August 28, 2023

Indian Metals & Ferro Alloys Limited: Ratings reaffirmed; assigned for enhanced amount

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term – Fund based - Term loan	10.25	8.43	[ICRA]AA-(Stable); reaffirmed
Short Term - Fund-based limits	685.00	735.00	[ICRA]A1+; Reaffirmed/Assigned for enhanced amount
Short Term - Non-fund based facilities	150.00	200.00	[ICRA]A1+; Reaffirmed/Assigned for enhanced amount
Short Term - Non-fund based facilities**	(685.00)	(735.00)	[ICRA]A1+; Reaffirmed/Assigned for enhanced amount
Long Term - Untied limits	30.25	15.07	[ICRA]AA-(Stable); reaffirmed
Total	**875.50**	**958.50**	

**Instrument details are provided in Annexure-1; **100% interchangeable with corresponding fund-based limits*

Rationale

The ratings reaffirmation factors in Indian Metals & Ferro Alloys Limited's (IMFA) improved credit metrics following the material deleveraging done since FY2022, supported by attractive ferrochrome spreads. The company's net debt levels fell to ~Rs.51 crore as on March 31, 2023 from ~Rs.655 crore as on March 31, 2020, leading to a significant improvement in its credit metrics, as reflected in the company's net debt/OPBDITA improving to 0.1 times in FY2023 from 1.6 times in FY2021 and 4.8 times in FY2020.

While the company's financial performance started moderating from Q2 of FY2023 due to the challenging operating environment, characterised by falling ferro chrome realisations and increasing raw material costs, the situation reversed in Q4 of FY2023 with ferro chrome prices inching up and raw material cost pressure abating. While ferro chrome prices have corrected in Q1 of FY2024, the reduction is costs has been steeper (given the significant correction in met coke and thermal coal prices), which has resulted in higher contribution margin on a sequential basis.

ICRA has noted that while the prices of stainless steel, which is the end user of ferro chrome, have retreated to the near pre-Covid level in most regions, the prices of ferro chrome remain significantly higher than the pre-Covid level. This anomaly is believed to have been caused by the rising production costs of Chinese smelters (largest ferro chrome producer globally, accounting for more than 40% of the global ferro chrome output). Chinese smelting costs remain heavily influenced by the seaborne price of chrome ore for which it is totally dependent on imports, mainly from South Africa (the second largest producer of ferro chrome globally). In this context, the ongoing logistics bottlenecks in South Africa have resulted in a steep price hike for imported chrome ore over the last few months. At present, the same remains significantly higher than the pre-Covid and long-term median levels, resulting in an increased cost of production for Chinese smelters. In addition, for South Africa, rising electricity costs, which influence their smelting costs, have been rising steeply, resulting in an increased cost of production for South African smelters. Hence, an upward shift in the cost curve for the leading ferro chrome producers globally is unlikely to lead to a mean reversion of ferro chrome prices over the near term. This in turn, positively impacts IMFA, given its integrated nature of operations, supported by captive chrome ore. Additionally, with met coke prices (accounting for almost 25% of the overall cost for IMFA, for which the company is entirely dependent on external sources) expected to soften in the remaining quarters of FY2024, IMFA's ferro chrome spreads are likely to remain above the long-term median level for FY2024, leading to another year of healthy earnings and comfortable credit indicators.

The ratings also factor in the greater visibility towards recovery of a large part of the invested capital for the Utkal-C coal block, following successful reauctioning of the block to Jindal Steel & Power Limited (JSPL) in February 2022. The ratings continue to favourably factor in the experience of the promoters in the ferro-alloy industry and the established track record of the company as one of the largest exporters of ferro chrome from India. The ratings also consider IMFA's competitive cost structure, on a global scale, on account of the integrated nature of its operations (it is largely self-reliant in terms of chrome ore and power). ICRA notes that the transition to an auction-based regime has led to an elevated premia for awarding chrome ore mines, which gives IMFA a distinct competitive edge in terms of costs, as its captive mines awarded under the earlier allotment regime are valid till 2049 and 2055. The ratings also consider the company's strong liquidity profile, as reflected in the sizeable cash and liquid investment portfolio of ~Rs.271 crore as of end-March 2023 and ~Rs.317 crore as of end-June 2023. Besides, the established relationships with domestic banks and financial institutions impart the company with considerable financial flexibility.

