

## **Assignment:**

### **Assessment:**

- To Prepare detailed credit appraisal note including business, financials, management and facilities assessment key risks and mitigants and recommendation comments for Approval based on shared case study
- To decide on loan amount you would recommend and defend it with assessment.

### **Credit Appraisal Note:**

Name of company:	M/s XYZ Pvt. Ltd	Address	A-35, Adityapur Industrial Area, Jamshedpur-832109
Industry	Steel	Segment	Manufacturing
Shareholding pattern	Promoters- 100%	Guarantors	Shri ram Kumar & shri Arun Kumar
External Rating	Nil	Internal Rating	CR-5 (Fair Risk)
Takeover	yes –Wells Fargo	Vintage	NTB, 49 years in banking
Banking Arrangement	NA	Credit Manager	Premkumar
Next review date	25-12-2024	Nature of Lending	Secured – collateral

### **Limit Summary: (INR lakhs)**

	<1 years		1-5 years		>5 years	
	Existing	Proposed	Existing	Proposed	Existing	Proposed
Borrower Limits - Funded	-	125.85	-	-	-	177
Non – Funded	-	-	-	-	-	-
Total Exposure	-	125.85	-	-	-	177

### **Proposal Summary:**

Type of request	Cash Credit working capital limit of INR 2 Cr and term loan of INR 2 Cr for purchase of machinery and building development
Facility requested	CC- 75.85 lakhs Bill Discounting – 50 lakhs Term loan – 177 lakhs
Purpose of Facility	1)Takeover of existing CC limit of 66 lakhs from Wells Fargo and enhancement of 9.85 lakhs as CC limit and 50 lakhs as bill discounting facility 2)Term Loan of 177 lakhs for expansion of machining unit and building renovation.

Facilities (INR lakhs)	Existing	Existing	Proposed	Incremental
	Wells Fargo	ROBO Bank	XYZ bank	
CC limit	66	-	75.85	+9.85
Bill Discounting	-	-	50	+50
Term Loan	-	98	177	+177
Total	66	98	302.85	+236.85

**Waivers, Extensions, exceptions to bank policies, risk appetite framework / SDR clause and other deviations sought in CAM**

1. Deviation in maximum tenor offered for term loan with proposed term loan for 6 years including 1 year moratorium
2. Collateral offered for WC limit 60% of total funding while requirement is 100% of the funding

**Security details:**

S.no	Facility Type	Security type	Security details	Security value	Guidelines
1	Working Capital – CC limit	Current asset	Pari passu charge on current assets created out of the proposed facility	-	Charge to be created before disbursement
2		Property Immovable asset	Land mortgage pertaining to land where manufacturing plant is set up	75.51 lakhs	Land mortgage to be coXYZeted prior to the disbursement
3		Personal guarantee	PG of promoters	Net worth of promoters	PG to be signed
4	Term Loan	Hypothecation of Machineries	Machineries brought through proposed funding	187 lakhs	Hypothecation to be created on Machineries within 60 days of first tranche of disbursement
4		Property Immovable asset	Land mortgage pertaining to land where manufacturing plant is set up	177 lakhs	Land mortgage to be coXYZeted prior to the disbursement
5		Personal guarantee	PG of promoters	Net worth of promoters	PG to be signed

Note: Total Land value mortgage to be created is 252.51 lakhs

**Key conditions:**

Disbursement – We propose disbursement of CC limit based on the drawing power availability(to be assessed quarterly) and bill discounting based on bills submitted, with respect to term loan disbursement 50% of Term loan to be disbursed directly to suppliers based on Performa invoice and remaining 50% after installation of machinery and field inspection.

**Internal Rating**

Total Score Obtained	71/100
	CR-5 (Fair Risk)
External rating	None

The overall rating is found to be satisfactory, strength is derived from strong order book from existing buyers and consistent growth in previous audited financials at approx. 20%

**Banking arrangement and code of conduct:**

The company is currently banking with wells Fargo for their working capital with CC limits of 66 lakhs and term loan from ROBO bank with current outstanding of 0.98 lakhs as on 25-12-2008

Account conduct: satisfactory

**Borrower Overview**

Shareholding Pattern:

Name of Promoters	Share holding %	Value
Ram Kumar	50%	32.48 Lacs
Arun Kumar	50%	36.22 Lacs

**Company overview:**

M/s XYZ(XYZ) is involved in manufacturing of resistance grids, CI Graded Casting, Bright bars etc used in Automobile, Mining, Steel industries. It produces various grades of castings viz. steel Iron Malleable Cast Iron, SG Cast Iron Steel and Alloy Steel.

