Press Release

Calstar Sponge Limited

January 04, 2023

Rating Upgraded

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	24.00	ACUITE BBB+ | Stable | Upgraded | Positive to Stable	-
Bank Loan Ratings	15.30	-	ACUITE A2 | Upgraded
Total Outstanding Quantum (Rs. Cr)	39.30	-	-
Total Withdrawn Quantum (Rs. Cr)	0.00	-	-

Rating Rationale

Acuité has upgraded the long-term rating to **'ACUITE BBB+' (read as ACUITE triple B plus)** from '**ACUITE BBB' (read as ACUITE t riple B)** and also upgraded the short-term rating to **'ACUITE A2' (read as ACUITE A two)** from **'ACUITE A3+' (read as ACUITE A three plus)** on the Rs.39.30 Cr bank facilities of Calstar Sponge Limited (CSL). The outlook is revised from 'Positive' to **'Stable'.**

Rationale for the rating

The upgrade in the rating factors in the continual increase in the scale of operations and improvement in the financial risk profile of CSL, supported by the rally in steel prices and expected continuation of healthy performance in the current year as well, on account of sizeable cost savings emanating from the successful commissioning of WHRB captive power plant of 12 MW. Acuité notes that while steel prices have moderated from the all-time highs of April 2022 following the global uncertainty, the structural cost savings from such low-cost power arrangement would gradually reflect in CSL's earnings in FY2023 and FY2024. Moreover, CSL's scale of operations are expected to remain in the growth trajectory supported by the ramp-up in its production capacity in the last quarter of the current year, driven by the Government's thrust on infrastructure projects and pick-up in demand from the end-user industries such as real estate and construction. The low working capital intensity and prudent capital allocation policy, supported by its low receivable and inventory holding periods further supports the rating upgrade. The rating continues to draw comfort from the extensive experience of the promoters in the steel industry. Acuité notes that CSL's competitive capital cost and robust leverage levels have helped it to maintain a healthy financial risk profile.
The rating is, however, constrained by the company's margins being susceptible to the volatility in raw material prices along with the company's exposure to the inherent cyclicality in the steel industry. The rating is also constrained by the company's moderate client concentration risks, as the top-two clients accounted for ~28 per cent of the overall sales in FY2022.

About the Company

Calstar Sponge Limited (CSL) was incorporated in the year 2004, established by Mr. Tulsi Ram

Agarwal and Mr. Vikas Agarwal for the manufacturing of angles, sponge iron and billets. The current directors of the company are Mr. Tulsi Ram Agarwal, Mr. Vikas Agarwal, Mr. Rajiv Agarwal and Mr. Vinay Agarwal. CSL has two manufacturing facilities in West Bengal near Durgapur at Jamuria and Bamunara. Currently, the company has integrated steel manufacturing facilities for sponge iron (capacity- 1,46,000 MTPA), Billet (capacity – 73,000 MTPA) and a captive power plant of 12 MW in Jamuria Unit. The old Bamunara unit of Billet (capacity – 72,000 MTPA) and Rolling Mill Unit (48000 MTPA) has been rented out since May '22 of FY23 on a rental income of Rs 2.4cr per annum.

Analytical Approach

Acuité has taken a standalone view of the business and financial risk profile of CSL to arrive at the rating.

Key Rating Drivers

Strengths

Experienced management and established relationship with customers

CSL is promoted by Mr. Tulsi Ram Agarwal, Mr. Vikas Agarwal, Mr. Rajiv Agarwal and Mr. Vinay Agarwal who has nearly two decades of experience in the iron and steel industry. The long standing experience of the promoters and long track record of operations has helped them to establish comfortable relationships with key suppliers and reputed customers. Further, the clientele consists of majorly reputed players like SRMB Srijan Pvt Ltd. (ACUITE A+/Stable/A1+)and Shyam Steel Industries(CRISIL AA-) to name a few, which mitigates counterparty credit risk. Acuité derives comfort from the long experience of the management and believes this will benefit the company going forward, resulting in steady growth in the scale of operations.

