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## National Steel and Agro Industries Ltd.

Mr. Umesh, the head of Corporate Banking branch of Universal Bank's (UB) Indore Branch, had received a request from National Steel and Agro Industries Ltd (National Steel), a long-time customer, for renewal of working capital facilities. UB was the leader of a consortium of 11 banks and hence Umesh had to do the credit analysis and assess the company's credit requirements and share the report with all the consortium members and the head office of the bank for approval.

### About the Company

National Steel was established by Shri Santosh Shahra in 1985 and presently he was acting as the Executive Chairman of the company. The company belonged to the Ruchi Soya Group, the largest edible oil manufacturer in India. The manufacturing facilities of the company were located at Village Sejwaya, Dhar District, Madhya Pradesh. The company had obtained ISO certificates for quality (ISO 9001: 2008) and environment (ISO 14001: 2004). It also had grid-connected captive power plants at its factory premises and was almost self-reliant for electricity. It sold the surplus power to the Madhya Pradesh State Electricity Board.

**Businesses:** National Steel had two major business divisions – manufacturing galvanised flat steel products and trading in agro products.

Its steel product range included cold rolled (coils, slits and sheets) and galvanised products

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(coils, slits and sheets—plain and corrugated). The products were offered in annealed and full hard conditions in thickness range of 0.14 mm to 1.5 mm. Colour coated products including coils, slits, profiles, and sheets (plain and corrugated) were made by the company. It also offered value added products on specific orders. A flow diagram showing the company's manufacturing process is shown in Chart 1.

National Steel's other major business was trading agro products. It procured pulses, beans, soya seeds, yellow peas, etc. from both domestic and foreign markets and sold the same. The share of the trading business was nearly 50% of its total revenue.

## Competitive Landscape

National Steel competed in both the steel manufacturing and agro trading industries, each having a unique competitive environment. Here's an overview of how National Steel stands compared to competitors in both industries:

**Steel Industry:** The Indian steel industry has been dominated by large players such as Tata Steel, JSW Steel, and Steel Authority of India Limited (SAIL). National Steel, although smaller, carved out its market with a significant share in galvanised flat steel products. While its share price had underperformed compared to the broader Nifty50 index, it outperformed the Nifty Metal index, indicating a relative strength within the metal industry.

**Agro Trading Industry:** National Steel had also been a part of the highly competitive agro trading industry, particularly in pulses, beans, and soya. Large agro traders such as ITC and Adani Wilmar posed significant competition, especially in procuring raw materials from international markets. National Steel's ability to navigate fluctuating commodity prices and currency exchange rates was critical to its success in this segment.

## Industry-Specific Considerations

National Steel's two key business divisions, steel manufacturing and agro product trading, had distinct working capital requirements due to the nature of their business cycles:

**Steel Manufacturing:** Steel production requires long lead times, with substantial investments in raw materials like hot rolled coils (HRCs), zinc, and paints. The working capital cycle in this industry is longer due to extended periods for production, storage, and distribution. Given the extended lead time and the cyclical nature of the steel industry, National Steel's steel division would require higher cash credit limits to cover its inventory and operational expenses.

**Agro Trading:** Agro trading involves shorter lead times compared to manufacturing, but the business is more volatile due to price fluctuations in agricultural commodities and foreign exchange risks from international procurement. The liquidity required to handle large volumes of trading in pulses and soya seeds results in high demand for Letter of Credit (LC) facilities. Agro products trading also entails significant risk from weather conditions, geopolitical factors, and global commodity price swings, which could impact cash flow and working capital needs.

National Steel's domestic business was concentrated in Madhya Pradesh, India. It also exported its products to various countries including the USA, EU, UAE and Africa. However, export was made against specific orders from customers only.

Of late, the company had entered into power distribution and transmission business and it had already completed projects worth Rs. 21 crore in Madhya Pradesh.

## Financials

The company had achieved net sales of Rs. 3883 crore during 2014-15 which was about 10% higher than that of the previous year. Its export revenue was around 20% of its total sales, that is, Rs. 556 crore and foreign currency expenses totaled Rs. 1165 crore. Its net worth was Rs. 360 crore against total assets of Rs. 1440 crore. Though the company had reported profits during the last five years it did not pay any dividend to its shareholders. The summarised balance sheet, profit and loss account and the details of forex revenue and expenses are presented in Exhibit 1, Exhibit 2, and Exhibit 3 respectively. Projected financials for the year 2015-16 are shown in Exhibit 4.