XYZ, incepted in 1972, was carrying out the work of foundry of small & medium casting and has recently started manufacturing of bright steel bars used in the Automobile Industry. The company mainly caters to Tata Steel and Tata Motors ancillaries. Recently, the company has been receiving orders for machined casting from Tata Motors.

Social cultural aspect of the area	It is located in Adityapur Industrial Area.
Industrial Climate and its suitability for the product	The product suits the requirement of <b>Tata Motors, Tata Steel, UCIL, SAIL Bokaro, etc.</b>
Any restriction prevailing in the locality	Nil
Incentives / concessions/ low tariff for electricity /land allotment/ SEZ benefits / tax benefits	As applicable in the state
Land Area	45,000 SQFT of land area. The build-up was 15,000SQFT & they have renovated 7,000SQFT area last year
Transportation and Communication	There is good communication and transportation facility
Power source	There is a connected load of 335KVA from State Electricity Board. They have recently added one DG set as stand by arrangement. Additional load of 50 KVA is required for the proposed expansion
Production Activities	Manufacturing of all types of Resistance grids, CI graded castings, Bright bars etc. The company is intended to produce various grades of castings viz. Cast Iron, Malleable Cast Iron, SG Cast Iron, Steel & Alloy Steel.
Manufacturing Process	The casting materials are melted & molded as per the design. The heat treatment takes place for stabilizing the molecular realignment. The treated material is machined for giving finishing touch. The process consists of sand preparation, moulding, fettling, heat treatment etc. They have also started the production of Bright Bars. These are cold processed steels bars, manufactured from suitably tested and selected Raw Materials. Bright Bars are used as raw material for Engineering Industry viz. Automobile, Railways, Textile etc.

	<p>Capacity: On the basis of production in 2 shifts per day the capacity as follows:</p> <ol style="list-style-type: none"> <li>Around 1100MT per annum including 240 TPA of Cast Iron, Malleable Cast Iron of 240TPA, SG Casting of 360 TPA, Steel and Alloy Steel Casting of 360TPA. However production depends on the type and size of casting The proposed installed capacity is 6000MT per annum including the existing installed capacity of 2400MT</li> <li>Bright Steel bars (1800 MT/ annual on three shifts)</li> </ol>
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### **Key Managerial Personnel:**

- Shri Ram Kumar, Director of the company, is a qualified diploma engineer. He is quite experienced in the present line of activity
- Shri Arun Kumar, the key person of the company, completed MBA in Finance Discipline. He manages the day to day affairs of the company with consultation with other director and technical personnel.

Assumption: their sons/daughter are involved in business for last 5 or 10 years.

### **Industry analysis:**

XYZ serves **Automobile, Mining, and Steel industry players**, which are strongly driven by the **macroeconomic conditions** of the country. It is forecasted to have strong growth, fueled by increased government spending on national infrastructure. **The growing income of the middle class and a rising youthful population contribute** to the expanding demand in the Indian automobile industry, projected to reach **US\$ 300 billion by 2026**.

The automobile industry is XYZ's primary driver, fueled by Tata Motors' surge in orders. Another significant contributor to XYZ's business comes from the steel industry, where India holds the **second position globally** in terms of production. XYZ is associated with two leading market players in this sector, namely **TATA Steel and SAIL**. The steel industry, as a whole, is anticipated to grow at a **CAGR of 2.8% from 2023 to 2030**.

