



Vardhman

Delivering Excellence. Since 1965.

VARDHMAN SPECIAL STEELS LIMITED

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Ref. VSSL:SCY:JAN:2020-21

Dated: 25-Jan-2021

BSE Limited,
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Rotunda Building, P.J. Towers,
Dalal Street, MUMBAI-400001.
Scrip Code: 534392

The National Stock Exchange of India Ltd,
Exchange Plaza, Bandra-Kurla Complex,
Bandra (East),
MUMBAI-400 051
Scrip Code: VSSL

SUB: REVISION IN CREDIT RATING

Dear Sir/Madam,

This is to inform you that all ratings assigned by CRISIL are kept under continuous surveillance and review. In this regard, we would like to inform you that CRISIL has revised the outlook for long-term Bank Loan facilities of the Company from "AA/Negative" to "AA/Stable" and re-affirmed the credit rating for long term and short term Bank loan facilities and for Commercial Papers.

A copy of the letter received from the credit rating agency is enclosed herewith for your information.

Thanking you,

Yours faithfully,
For **VARDHMAN SPECIAL STEELS LIMITED**



(SONAM TANEJA)
COMPANY SECRETARY

YARNS | FABRICS | THREADS | GARMENTS | FIBRES | **STEELS**

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Rating Rationale

January 22, 2021 | Mumbai

Vardhman Special Steels Limited

Ratings reaffirmed at 'CRISIL AA / CRISIL A1+' ; outlook revised to 'Stable'

Rating Action

Total Bank Loan Facilities Rated	Rs.546.52 Crore
Long Term Rating	CRISIL AA/Stable (Reaffirmed and outlook revised to 'Stable')
Short Term Rating	CRISIL A1+ (Reaffirmed)

Rs.150 Crore Commercial Paper	CRISIL A1+ (Reaffirmed)
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1 crore = 10 million

Refer to Annexure for Details of Instruments & Bank Facilities

Detailed Rationale

CRISIL Ratings has revised its outlook on the long-term bank facilities of Vardhman Special Steels Limited (VSSL) to 'Stable' from 'Negative' while reaffirming the rating at 'CRISIL AA'. The rating on the short-term bank facility and debt programmes has been reaffirmed at 'CRISIL A1+'.

The outlook revision reflects better than expected operating performance in fiscal 2021 with recovery in demand for passenger vehicle and two wheeler segment, which drives about 75% of the company's revenue. The second half of the fiscal will witness positive growth leading to overall revenue decline limited to 10% for the year compared to earlier expectation of more than 20% decline. Further operating margins are expected to improve at 5.5-6.0% for fiscal 2021 on the back of price hikes taken by the company and higher capacity utilisation. Over the fiscal 2022 and 2023, growth of 12-15% is expected and margins to improve to 7-8% level.

Going forward, the operating performance of VSSL will be benefitted through technical know-how of Aichi Steel Corporation, Japan (ASC, a Toyota Group Associate). In August 2019, VSSL entered into a technical assistance agreement with which also acquired 11.46% in VSSL for Rs 50 crore. The tie up intends to reduce operational costs, improve the product quality and improve process efficiencies. Also VSSL will benefit from access to the clientele of ASC. The equity infusion of Rs 50 crore has also improved the financial risk profile of the company and the proceeds would be utilised for funding any capex under this collaboration. Annual capex of Rs 20-30 crore is expected over the medium term.

Financial risk profile is marked with improving debt protection metrics. Gearing is expected to improve to about 0.5 time in fiscal 2022 while Interest coverage to remain about 3.5 times in fiscal 2022 compared to 2 times in fiscal 2021. The liquidity remains comfortable at Rs 80 crore at November end (Rs 50 crore in the form of cash & equivalents while Rs 30 crore in unutilized bank lines). Cash accruals are expected in the range of Rs 40-50 crore per annum over the fiscal 2022-23 to be sufficient to cover annual debt obligations of Rs 25-30 crore.

The ratings of VSSL continue to reflect the parentage of the Vardhman group, whose flagship company, Vardhman Textiles Ltd (VTXL; rated 'CRISIL AA+/FAAA/Stable/CRISIL A1+') is the largest shareholder in VSSL. The ratings also factor in established market position coupled with considerable backward integration as well as average albeit improving financial risk profile. These rating strengths are partially offset by susceptibility to cyclicalities in end-user industries.

