (Pronounced BWR Triple B Minus) **(Ratings watch with developing implications)***
Working Capital (Fund Based)		**695.00**		
LC & BG (Non-fund based)**	**Short Term**	**403.00**	**BWR A3** (BWR A Three)	**BWR A3** (Pronounced BWR A Three)
Total		**2152.07**	**(INR Two Thousand One Hundred and Fifty Two Crores and Seven Lacs only)**	

** Ratings watch with developing implications in view of pending merger of Orissa Manganese & Mineral Ltd., Adhunik Metaliks Ltd. and Zion Steel Ltd.*
*** Non fund based limits of LC/FLC/BG are interchangeable between Short term and long term*

The rating has, inter alia, factored AML's established presence in steel, mining and power sectors in the eastern part of the Country. AML has made investment in fully integrated business model to create cost effective steel in India. The rating is however constrained by high working-capital requirement, very low profitability and current ratio, high inventory level coupled with significant long term borrowings and the risks associated with the current expansion plans. The Rating has also factored the on-going amalgamation process of its group companies, OMML (Orissa Manganese & Minerals Ltd), AML (Adhunik Metaliks) and ZSL (Zion Steel Ltd) in to one entity i.e. OMML. The Ratings watch with developing implication reflects the ongoing merger process of AML & ZSL in to OMML, which is expected to be completed post High Court approval. The proposed merger is expected to be cost effective to the Group.

BWR has essentially relied upon the audited financial results of AML up to FY13 (12M), unaudited FY14 (9M, Mar ending 2014), projected financials and clarifications/information provided by the Company.

[1] ***Please refer to www.brickworkratings.com for definition of the Ratings***

Background:

Adhunik Metaliks Limited (AML) is the flagship company of the Adhunik Group and having more than ten years presence in the Industry. AML was incorporated in 2001 as Neepaz Metaliks Pvt. Ltd. and later renamed as Adhunik Metaliks Ltd. in 2005. Adhunik group is an established player in the Iron & Steel and Ferro-Alloys industry with a presence largely in Eastern India. The group has various activities like manufacturing, processing, trading of iron & steel scrap and various steel products – both finished steel & intermediates, and has set up manufacturing facilities in the States of West Bengal, Orissa, Jharkhand and Meghalaya. The company has capacity of 450,000 TPA of steel, 3,00,000 TPA of sponge iron, 2,13,792 TPA of pig iron , 46,880 TPA of ferro alloys, 267,300 TPA of sinter, 1,20,000 TPA coke oven and 34 MW captive power.

AML is engaged in the manufacturing of alloy and carbon steel products catering to the auto, power, engineering, oil and gas sectors. Also, the Company is engaged in the merchant mining of iron ore, manganese ore and mineral value addition through pellet manufacturing through its 100% subsidiary Orissa Manganese and Minerals Limited. In addition, it has power generation capacities through step down subsidiary i.e. Adhunik Power and Natural Resources Limited (APNRL).

On-going Merger:

Adhunik Group is in the process of amalgamating three of its Group companies, OMML (Orissa Manganese & Minerals Ltd), AML (Adhunik Metaliks) and ZSL (Zion Steel Ltd) in to one entity i.e. OMML. The merger is proposed to be effective from July 2012. The amalgamation process will require one to two months for completion subject to obtaining the necessary approvals. At present the Company is waiting for the High Court approval. With amalgamation of these three companies, the existing loans of the three amalgamating companies will get merged in the books of OMML. Lenders have already been sanctioned loans under the Obligor and Co-obligor structure. AML and OMML have been sanctioned new loans in lieu of their earlier facilities as a part of debt consolidation, therefore the repayment of all the term loans in initial five years will be around 35% and balance will be in remaining 5 years. It is expected that the merger will lead to significant cost and operational efficiencies that will help the Group in keeping its business competitiveness in the long run.