Macroeconomic factors such as inflation and recession, and variables like **China's export potential, fluctuations in raw material prices, including iron ore & scrap steel, and cooking coal, impact industry**. The steel industry is further characterised by **price wars** and substantial trade **discounts**. Government regulations, such as duty-free imports of raw materials and antidumping policies to safeguard domestic players, are in place. Generally, the threat of new entrants in the steel industry is low due to significant **captive investments and manufacturing processes**. The bargaining power of buyers is substantial, while the power of suppliers is low owing to the **commoditized nature of the product**. Moreover, the industry faces a notable threat of substitutes, **particularly in the automobile sector, where the use of lighter materials like aluminum, reinforced plastics, and fiberglass provides a competitive advantage**.

### **Competitor Analysis:**

XYZ encounters competition from numerous Small and Medium Enterprises (SME) and Micro, Small, and Medium Enterprises (MSME) operating in the same domain. Jamshedpur alone hosts over 18 small-scale iron casting and approximately 20 bright bars manufacturers, akin to XYZ. Despite this, the crucial factor lies in sustaining pivotal connections with buyers, and XYZ has demonstrated a robust rapport with industry stakeholders, securing steady orders from buyers.

**Financial analysis:**

	Mar'06 Audited	Mar'07 Audited	Mar'08 Est.	Mar'09 Proj	Mar'10 Proj	Mar'11 Proj
Paid up Capital	40.30	70.30	80.30	90.30	90.30	90.30
Reserves & Surplus	15.75	18.72	58.73	125.39	171.90	220.90
Tangible Net worth	55.85	88.84	129.04	207.69	256.20	307.20
Long Term Liabilities	52.85	97.46	282.65	299.93	211.87	142.00
Current Liability	62.5	65.96	265.59	264.93	263.0	259.0
Current Assets	68.58	158.66	275.27	274.47	310.83	333.51
Net Working Capital	6.08	92.70	9.68	9.54	47.83	74.51
Current Ratio	1.10	2.40	1.04	1.04	1.18	1.29
Total Funded Debt	115.35	163.42	548.24	564.86	474.87	401.0
DER (TFD/TNW)	2.07	1.84	4.24	2.72	1.85	1.31
Net Sales	352.57	415.37	500.00	1129.80	1287.00	1373.00
Cash	13.60	17.79	23.63	99.52	110.14	103.98
Short Term loan(total debt – long term liabilities)	62.5	65.96	265.59	439.47	263	259

**Revenue:**

The Company has been showing consistent growth with 18% growth in FY-07 and 20% growth in FY-08 and expected to grow at minimum of 30% in FY-09, Company caters to dominant players in Industry like TATA motors, TATA steel, SAIL and UCIL with TATA group being the drivers of topline.

**Forecast:** Company is showing strong growth but it has not met its projections previously, it is expected to reach topline of 650 lakhs in FY-09 at 30% growth due to increased contribution from TATA motors (bright bars) and existing order book of 50 lakhs. (Additional 10% in revenue is attributed to 50 lakhs existing orders). Despite doubling production capacity entity It is proposed to keep under watchlist for doubling the revenue and its expected to reap the benefits post FY-09.

**Profitability Margin (EBITDA/ PAT margin):** Limited info available, however it expected to be strong based on available info on reserves and surplus and its growth in net worth

Note: couldn't find info on COGS and estimation of COGS using creditor data or inventory days is not the actual data representing financials.

**Tangible net worth:** Promotors has infused around and INR 14.45 lakhs in FY-07 and is currently at 88.84 in FY-07 and as per Provisionals they will be closing at 129.04 lakhs fueled by reserves & surplus generated in FY-08

**Liquidity position:** the current ratio has improved over years from 1.1 to 2.4 in FY-07 it will decrease to 1.04 in presence of higher short term loans as per provisional data given

**Working capital Assessment:**

**MPBF method II (as per projections FY-09)** =  $274.47 - 80 - (25\% \times 274.47)$  (for current liability creditors 80 lakhs alone has been considered to calculate funding limit and other current liabilities is considered to be negligible except STL which will be entirely funded by XYZ bank)

**= 125.85 lakhs**

We can fund only up to 125.85 lakhs against 265 lakhs shown as short-term loan in projections FY-09, any funding higher than 125 lakhs will decrease liquidity position.

