Panama Petrochem Limited (Revised)

July 01, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term Bank Facilities	49.00	CARE A-; Stable (Single A minus; Outlook: Stable)	Revised from CARE A; Negative (Single A; Outlook: Negative)
Short term Bank Facilities	600.00	CARE A2+ (A Two Plus)	Revised from CARE A1; (A One)
Total Facilities	Rs.649.00 (Six Hundred and Forty Nine Crore Only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in rating assigned to the bank facilities of Panama Petrochem Limited (PPL) factors in weaker than envisaged financial performance for FY19 marked by weakening of debt coverage indicators and moderation in liquidity indicators marked by elongation in working capital cycle. Marginal decline in operating profit margin (impacting cash accruals) coupled with elevation in working capital cycle translated into negative operating cash flow for FY19.

The ratings continue to derive strength from the extensive experience of the promoters in the petrochemical industry with diverse product offerings. The rating also favourably factors in its long-standing relationship with reputed clientele and addition of new clientele, which has further diversified its client base.

The ratings are however, tempered by subdued demand from end user industries leading to a decline in sales volume for FY19; albeit the same was partially offset by improving sales realization. Furthermore, PPL reported a marginal decline in operating profit margin in FY19 on the back of higher selling expenses and forex losses, which in turn led to weakening of debt coverage indicators. PPL's liquidity profile moderated during FY19 marked by elongation in working capital cycle coupled with lower cash accruals and reduced cash and bank balance as on March 31, 2019. The ratings also continue to be tempered by PPL's limited value addition translating into modest profitability, and susceptible of profit margins to volatility in the prices of key raw materials and foreign exchange fluctuations.

Detailed description of the key rating drivers

Key Rating Strengths

Extensive experience of the promoters in the Petrochemical business with diverse products offerings

The Rayani family has been in the petrochemicals business for over three decades. Mr Amirali Rayani is the Chairman of PPL and his son Mr. Amin Rayani is the Managing Director & CEO, in charge of the day-to-day operations. They are assisted by a team of qualified and experienced professionals for various functions such as operations, marketing, finance, etc.

PPL manufactures over 80 product variants of base oil, which is used across broad industry segments such as printing ink, resin, cosmetics, rubber products, pharmaceuticals, engineering, textiles, machinery manufacturing chemical and petrochemical industries etc. Cosmetics industry accounts for the highest share of revenue (23% of revenue) followed by Inks/coatings (21% of revenue) and textile (19% of revenue).

Subdued demand from end user industry led to decline in sales volume for FY19; albeit same was partially offset by improving sales realization

PPL reported 4% decline in its Total Operating Income during FY19; the decline was attributed to decline in sales volume witnessed during the year. PPL reported a sizeable decline in sales volume for most of its product segments, with maximum decline in volume sold in the ink and cosmetics segments. Despite reporting the sizable decline in sale volume of key revenue contributing products, the decline in Net Sales for FY19 was arrested to decline of 4% on back of higher sales realization witnessed during the year. Further, subdued demand coupled with elevated installed capacity, led to a decline in capacity utilization in FY19 to 82% (P.Y. 119%).

Catering to demand from reputed and diversified clientele, however, sharp decline in export sales in FY19

PPL caters to the demand of reputed and a diversified clientele with includes industry majors such as Hubergroup (for Inks), Gulf Oil & IOCL (for lubricants), Dabur (for cosmetics) etc. PPL receives monthly orders from its clients with monthly price resets thus, the fluctuations in raw material prices and exchange rates is passed on to its customers with a lag of one month. PPL also exports to over 40 countries globally such as South America, Africa, Europe and Far East. In FY19, export sales witnessed a decline on account of muted demand from end users.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Key Rating Weaknesses

Moderation in operating profit margin and consequent deterioration in debt coverage

PPL reported weakened operating profit margin for FY19 largely on account of higher selling and distribution expenses and higher forex losses for FY19. Generally, the key raw material cost constitutes 80-85% of overall manufacturing cost. For FY19, the constitution of material cost in overall cost structure reduced to 84% (FY19) from 86% in FY18, this translated into stable gross margins for FY19. However, the PBILDT margins were impacted due to higher freight outward cost and reported forex loss of Rs.10.29 crore. Further, the RoCE% also weakened during FY19 as company relied more on short term debt to fund its working capital which pushed up the capital deployment in business, while operating margins remained weak. Higher utilization of working capital limits resulting in high interest expense, coupled with decline in PBILDT levels and lower cash accruals led to worsening of interest and debt coverage indicators of the company for FY19.

