

April 08, 2021

Tata Metaliks Limited: Ratings continue to remain on Watch with Developing Implications

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
CP Programme ¹	100.00	100.00	Rating of [ICRA]A1+& continues to remain on Watch with Developing Implications
LT- Fund-based limits	318.00	318.00	Rating of [ICRA]AA-& continues to remain on Watch with Developing Implications
ST- Non-fund based limits	340.00	340.00	Rating of [ICRA]A1+& continues to remain on Watch with Developing Implications
Total	758.00	758.00	

LT- Long term; ST- Short term; *Instrument Details are provided in Annexure 1

Rationale

The ratings of Tata Metaliks Limited (TML) continues to remain on Watch with Developing Implications, owing to the ongoing merger with Tata Steel Long Products Limited (TSLPL, rated at [ICRA]A1+), subject to receipt of requisite statutory and regulatory approvals. ICRA will continue to monitor the development of the merger process and the timelines involved and will take appropriate action as may be required.

The rating action considers an estimated improvement in profitability and debt coverage indicators in FY2021 on the back of a significant increase in pig iron prices, supported by a recovery in demand from addressable markets. In 9M FY2021, TML's operating profit margins improved by 900 basis points (bps) to reach ~20.0%, leading to comfortable debt coverage indicators with interest coverage and Total Debt/OPBDITA at around 14.0 times and 0.21 times (annualised), respectively against 8.3 times and 1.15 times, respectively in FY2020. With pig iron prices improving further in January-March 2021, the financial performance of the company is expected to improve further in Q4 FY2021, leading to strong debt coverage indicators. ICRA expects TML's interest coverage for FY2021 to be ~16x and DSCR to be ~11x. While the capital structure remains strong, with total debt to tangible net worth estimated to be ~0.2x as of end FY2021, the company also has adequate cushion in working capital limits, thus imparting considerable financial flexibility. Although the company has sizeable capital expenditure (capex) plans over the medium term, healthy accruals to reserves would continue to keep the capital structure conservative.

The ratings continue to favourably factor in the integrated nature of TML's business, which reduces the vulnerability of the company's cash flows to fluctuation in input prices. The company has undertaken various process improvement initiatives in the recent past, which have strengthened its operating profile. The ratings further consider the established presence of the company in the DIP business, the long-term outlook of which continues to remain favourable, thus mitigating the risks associated with the cyclical nature in the pig iron business to an extent. In the pipe business, volumes were impacted in 9M FY2021, impacting DIP profitability. However, TML has a healthy order book, which is expected to keep the capacity utilisation at an elevated level, going forward. While the company has plans to increase the capacity of DI pipes over the medium term, it

¹ While assigning the rating, ICRA notes that the proceeds from the rated CP Programme are intended to be utilized for funding the working capital requirements, as per the objects of the issue. A deviation from the above that has the effect of exerting pressure on the asset-liability position of the company would be a rating sensitivity.

would remain exposed to the cyclical nature of the pig iron business till the enhanced DIP capacities are commissioned. Moreover, the fixed price lowest bidder (L-1)-based nature of the DIP business keeps realisations under check for all DIP players, including TML. While the large capex plans expose the company to project implementation risks, the experience of the management in setting up and managing such facilities in the past mitigate such risks to a large extent. In addition, it would strengthen the operating profile of the company with increasing share of revenue from the value-added DIP business and further improvement in the operating cost structure. The healthy long-term demand outlook for the DIP business also reduces demand related risks once the enhanced facilities are commissioned. ICRA expects TML's cash flows to remain comfortable relative to its debt service obligations, going forward. The ratings continue to be supported by the company's high financial flexibility with established relationships with banks, and its status as a 60.03% subsidiary of TSL.

Key rating drivers and their description

Credit strengths

Strong financial risk profile and healthy debt coverage indicators; significant improvement estimated in FY2021 – The financial performance remained strong with healthy profits and cash generation in the last three financial years. There is no long-term debt as on date, leading to a conservative capital structure. In FY2021, the profitability and debt coverage indicators are estimated to further improve on the back of a significant increase in pig iron prices, supported by a strong rebound in demand. In 9M FY2021, TML's operating profit margins improved by 900 basis points (bps) to reach ~20.0%, leading to comfortable debt coverage indicators with an interest coverage and Total Debt/OPBDITA at around 14.0 times and 0.21 times (annualised), respectively against 8.3 times and 1.15 times, respectively in FY2020. With pig iron prices improving further during January-March 2021, the financial performance of the company is expected to improve further in Q4 FY2021 as well, leading to strong debt coverage indicators. ICRA expects TML's interest coverage for FY2021 to be ~16x and DSCR to be ~11x. While the capital structure remains strong, with total debt to tangible net worth estimated at ~0.2x as of end FY2021, the company also has adequate cushion in working capital limits, thus imparting considerable financial flexibility.

