

December 30, 2022

## Nezone Tubes (Utkal) Limited: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based Limits – Cash Credit/ WC DL/ POF	110.00	120.00	[ICRA]A+ (Stable), reaffirmed
Short-term – Non Fund-based Limits – Letter of Credit/ Bank Guarantee <sup>§</sup>	(53.00)	(55.00)	[ICRA]A1, reaffirmed
Short-term – Non Fund-based Limits – Bank Guarantee/ Forward Contract/ Derivative	4.00	4.00	[ICRA]A1, reaffirmed
Long-term/ Short-term – Unallocated Limits	26.00	16.00	[ICRA]A+ (Stable)/ [ICRA]A1, reaffirmed
<b>Total</b>	<b>140.00</b>	<b>140.00</b>	

<sup>§</sup> Letter of Credit/ Bank Guarantee is the sub-limit of cash credit/ working capital demand loan

\*Instrument details are provided in Annexure-I

### Rationale

For arriving at the ratings, ICRA has considered the consolidated business risk profile of Nezone Tubes Limited (NTL, rated at [ICRA]A+ (Stable)/ [ICRA]A1), Nezone Tubes Tn Limited (NTTL, rated at [ICRA]A+ (Stable)/ [ICRA]A1), Nezone Tubes (Utkal) Limited (NTUL, rated at [ICRA]A+ (Stable)/ [ICRA]A1) and Nezone Strips Limited (NSL, rated at [ICRA]A+ (Stable)/ [ICRA]A1), referred to as the Nezone Group/ Group, given the close business, financial and managerial linkages among them.

The reaffirmation of the ratings considers the long experience of the promoters and an established position of the Nezone Group in the steel-tube manufacturing business, supported by a strong distribution network, regular capacity addition and optimum utilisation of the same. The ratings also factor in the Group's competitive advantage arising from a diversified product portfolio and its ability to change the product mix, as per market demand. Besides, the Group's raw material sourcing arrangement with reputed suppliers ensures high quality of finished products. ICRA notes that the Group recorded a sizeable inventory gain due to a steady rise in steel prices over the past two years, which along with improved margin on sales had a positive impact on the operating profit. However, in the current fiscal, ICRA expects the Group to incur inventory loss due to a drop in steel prices. Moreover, reduced margin on sales would also have an adverse impact on the OPM of the Group in FY2023 compared to FY2022. Nevertheless, the ratings continue to derive comfort from the comfortable financial risk profile of the Group, reflected by healthy cash accruals, a conservative capital structure and strong debt protection metrics.

The ratings are, however, constrained by limited value addition and price-based competition in the steel-tube industry, which keeps the Group's operating margin under check. Moreover, cyclicity inherent in the steel business is likely to keep margins and cash flows vulnerable to fluctuations in the raw material prices and demand of final products. The ratings are also impacted by the significant receivables and inventory holding, which are likely to keep the Group's working capital intensity of operations at a high level.

The Stable outlook on the long-term rating reflects ICRA's opinion that the Nezone Group will be able to maintain its business position, given its established track record of operation in the steel tube manufacturing business. Besides, the financial risk profile of the Group is likely to remain comfortable, going forward, along with adequate cash flows relative to its debt service obligations.

## Key rating drivers and their description

### Credit strengths

**Established position of the Nezone Group in the steel-tube manufacturing business** – The Nezone Group has been involved in the steel-tube manufacturing business for more than three decades, and has a firm footprint mainly in the eastern, north eastern and southern India. The Group's established brand, Nezone, in the steel-tube industry and the promoters' long experience in the business strengthen its operational profile.

**Diversified product profile and ability to change the product mix as per market demand lead to competitive advantages** – The Group has a diversified product mix including mild steel black pipe, galvanised pipe, GP strips and precision tubes of various specifications, which are used for multiple purposes. MS black pipes/sections are mainly used for fabrication, structural purpose and scaffolding, whereas galvanised pipes are used in water pipe lines (mainly drinking water and irrigation) and gas pipelines. Over the years, MS black pipe has remained the key revenue driver for the Group. Moreover, the Group's flexibility to change the product mix as per demand from the customers renders competitive advantage to an extent.