Analytical Approach

CRISIL has applied its parent notch-up framework to factor in the parentage of Vardhman Group (whose flagship company, VTXL is the largest shareholder in the VSSL) with 59% shareholding in VSSL.

Key Rating Drivers & Detailed Description

Strengths:

* Strong support from Vardhman group

VSSL, prior to its demerger from VTXL, was the steel division of the latter. Operations continue to be largely controlled by the management of VTXL even after the demerger. That's because around 59% of the equity shares are owned by VTXL, its promoters, and other promoter-holding/investment companies, while the rest is owned by the public. VSSL receives strong support from the group such as using of the Vardhman group logo, common banking and treasury operations with VTXL. Any major change in the shareholding will be key rating sensitivity factor.

* Established market position

Market position is supported by a strong customer base, including automotive original equipment manufacturers and other established players in the engineering segment. Contribution from the top 5 customers remain at about 30%. Company has diversified presence across segments with about 70-75% contribution from passenger vehicle and two wheelers. In-house manufacturing of ingots and billets, along with ability to pass on price increases, resulted in moderate operating efficiency. The management's focus on the steel business, high capacity utilisation (around 95%), and considerable backward integration (around 90%) should drive growth in operating income and improve the business risk profile over the medium term.

* Average albeit improving financial risk profile

The interest coverage ratio is expected to improve to about 3.5 times in fiscal 2022 compared to estimated 2 times in fiscal 2021. Gearing improved on account of equity infusion of Rs 50 crore by ASC in fiscal 2020. The gearing to remain at 0.5 time at the end of fiscal 2022 with no major debt addition expected over the medium. With moderate annual capex plan of Rs 20-30 crore over the medium term, to be funded through cash surplus received from equity infusion and internal accruals, the debt levels are expected to remain stable.

Weaknesses:

* Susceptibility to cyclicalities in end-user industries

The company is a small player in the alloy steel industry, with only about 3% of the total capacity in India. Its products are used in the automotive, tractor, bearings, engineering, and allied industries; it is dependent on companies in the automotive sector for over 85% of revenue. This dependence subjects the company to risks related to cyclicalities in the automotive segment as witnessed during the recent years of economic slowdown. Further, vulnerability to fluctuations in input prices persists.

Liquidity Strong

VSSL has adequate liquidity driven by expected cash accruals of Rs 40-50 crore per annum over medium term. The company has a working capital limits of Rs 200 crore which was utilized at around 70% for seven months ended November 2020. Further, VSSL also maintains Rs 50 crore in the form cash and equivalents. Presently the company has no major capex plan and focus is on increasing existing capacity utilization. Any capex in future will be jointly done with ASC.

Outlook Stable

CRISIL believes the operating performance will recover in line with the recovery in end user industry, while support from Vardhman group should continue. The tie-up with ASC is also expected to support business and financial risk profile.

Rating Sensitivity factors**Upward factors:**

- * Improvement in credit rating of VTXL
- * Substantial improvement in scale and operating profitability leading to cash accruals of Rs 100 crore and RoCE of over 15% on sustained basis
- * Improvement in financial risk profile debt/EBITDA below 1.5 times

Downward factors:

- * Weakening of the capital structure such as gearing is increased beyond 1 times and deterioration in debt protection metrics on sustainable basis for instance, interest cover remaining below 2.25 times on consistent basis or
- * Operating margin remaining below 5% on consistent basis or
- * Reduction in support from, or downward rating action on, VTXL.

About the Company

The Vardhman group ventured into the steel business in 1972 by setting up Oswal Steels to manufacture special and alloy steels, with initial capacity of 0.5 lakh tpa. In 1986, the firm acquired a plant in Ludhiana, Punjab, and its capacity was increased to 1 lakh TPA. Oswal Steels became a division of VTXL in 1992. VTXL demerged its steel division as VSSL effective January 1, 2011. VSSL has capacity to manufacture 1.8 lakh TPA of steel billets and 2.1 lakh tpa of steel rolled products. Its manufacturing unit is equipped with a 30-tonne ultra-high-power electric arc furnace with an electro-magnetic stirrer, a vacuum degassing system, and a bloom caster.