The breakup of key financials of the company is given in Table 1.

**Table 1: Key Financials of National Steel's Manufacturing and Trading Businesses**

	<b>Mar-15</b>	<b>Share (%)</b>	<b>Mar-14</b>	<b>Share (%)</b>
<b>Revenue from Operations</b>	<b>3883.87</b>		<b>3499.43</b>	
Manufacturing	2058	53	1858.73	53
Trading	1826	47	1640.69	47
<b>Profit (EBITDA)</b>	<b>186.53</b>		<b>174.98</b>	
Manufacturing	146.15	78	141.72	81
Trading	40.38	22	33.26	19
<b>Segment Assets</b>	<b>1429.45</b>		<b>1263.74</b>	
Manufacturing	1078.06	75	1000.95	79
Trading	351.39	25	262.80	21

National Steel's shares had been listed on both the Bombay Stock Exchange (BSE) and National Stock Exchange (NSE) and the movement of its share prices in relation to Nifty50 Index and the Nifty Metal Index is given in Chart 2. The chart shows that both the metal index and the company had underperformed in the overall market during the last two years. However, the company's stock had outperformed the metal index.

## Working Capital Requirements

The company requested its banks to provide various working capital facilities totaling Rs. 1650 crore during 2015-16. It needed a cash credit of Rs. 200 crore and the following non-fund based facilities with interchangeability:

**Letter of Credit:** National Steel requested its bankers to sanction inland LC limit of Rs. 350 crore and import LC limit of Rs. 610 crore for the year 2015-16. The raw material for manufacturing steel and agro products for trading were available in both the domestic and foreign markets. However, the company imported both raw material as well as agro products depending on currency rates. It imported if currency rates were favourable and if not it largely procured from the domestic market. The cycle length of LC for the company is given in Table 2 and other details necessary for assessing its LC requirement are presented in Exhibits 5 and 6.

**Table 2: LC Cycle of National Steel**

	<i><b>Domestic Goods</b></i>	<i><b>Imported Goods</b></i>
Lead time	15	45
Sailing time	--	30
Port clearances, transportation to plant, etc.	--	30
Holding and loading	45	45
Credit period offered to customers	45	45
Total	105 days	195 days

**Buyers Credit:** The Company availed Buyer's Credit from a bank abroad depending on suitable quotes and it had requested UB and other members of the consortium to provide necessary support for the same.

**Bank Guarantees:** The Company was in need of BGs for receipt of advance from customers, and also for procurement.

To carry on its power distribution and transmission business the company needed BG for the purpose of bidding, mobilization advances, machinery advances, and performance guarantees for a period of 36 months.

During 2014-15, the company availed BG of Rs. 10 crore for its manufacturing and trading divisions and Rs. 20 crore for its power business.

The company was using EPBG (Export Performance Bank Guarantee) to receive advance payment from its foreign customers and the same was used to pay for imported raw material. It had requested the banks to sanction EPBG of Rs. 700 crore for the year 2015-16.

## Credit Risk Rating

National Steel had obtained credit risk rating done by ICRA Ltd and the rating grades for various facilities of the company for the year 2015 are as follows:

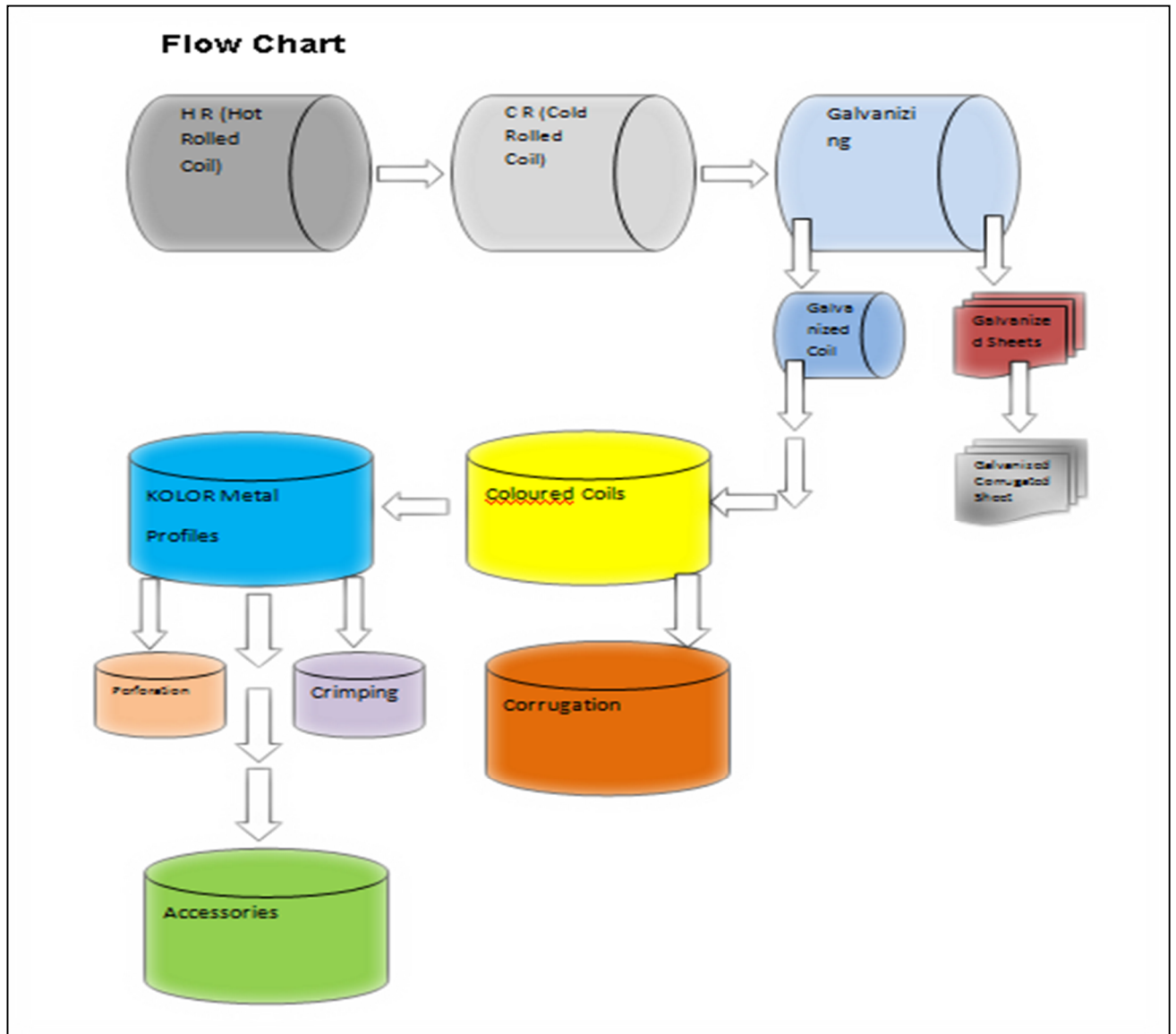
<b>Type of Credit Facility</b>	<b>Rating Grade</b>	<b>Risk</b>
Unallocated	A3+A3+	Moderate credit quality and the risk is higher than average
Short term non-fund facilities		
Long term fund-based facilities	BBB BBB	Moderate credit quality and the risk is higher than average
Term loans		

The key questions in Umesh's mind were:

- Given the projected growth and stable profitability, should UB renew the full working capital facilities requested by National Steel?
- What method shall be appropriate for determining the working capital limits?
- Considering the volatile nature of the agro trading division, should UB impose stricter conditions, such as currency hedging or collateralization of the agro division's working capital?

Umesh entrusted the responsibility of credit analysis of National Steel and finding answers to these questions to Ms. Flora, the credit analyst and advised her to place the report before the credit committee of the branch within three days.

Chart 1: Manufacturing Process at National Steel



Source: [www.nsail.com/steel.bhp](http://www.nsail.com/steel.bhp) (accessed on July 4, 2016)

