ICRA

December 07, 2023

Sunvik Steels Private Limited: [ICRA]A-(Stable); assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. Crore)	Rating Action
Long-term Fund-based Term Loan	30.00	[ICRA]A-(Stable); assigned
Total	**30.00**	

**Instrument details are provided in Annexure-I*

Rationale

The assigned rating favourably factors in the extensive experience of the promoters of Sunvik Steels Private Limited (SSPL) in the steel industry and the company's established position as one of the leading thermo-mechanically treated (TMT) bar manufacturers in Karnataka. ICRA notes that the company's operating profile benefits from the integrated nature of operations, supported by manufacturing facilities for sponge iron and billet as well as captive power generation, which in turn lead to an efficient cost structure and results in healthy contribution levels. The company also benefits from the location-specific advantages due to its proximity to raw material sources (mainly iron ore/iron ore pellets), which results in freight cost savings, thereby supporting the operating profit margin (OPM). ICRA also notes the diversified customer base of SSPL, supported by a wide network of over 500 dealers. Recently, the company set up a 70,000-MTPA wire rod mill to diversify its product profile and revenue base. Going forward, the company is likely to witness continued growth in revenues and profitability, led by the ramp-up of the recently operationalised wire rod mill.

The rating is constrained by the company's leveraged capital structure, given that it incurred huge debt-funded capex between FY2021 and H1 FY2024 towards expanding its capacity, setting up wire rod mill, investing in captive power sources, among others. While the company's operating performance consistently improved during the said period, debt-funded nature of the capex led to an increase in the leverage levels and a moderation in the credit metrics. Going forward, the ability of the company to ramp up operations of its new capacities in a timely manner would be an important credit rating factor. The ratings are also tempered by the highly commoditised and fragmented nature of the secondary steel industry, resulting in intense competition, thereby limiting the company's pricing flexibility. The company's margins remain susceptible to volatility in raw material prices. Additionally, the company remains exposed to the inherent cyclicality in the steel industry, which keeps its profits and cash flows volatile.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company will continue to benefit from its integrated nature of operations, which along with the ramp-up of new capacities and limited capital expenditure (capex) plans are expected to keep the credit metrics at comfortable levels over the near-to-medium term.

Key rating drivers and their description

Credit strengths

Extensive experience of promoters in the steel business and established track record of operations; location specific advantages – Operating for around two decades in the steel industry, the company has established itself as one of the leading TMT bar manufacturers in Karnataka. The company is promoted by Mr. Vivek Kejriwal, who has over 20 years of experience in the steel industry. The company also benefits from the location-specific advantages due to its proximity to raw material sources (mainly iron ore/iron ore pellets), which results in freight cost savings, thereby supporting OPM. ICRA also notes the diversified customer base of SSPL, supported by a wide network of over 500 dealers.

Backward integrated operations support cost competitiveness and result in healthy contribution levels – SSPL has manufacturing facilities for sponge iron, which along with scrap serves as a feedstock for manufacturing MS billets. It further manufactures TMT bars using mostly in-house produced MS billets, which give SSPL a cost advantage over other secondary steel producers, which depend on sourcing costlier inputs from the market. Additionally, SSPL has captive power sources in the form of 10-MW waste heat recovery boiler (WHRB), 10-MW solar plant (increased by 5 MW in the current fiscal) and 8-MW wind power plant, which cater to around 60-70% of the company's energy requirement. The company has also entered into power purchase agreements (PPA) under the group captive model to source power at cheaper rates, thereby minimising dependance on high tariff power from the grid. All these factors support the cost competitiveness of SSPL and result in healthy contribution levels. Going forward, after the wire rod mill is set up, the operational profile is expected to further improve and result in continued healthy contribution levels.

Improving operating profile; healthy revenue growth and OPM expansion witnessed in the recent years – The company's revenues increased at a healthy compounded annual growth rate (CAGR) of 14% during FY2018-FY2023 and touched Rs. 776 crore in FY2023 on the back of volume and realisation growth. The OPM has expanded from 4.1% in FY2018 to 8.9% in FY2023, led by an increase in the share of margin accretive TMT bars within the overall sales mix and benefits of investment in captive power sources, leading to a substantial reduction in power costs. In the current fiscal, the company has set up a 70,000-MTPA facility for manufacturing wire rods, which have diversified applications across various industries. To meet billet requirement for the same, the company is expanding its induction furnace capacity by 50,000 MTPA (expected to be completed in December 2023). The company has also set up an additional 5-MW solar plant in the current fiscal to meet the incremental power requirements. Going forward, the company's revenue and profitability growth would be largely led by the ramp-up of the recently operationalised wire rod mill.