Significant improvement in operating income

Supported by a strong rebound in steel demand post unlocking of the economy, CSL witnessed an improvement in its scale of operations marked by its revenues of Rs. 362.37 Cr in FY2022 as against Rs. 150.39 Crs in FY2021. The average realisations for sponge iron rallied sharply since FY2021 and improved by 48 per cent in FY2022. Such buoyant realisations led to a robust growth in the company's operating income in FY2022. This in turn kept CSL's EBITDA healthy at Rs. 30.80 crore in FY2022 vis-à-vis Rs. 16.85 crore in FY2021. The healthy financial performance continued in 7MFY2023 (prov) with the company achieving revenue of Rs. 220.39 Cr as the average realisations for sponge iron improved further by 4 per cent in H1 FY2023 compared to FY2022. However, Acuité believes the softening of realisations in recent months, in tandem with demand slowdown in the international market, is likely to result in a moderation in its profitability, going forward.

The operating margin moderated to 8.50 per cent in FY2022 from 11.21 per cent in FY2021 on account of rise in raw material costs. The PAT margin also declined to 5.13 per cent in FY2022 from 7.67 per cent FY2021. However, with the commissioning of the new billet plant and the captive power plant since December 2021, the integrated nature of operations is expected to enhance the operating efficiencies and mitigate the risks arising from the falling realisations and elevated coal and energy costs to some extent. The company's steel melting operation is highly power intensive. However, Acuité expects power generated through CSL's captive WHRB power plant at a cheap rate will meet a major part of its overall power requirement, which would positively impact the cost structure going forward.

Healthy financial risk profile, aided by low working capital intensity

The company's financial risk profile is marked by high net worth, low gearing and robust debt protection metrics. The tangible net worth of the company improved to Rs.100.68 Cr as on

March 31, 2022 from Rs.82.19 Cr as on March 31, 2021, on account of ploughing back of profits. Gearing of the company stood comfortable below unity at 0.12 as on March 31, 2022. As on March 31, 2022, the debt mainly comprised of short-term borrowings pertaining to cash credit utilisation. A low working capital intensity helped in limiting its dependence on external borrowings, thereby, strengthening its capital structure and coverage indicators. Total outside Liabilities/Tangible Net Worth (TOL/TNW) stood low at 0.45 times as on March 31, 2022 as against 0.35 times as on March 31, 2021. The robust debt protection metrics of the company is marked by Interest Coverage Ratio (ICR) at 89.87 times in FY 2022 as against 33.77 times in FY 2021; and Debt Service Coverage Ratio (DSCR) at 62.69 times in FY 2022 as against 24.81 times in FY 2021. The surge in earnings in FY2022 supported by minimal debt and high accruals led to further improvement in the credit metrics. Net Cash Accruals/Total Debt (NCA/TD) stood at 2.05 times as on March 31, 2022. Calibrated capex undertaken by CSL over the past two years, funded through internal accruals and fixed deposits together with low reliance on debt owing to healthy surplus cash accrual generation capacity of the business, has also helped it maintain comfortable leverage. Commensurate returns from the planned capex and optimal capacity utilisation will remain key credit monitorable for CSL.

Weaknesses

Inherent cyclical nature of the steel industry

The group's performance remains vulnerable to cyclicality in the steel sector given the close linkage between the demand for steel products and the domestic and global economy. The end-user segments such as real estate, civil construction and engineering also display cyclicality. Further, operating margins are vulnerable to volatility in the input prices (iron ore and coal) as well as realisation from finished goods. The prices and supply of the main raw material, iron ore, directly impacts the realisations of finished goods. Any significant reduction in the demand and prices adversely impacting the operating margins and cash accruals of the group will remain a key monitorable.

Client concentration risks

The company's operations are mainly concentrated in the eastern region, exposing it to geographical concentration risk. Any slowdown in steel demand in its key addressable markets in the eastern region could lead to an overall decline in its revenues and profits in the future. The customer concentration continues to be high, with around 28 per centof the sales being made to SRMB Srijan Pvt Ltd. (ACUITE A+/Stable/A1+)and Shyam Steel Industries, based in West Bengal.

Rating Sensitivities

- Growth in revenue with sustainability of the profitability margins
- Any deterioration of its financial risk profile and liquidity position
- Any elongation of the working capital cycle leading to deterioration in debt protection metrics
- Stabilization of operations post commissioning of capex

Material covenants

None

Liquidity Position: Strong

The company's liquidity position is strong, supported by healthy retained cash flows and sufficient undrawn limits. The company's negligible repayment obligation of ~Rs. 0.04 Cr in FY22 was comfortably serviced from the sufficient net cash accruals which stood at Rs.24.57 Cr as on March 31, 2022. The fund based limit remains moderately utilised at only ~22.34 per cent over the eight months ended November, 2022. The current ratio stood comfortable at 1.33 times as on March 31, 2022. The cash and bank balances of the company stood at Rs.18.77 Cr as on March 31, 2022, of this Rs.18.73 Cr is retained as current account balance and remaining as unencumbered cash. Further, the working capital management of the company is efficient as reflected by Gross Current Assets (GCA) of 39 days as on March 31, 2022 as against 89 days as on March 31, 2021. Acuité believes that going forward the company will continue to maintain adequate liquidity position owing to steady accruals backed by improvement in earnings led by high demand.