The ratings are, however, tempered by IMFA's exposure to the inherent cyclicality of the ferro-chrome industry. Prices of ferro chrome, which are primarily used as an input for producing stainless steel, have witnessed a considerable volatility in the past, which makes IMFA's cash flows volatile as well. In addition, surplus power generating capacity continues to be a drag on the company's return on capital employed (RoCE). The ratings also remain constrained by the execution and operational risks associated with the large-scale capex programme of ~Rs.1,600 crore towards setting up of a greenfield ferrochrome unit at Kalinganagar and brownfield mine expansions at Sukinda and Mahagiri. Besides the long gestation period, if the project commissioning coincides with a cyclical downturn in the sector, the capacity ramp-up could potentially get delayed. ICRA understands that mine expansion would account for 65-70% of the planned capex, to be phased out over the next 7-8 years. The company is likely to largely fund the expansion through internal accruals. Any significant debt contracted to fund the capex, which weakens the coverage metrics, will be a credit negative.

The Stable outlook on the long-term rating reflects ICRA's expectations that IMFA will benefit from the upward shift in the cost curve for the leading ferro chrome producers globally, which is likely to keep ferro chrome prices attractive over the near-to-medium term, helping keep the company's profits and cash accruals at attractive levels in FY2024.

Key rating drivers and their description

Credit strengths

Credit metrics expected to remain healthy over the near-to-medium term, aided by healthy spreads – Healthy cash flows on account of improved ferrochrome spreads helped the company embark on a deleveraging strategy since FY2022. The company's net debt levels fell to ~Rs.51 crore as on March 31, 2023 from ~Rs.655 crore as on March 31, 2020, leading to a significant improvement in its credit metrics. This is reflected by the company's net debt/OPBDITA improving to 0.1 times in FY2023 from 1.6 times in FY2021 and 4.8 times in FY2020.

An upward shift in the cost curve for the leading ferro chrome producers globally is unlikely to lead to a mean-reversion of ferro chrome prices over the near term. This in turn positively impacts IMFA, given its integrated nature of operations, supported by captive chrome ore. Additionally, with met coke prices (accounting for almost 25% of the overall cost for IMFA, for which the company is entirely dependent on external sources) expected to soften in the remaining quarters of FY2024, IMFA's ferro chrome spreads are likely to remain above the long-term median levels for FY2024, leading to another year of healthy earnings and comfortable credit indicators.

Greater visibility towards recovery of invested capital for the Utkal-C coal block – IMFA invested around Rs.375 crore towards land and surface infrastructure for the Utkal-C coal block, through its subsidiary, Utkal Coal Limited (UCL), which was deallocated by the Supreme Court in September 2014. In February 2022, the Ministry of Coal reauctioned the said coal block, and the same was won by JSPL. The exact amount of the upfront payment for the Utkal-C block is yet to be calculated by the nominated authority. However, the amount invested towards land acquisition is eligible for a 12% simple rate of interest since the date of purchase. So, ICRA believes that IMFA is likely to be able to recover a sizeable portion of the invested amount, which is expected to further strengthen the company's liquidity profile. The company has already received Rs.20.69 crore in FY2023, as part compensation towards the statutory expenses.

Long experience of the promoters; company one of the largest exporters of ferro chrome – The promoters have an experience of more than five decades in operating / managing ferro-chrome plants. IMFA is one of the leading domestic producers and exporters of ferro chrome. The total installed capacity is 190 MVA across six furnaces located at two manufacturing sites in Odisha. IMFA exports ~90% of its total annual production. The long-term volume contracts that IMFA has with some of the global leaders in the stainless-steel industry, mitigate demand risks to an extent.

Competitive cost structure due to integrated nature of operations – Chrome ore and power are the two most important cost drivers of ferro-chrome producers, apart from met (metallurgical) coke. IMFA has two operational chrome ore mines with a peak annual mining capacity of ~6.5 lakh metric tonnes (MT). ICRA notes that the transition to an auction-based regime has led to an elevated premia for awarding chrome ore mines, which gives IMFA a distinct competitive edge in terms of costs, as its captive mines awarded under the earlier allotment regime are valid till 2049 and 2055. Its captive power generation capacity (post de-rating of its old plant) stands at 204.5 MW. The company's integrated nature of operations, (largely self-reliant in chrome ore and power) results in a competitive cost structure. The chrome ore mines' proximity to the plants benefits the company owing to low inward freight costs. For its power unit, IMFA sources domestic coal from a mix of linkages, washery rejects and through e-auction. The location of the plants in the coal-rich region of Odisha results in a competitive landed cost of coal. Moreover, the location of the manufacturing sites close to ports helps in controlling the outward freight cost.

