Press Release

Gagan Ferrotech Limited

January 08, 2021

Ratings

Sl. No.	Facility	Amount (Rs. Crore)	Ratings	Rating Action
1	Long Term Bank Facilities- Cash Credit	150.00	IVR A/Stable (IVR Single A with Stable Outlook)	Reaffirmed
2	Long Term Bank Facilities-Term Loan	60.72	IVR A/Stable (IVR Single A with Stable Outlook)	Reaffirmed
3	Short Term Bank Facilities-Letter of Credit/Bank Guarantee	93.75	IVR A1 (IVR Single A One)	Reaffirmed
	Total	**304.47 (Rupee Three hundred and Four crore and forty-seven lakhs only)**		

Details of Facilities are in Annexure 1

Detailed Rationale

The reaffirmation of ratings assigned to the bank facilities of Gagan Ferrotech Limited (GFL) continues to favourably factor in extensive experience of its promoters in the steel industry, locational advantage, benefits emanating from established brand with a strong market presence in Eastern India, expected benefit from capex which is being completed, sustained growth in operating profit & operating margin over the years, comfortable financial risk profile marked by satisfactory gearing with healthy debt protection metrics and prudent working capital management with healthy liquidity. However, these rating strengths are partially offset by vulnerability of the operating margins to fluctuating raw material prices given the commoditised nature of its products, intense competition in the operating spectrum and exposure to cyclicality in the steel industry.

Key Rating Sensitivities:

- Upward Rating Factors - Significant growth in scale of business with improvement in profitability metrics thereby leading to overall improvement in cash accruals which is higher than Infomerics expectation could lead to a positive rating action.
- Downward Rating Factor - Sharp dip in operating income and/or profitability impacting the debt coverage indicators, deterioration in working capital management and moderation in overall gearing to more than 1.5 times could lead to a negative rating action.

Detailed Description of Key Rating Drivers

- **Extensive experience of the promoters in the steel industry**

Mr. Vinay Kumar Agarwal has over two decades of experience in trading and manufacturing of iron and steel products. GFL ventured into manufacturing process in 2006 by setting up a sponge iron plant and over the years has expanded into billet, TMT with a captive power plant. The long track record has helped the company to build a healthy relationship with its customers and suppliers which have resulted in stable business risk profile.

- **Locational advantage**

The manufacturing facilities of GFL is located in Durgapur, West Bengal which is known as steel hub and is in close proximity to various raw materials in the form of iron ore, pellets, pig iron and iron scrap. Further, sourcing of coal from South Africa is not an issue as the company has developed a strong relationship with miners of South Africa for procurement of imported coal which has led to timely delivery of the same for the past many years. Presence in steel belt reduces the business risk to an extent.

- **Established brand with a strong market presence in Eastern India**

The company has a long track record of over a decade in the iron and steel industry. The long track record has helped the company to position itself among the established players in the eastern market. Currently, GFL is selling its TMT Bars in the eastern parts of India mainly in West Bengal, Jharkhand and Assam. In addition, the company is exports TMT bars produced to Nepal, Bangladesh and Sri Lanka. The company has nearly 500 dealers at present in the above-mentioned states. GFL is selling its TMT bars under the brand name “Gagan”. The established presence is also reflected from the revenue of Rs.920.68 crore in FY2020 as against Rs.924.47 crore in FY2019. Also, during the current year, the company has clocked revenue of Rs.346.11 crore in six months ended Sept 2020 (provisional). Infomerics believes that GFL's business risk profile will be supported by its established position in eastern India supported by its strong brand presence.

- **Expected benefit from capex which is being completed**

The company is likely to benefit from the sizeable capex which is being completed. GFL has increased its capacity in all the product lines (i.e. sponge iron, billets and rolling products) to 2.4 Lakhs,3.2 Lakhs,3 Lakhs MTPA respectively from 1.28 Lakhs,2.64 Lakhs,1.7 Lakhs MTPA respectively. The enhanced capacity will benefit in overall improvement in top-line going forward. Further, Infomerics notes that the company has utilized its own fund significantly higher than it was initially planned. The company has manufacturing facility for sponge iron, which along with MS scrap serves as a feedstock for manufacturing of MS billets. The manufactured MS billets are used to produce TMT bars. Further, to support its operations the company also has a 12MW captive power generation capacity utilizing waste heat recovered from the sponge iron kilns, which is meeting majority of the electricity requirement. Access to captive power also plays a vital role in terms of operational integration due to energy intensive nature of manufacturing. Semi- integrated nature of operations coupled with proximity to the source of raw materials & end user market provides a competitive edge to the company.