Integrated nature of operations reduces vulnerability of cash flows to fluctuation in input prices – The company is one of the largest producers of foundry-grade pig iron in the country with an installed capacity of 550,000 metric tonnes per annum (MTPA). A significant portion (~40%) of the hot metal produced is used in the DIP business, and the rest of the pig iron, primarily of the foundry grade, is used by the foundry industry to manufacture castings. Over the years, TML has taken various cost improvement initiatives viz. commissioning of a sinter plant in FY2013, and a 10-MW power plant in FY2017, which operates on the flue gas of coke-oven plants (set up under BOOT basis). In January 2019, the company had commissioned a coal injection plant to partially replace coke with pulverised coal, which is expected to significantly save costs for the company. In February 2021, the company has commissioned another coke-oven capacity (under BOOT basis), which is likely to significantly reduce dependence on external coke. A new power plant (of 11.5 MW) is also likely to be commissioned shortly to meet the incremental demand for the enhanced DIP capacity.

Long-term favourable demand outlook for DIP in India; healthy order book position for the company – The DIP division has been operating at its full capacity for the last couple of years. The long-term demand outlook for DIP is likely to remain favourable, given the Government's thrust on infrastructure development. Though volumes were impacted in 9M FY2021, thus impacting DIP profitability, TML has a healthy order book of around 18-20 months, which is expected to keep the capacity utilisation at an elevated level, going forward.

Planned capital expenditure likely to further strengthen the operating profile of the company, going forward – The company has large capex plans over the medium term towards cost improvement initiatives as well as capacity addition for the DI pipe. While the first phase of DIP expansion is expected to commence operation by the last quarter of FY2022, the second phase would take another 9-10 months. However, ICRA notes that the entire portion of the balance capital cost is likely to be funded through internal accruals, given the healthy cash generation expected going forward. Besides, over the long term, it would strengthen the operating profile of the company with increasing share of revenue from the value-added DIP business and

further improvement in the operating cost structure. A healthy long-term demand outlook for the DIP business will also reduce demand related risks once the enhanced facilities are commissioned.

Status of the company as a part of the Tata Group – The ratings continue to be supported by the company’s high financial flexibility with established relationships with banks and status as a 60.03% subsidiary of TSL.

Credit challenges

Profit and cash flows exposed to the cyclical nature of the pig-iron business – Raw materials account for the major portion of the operational cost for pig iron players, including TML, and are thus important determinants of profitability. As pig-iron business is cyclical in nature, it is exposed to margin risks arising from temporary mismatch in prices of raw materials and pig iron, causing volatility in profitability and cash flows. The backward as well as forward integration facilities available with the company, however, mitigate such risks to an extent.

L-1 based bidding system for orders results in range-bound profitability in the DIP division – The major portion of DIP’s sales takes place through tenders where the lowest bidder is awarded the contract. This results in significant price-based competition, which keeps the profitability under check. However, healthy long-term demand outlook is expected to keep the capacity utilisation of the players at a healthy level.

Liquidity position: Strong

TML enjoys considerable financial flexibility for being a part of the Tata Steel Group, which has demonstrated its ability to refinance debt at attractive terms, given its established relationships with banks. ICRA notes that TML had liquid investment and cash balance of ~Rs. 186 crore as of December 2020 (including advances to a Group company). The capex is likely to be entirely funded through internal accruals.

Rating sensitivities

Positive factors – The near-term rating upgrade looks unlikely till the conclusion of the announced merger with Tata Steel Long Products Limited.