Susceptibility of its operating profit to volatility associated with key raw materials (which are derivatives of Crude Oil) and forex risk

Base oil, the key raw material used in the manufacturing of PPL's products is a derivative of crude oil and its price largely depicts the price volatility of crude oil. The price of crude oil is affected by factors like global demand, global production, geo-political factors and government regulations hence tend to remain highly volatile. Crude price has shown considerable volatility in the last financial year increasing to a high of $85 a barrel in September 2018 and declining to $52 a barrel in December 2018 however, for majority of the year, it hovered in the range of $66 -$67 a barrel. While PPL is able to pass on the price changes to its customers, it happens with a lag of one month and high volatility in prices may impact the profit margins adversely.

Besides, PPL is exposed to currency fluctuation risk mainly on account of its import payables and export receivables in foreign currency. The major exposures of the company are in U.S. dollars. As during FY19, the company's exports being less than imports, the company was a net importer and incurred forex losses of Rs.10.29 crore owing to currency fluctuations. The company's profit margins remain susceptible to foreign exchange fluctuation risk.

Liquidity profile

Though the liquidity indicators moderated during FY19, same remained adequate. The moderation in liquidity was on account of elongation in working capital cycle which increased from 53 days in FY18 to 88 days in FY19. Elongation in cycle also led to negative cash flow from operations. The cash and bank balance which was Rs.26.7 crore as on Mar. 31, 2018 reduced to Rs.7.25 crore as on Mar. 31, 2019. The utilization of bank facilities remained moderate at ~62% imparting some liquidity cushion. PPL does not have any term loan, hence there are no fixed debt repayment obligations.

Analytical approach: Changed from Standalone to Consolidated.

Change in approach from standalone to consolidated is primarily on account of parent and the subsidiary relationship, with subsidiary being in similar line of business. Demonstrated track record of supporting the subsidiary via explicit support extended through corporate guarantee. Panol Industries RMZ FZE, a 100% subsidiary of PPL has been consolidated.

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology-Manufacturing Companies
Financial ratios – Non-Financial Sector
Rating Methodology: Factoring Linkages in Ratings

About the Company

Incorporated in the year 1982, Panama Petrochem Limited (PPL) is promoted by the family members of Rayani family. PPL is engaged in the business of manufacturing of petroleum derivative products which find application in industries such as cosmetics & pharmaceuticals, Inks/Coatings, textiles, automobile, power, engineering, and rubber. The product portfolio includes liquid paraffin oils, petroleum jelly, ink oils, antistatic coning oil, rubber process oils, transformer oils, cable filling compounds and paraffin wax (some portion of wax is traded). Majority of PPL's income is derived from domestic market, under export sales it caters to countries like South America, Africa, Europe and Far East. PPL has four manufacturing facilities located at Ankleshwar (Gujrat), Daman (Union Territory), Taloja (Raigadh, Maharashtra) and Dahej (Bharuch, Gujarat) with an aggregate installed capacity of 210,000 MTPA as on March 31, 2019 (FY18: 180,000 MTPA).

Besides, PPL has overseas operations in UAE managed by its wholly owned subsidiary Panol Industries, RMC FZE (Panol). Panol has a manufacturing facility at Ras Al Khaimah (UAE) to manufacture Transformer Oils, Industrial Lubricants, Rubber Process Oils, etc. with an installed capacity of 30,000 MT per year.

Brief Financials (Rs. crore)	**FY18 (A)**	**FY19 (A)**
Total operating income	1,327.64	1,271.83
PBILDT	108.67	102.42
PAT	60.97	51.88
Overall gearing (times)	1.24	1.00
Interest coverage (times)	7.90	4.07

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Non- Fund based – ST – BG/LC	-	-	-	600.00	CARE A2+
Fund based – LT- Cash Credit	-	-	-	49.00	CARE A-; Stable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Non-fund-based - ST-BG/LC	ST	600.00	CARE A2+	1)CARE A1 (02-May-19)	1)CARE A1 (16-Oct-18)	1)CARE A1 (08-Jan-18) 2)CARE A1 (31-Oct-17) 3)CARE A1 (01-Sep-17) 4)CARE A1 (03-May-17)	1)CARE A1 (04-Oct-16)
2.	Fund-based - LT-Cash Credit	LT	49.00	CARE A-; Stable	1)CARE A; Negative (02-May-19)	1)CARE A; Stable (16-Oct-18)	1)CARE A+; Stable (08-Jan-18) 2)CARE A+; Stable (31-Oct-17) 3)CARE A+; Stable (01-Sep-17) 4)CARE A; Stable (03-May-17)	1)CARE A (04-Oct-16)

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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