**Strong distribution network, regular capacity increase and optimum utilisation of the same strengthen the Group's operating profile** – The Nezone Group has manufacturing facilities and distribution network spread across various states. The Group has been expanding its geographical presence and distribution network over the last few years, supported by regular capacity expansion and optimum utilisation of the same, positively impacting the business profile. The products are sold through a wide network of distributors and dealers across different regions of the country.

**Favourable financial risk profile characterised by a conservative capital structure and strong debt coverage metrics** – The capital structure of the Group continues to remain conservative on account of a healthy net worth and low reliance on external debt. The consolidated gearing and TOL/TNW stood at 0.5 times and 0.7 times, respectively as on March 31, 2022. In the current fiscal, the management undertook buyback of equity shares in NTL and NSL, and infused equity share capital of around Rs. 20 crore in NTTL for part funding the ongoing capex. This ultimately resulted in a cash outflow of around Rs. 45 crore by the Group in the current fiscal. Nevertheless, healthy accretion to reserves and reduced working capital borrowings would continue to keep the overall capital structure of the Group at a conservative level. The debt protection metrics have also remained strong over the past years owing to healthy profits as well as cash accruals and low gearing. Despite some deterioration expected in the current fiscal, the same would continue to remain strong, going forward.

### Credit challenges

**Limited value addition and price-based competition likely to keep operating margin under check** – The raw material cost accounted for around 80% of the Group's turnover over the last few years, reflecting a highly raw-material intensive nature of operations. This, along with limited value addition, is likely to keep the operating profitability of the Group under check.

**Fragmented nature of the industry leads to intense price-based competition** – The steel-tube industry is characterised by the presence of many unorganised players in addition to a few large companies. Intense price-based competition due to the fragmented nature of the industry exerts pressure on margins.

**Exposed to volatility in raw material prices** – Hot rolled coil (HRC) is the key raw material used for producing MS black pipe. Zinc is required in small quantity for the galvanisation process to convert MS black pipe into galvanised iron (GI) pipe. The Group remains exposed to significant volatility in prices of key raw materials like HRC and zinc as adequate raw material inventory needs to be maintained. The Group also suffered sizeable inventory losses in imported raw materials in the past due to an adverse fluctuation in steel prices and exchange rates, which in turn affected the consolidated margins.

**Likely deterioration in the profitability in the current fiscal, driven by declining realisations** – The Group recorded a sizeable inventory gain due to a steady rise in steel prices over the past two years, which along with improved margin on sales led to a steady increase in the operating profits. However, in FY2023, ICRA expects the Group to incur inventory loss due to a drop in steel prices. Moreover, reduced margin on sales would also adversely impact the OPM of the Group in FY2023. The Group

reported an OPM of 3.5% in 7M FY2023. However, the same is likely to increase in the full year given the better performance expected for the balance period of FY2023 on the back of relatively stable steel price as well as margin on sales. ICRA expects the net margin of the Group to remain at around 3-4% in the current fiscal. The cash accruals from business and RoCE of the Group are also estimated to deteriorate in FY2023 compared to the previous year.

**Significant receivables and inventory holding likely to keep the working capital intensity high** – Significant receivables and stocking requirements keep the Group’s working capital intensity of operations at a high level. In FY2021, the net working capital relative to the operating income, on a consolidated basis, stood at 35%. However, the same reduced to 31% in FY2022 due to a decline in the receivables along with the inventory holding. The Group’s working capital intensity of operations is likely to remain high, going forward.

### Liquidity position: Adequate

The Group generated positive fund flow from operations in FY2022, however, increased working capital requirement led to a negative cash flow from operations during the year. The Group has also demonstrated need-based funding in the form of unsecured loan from the directors and body corporate. The Group’s cash flow from operations is likely to remain comfortable compared to its debt service obligations in the near-to-medium term. The overall working capital utilisation of the Group stood at a moderate level of around 48% during the last 15 months, ended in October 2022. In view of limited capital expenditure plan, undrawn working capital limits and sustainability of funding support from Group companies, ICRA expects the overall liquidity position of the Nezone Group to remain adequate, going forward.