Healthy free cash/bank/liquid investment portfolio and established relationships with domestic banks and financial institutions impart financial flexibility – IMFA's liquidity profile remains strong, reflected in the sizeable cash and liquid investment portfolio of ~Rs.271 crore as of end-March 2023 and ~Rs.317 crore as of end-June 2023. The company also enjoys established relationships with domestic banks and financial institutions. As a result, it has a considerable financial flexibility.

Credit challenges

Exposure to the cyclical nature of the ferro-chrome industry results in volatile cash flows – The company remains exposed to the cyclical nature of the ferro-chrome industry. In the past, IMFA witnessed considerable volatility in cash flows following fluctuations in ferro-chrome prices. However, IMFA's status as one of the low-cost ferro-chrome producers makes it resilient to industry downcycles, when ferro chrome prices remain tepid.

Surplus power generating capacity continues to be a drag on the company's financials – IMFA has captive thermal power plants and solar power plants of 204.5 MW capacity, leading to energy cost savings. However, the installed generation capacity is significantly higher than its internal requirements of around 130 MW at present. Given the non-remunerative Odisha state grid tariff levels, and unavailability of coal from captive sources, as previously envisaged, following cancellation of the Utkal C block, the company has not been able to fully utilise its power generation capacity for the last few years. Such a large capital blockage, which are not generating any returns, has affected IMFA's overall RoCE.

Sizeable capex and associated risks – The company has announced a capex programme accumulating around Rs.1,600 crore, towards setting up of a greenfield ferrochrome unit (~1 lakh TPA) at Kalinganagar and brownfield mine expansions (expansion of Sukinda's capacity from 3.51 lakh TPA to 6 lakh TPA through switching from opencast to underground mining and increasing Mahagiri's underground mining capacity from 3 lakh TPA to 6 lakh TPA). The capex plans, which are large vis-à-vis IMFA's current balance sheet size, exposes the company to operational and execution risks. Besides the long gestation period, if the project commissioning coincides with a cyclical downturn in the sector, the capacity ramp-up could potentially get delayed. ICRA understands that mine expansion would account for 65-70% of the planned capex, to be phased out over the next 7-8 years. The company is likely to largely fund the expansion through internal accruals. Any significant debt contracted to fund the capex, which weakens the coverage metrics, will be a credit negative.

Environmental and Social Risks

Environmental considerations – Ferro alloy manufacturing is an energy-intensive process and requires a substantial use of fossil fuels, which results in greenhouse gas emissions, industrial waste generation, and environmental pollution. Increasing regulatory requirements to reduce greenhouse gas emissions and stricter air pollution standards may lead to higher costs for ferro alloy manufacturers in the medium term. This in turn leads to a greater focus on reducing the carbon footprint through various technological interventions. With many of these emerging low-carbon technologies yet to achieve commercial viability, this transition could entail a significant investment for ferro alloy manufacturers. Further, the company faces the risk of physical climate change from floods and drought in the form of disruption in raw material availability due to extreme weather events and impact on water availability due to drought.

Social considerations – Social risks for ferro alloy manufacturers manifest from health and safety of employees involved in the manufacturing activity. Casualties/ accidents at operating units due to gaps in safety practices could not only lead to production outages for ferro alloy manufacturers like IMFA, but also invite penal actions from regulatory bodies. The sector is exposed to labour-related risks and risks of protests/social issues with local communities, which might impact expansion/modernisation plans. Also, the adverse impact of environmental pollution in nearby localities could hamper smooth operations of the plant.

Liquidity position: Strong

IMFA's liquidity profile remains **strong**, as reflected in the large cash balance and liquid investment portfolio of ~Rs.271 crore as of end-March 2023 and ~Rs.317 crore as on end-June 2023, which impart a high degree of financial flexibility to the company. Notwithstanding the large-scale capex plans announced by the company, healthy retained cash flows expected going forward, along with a staggered capex programme will support the liquidity profile of the company. Overall, ICRA expects IMFA to be able to comfortably meet its capex commitments through internal sources of cash and yet be left with sizeable liquidity buffer (on-balance sheet liquidity plus unutilised credit lines).