Credit challenges

Leveraged capital structure – Over the past three years (FY2021 – FY2023), the company has incurred large debt-funded capex (~75% funded by debt and ~25% from internal accruals) towards capacity expansion and setting up solar/wind power plants. Besides, the company bought back equity shares and partly redeemed its preference shares during FY2020-FY2022, which resulted in cash outflow of ~Rs. 33 crore. These factors led to an increase in the gearing to 1.8x as on March 31, 2023, from 0.5x as on March 31, 2020. However, ICRA notes the improvement in the company's performance during this period in the form of higher sales volumes of billets and TMT bars and substantial power cost savings. In the current fiscal, the company has set up a wire rod mill with a capacity of 70,000 MTPA and is also expanding its induction furnace capacity by 50,000 MTPA (expected to be completed by December 2023). Besides, the company has set up an additional 5 MW solar power plant in the current fiscal to meet incremental power requirements for the new capacities. The capex for the above-mentioned projects is around Rs. 93 crore (partly incurred in FY2023 and the balance in YTD FY2024), which was funded by 80% debt and 20% internal accruals. While the company's operating performance consistently improved during the said period, debt-funded nature of the capex led to an increase in the leverage levels with total outside liabilities-to-tangible net worth ratio (TOL/TNW) of 2.3 times as on March 31, 2023, and a moderation in the credit metrics with total debt-to-operating profit ratio (Total Debt/OPBITDA) of 3.2 times as on March 31, 2023. While there are no major capex plans in H2 FY2024 and FY2025, the company has sizeable debt repayments of Rs. 26 crore in FY2024 (out of which ~Rs. 7.7 crore was repaid in 4M FY2024) and Rs. 36 crore in FY2025. Going forward, the ability of the company to ramp up operations of its new capacities in a timely manner would be an important credit rating factor.

Highly commoditised and fragmented nature of secondary steel industry; margins susceptible to volatility in raw material prices – The company operates in a highly commoditised industry with raw material and power cost accounting for 70-80% of the revenues. The secondary steel industry is intensely competitive owing to low product differentiation and low entry barriers. Intense competition in the industry limits pricing flexibility, which restricts scope for an improvement in profitability. The company's profit margins also remain susceptible to volatility in major raw material prices such as iron ore and scrap. ICRA, however, notes that the company has largely been able to pass on the increase in raw material prices to its customers.

Exposure to cyclicality inherent in steel industry; geographical concentration risk – The company's operations are vulnerable to any adverse change in the demand-supply dynamics in the end-user industries such as infrastructure, real estate, among others. The cyclicality inherent in these sectors is likely to keep the company's profits and cash flows volatile. Also, the company's operations are mainly concentrated in Karnataka, exposing it to the geographical concentration risk. A slowdown in steel demand in its key addressable markets could lead to an overall decline in its revenues and profits.

Liquidity position: Adequate

The company's liquidity position is **adequate** marked by cushion in the form of unutilised working capital limits and steady growth in fund flow from operations in the business, led by improving operating profile. The company's average working capital limit utilisation stood in the range of 75-80% during the 12-month period ended in September 2023. While there are no major capex plans in H2 FY2024 and FY2025, the company has sizeable debt repayments of Rs. 26 crore in FY2024 (out of which ~Rs. 7.7 crore was repaid in 4M FY2024) and Rs. 36 crore in FY2025. Given the increasing revenues and improving profit margins, the fund flows in FY2024 and FY2025 are likely to be sufficient to meet the debt servicing and incremental working capital requirements, thereby limiting reliance on external debt.

Rating sensitivities

Positive factors – The rating could be upgraded if the company is able to increase its revenues and/or profitability, which leads to an improvement in the overall financial profile and the liquidity position.

Negative factors – The rating could be downgraded if there is a deterioration in the company's earnings or in case of large debt-funded capex/investment, which adversely impacts the credit metrics and/or the liquidity position. Specific credit metric for rating downgrade includes debt service coverage ratio (DSCR) remaining below 1.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology](#) [Iron and Steel](#)
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

About the company

Incorporated in 2003, SSPL manufactures sponge iron, billets and TMT bars. The company's manufacturing unit is in Tumkur district, Karnataka, and supplies TMT bars and other products all over Karnataka and other states in South India. The capacities include 90,000 MTPA of sponge iron; 1,50,000 MTPA of billets (to be expanded by 50,000 MT in December 2023), 1,50,000 MTPA of TMT bars and wire rod mill of 70,000 MTPA (operationalised in the current fiscal). The company also has a 10-MW waste heat recovery boiler, 10-MW captive solar plant (increased by 5 MW in the current fiscal) and 8-MW captive wind power plant. The company sells its TMT bars under the brand names, Sunvik and Om Sai.

Key financial indicators (Standalone, Audited)

	FY2022	FY2023
Operating Income	654.7	776.3
PAT	25.5	27.0
OPBDIT/OI	7.4%	8.9%
PAT/OI	3.9%	3.5%
Total Outside Liabilities/Tangible Net Worth (times)	2.6	2.3
Total Debt/OPBDIT (times)	3.3	3.2
Interest Coverage (times)	6.4	4.3

Source: Company; PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; All ratios as per ICRA calculations

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 (Rs. Crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					07-Dec-2023	-	-	-
1	**Fund-based Term Loan**	Long-term	30.00	30.00*	[ICRA]A-(Stable)	-	-	-

*as on date

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based Term Loan	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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. Crore)	Current Rating and Outlook
NA	**Term Loan**	FY2024	8-9%	FY2030	30.00	[ICRA]A-(Stable)

Source: Company

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

Annexure II: 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.

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