### Rating sensitivities

**Positive factors** – ICRA may upgrade the ratings if there is a significant increase in revenue, profits and cash accruals of the Group on a sustained basis. Specific credit metric that may trigger ratings upgrade include a consolidated RoCE of more than 20% on a sustained basis.

**Negative factors** – ICRA may downgrade the ratings if adverse fluctuation in steel prices results in a significant deterioration in the Group’s profitability and/or a stretch in the working capital cycle exerts pressure on the liquidity position. Specific credit metric that may trigger a rating downgrade include consolidated interest coverage of less than 6.0 times on a sustained basis.

### Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Ferrous Metal Entities</a> <a href="#">Rating Approach – Consolidation</a>
Parent/ Group support	Not applicable
Consolidation/ Standalone	For arriving at the ratings, ICRA has considered the consolidated business risk profiles of Nezone Tubes Limited, Nezone Tubes Tn Limited, Nezone Tubes (Utkal) Limited and Nezone Strips Limited (as mentioned in Annexure-2), given the close business, financial and managerial linkages among them.

### About the company

Incorporated in 2016 by the promoters of Nezone Group, Nezone Tubes (Utkal) Limited (NTUL) manufactures mild steel (MS) black pipe and full hard cold rolled strip (FHCR). The manufacturing facilities of the company are located in Kalinganagar, Odisha. NTUL commenced its commercial operation with an installed MS black pipe production capacity of 84,000 metric tonnes per annum (MTPA) in July 2019. Subsequently, the company commissioned a cold rolling capacity of 30,000 TPA for production of FHCR strip. The company enhanced its tube mill production capacity by 12,000 MTPA and commissioned a

galvanising unit with an annual production capacity of around 18,000 metric tonnes (MT) for manufacturing MS black/ galvanised pipe/ GP strips in May 2021.

The Nezone Group has been involved in the steel-tube manufacturing business for more than three decades, and has a firm footprint mainly in the eastern, north eastern and southern India. Overall, the Group has tube mills with a total production capacity of 4,01,000 MTPA, cold-rolling unit with a total production capacity of 65,000 MTPA and galvanising capacity of 38,000 MTPA. The entire range of products are sold under the brand, Nezone.

#### Key financial indicators

	Nezone Tubes (Utkal) Limited – Standalone			Nezone Group – Consolidated		
	FY2021 (Audited)	FY2022 (Audited)	7M FY2023 (Provisional)	FY2021 (Audited)	FY2022 (Audited)	7M FY2023 (Provisional)
<b>Operating income</b>	370.2	746.7	480.0	1,496.4	2,141.9	1,484.2
<b>PAT</b>	13.6	33.9	13.1	79.7	105.9	23.0
<b>OPBDIT/OI</b>	8.6%	8.5%	5.5%	8.9%	7.9%	3.5%
<b>PAT/OI</b>	3.7%	4.5%	2.7%	5.3%	4.9%	1.5%
<b>Total outside liabilities/Tangible net worth (times)</b>	2.7	2.5	-	0.6	0.7	-
<b>Total debt/OPBDIT (times)</b>	3.2	2.9	-	1.5	1.8	-
<b>Interest coverage (times)</b>	3.6	5.8	-	7.8	10.7	-

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Source: Nezone Tubes Limited, Nezone Tubes Tn Limited, Nezone Tubes (Utkal) Limited, Nezone Strips Limited, ICRA Research, ICRA Estimate

