Press Release

Vallabh Steel Limited

10 July, 2017

Rating downgraded/Outlook revised

Total Bank Facilities Rated*	Rs.60.00 Cr
Long Term Rating	SMERA BB+/Stable (Downgraded from SMERA BBB and outlook revised from 'Negative')
Short term Rating	SMERA A4+ (Downgraded from SMERA A3+)

**Refer Annexure for details*

Rating Rationale

SMERA has downgraded the long-term rating to **'SMERA BB+' (read as SMERA double B plus)** from 'SMERA BBB' and short term rating to **'SMERA A4+' (read as SMERA A four plus)** from 'SMERA A3+' (read as SMERA A three plus) on the Rs. 60.00 crore bank facilities of Vallabh Steel Limited (VSL). The outlook is revised from 'Negative' to **'Stable'.**

VSL, incorporated in 1980 is engaged in the manufacturing of cold rolled coils and ERW Black and galvanised pipes. The manufacturing plant is located at Ludhiana, Punjab and has installed capacity of 40,000 MTPA for cold rolled coils and 7,500 MTPA for galvanised pipes. The downgrade is in view of significantly lower than expected growth in revenues and likelihood of reduced funding support from promoters going forward, since the promoters may be required to extend support to Vardhaman Industries Limited (VIL), a much larger company which has been recently classified as a Non Performing asset.

Analytical approach: During the previous rating exercise, SMERA had combined the business and financial risk profiles of VIL and VSL for analytical purposes. The consolidated approach was based on the premise that these companies, collectively referred to as the Vallabh group, were in the same line of business, and under the same promoter group and management and there would be operational and financial linkages.

However, SMERA has now adopted a standalone approach owing to the following reasons: No operational linkages between the companies since FY2015-16, separate directors in both the companies and the companies not being disclosed as related to each other in their respective annual reports. VSL has not extended any financial support to VIL as was envisaged during the initial rating. This indicates an absence of financial fungibility even in times of distress. Hence SMERA has decided to adopt a standalone approach.

List of key rating drivers and their detailed description:

Strengths:

Assured offtake from JSW Vallabh Tinplate Private Limited (JSW VTPL): VSL entered into a sale agreement with JSW VTPL in August 2015 with minimum off take clause thereby providing revenue visibility over the medium term. The agreement is for three years. The pricing is reviewed monthly and based on JSW's HR price. While on the one hand, VSL is assured of a definite offtake on account of the agreement, the same also exposes VSL to customer concentration risk. Presently, sales under the agreement are expected to contribute around 60 per cent to VSL's revenue. Any business pressure faced by JSW VTPL could translate into pressure for VSL.

SMERA believes that the assured offtake from JSW VTPL protects the company's revenues from threat of cheaper imports.

Weaknesses:

Uneven revenue trend: Revenues of VSL have been uneven during the period under study. Revenues declined from Rs.169.60 crore in FY2013-14 to Rs.137.70 crore in FY2014-15. In FY2015-16, revenues improved marginally by 3 per cent to Rs.141.92 crore. As per FY2017 (Provisional), revenue stood at Rs.119.98 crore, a 15 per cent decline over the previous year. The net cash accruals also declined during the period under study from Rs.3.70 crore in FY2013-14 to Rs.2.00 crore in FY2015-16. As per FY2017 (Provisional), the net cash accruals stood at Rs.3.78 crore.

Moderate financial risk profile: The financial risk profile of VSL continues to remain average marked by gearing of 1.14 times as on 31 March, 2016 as against 1.19 times in the previous year. The networth stood at Rs.43.82 crore as on 31 March, 2016. The coverage indicators are moderate with interest coverage ratio of 1.58 times and debt service coverage ratio of 1.49 times for FY2015-16. The profitability of VSL continues to remain low with ROCE at 6.22 per cent in FY2015-16 (5.12 per cent in FY2014-15) while NCA/TD fell to 0.04 times in FY2015-16 from 0.06 in FY2014-15.

Working capital intensive operations: The working capital cycle of the company is elongated due to high debtor days of 147 days. Further, the gross current asset days stood at 216 days for FY2016 as against 213 days in the previous year. Significant elongation in the working capital cycle is likely to translate into increased dependence on external funding. The average cash credit limit utilisation has been 78.89 per cent for the last six months ended 31 March, 2017.

Susceptibility of performance to changes in regulatory regime: The iron and steel sector has been facing competition from imports from countries like China. The government has imposed an anti-dumping duty on certain steel products from China. However, VSL's operations are susceptible to unfavourable changes in the import regulations.

Outlook - Stable

SMERA believes that the outlook on VSL will remain stable over the medium term. The outlook may be revised to 'Positive' in case the company registers significant increase in its revenue and profitability while improving its liquidity position and coverage indicators. The outlook may be revised to 'Negative' in case of deterioration in its financial risk profile and elongation of working capital cycle.

About the Rated Entity – Key Financials

For FY2015-16, VSL reported net profit after tax (PAT) of Rs.1.36 crore on operating income of Rs.141.92 crore as compared with PAT of Rs.2.28 crore on operating income of Rs.137.70 crore in FY2014-15. The tangible networth stood at Rs.43.82 crore as on 31 March, 2016 as against Rs.42.45 crore in the previous year. As per provisional financials for FY2016-17, VSL reported net profit after tax (PAT) of Rs.0.73 crore on operating income of Rs.119.98 crore.

Applicable Criteria

- Manufacturing Entities – https://www.smera.in/criteria-manufacturing.htm
- Application of Financial Ratios and Adjustments: https://www.smera.in/criteria-fin-ratios.htm
- Default Recognition: https://www.smera.in/criteria-default.htm

Note on complexity levels of the rated instrument:
https://www.smera.in/criteria-complexity-levels.htm

Status of non-cooperation with previous CRA: CRISIL Ratings in its press release dated February 20, 2017 inter alia stated the following 'CRISIL has been consistently seeking information and a discussion with the management of Vallabh Steels Limited (VSL) since June 2016. Despite several emails and calls, the company has not submitted any information. CRISIL had, through letter dated February 9, 2017, informed the company of the extant guidelines and requested for cooperation. The issuer, however, remains non-cooperative.

The investors, lenders and all other market participants should exercise due caution while using the rating assigned/reviewed with the suffix 'ISSUER NOT COOPERATING'. These ratings lack a forward looking component as it is arrived at without any management interaction and is based on best available or limited or dated information on the company.'

Any other information: None

Rating History (Upto last three years):

Date	Name of the Facilities	Term	Amount (Rs. Crore)	Ratings/ Outlook
14 March, 2016	Cash Credit	Long Term	43.00	SMERA BBB/Negative (Assigned)
	Term Loan	Long Term	7.00	SMERA BBB/Negative (Assigned)
	Inland Letter of Credit	Short Term	10.00	SMERA A3+ (Assigned)

***Annexure – Details of instruments rated:**

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Crore)	Ratings/ Outlook
Cash Credit	N.A.	N.A.	N.A.	45.00	SMERA BB+/Stable (downgraded, outlook revised)
Term Loan	N.A.	N.A.	N.A.	7.00	SMERA BB+/Stable (downgraded, outlook revised)
Inland Letter of Credit - I	N.A.	N.A.	N.A.	8.00	SMERA A4+ (downgraded)

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ABOUT SMERA

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