October 07, 2022

Kothari Metals Limited: Long-term rating upgraded, short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term-Interchangeable	(101.00)[1]	(101.00)[1]	[ICRA]A-(Stable); upgraded from [ICRA]BBB+(Stable)
Non fund based limits	264	264	[ICRA]A2+; reaffirmed
Total	**264**	**264**	

**Instrument details are provided in Annexure-1*

Rationale

The long-term rating upgrade of Kothari Metals Limited (KML) factors in the healthy improvement in revenues and operating margins in FY2022, which is expected to continue in the current fiscal as well. The revenues grew by around 75% on account of increased metal prices. The improvement in operating margins was a result of improvement in the premium on nickel compared with contracted terms with the supplier, which resulted in healthy improvement in cash accruals to Rs 82 crore in FY2022 from Rs 26 crore in FY2021. The operating margins are expected to be healthy in the current fiscal as well. However, the movement in market premium compared with contracted rates will remain a key monitorable. Further, the healthy accruals in two fiscals resulted in a comfortable liquidity, with free cash and bank balance of around Rs. 80 crore in June 2022 and adequate cushion in non-fund based limits as well.

The ratings continue to consider KML's continued healthy financial performance, with an interest coverage of around 41 times in FY2022 over 16.5 times in FY2021. The rating action also notes KML's demonstrated ability to grow its business in a market that is prone to volatility in demand and prices. The ratings consider the vast experience of the promoters of nearly four decades in the metal and non-metal trading businesses, along with its established relationships with international suppliers of nickel and other materials. The company's strategy of procuring a significant quantity of metals from the primary manufacturers keeps its costs low. The ratings also derive comfort from KML's large, diversified and reputed customer base, with low counterparty risk. Moreover, the customer concentration risk is low as sales to top-20 customers contributed ~40% to the overall sales in FY2022.

The ratings are, however, constrained by KML's low operating margin albeit an improvement in FY2022 due to the limited value-additive nature of the trading business. ICRA notes that the company maintains a certain level of freehold inventory, exposing its margins to volatility in metal prices. However, the same is mitigated to some extent by the hedging strategy adopted by the company. Also, the supplier concentration risk remains on the higher side as the top-two suppliers account for over 50% of its total purchases. ICRA, however, notes that the said suppliers are among the largest producers of metals, globally. KML imports a major portion of the materials traded, which exposes its cash flows to the risks of foreign exchange fluctuations. A formal hedging mechanism adopted by the company, however, largely mitigates the said risk.

The Stable outlook on the [ICRA]A- rating reflects ICRA's opinion that KML would continue to benefit from the lack of domestic manufacturing capacities for most of the metals that it trades in, and a stable long-term demand outlook for these metals in the country.

[1] *Sublimit of current Letter of Credit facilities*

Key rating drivers and their description

Credit strengths

Healthy improvement in performance in FY2022, likely to be sustained in current fiscal – KML's revenues grew by 75% in FY2022 due to rise in metal prices. Moreover, the operating margins improved on account of premiums on nickel due to supply-side constraints. This performance is expected to be healthy in the current fiscal as well as the company has already achieved Rs 829 crore of revenues till September 20, 2022. KML is a debt-free company, which leads to favourable debt coverage indicators and a comfortable capital structure. Moreover, a large portfolio of free cash and liquid investment, unutilised bank lines and heathy cash accruals from business provide high financial flexibility to the company. KML reported close to Rs. 80 crore of cash and investments as on June 30, 2022.

Vast experience of promoters; established relationships with international suppliers – KML's promoters have an experience of over four decades in the business of metal trading. Long association with the industry has enabled the company establish good relationships with primary metal manufacturers and miners, globally.

Diversified customer base with reputed profile – KML has a diversified customer base across auto, ferrous and non-ferrous metal manufacturers, battery manufacturers, etc. The top-20 customers have contributed around 30-40% to KML's revenue over the years. Its customers enjoy a healthy credit profile, which reduces counterparty risks. Moreover, the company's sales are backed by the letter of credit, which secures payments.

Prudent hedging policy – KML follows a prudent hedging policy, whereby it mitigates the risks arising out of fluctuations in commodity prices as well as exchange rates.

Credit challenges

Low value addition limits profit margins – KML's trading business is low value additive in nature, which limits its profit margins. Historically the operating margins have been around 3% albeit some improvement in FY2022. The premium of metals, especially Nickel, has seen a healthy increase in the past one year and shall be a key monitorable.

High supplier concentration risk – KML has high supplier concentration risk as over 50% of the company's metal procurement is made from two international suppliers. Moreover, the dependence on certain metals such as nickel is high to an extent of 50% of the overall revenues.

Liquidity position: Adequate

KML is expected to maintain an **adequate** liquidity position, aided by its healthy cash flow from business, zero debt repayment liability and minimal capital expenditure requirement. The company's unutilised limits provide additional support to its liquidity.

Rating sensitivities

Positive factors – ICRA could upgrade KML's ratings, if the company is able to sustainably scale-up its operations, while maintaining healthy operating margins and a comfortable liquidity position.

Negative factors – Significant decline in revenues or operating profitability could exert pressure on the ratings. Considerable deterioration in the liquidity position owing to stretch in the working capital cycle, or TOL/TNW higher than 1.5 times, on a sustained basis, may trigger a downward rating revision.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology](#)
Parent/Group Support	None
Consolidation/Standalone	Standalone

About the company

Established in 1977, Kothari Metals Limited trades in ferrous and non-ferrous metals. The company is involved in importing and trading of products like pure nickel, tin ingot, silicon metal, magnesium ingot, ferro chrome, etc. These metals are sold to customers across the auto, ferrous and non-ferrous metals, defence and battery sectors in India. The company has its head office in Kolkata and branches/warehouses across India.

Key financial indicators

Consolidated	FY2021(A)	FY2022(P)
Operating Income (Rs. crore)	861.2	1505.5
PAT (Rs. crore)	19.0	80.5
OPBDIT/OI (%)	3.0%	7.2%
PAT/OI (%)	2.2%	5.3%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	1.1
Total Debt/OPBDIT (times)	0.3	0.0
Interest Coverage (times)	16.5	41.3

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; A-Audited,P-Provisional

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Mar 31,2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					October 07,2022	September 20,2021	August 07,2020	August 13,2019
1	Long term-Interchangeable	Long term	(101.0) ^	-	**[ICRA]A- (Stable)**	**[ICRA]BBB+(Stable)**	**[ICRA]BBB+(Stable)**	**[ICRA]BBB+(Stable)**
3	Non fund based limits	Short term	264	-	**[ICRA]A2+**	**[ICRA]A2+**	**[ICRA]A2+**	**[ICRA]A2+**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long term-Interchangeable	Simple
Non fund based limits	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, are available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long term-Interchangeable	-	-	-	(101.00)	[ICRA]A-(Stable)
NA	Non fund based limits	-	-	-	264	[ICRA]A2+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Not Applicable

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

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