Rating sensitivities

Positive factors – The long-term rating could be upgraded if the company is able to commission the upcoming expansion of the greenfield ferro chrome project within the budgeted timeline and costs, and quickly stabilises the operations thereafter. Specific metrics that could lead to an upgrade include Net Debt/OPBDITA of less than 0.5 times on a sustained basis, following commissioning of the upcoming expansion.

Negative factors – The ratings could witness pressure if any adverse movement in realisations/ costs significantly affects margins, leading to a material deterioration of the credit metrics. Specific triggers that could lead to ratings downgrade include Net Debt/OPBDITA of higher than 1.0 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	As on March 31, 2023, IMFA had three subsidiaries, a) Utkal Coal Ltd., b) IMFA Alloys Finlease Ltd., and c) Indmet Mining Pte Ltd. Out of these, Utkal Coal Ltd. and Indmet Mining Pte Ltd. are yet to commence operations. The operations of IMFA Alloys Finlease Ltd. are not meaningful compared to IMFA's current scale. Moreover, there is no external debt in IMFA's subsidiaries. Therefore, for arriving at the ratings, ICRA has considered the standalone financials of IMFA.

About the company

Indian Metals & Ferro Alloys Limited (IMFA), promoted by Late Dr. Bansidhar Panda, was incorporated in November 1961. The company primarily produces ferro alloys, including charge chrome (high carbon ferro chrome), and has an installed furnace capacity of 190 MVA (2,84,000 metric tonnes per annum (MTPA)) in its two plant sites at Therubali and Choudwar, in Odisha. The company's operations are supported by a 200-MW captive thermal power plant at Choudwar, captive chromite mines and a 4.5-MW solar power plant.

Key financial indicators (Audited)

IMFA (Standalone)	Standalone		
	FY2021	FY2022	FY2023
Operating income (Rs. crore)	1844.2	2603.0	2676.4
PAT (Rs. crore)	166.8	507.9	225.7
OPBDIT/OI (%)	18.3%	30.9%	19.0%
PAT/OI (%)	9.0%	19.5%	8.4%
Total outside liabilities/Tangible net worth (times)	1.1	0.6	0.4
Total Debt/OPBDIT (times)	2.0	0.6	0.6
Net Debt/OPBDIT (times)	1.6	0.4	0.1
Interest coverage (times)	5.9	13.1	7.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA – Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2024)				Chronology of Rating History for the past 3 years					
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Aug 16, 2023 (Rs. crore)	Date & Rating in FY2024	Date & Rating in FY2023	Date & Rating in FY2022		Date & Rating in FY2021		
					Aug 28, 2023	Mar 15, 2023	Mar 4, 2022	Sep 27, 2021	Mar 22, 2021	Jan 25, 2021	Apr 7, 2020
1	**Term loan**	Long-term	8.43	8.43	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Positive)	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Negative)
2	**Fund-based limits**	Short-term	735.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A2+	[ICRA]A2+
3	**Non-fund based facilities**	Short-term	200.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A2+	[ICRA]A2+
4	**Non-fund based facilities ****	Short-term	(735.00)	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1	[ICRA]A2+	[ICRA]A2+
5	**Untied lmits**	Short-term	-	-	-	-	-	-	[ICRA]A1	[ICRA]A2+	-
6	**Untied limits**	Long-term	15.07	-	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	-	-	-	-

***100% interchangeable with corresponding fund-based limits*

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term loan	Simple
Fund-based limits	Simple
Non-fund based facilities	Very simple
Non-fund based facilities**	Very simple
Untied limits	NA

***100% interchangeable with corresponding fund-based limits*

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-1: Instrument details

ISIN No.	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	**Term loan**	FY21	NA	FY25	8.43	[ICRA]AA-(Stable)
NA	**Fund-based limits**	NA	NA	NA	735.00	[ICRA]A1+
NA	**Non-fund based facilities**	NA	NA	NA	200.00	[ICRA]A1+
NA	**Non-fund based facilities****	NA	NA	NA	(735.00)	[ICRA]A1+
NA	**Untied limits**	NA	NA	NA	15.07	[ICRA]AA-(Stable)

Source: Company; ***100% interchangeable with corresponding fund-based limits*

Please Click here to view details of lender-wise facilities rated by ICRA

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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