Outlook: Stable

Acuité believes that the outlook on the company will remain 'Stable' over the medium term on account of the long track record of operations, experienced management, sound business position, healthy financial risk profile and efficient working capital management. The outlook may be revised to 'Positive' in case of significant growth in revenue while achieving sustained improvement in operating margins and working capital management. Conversely, the outlook may be revised to 'Negative' in case of decline in the company's revenues or profit margins, or in case of deterioration in the company's financial risk profile or elongation in its working capital cycle.

Other Factors affecting Rating

None

Key Financials

Particulars	Unit	FY 22 (Actual)	FY 21 (Actual)
Operating Income	Rs. Cr.	362.37	150.39
PAT	Rs. Cr.	18.58	11.53
PAT Margin	(%)	5.13	7.67
Total Debt/Tangible Net Worth	Times	0.12	(0.02)
PBDIT/Interest	Times	89.87	33.77

Status of non-cooperation with previous CRA (if applicable)

Crisil, vide its press release dated February 26th, 2022 had downgraded the rating of Calstar Sponge Limited to 'CRISIL B/Stable/A4; ISSUER NOT COOPERATING'.

Any other information

None

Applicable Criteria

- Default Recognition :- https://www.acuite.in/view-rating-criteria-52.htm
- Manufacturing Entities: https://www.acuite.in/view-rating-criteria-59.htm
- Application Of Financial Ratios And Adjustments: https://www.acuite.in/view-rating-criteria-53.htm

Note on complexity levels of the rated instrument

In order to inform the investors about complexity of instruments, Acuité has categorized such instruments in three levels: Simple, Complex and Highly Complex. Acuite' s categorisation of the instruments across the three categories is based on factors like variability of the returns to the investors, uncertainty in cash flow patterns, number of counterparties and general understanding of the instrument by the market. It has to be understood that complexity is different from credit risk and even an instrument categorized as 'Simple' can carry high levels of risk. For more details, please refer Rating Criteria "Complexity Level Of Financial Instruments" on **www.acuite.in**

Rating History

Date	Name of Instruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
07 Feb 2022	Proposed Bank Facility	Short Term	1.80	ACUITE A3+ (Assigned)
	Cash Credit	Long Term	14.00	ACUITE BBB | Positive (Reaffirmed)
	Proposed Bank Facility	Long Term	10.00	ACUITE BBB | Positive (Assigned)
	Bank Guarantee	Short Term	5.00	ACUITE A3+ (Reaffirmed)
	Letter of Credit	Short Term	8.50	ACUITE A3+ (Reaffirmed)
11 Nov 2020	Bank Guarantee	Short Term	5.00	ACUITE A3+ (Assigned)
	Letter of Credit	Short Term	8.50	ACUITE A3+ (Upgraded from ACUITE A3)
	Cash Credit	Long Term	14.00	ACUITE BBB | Stable (Upgraded from ACUITE BBB- | Stable)
03 Nov 2020	Letter of Credit	ShortTerm	8.50	ACUITE A3 (Upgraded from ACUITE A4+)
	Cash Credit	Long Term	14.00	ACUITE BBB- | Stable (Upgraded from ACUITE BB+)
	Bank Guarantee	ShortTerm	5.00	ACUITE A3 (Assigned)

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Complexity Level	Quantum (Rs. Cr.)	Rating
Indian Bank	Not Applicable	Bank Guarantee/Letter of Guarantee	Not Applicable	Not Applicable	Not Applicable	Simple	6.80	ACUITE A2 | Upgraded
Indian Bank	Not Applicable	Cash Credit	Not Applicable	Not Applicable	Not Applicable	Simple	24.00	ACUITE BBB+ | Stable | Upgraded | Positive to Stable
Indian Bank	Not Applicable	Letter of Credit	Not Applicable	Not Applicable	Not Applicable	Simple	8.50	ACUITE A2 | Upgraded

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About Acuité Ratings & Research

Acuité is a full-service Credit Rating Agency registered with the Securities & Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI) for Bank Loan Ratings under BASEL-II norms in the year 2012. Acuité has assigned ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.

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