- **Sustained growth in operating profit & operating margin over the years**

The EBIDTA margin of the company improved from 5.89% in FY19 to 6.37 % in FY20. The improvement in profitability is majorly due to better cost management and reduction in raw material cost during the period under review. Infomerics believes that the company will maintain a same level of operating income & operating margin in FY21.

- **Comfortable financial risk profile marked by satisfactory gearing with healthy debt protection metrics**

The financial risk profile of GFL is marked by its healthy net worth base, comfortable gearing and healthy debt protection metrics. The net worth stood healthy at of Rs.451.66 crore as on March 31, 2020 as against Rs.414.29 crore in the previous year. To arrive at the net worth, Infomerics has considered Rs.53.31 crore of unsecured loans from promoters/ directors as quasi equity as the same is subordinated to the bank facilities. Long term Debt equity stood comfortable at 0.16 times as on March 31, 2020 as compared to 0.06 times in as on March 31, 2019. The overall gearing ratio has remained at less than unity in the past three years ended March 31, 2020. The interest coverage ratio and DSCR stood healthy at 6.83 times and 5.49 times respectively in FY2020 as compared to 7.07 times and 6.25 times respectively in

FY2019. Total debt to GCA also remained comfortable at 4.38 years in FY20 (2.99 years in FY19). Moreover, total indebtedness of the company as reflected by TOL/ANW also remained comfortable at 0.75x as on March 31, 2020 (0.45x as on March 31, 2019). Going forward, Infomerics believes the financial risk profile to remain healthy as GFL has lower reliance on external debt and maintained a conservative capital structure.

- **Prudent working capital management with healthy liquidity**

The working capital cycle is moderate on account of better debtor and inventory management by the company. The debtor days on an average, stood between 45-65 days during the period under review (FY2018-2020). GFL on an average, provides credit period of 30-75 days to its customers. The inventory is generally maintained between 40-71 days for its raw materials such as coal, while ~ 30 days for iron ore and 10 days for its finished products in the form of sponge iron, billet and TMT bars. The raw materials are majorly procured on advance terms from the suppliers. Further, the working capital limit utilisation remained low at ~ 46.01 percent for its working capital facilities of Rs.155 crore during the trailing 12 month ended September 2020. The net cash accruals of the company stood at around Rs.46.29 Cr. in FY20 as against loan obligations of Rs.17.40 crore in the same period. Infomerics expects the liquidity position of the company to be sustained at strong levels as capex has been completed.

Key Rating Weaknesses

- **Susceptibility of profitability to volatility in raw material prices and finished goods**

The degree of backward integration defines the ability of the company to withstand cyclical downturns generally witnessed in the steel industry. The major raw materials required for manufacturing billets are coal, iron ore and sponge iron while billets are the main raw material for producing TMT bars. However, it does not have any backward integration for its basic raw materials (iron ore & coal) and has to purchase the same from open market. Since the raw material is the major cost driver (constituting about 80% of total cost of sales in FY20) and raw material prices are volatile in nature, the profitability of the company is susceptible to fluctuation in raw material prices (though the prices of finished goods move in tandem with raw material prices, there is a time lag). Further, finished steel prices are also highly volatile and prone to fluctuations based on global demand supply situations and other macro-economic factors.

- **Intense competition**

The steel manufacturing businesses is characterized by intense competition across the value chain due to low product differentiation, and consequent intense competition, which limits the pricing flexibility of the players, including GFL.

- **Cyclicality in the steel industry**

The domestic steel industry is cyclical in nature and is likely to impact the cash flows of the steel players, including GFL. The steel industry is cyclical in nature and witnessed prolonged periods where it faced a downturn due to excess capacity leading to a downtrend in the prices. Further, the company's operations are vulnerable to any adverse change in the demand-supply dynamics in the real estate sector.

