

Press Release

Arun Steel Agencies

July 05, 2019



Rating Downgraded

Total Bank Facilities Rated*	Rs.24.50 Cr.
Long Term Rating	ACUITE BB+ / Outlook: Stable (Downgraded from ACUITE BBB- /Stable)

* Refer Annexure for details

Rating Rationale

Acuite has downgraded long-term rating to '**ACUITE BB+**' (read as **ACUITE double B plus**) from **ACUITE BBB-** (read as **triple B minus**) to the Rs. 24.50 crore bank facilities of Arun Steel Agencies AGENCIES (ASA). The outlook is '**Stable**'.

The rating downgrade reflects sharp decline in the profitability margins, though the revenues are in line with the expectations. Operating margins have deteriorated to 3.46 per cent in FY2019 (provisional) against 5.49 per cent in FY2018; owing to volatile raw material prices, market penetration among others. However the rating continues to reflect improving scale of operations, its promoters' extensive experience in the steel industry and efficient working capital management. These strengths are partially offset by Average financial risk profile and stiff competition in the Steel industry.

About the firm

Arun Steel Agencies (ASA) established in 1994 as a proprietorship concern is promoted by Mr. V.C Arunai Vadivelan. Arun Steel is the sole authorised distributor of JSW Steel Limited for exclusive supply of steel wire rod coils across Tamil Nadu. The firm has its registered office and two warehouses located in Chennai and one is located at Trichy (Tamilnadu) for stocking inventory.

About the Group entity

The promoters during 2018 promoted a partnership concern 'Arun Steel Traders (AST)' as Mr V.C. Arunai Vadivelan and his wife Ms Sasikala and his son Mr. Sujjeth as partners. The firm is an authorised distributor jointly with its group firm 'Arun Steel Agencies' for exclusive supply of steel wire rod coils in Coimbatore region. AST started its operations in December, 2018. JSW, its principal has given an overall volume of 30600 metric tonnes (MOU) for both the firms.

Analytical Approach

Acuite has consolidated the business and financial risk profiles of ASA and AST (herewith referred to as ARUN STEEL group or group) to arrive at the rating. The consolidation is on account of common promoters and same line of business. Extent of Consolidation: Full

Key Rating Drivers

Strengths

Extensive experience of promoters and Long association with JSW:

Mr. V.C Arunai Vadivelan has nearly three decades of experience in the field of steel trading. The firm is initially engaged in the trading of steel products like Bright Bars, HR Coils/Sheets till 2000. From 2001 onwards, the firm is dealing only in Wire Rod coils. The firm has been dealing with JSW Steel Ltd since 2004, and long and healthy association with JSW supported in regular and steady supplies; leading to major revenue driver for the firm. Further, regular off-take by its vintage customers led to moderate growth in revenues over the past three years through FY2019 at a compound annual growth rate (CAGR) of 17.7 per cent at Rs.171.44 crores in FY2019 (Prov). To facilitate concentrated efforts and higher market share in Coimbatore region, the promoters have established 'Arun Steel Traders' and commenced operations in December 2018. Acuite believes that Arun Steel group will continue to benefit from its experienced promoter and long track record of operations in improving its business risk profile over the medium term. Further the revenue profile is expected to improve backed by regular off-take and moderate demand from the end user segment particularly automobile sector.

Efficient working capital management

The Group's operations are efficiently managed with gross current asset (GCA) days of about 90 days historically; comprises of inventory days of about less than a month, and extends credit of about two months. Its bank limits are utilized to the extent of about 93 per cent for past six months ended March 2019. Acuite believes that, being trading nature of operations with diversified client base, the working capital operations continues to be efficient and expected to be at similar levels over the medium term.

Weaknesses

Average financial risk profile

The financial risk profile of the group is average, marked by high gearing (debt-to- equity), high total outside liabilities to total networth (TOL/TNW) and moderate debt protection metrics. The networth of the group is modest at Rs. 10.07 Crs in FY2019 (provisional) as against Rs.8.49 Crs in FY2018. The group's gearing and TOL/TNW are high at 2.84 and 3.42 times as of March 31, 2019 as against 2.82 and 2.84 times in FY2018; high being trading nature of operations and modest margins. Its debt protection metrics are comfortable: Interest Coverage Ratio (ICR) at 2.14 times and Net Cash Accruals to Total Debt (NCA/TD) at 0.11 in FY2019 (provisional) vis-à-vis 3.29 and 0.22 times as on March 31, 2018; deterioration is owing to decline in its profitability margins in FY2019 owing to competition, expanding markets and client addition. Net cash accruals for FY2019 stood at Rs.2.23 crore. The group's cash accruals are expected to improve and be in the range of Rs.3.50-4.00 crore with repayment obligations nil. However, Acuite believes that trading nature of operations and expected improvement in revenue profile is expected to constrain the financial risk profile at similar levels over the medium term.

