

India Ratings Revises Panchmahal Steel's Outlook to Negative; Affirms at 'IND BBB'

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India Ratings and Research (Ind-Ra) has revised Panchmahal Steel Limited's (PSL) Outlook to Negative from Stable, while affirming its Long-Term Issuer Rating at 'IND BBB'. The instrument-wise rating actions are as follows:

| Instrument Type | Date of Issuance | Coupon Rate | Maturity Date | Size of Issue (million) | Rating/Outlook | Rating Action |
|--------------------------------------|------------------|-------------|---------------|-------------------------|--------------------------|---|
| Fund-based working capital limit | - | - | - | INR900 | IND BBB/Negative/IND A3+ | Outlook revised to Negative from Stable; Affirmed |
| Non-fund-based working capital limit | - | - | - | INR1,320 | IND A3+ | Affirmed |

The Outlook revision reflects a significant decline in PSL's EBITDA margin during FY23, resulting in deterioration in the credit metrics, and Ind-Ra's expectation that the operational performance will remain vulnerable to raw material price fluctuations over the near term.

Key Rating Drivers

Sharp Decline in EBITDA Margin in FY23: PSL's EBITDA margin declined significantly to a modest 3.19% in FY23 (FY22: 13.44%) and its EBITDA per tonne too dropped, on account of high volatility in the input cost and reduced demand. The return on capital employed also deteriorated to 3% in FY23 (FY22: 29%). Ind-Ra expects the margins to remain susceptible to fluctuations in the raw material prices and thus margin to improve yoy but remain moderated over the near-to-medium terms.

Presence in a Highly Competitive and Cyclical Stainless-Steel Industry: PSL's products are specialised stainless-steel products such as stainless-steel wire, bright bar and wire rod used in various industries, with automobiles and capital goods being large demand segments. Thus, the demand for such products is largely linked to the demand in these segments which closely follow the macroeconomic cycle. Furthermore, the presence of a large number of unorganised players in the stainless-steel products manufacturing industry results in limited bargaining power of the players, thus restricting their profitability.

Continued Medium Scale of Operations: After growing 69% yoy during FY22, PSL's revenue fell 14.7% yoy to INR4,871 million in FY23, due to subdued demand from the end-user market resulting in a reduction in the sales volume. Weak international demand, continued geopolitical tensions (the Russia-Ukraine war) and global inflationary headwinds impacted overall exports in FY23. Thus, PSL's export revenue fell around 5% yoy in FY23 to 20%. During 1QFY24, the company achieved a revenue of INR1,073.7 million. PSL expects to report an improved yoy revenue performance during 2QFY24 on the back of an outstanding orderbook of INR500 million-600 million at end-July 2023 which is likely to be executed during 3QFY24. The scale of operations remains medium. Ind-Ra expects PSL's revenue to improve moderately over the medium term due to an increase in its capacity utilisation on the back of the likely recovery from domestic and export markets.

Deterioration in Credit Metrics: PSL's credit metrics deteriorated yoy in FY23 owing to a decline in the absolute EBITDA to INR155.34 million in FY23 (FY22: INR768.10 million; FY21: INR247.13 million). The interest coverage (operating EBITDA/gross interest expense) was 2.19x in FY23 (FY22: 13.02x, FY21: 2.43x) and the net financial leverage (adjusted net debt/operating EBITDA) was 6.54x (1.04x, 5.25x). However, Ind-Ra expects the credit metrics to improve yoy in FY24, backed by a likely improvement in the operating performance amid the absence of any debt-funded capex.

Liquidity Indicator - Stretched: The average maximum utilisation of PSL's fund-based limits was 71.42% over the 12 months ended July 2023. PSL's cash and cash equivalents stood at INR0.44 million in FY23 (FY22: INR30.83 million, FY21: INR8.25 million). The company's net working capital cycle elongated to 157 days in FY23 (FY22: 144 days, FY21: 204 days); the creditor days reduced to 21 (30, 48) since PSL made early payments to its suppliers. PSL's cash flow operations turned negative at INR367 million in FY23 (FY22: INR322 million), majorly on the back of a fall in the absolute EBITDA. Consequently, the free cash flows turned negative at INR434 million in FY23 (FY22: INR263 million). However, comfort can be derived from the company not having any debt-funded capex over the near term and its nil reliance on term debt. Ind-Ra expects the cash flows to remain positive over the medium term, supported by positive changes in working capital, along with a yoy improvement in operating profitability.