Negative factors – Pressure on the ratings could emerge in case of a significant reversal in the industry conditions, leading to weakness in credit metrics on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Ferrous Metals Industry
Parent/Group Support	Parent/Group Company: Tata Steel Limited (TSL) TML is a 60.03% subsidiary of TSL, with proven track record of financial support received from the parent in the past. However, going forward, ICRA does not envisage any requirement of financial support.
Consolidation/Standalone	For arriving at the ratings, ICRA has analysed TML on a standalone basis.

About the company

TML was set up as a joint venture between (JV) TSL and West Bengal Industrial Development Corporation (WBIDC) in 1991 to manufacture pig iron. The company had two manufacturing units – one in Kharagpur, West Bengal and the other in Redi, Maharashtra. However, due to sustained losses in the Redi unit, it was closed in FY2013. TML is a part of the Tata Group of Companies, with TSL owning 60.03% of the company's equity capital. TML also manufactures DIP in its Kharagpur plant, a forward integration unit of the pig iron business. The DIP business was set up in 2007 in collaboration with Kubota Corporation of Japan (KC) and Metal One Corporation of Japan (MOC). The respective stakes of TML, KC and MOC in the JV stood at 51%, 44% and 5%, respectively. Subsequently, TML increased its stake in the DIP business to 100%, making it a wholly-owned subsidiary. TML merged the wholly-owned subsidiary, Tata Metaliks DI Pipes Limited, with itself, with effect from April 1, 2016. In November 2020, a merger with TSLPL has been announced, which is currently ongoing and is subject to receipt of requisite statutory and regulatory approvals.

Key financial indicators (audited)

TML Standalone	FY2019	FY2020	9MFY2021
Operating Income (Rs. crore)	2,155.11	2,050.63	1,255.80
PAT (Rs. crore)	181.89	165.96	144.82
OPBDIT/OI (%)	14.24%	14.02%	19.60%
RoCE (%)	29.82%	23.29%	
Total Outside Liabilities/Tangible Net Worth (times)	0.78	0.82	
Total Debt/OPBDIT (times)^	0.63	1.15	0.21
Interest Coverage (times)	6.90	8.30	13.96
DSCR (times)	2.62	6.93	

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net Worth + Deferred Tax Liability - Capital Work in Progress); DSCR: (PBIT + Mat Credit Entitlements - Fair Value Gains through P&L - Non-cash Extraordinary Gain/Loss)/(Interest + Repayments made during the Year); ^without considering lease liability

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2022)			Rating History for the Past 3 Years								
		Type	Amount Rated	Amount Outstanding (Dec 2020)	Current Rating	FY2021			FY2019		FY2018		
					April 08, 2021	Nov 24, 2020	June 29, 2020	Feb 28, 2019	Sep 13, 2018	Nov 27, 2017	Sep 15, 2017	April 12, 2017	
1	Fund Based Limits	Long Term	318.00	69.0	[[ICRA]AA-&	[[ICRA]AA-&	[[ICRA]AA-(Stable)	[[ICRA]AA-(Positive)	[[ICRA]AA-(Stable); O/s	[[ICRA]AA-(Stable)	[[ICRA]A+(Positive)	[[ICRA]A+(Positive)	
2	Term Loan	Long Term	-	-	-	-	Withdrawn	[[ICRA]AA-(Positive)	[[ICRA]AA-(Stable); O/s	[[ICRA]AA-(Stable)	[[ICRA]A+(Positive)	[[ICRA]A+(Positive)	
3	Non fund based Limits	Short Term	340.00	-	[[ICRA]A1+&	[[ICRA]A1+&	[[ICRA]A1+	[[ICRA]A1+	[[ICRA]A1+; O/s	[[ICRA]A1+	[[ICRA]A1+	[[ICRA]A1+	
4	Commercial Paper	Short Term	100.00	-	[[ICRA]A1+&	[[ICRA]A1+&	[[ICRA]A1+	[[ICRA]A1+	[[ICRA]A1+; assigned	-	-	-	

& denotes watch with developing implications

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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	Fund Based Bank Facilities	NA	NA	NA	318.00	[ICRA]AA-&
NA	Non-Fund Based facilities	NA	NA	NA	340.00	[ICRA]A1+&
NA	Commercial Paper	Unplaced	Unplaced	Unplaced	100.00	[ICRA]A1+&

Source: Company; & denotes watch with developing implications

Annexure-2: List of entities considered for consolidated analysis

Company Name	TML Ownership	Consolidation Approach
Not Applicable		

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