For the six months ended 30th September 2020, VSSL posted revenue of Rs 315 crore and operating profit of Rs 12 crore as against Rs 453 crore and Rs. 23 crore respectively for similar period in corresponding year.

Key Financial Indicators

Particulars	Unit	2020	2019
Revenue	Rs crore	852	1121
Profit After Tax (PAT)	Rs crore	2	22
PAT Margin	%	0.3	2.0
Adjusted debt/adjusted networkth	Times	0.64	0.92
Interest coverage ratio	Times	1.93	2.95

Any other information: Not applicable

Note on complexity levels of the rated instrument:

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Annexure - Details of Instrument(s)

ISIN	Name of Instrument	Date of Allotment	Coupon Rate (%)	Maturity Date	Issue Size (Rs. Crore)	Complexity Level	Rating Assigned with Outlook
NA	Commercial Paper	NA	NA	7-365 days	150	Simple	CRISIL A1+
NA	Cash Credit	NA	NA	NA	200	NA	CRISIL AA/Stable
NA	Corporate Loan	NA	NA	Sep-24	43	NA	CRISIL AA/Stable
NA	Corporate Loan	NA	NA	Jun-25	57.44	NA	CRISIL AA/Stable
NA	Letter of credit & Bank Guarantee	NA	NA	NA	100	NA	CRISIL A1+
NA	Term Loan	NA	NA	July-26	37.95	NA	CRISIL AA/Stable
NA	Proposed Long Term Bank Loan Facility	NA	NA	NA	108.13	NA	CRISIL AA/Stable

Annexure - Rating History for last 3 Years

Instrument	Current			2021 (History)		2020		2019		2018		Start of 2018
	Type	Outstanding Amount	Rating	Date	Rating	Date	Rating	Date	Rating	Date	Rating	Rating
Fund Based Facilities	LT	446.52	CRISIL AA/Stable	--	--	21-05-20	CRISIL AA/Negative	10-12-19	CRISIL AA/Negative	28-12-18	CRISIL AA/Stable	CRISIL AA-/Positive
			--	--	--		--		--	26-06-18	CRISIL AA/Stable	--
			--	--	--		--		--	16-02-18	CRISIL AA-/Positive	--
Non-Fund Based Facilities	ST	100.0	CRISIL A1+	--	--	21-05-20	CRISIL A1+	10-12-19	CRISIL A1+	28-12-18	CRISIL A1+	CRISIL A1+
			--	--	--		--		--	26-06-18	CRISIL A1+	--
			--	--	--		--		--	16-02-18	CRISIL A1+	--
Commercial Paper	ST	150.0	CRISIL A1+	--	--	21-05-20	CRISIL A1+	10-12-19	CRISIL A1+	28-12-18	CRISIL A1+	--
			--	--	--		--		--	26-06-18	CRISIL A1+	--
			--	--	--		--		--	16-02-18	CRISIL A1+	--
Short Term Debt (Including Commercial Paper)	ST		--	--	--		--		--		--	CRISIL A1+

All amounts are in Rs.Cr.

Annexure - Details of various bank facilities

Current facilities			Previous facilities		
Facility	Amount (Rs.Crore)	Rating	Facility	Amount (Rs.Crore)	Rating
Cash Credit	200	CRISIL AA/Stable	Cash Credit	200	CRISIL AA/Negative
Corporate Loan	100.44	CRISIL AA/Stable	Corporate Loan	127.85	CRISIL AA/Negative
Letter of credit & Bank Guarantee	100	CRISIL A1+	Letter of credit & Bank Guarantee	175	CRISIL A1+
Proposed Long Term Bank Loan Facility	108.13	CRISIL AA/Stable	Proposed Term Loan	30.07	CRISIL AA/Negative
Term Loan	37.95	CRISIL AA/Stable	Term Loan	13.6	CRISIL AA/Negative
Total	546.52	-	Total	546.52	-

Links to related criteria[CRISILs Approach to Financial Ratios](#)[CRISILs Bank Loan Ratings - process, scale and default recognition](#)[Rating criteria for manufacturing and service sector companies](#)[Rating Criteria for Steel Industry](#)[CRISILs Criteria for rating short term debt](#)[Criteria for Notching up Stand Alone Ratings of Companies based on Parent Support](#)

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