Further to **reduce risk of non-repayment**, capital intensive process of operations, to increase borrower ability to build inventory and **improve utilization of funds** a part of facility is proposed to be offered as Bill discounting for those receivables to be received from TATA group. This is offered on preview of company limited ability in building inventory and **DP is restricted to a availability of 50 lakhs or lower in the past despite higher liquidity requirements**. (based on data available on debtors stock and creditors, inventory margin is 75%, debtor margin is 60%)

Name of Facility	Maximum Limit
CC limit	75.85 lakhs for 12 months
Bill Discounting for supplier made to TATA	50 lakhs with tenure of 90 (+ 10 or -10) days

Note: debtor days is found to be 91 for FY-07, 87 for FY-08 and based on projection it decreases to 38 days and not 30 days as mentioned in the note

Assumption: upon verifying bank statements and sales data payment cycle for bills of TATA motors is around 90 days.

Buyer Profile:

**TATA Motors Ltd:** As per recent rating available as on May,2023 TATA Motors has been rated as AA/stable by Crisil.

Rating derives strength from strong legacy in luxury auto segment and dominant market position in CV segment. Liquidity position is strong with annual cash accrual is projected at Rs 35,000-45,000 crore over the medium term, Additionally, liquidity remains supported by strong financial flexibility, being a part of the Tata group.

Particulars	Unit	2022	2021
Revenue	Rs crore	275836	246295
Profit After Tax (PAT)	Rs crore	-10598	-12841
PAT Margin	%	-3.84	-5.21
Interest coverage	Times	4.39	7.05
Net debt/tangible networth	Times	1.38	1.22

**TATA steel:** Tata Steel has a BBB- credit rating from Standard & Poor's1 and a Baa3 long-term issuer rating from Moody's Investors Service. As per ICRA rating as on June,2023 rating has been reaffirmed at [ICRA]A1+, the rating derives strength from strong financial risk profile, diversified product mix and large scale operations globally. Liquidity position has been assessed as adequate, supported by free cash/bank/liquid investment balances of around Rs.17,083crore as on March 31, 2023 and healthy retained cash flow of Rs. 20,000-25,000 crore annually expected over the medium term.

**Key financial indicators (Audited)**

TSL Consolidated	FY2022	FY2023
Operating Income (Rs. crore)	243,959.2	243,352.7
PAT (Rs. crore)	41749.3	8075.3
OPBDIT/OI (%)	26.6%	13.3%
PAT/OI (%)	17.1%	3.3%
Total Outside Liabilities/ (Tangible Net Worth+ Minority Interest) (times)	1.4	1.7
Total Debt/OPBDIT (times)	1.2	2.6
Interest Coverage (times)	11.9	5.1

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

**Data discrepancy:**

In FY-07 Audited financials long term debt is 97 lakhs and total debt is 163 lakhs indicating short term loan as **65 lakhs and current liability is also mentioned as 65 lakhs, it shows accounts payable is Zero and not 70.50 lakhs**, creditors are paid on same day of purchase, in this scenario funding working capital limit of INR 2 Cr can be considered as per MPBF method considering take over of existing WC limit and collateral availability. Info on COGS is not available for cross verifying inventory and creditor days with actuals

**Gearing Ratio:**

Gearing ratio has been within the prescribed levels, however projections shows higher leverage of tangible net-worth hence following modifications are proposed:

	Mar'06	Mar'07	Mar'08	Mar'09
	Audited	Audited	Est.	Proj
Long Term Liabilities	52.85	97.46	282.65	125.39
Total Funded Debt	115.35	163.42	548.24	564.86
Short term loan(STL)	62.5	65.96	265.59	439.47
Tangible Net worth	55.85	88.84	129.04	125.39
Gearing ration based on projections	2.07	1.84	4.25	4.50
Revised STL			125	125
Revised Long term debt obligation			269	260
<b>Proposed equity infusion</b>			<b>60</b>	<b>60</b>
Revised Debt/TNW	<b>2.07</b>	<b>1.84</b>	<b>2.08</b>	<b>2.08</b>

Note: 82 lakhs is existing term loan obligation of ROBO bank in FY-08 and 90 lakhs in FY-09 as sufficient info is not available. FY-09 is the moratorium year

**Term Loan Limit assessment:**

To attain coXYZete autonomy and enhance quality standards, there is a proposed budget to expand the machining unit. This expansion involves the installation and replacement of machines to enable in-house coXYZetion of all machining tasks.