Highly fragmented and competitive business

Arun Steel Agencies' profitability margins are moderate in the range of 3.50 – 5.50 per cent over the past three years through FY2019; due to trading nature of operations. However, EBITDA margins declined from 5.49 per cent in FY2018 to 3.46 per cent in FY2019 (provisional). Further, volatile prices and commodity nature of products, without any volume and value commitment from the customers, is exposed to price sensitivity. Further, the prices of steel are linked to global prices due to changes in inputs costs. However, volatility in prices, to some extent, has been offset by moderate inventory levels being maintained by the group. Sustenance of the growth and profitability are key rating sensitivity factors over the medium term.

Liquidity Position:

Liquidity of Arun Steel Group is adequate marked by generation of cash accruals of Rs.2.33 crore in FY2019; and Rs.5.17 Crs in FY2018. Arun Steel Group is expected to generate cash accruals in the range of Rs.3.50 to 4.00 crore over the medium term against nil repayment obligations. It has a conservative debt approach as working capital cycle is reflected by the group's moderate bank limit utilisation levels at about 93 per cent for the past six months ended March 2019. The current ratio of Arun Steel Group is moderate at 1.36 times as on March 31, 2019. Acuite believes that the liquidity Arun Steel group continues to remain moderate supported by adequate accruals to backing the incremental working capital requirements.

Outlook: Stable

Acuite believes that the outlook on Arun Steel Group will remain 'Stable' over the medium term on account of its experienced promoter and long track record of operations. The outlook may be revised to 'Positive' in case of significant improvement in its revenues while maintaining the profitability margins and improving its capital structure. Conversely, the outlook may be revised to 'Negative' in case of any stretch in its working capital management or any significant unplanned debt-funded capital expenditure or significant withdrawal of capital leading to deterioration of its financial risk profile and liquidity.

About the Rated Entity - Key Financials

	Unit	FY19 (Prov)	FY18 (Actual)	FY17 (Actual)
Operating Income	Rs. Cr.	171.44	135.32	123.83
EBITDA	Rs. Cr.	5.93	7.43	5.72
PAT	Rs. Cr.	3.03	5.11	3.89
EBITDA Margin	(%)	3.46	5.49	4.62
PAT Margin	(%)	1.77	3.78	3.14
ROCE	(%)	16.46	25.01	22.37
Total Debt/Tangible Net Worth	Times	2.84	2.82	3.66
PBDIT/Interest	Times	2.14	3.29	3.23
Total Debt/PBDIT	Times	4.83	3.22	3.64
Gross Current Assets (Days)	Days	92	86	84

Any other information

Not Applicable

Applicable Criteria

- Default Recognition - <https://www.acuite.in/view-rating-criteria-17.htm>
- Trading entities- <https://www.acuite.in/view-rating-criteria-6.htm>
- Application of Financial Ratios and Adjustments: <https://www.acuite.in/view-rating-criteria-20.htm>

Note on complexity levels of the rated instrument

<https://www.acuite.in/criteria-complexity-levels.htm>

Rating History (Upto last three years)

Date	Name of Instrument / Facilities	Term	Amount (Rs. Cr.)	Ratings/Outlook
05-Nov-2018	Cash Credit	Long Term	9.50	ACUITE BBB- / Stable (Assigned)
	Secured Overdraft	Long Term	10.00	ACUITE BBB- / Stable (Assigned)
	Cash Credit	Long Term	5.00	ACUITE BBB- / Stable (Assigned)

*Annexure – Details of instruments rated

Name of the Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. Cr.)	Ratings/Outlook
Cash Credit	Not Applicable	Not Applicable	Not Applicable	9.50	ACUITE BB+ / Stable (Downgraded from ACUITE BBB- /Stable)
Overdraft	Not Applicable	Not Applicable	Not Applicable	10.00	ACUITE BB+ / Stable (Downgraded from ACUITE BBB- /Stable)
Cash Credit	Not Applicable	Not Applicable	Not Applicable	5.00	ACUITE BB+ / Stable (Downgraded from ACUITE BBB- /Stable)

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About Acuité Ratings & Research:

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