Established Presence in Steel Industry: PSL has a presence of about five decades in the steel market and produces various modified chemistries for customer-specific applications. It has fully integrated facilities from steel melting to cold finishing and offers a range of stainless-steel grades, in hot rolled wire rod & bars and cold finished bars & wires. PSL operates with an installed capacity of 72,000 metric tonnes per annum (mtpa) for bars, rods, coils & wires and a stainless-steel melting shop of 1,50,000mtpa for steel billets. The company also has an established marketing network in both domestic and export market, which has supported it in building an established client base and a strong market position over the years.

Forex Risk: PSL's imports account for over 75% of its purchases and exports account about 20% of its sales, thus, on an average, 20% of the forex risk is mitigated through natural hedging. According to the management, the cost of hedging is higher than the forex loss the company incurs and hence no hedging is opted for.

Rating Sensitivities

Positive: An increase in the scale of operations with an improvement in the credit metrics and liquidity, leading to the interest coverage increasing above 3x, on a sustained basis, will be positive for the ratings.

Negative: Substantial deterioration in the scale of operations and profitability, leading to deterioration in the liquidity position and the interest coverage staying below 3x, will be negative for the ratings.

Company Profile

Based in Vadodara, Gujarat, PSL is a company promoted by Ashok Malhotra in 1972. The company is listed on BSE Ltd. It is engaged in the manufacturing of stainless-steel products such as wires, welding wires, wire rod, wire bars and wires for knitting, with an installed capacity of 72,000mtpa that was utilised at 27% as on 31 March 2023. PSL has fully integrated facilities from steel melting to cold finishing, with range of stainless-steel grades, in hot rolled wire rod & bars and cold finished bars & wires.

FINANCIAL SUMMARY

| Particulars | 1QFY24 | FY23 | FY22 |
|-----------------------------|----------|----------|----------|
| Revenue (INR million) | 1,073.70 | 4,871.24 | 5,713.37 |
| EBITDAR (INR million) | 43.11 | 155.34 | 768.10 |
| EBITDAR margin (%) | 4.02 | 3.19 | 13.44 |
| Gross interest coverage (x) | 1.87 | 2.19 | 13.02 |
| Net leverage (x) | NA | 6.54 | 1.04 |
| Source: PSL; Ind-Ra | | | |

Non-Cooperation with previous rating agency

Not applicable

Solicitation Disclosures

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

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Rating History

| Instrument Type | Rating Type | Rated Limits (million) | Current Ratings/Outlook | Historical Rating/Outlook | |
|--------------------------------------|----------------------|------------------------|--------------------------|---------------------------|------------------------|
| | | | | 2 August 2022 | 2 August 2021 |
| Issuer rating | Long-term | - | IND BBB/Negative | IND BBB/Stable | IND BBB-/Stable |
| Fund-based working capital Limit | Long-term/Short-term | INR900 | IND BBB/Negative/IND A3+ | IND BBB/Stable/IND A3+ | IND BBB-/Stable/IND A3 |
| Non-Fund based working capital Limit | Short-term | INR1,320 | IND A3+ | IND A3+ | IND A3 |
| Term loan | Long-term | - | - | WD | IND BBB-/ Stable |

Bank wise Facilities Details

[Click here to see the details](#)

Complexity Level of Instruments

| Instrument Type | Complexity Indicator |
|-----------------------|----------------------|
| Fund-based limits | Low |
| Non-Fund-based limits | Low |

For details on the complexity levels of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

Contact

Primary Analyst

Roma Gupta

Senior Analyst

India Ratings and Research Pvt Ltd

Wockhardt Towers, 4th Floor, West Wing, Bandra Kurla Complex, Bandra East, Mumbai - 400051

For queries, please contact: infogrp@indiaratings.co.in

Secondary Analyst

Ashish Kambli

Senior Analyst

+91 22 40356181

Chairperson

Abhash Sharma

Senior Director

+91 22 40001778

Media Relation

Ameya Bodkhe

Marketing Manager

+91 22 40356121

APPLICABLE CRITERIA

Evaluating Corporate Governance

Short-Term Ratings Criteria for Non-Financial Corporates

Corporate Rating Methodology

The Rating Process

DETAILED FINANCIAL SUMMARY

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