Analytical Approach: Standalone

Applicable Criteria:

Rating Methodology for Manufacturing Companies

Financial Ratios and Interpretation (Non-financial sector)

Liquidity: Adequate

The liquidity of the company is expected to remain adequate in the near to medium term with sufficient accruals and absence of any significant term debt repayment. The net cash accruals of the company stood at around Rs.46.29 Cr. in FY20 as against loan obligations of Rs.17.40 crore in FY20. Further, the company has projected to earn a cash accrual in the range of Rs. 46-62 crore as against its debt repayment obligations in the range of ~Rs.17-19.5 crore during FY21-23. Moreover, the Overall gearing ratio was comfortable at 0.45x as on March 31, 2020 (A) indicating a sufficient gearing headroom and the average CC utilisation for the past twelve months ended May, 2020 remained low at ~46% indicating a sufficient cushion. The free cash and bank balance of the company remained moderate at Rs.0.57 crore as on November 30, 2020.

About the Company

Incorporated in 1993, Gagan Ferrotech Limited (formerly, Gagan Commodities Private Limited) is a Kolkata based company promoted by Mr. Vinay Kumar Agarwal and Mr. Deepak Agarwal. Post incorporation, the company was trading in coal and since 2006, the company started its operations with setting up of 66,000 metric tonne per annum (MTPA) sponge iron plant at Asansol (West Bengal). Over the years, GFL expanded its sponge iron capacity and as a part of forward integration initiative set up facility for billets & rolling mill in 2010. Moreover, in order to strengthen the entire value chain, GFL has also set up captive power plant 2011. The present capacity of GFL stands at 2,40,000 MTPA for sponge iron, 3,20,000 MTPA for billets and 3,00,000 MTPA for rolling mill (TMT bars and wire rods). In addition, the company has a captive power plant of 12 MW. The TMT bars and wire rods are sold under the brand name ‘Gagan’.

In 2016, the entire stake of Mr. Deepak Agarwal in GFL was taken over by Mr. Vinay Kumar & family after a mutual agreement. Currently, the day to day affairs of GFL are managed by Mr. Vinay Kumar Agarwal.

Financials (Standalone):

(Rs. crore)

For the year ended* / As On	31-03-2019	31-03-2020
	Audited	Audited
Total Operating Income	924.47	920.68
EBITDA	54.47	58.66
PAT	23.03	26.97
Total Debt	127.33	202.85
Adjusted Tangible Net worth	414.29	451.66
EBITDA Margin (%)	5.89	6.37
PAT Margin (%)	2.48	2.91
Overall Gearing Ratio (x)	0.31	0.45

*Classification as per Infomerics’ standards

Status of non-cooperation with previous CRA: Acuité has moved the rating of GFL into the Issuer Non-Cooperating category as the company did not co-operate in the rating procedure despite repeated follow ups as per the Press Release dated December 05, 2019.

Any other information: Nil

Rating History for last three years:

Sr. No.	Name of Instrument/Facilities	Current Rating (Year 2020-21)			Rating History for the past 3 years		
		Type	Amount outstanding (Rs. Crore)	Rating	Date(s) & Rating(s) assigned in 2019-20 (Dec 31,2019)	Date(s) & Rating(s) assigned in 2018-19	Date(s) & Rating(s) assigned in 2017-18
1.	Cash Credit	Long Term	150.00	IVR A/ Stable Outlook	IVR A/ Stable Outlook	-	-
2.	Term Loan	Long Term	60.72	IVR A / Stable Outlook	IVR A / Stable Outlook		
3.	Letter of Credit/Bank Guarantee	Short Term	93.75	IVR A1	IVR A1		

Note on complexity levels of the rated instrument: Infomerics has classified instruments rated by it on the basis of complexity and a note thereon is available at www.infomerics.com.

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About Infomerics:

Infomerics commenced rating & grading operations in April 2015 after having spent over 25 years in various segments of financial services. Infomerics is registered with the Securities and Exchange Board of India (SEBI) and accredited by Reserve Bank of India. It is gradually gaining prominence in domestic rating and/or grading space. Infomerics is striving for positioning itself as the most trusted & credible rating agency in the country and is gradually widening its product portfolio. Company’s long experience in varied spectrum of financial services is helping it to fine-tune its product offerings to best suit the market.

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Annexure 1: Details of Facilities

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility (Rs. Crore)	Rating Reaffirmed/ Outlook
Long Term Bank Facilities –Cash Credit	-	-	-	150.00	IVR A / Stable Outlook
Long Term Bank Facilities –Term Loan	-	-	Dec’2025	60.72	IVR A/ Stable Outlook
Short Term Bank Facilities –Letter of Credit/Bank Guarantee	-	-	-	93.75	IVR A1