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

## Rating history for past three years

Instrument	Type	Current rating		Chronology of rating history for the past 3 years					
		Amount rated (Rs. crore)	Amount outstanding as on Mar 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022		Date & rating in FY2021	Date & rating in FY2020	
				Dec 30, 2022	Jan 6, 2022	Apr 7, 2021	-	Mar 6, 2020	Jan 3, 2020
1 Term Loan	Long Term	-	-	-	-	[ICRA]A (Stable)	-	[ICRA]A-(CE) (Stable)	[ICRA]A-(CE) (Stable)
2 Cash Credit/ WCDL/ PBD	Long Term	120.00	118.61	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	-	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)
3 Non-fund Based (Interchangeable)	Long Term/ Short Term	-	-	-	-	-	-	[ICRA]BBB- (Stable)/ [ICRA]A3	[ICRA]BBB- (Stable)/ [ICRA]A3
4 Purchase Order Financing	Short Term	-	-	-	-	[ICRA]A1	-	-	-
5 Bank Guarantee/ Forward Contract/ Derivative	Short Term	4.00	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	-	-	-
6 Letter of Credit/ Bank Guarantee <sup>§</sup>	Short Term	(55.00)	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	-	-	-
7 Unallocated Limits	Long Term/ Short Term	16.00	NA	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	-	-	-

<sup>§</sup> Letter of Credit/ Bank Guarantee is the sub-limit of cash credit/ working capital demand loan

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based Limits – Cash Credit	Simple
Short-term – Non Fund-based Limits – Interchangeable	Very Simple
Short-term – Non Fund-based Limits – Bank Guarantee/ Forward Contract	Very Simple
Long-term/ Short-term – Unallocated Limits	Not Applicable

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: [Click Here](#)

**Annexure I: Instrument details**

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash Credit/ WCDL/ PBD	-	-	-	60.00	[ICRA]A+ (Stable)
NA	Cash Credit/ WCDL	-	-	-	50.00	[ICRA]A+ (Stable)
NA	Purchase Order Financing	-	-	-	10.00	[ICRA]A+ (Stable)
NA	Letter of Credit <sup>§</sup>	-	-	-	(50.00)	[ICRA]A1
NA	Letter of Credit <sup>§</sup>	-	-	-	(3.00)	[ICRA]A1
NA	Bank Guarantee <sup>§</sup>	-	-	-	(2.00)	[ICRA]A1
NA	Bank Guarantee	-	-	-	1.00	[ICRA]A1
NA	Forward Contract/ Derivative	-	-	-	3.00	[ICRA]A1
NA	Unallocated Limits	-	-	-	16.00	[ICRA]A+ (Stable)/ [ICRA]A1

Source: Nezone Tubes (Utkal) Limited

§ Letter of Credit/ Bank Guarantee is the sub-limit of cash credit/ working capital demand loan

[Please click here to view details of lender-wise facilities rated by ICRA](#)

**Annexure II: List of entities considered for consolidated analysis**

Company Name	Ownership	Consolidation Approach
Nezone Tubes Limited	-	Full Consolidation
Nezone Tubes Tn Limited	-	Full Consolidation
Nezone Strips Limited	-	Full Consolidation

Source: Annual report of Nezone Tubes Limited, Nezone Tubes Tn Limited, Nezone Tubes (Utkal) Limited, Nezone Strips Limited for 2021-22

## ANALYST CONTACTS

**Mr. Jayanta Roy**  
+91 33 7150 1120  
[jayanta@icraindia.com](mailto:jayanta@icraindia.com)

**Mr. Kaushik Das**  
+91 33 7150 1104  
[kaushikd@icraindia.com](mailto:kaushikd@icraindia.com)

**Mr. Sujoy Saha**  
+91 33 7150 1184  
[sujoy.saha@icraindia.com](mailto:sujoy.saha@icraindia.com)

**Mr. Sandipan Kumar Das**  
+91 33 7150 1190  
[sandipan.das@icraindia.com](mailto:sandipan.das@icraindia.com)

## RELATIONSHIP CONTACT

**Mr. Jayanta Chatterjee**  
+91 80 4332 6401  
[jayantac@icraindia.com](mailto:jayantac@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**  
Tel: +91 124 4545 860  
[communications@icraindia.com](mailto:communications@icraindia.com)

## Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

[info@icraindia.com](mailto:info@icraindia.com)

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## ICRA Limited



### Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001

Tel: +91 11 23357940-45



### Branches



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