Proposed cost of purchasing machinery and renovating building:

SL No.	Description	Qty.	Base Price (in Lac)	Tax	Total Price (in Lac)
1	CNC Machine Fully Automatic	2	10	10%	22
2.	Surface Grinder	10	5	10%	55
3.	Box Drilling Machine	10	5	10%	55

4.	Batliboi Heavy Duty Vertical Milling Machine	10	5	10%	55
5	Improvement in Building	1	50	0%	50
Plant & Machinery Total Cost					<b>237</b>

It is proposed to fund 75% of total budget i.e 177 lakhs with covenant to infuse fresh equity for 25% (60 lakhs) of cost into company, **it further caters to maintain liquidity and strengthen equity position of the company.**

Moratorium is proposed for 1 year considering the **time requirement to procure, Installation and initiate production process**, proposed tenure is 6 years including moratorium period, proposed based on strength of collateral given (equal to proposed loan of 177 lakhs) and additional hypothecation of machineries, also funding to be restricted to procurement of machineries where payment to be issued to supplier's banks account and not for building renovation.

#### Key Risks & Mitigants

Key Risks	Mitigants
Buyer concentration - Any vertical integration by TATA steel and subsequent supply to TATA motors and change in suppliers by TATA motors as they are major drivers of Top line.	Assumption : due to increased orders TATA motors has entered into agreement with XYZ  Presence of existing orders and agreement from TATA motors reduce risk in near future, Further presence of Bill discounting facility will help us to closely monitor transactions pertaining to TATA group  Also market leaders association is taken as strategy by the entity to build trust and remain in the game withstanding future competition.
Increased Competition in segment	While competition is immense, XYZ has proven track record and a positive sign by increasing orders value from existing buyers, Further strong vintage of XYZ directors gives us more trust despite growing competition
Risk of excess production or obsolescence stocks – while proposed doubling of production capacity is backed by increasing orders, its still hypothetical to drive double in revenue due to a 50 lakhs in-hand orders	Reduction on exposure on CC limit will help us mitigating the risk, further presence of 1 year moratorium and proposed equity infusion will help us to monitor the company over next 1 year and take corrective actions for increasing or decreasing the limit  Further presence Of collateral at 83% of exposure reduce the POD & Loss given default, in addition we also have 187 lakhs worth of machinery hypothecated to loan that further reduces LGD

#### Recommendation:

The proposal is recommended for INR 125.85 lakhs for working capital and INR 177 lakhs as a term loan. This recommendation is supported by a solid track record and the presence of industry leaders in the target buyer segments. Additionally, the proposal gains strength from the collateral provided, which covers 145% of the total funding amount.



## **Assumptions**

(taken bcz of missing details in case study):

1. Client provides collateral of industrial land area equivalent to Term loan and WC – CC limit and bank collateral requirement is in ratio of 1:1
2. In estimation of FY-08 financials creditors is only 80 lakhs but current liability is 265.59 lakhs so assumption is they have included 1.6 Cr and CPLDT as proposed cash credit limit into Provisionals for FY-08
3. Reserves & surplus is available from retained earnings and not from sale of assets or any other surplus
4. No bad debtors in the book
5. As per credit policy debt to TNW for manufacturing entity can be till 3.5
6. EBITDA and PAT margin a growing in line with revenue growth

## **Queries for RM:**

1. Revised Projections or clarification as proposed inc in revenue is not catered to inc in CL or CL, if its correct justification for proposed reduction in debtor, inventory and creditor days
2. Audited financials of FY-05, 3 years audited financials for analysis
3. Vintage of association with buyers, TOP buyers, TOP suppliers list
4. Agreement with buyers if any in place
5. Sanction letter and Repayment schedule for existing loan with loan account statement
6. Proposed successors for key management
7. Details of suppliers of machinery for term loan, their GST and basic KYC and contact details
8. Expected life of proposed machineries
9. Timeline for procurement and installation and production from the installed capacity
10. Buyers breakup in contribution to Top line
11. CC statement
12. Justification for failure in meeting projection proposed for FY-06, 07
13. Collateral land details, valuation if any