**Exhibit 1: Balance Sheet of National Steel and Agro Industries Ltd.**

	<b>Mar-15</b>	<b>Mar-14</b>	<b>Mar-13</b>	<b>Mar-12</b>	<b>Mar-11</b>	<b>Mar-10</b>
Share capital	99.51	99.51	99.51	99.51	99.51	87.61
Reserves	260.02	233.72	205.81	179.47	153.30	114.43
<b>Net Worth</b>	<b>359.53</b>	<b>333.23</b>	<b>305.32</b>	<b>278.98</b>	<b>252.81</b>	<b>202.04</b>
Long-term borrowings	47.31	66.18	80.45	110.61	114.64	288.60
Deferred tax liability	30.62	31.12	32.18	31.78	33.37	34.53
Other long-term liabilities	0.00	0.00	2.12	1.01	0.00	0.00
<b>Current Liabilities and Provisions:</b>	<b>1002.08</b>	<b>852.38</b>	<b>828.43</b>	<b>797.05</b>	<b>725.71</b>	<b>439.67</b>
Short-term borrowings	234.70	242.49	212.63	179.53	210.20	0.00
Trade creditors	721.23	567.58	584.07	581.04	472.40	403.54
Other current liabilities	20.02	23.56	20.71	26.08	30.50	27.83
Provisions	26.13	18.75	11.02	10.41	12.61	8.30
<b>Total</b>	<b>1439.54</b>	<b>1282.91</b>	<b>1248.50</b>	<b>1219.44</b>	<b>1126.52</b>	<b>964.85</b>
Net fixed assets	191.65	202.79	221.38	179.30	188.96	187.65
Capital work-in progress	20.74	1.06	1.13	48.00	12.21	7.45
Investments	2.84	2.79	2.79	2.79	2.79	2.79
<b>Current Assets &amp; Loans and Advances</b>	<b>1224.31</b>	<b>1076.27</b>	<b>1023.20</b>	<b>989.34</b>	<b>922.56</b>	<b>766.76</b>
Inventory	534.65	442.64	403.37	512.86	479.00	414.87
- Raw material	399.13	268.88	195.79	330.77	279.12	242.19
- Work-in-process	0.00	0.00	0.00	0.00	0.00	27.02
- Finished goods	135.52	173.76	207.58	182.09	199.88	145.66
Receivables	430.98	408.55	398.60	337.48	313.76	273.29
Cash and bank balance	113.04	89.71	93.76	59.24	60.01	37.59
Loans and advances	142.83	128.62	125.95	76.20	66.13	41.02
Other current assets	2.81	6.75	1.53	3.55	3.66	0.00
Miscellaneous expenses not written off	0.00	0.00	0.00	0.00	0.00	0.20
<b>Total Assets</b>	<b>1439.54</b>	<b>1282.91</b>	<b>1248.50</b>	<b>1219.44</b>	<b>1126.52</b>	<b>964.85</b>
Current portion of long-term debt	20.76	23.87	27.42	27.42	26.48	0.00

**Exhibit 2: Profit and Loss Account of National Steel and Agro Industries Ltd.**

	<b>Mar-15</b>	<b>Mar-14</b>	<b>Mar-13</b>	<b>Mar-12</b>	<b>Mar-11</b>
<b>Net Sales</b>	<b>3883.87</b>	<b>3499.43</b>	<b>3484.35</b>	<b>2784.90</b>	<b>2540.24</b>
Raw material cost	3437.53	3087.33	3070.79	2424.98	2238.57
Employee cost	40.92	34.57	33.26	27.84	26.36
Power and fuel	67.80	60.58	53.65	43.88	38.27
Other manufacturing expenses	36.10	32.66	32.15	30.96	26.12
Depreciation	15.28	20.57	19.15	17.54	17.83
General and administration expenses	17.42	14.49	14.16	13.09	9.84
Selling and distribution expenses	95.48	78.40	96.89	78.05	70.34
Miscellaneous expenses	5.64	12.75	14.73	11.97	3.24
Less: Expenses capitalised	0.00	0.00	0.00	0.00	0.00
Total operating cost	3716.16	3341.35	3334.78	2648.30	2430.56
<b>EBIT</b>	<b>167.71</b>	<b>158.07</b>	<b>149.57</b>	<b>136.60</b>	<b>109.68</b>
Interest	136.42	127.05	124.89	109.81	83.93
PBT and extraordinary items	31.29	31.02	24.68	26.79	25.75
Other income/expenses	17.10	12.14	12.37	7.27	13.62
Exceptional income/expenses	0.00	0.00	0.00	0.00	0.00
PBT	48.40	43.16	37.05	34.06	39.37
Tax	18.25	12.70	8.16	5.33	7.13
<b>PAT</b>	<b>30.15</b>	<b>30.46</b>	<b>28.89</b>	<b>28.73</b>	<b>32.24</b>
Dividend	0.00	0.00	0.00	0.00	0.00