Merger process of AML, ZSL and OMML is under the consolidated scheme. Firstly ZSL will merge in to AML with swap ratio of 17:1. After merger with ZSL, AML will get merged in to OMML with swap ratio of 1:1, in turn the merged entity will increase its number of shares to

127159262 from 123499536. It is proposed to merge ZSL and reverse merger AML with OMML pursuant to a court approved scheme of amalgamation. Post-merger OMML will have integrated

plant with a cost effective business model supported by their captive iron ore, coal washery, captive power, sinter, direct reduced iron facility, blast furnace, ferro alloy, coke oven batteries and railway sidings. The whole process is in its advance stages of completion and expected to be completed by with in next two to three months.

Financial Performance:

On a standalone basis, the Company's operating revenue has decreased to ₹ 1653.78 Cr in FY13 (12 Months) from ₹ 1858.42 Cr in FY12 (15 Months). However the figures are not comparable as FY12 consists of 15 months period. PAT has shown some improvement to ₹ 2.82 Cr in FY13 from a loss of ₹ 0.52 Cr in FY12 mainly due to lower finance cost and depreciation. as compared to ₹ 1321.91 Cr in FY13 (9M) and however, PAT imporved to ₹ 10.68 Cr in FY14 from profit of ₹ 2.25 Cr in FY13 (9M). Total borrowings decreased marginally to ₹ 1359.35 Cr in FY13 from ₹ 1435.92 Cr in FY12 as against the tangible Net-worth of ₹ 680.14 Cr in FY13 from ₹ 676.82 Cr in FY12. The tangible Net-worth is exclusive of revaluation reserves of ₹ 543.16 Cr in FY13 and ₹ 562.84 Cr in FY12.

On a Consolidated basis, the Company's operating revenue has decreased to ₹ 1859.12 Cr in FY14 (9M) from ₹ 2255.26 Cr in FY13 (9M). Also, PAT decreased to ₹ 51.10 Cr in FY14 (9M) from ₹ 97.09 Cr.

Risk Assessment:

AML has long term agreement with OMML for the supply of 1.00 MTPA high grade Iron ore fines. It is expected that the proposed merger will provide better accessibility to raw material supplies. Its strategically located manufacturing unit in Sundergarh (Orissa) makes it possible to procure 90% of all raw materials (iron ore, coal, coke, limestone, power, and manganese ore, among others) from within 200 km of the Company's manufacturing unit. It is having non-coking coal linkage with Mahanadi Coalfields and through e-auction route. AML sources ~40% of its power requirement from 34 MW captive power plant and rest from State Electricity grid. Its integrated business is expected to provide most cost effective steel manufacturing unit and improved up on operating margins.

At present AML has weaknesses in the form of very low profitability margins (~0.17%) and current ratio of 0.77 in FY13. They also have high inventory level coupled with significant long term borrowings of ` 1359.35 Crs, along with the risks associated with the current expansion plans. The proposed merger and timely completion of on-going expansion plans are expected to provide further boost to its performance. After the merger, its entire debt would be shifted to merged entity i.e. OMML and new debt repayment schedule will reduce burden of debt repayment for next two-three years. The merged entity is expected to provide ~3-5% profitability margins in near future from current level of ~2.5% in 9M FY14 (considering OMML and AML financials only for 9M FY14). Similarly Operating margins expected to improve from ~24% in FY13 to ~29-30% in coming years.

Outlook:

AML is the flagship Company of Adhunik Group. It has a strategically located manufacturing unit in Sundergarh (Orissa) for raw material supply of Iron ore, Coal etc. It also has long term agreement with Orissa Mining Corporation for supply of 1.0 MTPA high grade iron ore fines. AML is in the process of building fully integrated and cost effective steel manufacturing unit. The on-going amalgamation process will require another month or two for completion after obtaining the necessary High Court approval. The Rating Outlook reflects this position. It is expected that the merged entity will build significant economies of scale, improve operational efficiency by cutting inventories and smoothening the flow of operations, and help the Group expand its presence in the industry.

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