Source: Ace Equity



**Exhibit 3: Forex Transactions of National Steel and Agro Industries Ltd.**

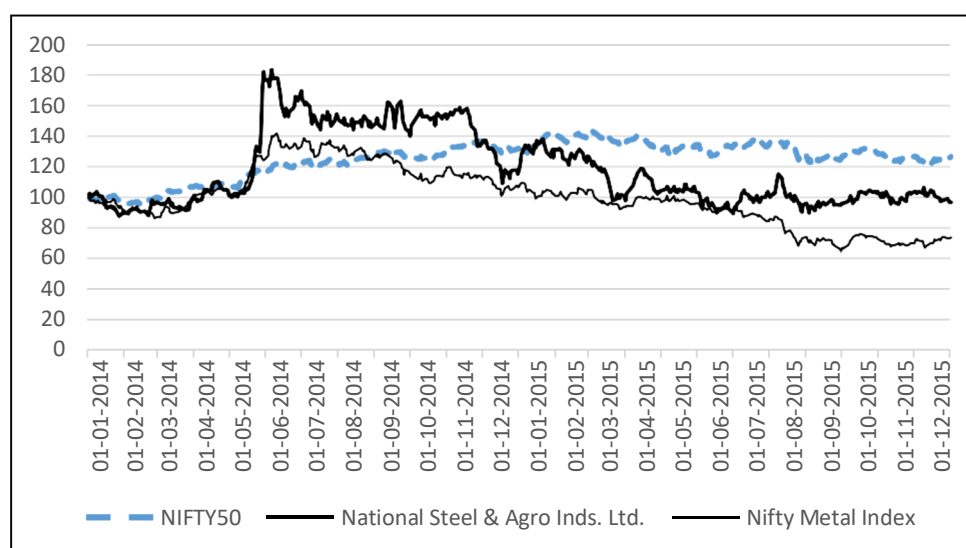
<b>DESCRIPTION</b>	<b>Mar-15</b>	<b>Mar-14</b>
<b>EXPORTS</b>		
Total Inflow in Foreign Currency	556.16	352.93
Exports - FOB Value	556.16	352.93
<b>IMPORTS</b>		
Total Outflow in Foreign Currency	1165.12	154.19
Imports - CIF Value	1141.45	146.04
Raw Materials	473.08	15.38
Traded Goods	668.37	130.66
<b>Total Capital Outflow</b>	17.91	0.20
Capital Goods	17.91	0.20
Expenditure in Foreign Currency	5.76	7.94

Source: Ace Equity

**Exhibit 4: Projected Financials for the Year 2015-16**

	<b>2015-16</b>
Paid Up Capital	44.50
Tangible Net worth	417.31
Medium & Long-Term Loans	0.00
Current Liabilities	611.23
Net Block	222.44
Investments in Group Companies	2.79
Current Assets	1184.60

	<b>2015-16</b>
Gross Sale	3887.01
Domestic	3063.07
Exports	823.94
Net Sales	3735.81
Other Income	3.35
EBIDTA	204.35
Depreciation	26.85
Interest	105.13
Taxes	24.68
Net Profit / (Loss)	54.68

**Chart 2: Relative Movement in National Steel's Share Price**

Source: Data from Ace Equity compiled and analysed by the author.

**Exhibit 5: Details for Assessment of LC for Steel Business**

	<b>HRCs</b>		<b>Zinc</b>		<b>Paints</b>		<b>CRCs</b>	<b>Stores</b>
	<b>Domestic</b>	<b>Import</b>	<b>Domestic</b>	<b>Import</b>	<b>Domestic</b>	<b>Import</b>	<b>Imports</b>	<b>Domestic</b>
Total Purchase	597.7	700.78	131.79	164.14	36.85	55.6	82.31	11
Purchase under LC	80%	100%	80%	100%	100%	100%	100%	90%
Purchase through EPBG Cash Flow	0	660	0	0	0	0	0	0

**Exhibit 6: Details for Assessment of LC for Trading Business**

	<b>Agro Products</b>	
	<b>Domestic</b>	<b>Import</b>
Total Purchase	596.37	894.56
Purchase Supposed to be under LC	95%	95%
Purchase through EPBG Cash Flow	0	0