Panama Petrochem Limited (Revised)

August 6, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-Term Bank Facilities	**49.00**	**CARE A-; Stable [Single A Minus; Outlook : Stable]**	Reaffirmed
Short-Term Bank Facilities	**600.00**	**CARE A2+ [A Two Plus]**	Reaffirmed
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 ratings assigned to the bank facilities of Panama Petrochem Limited (PPL) continues factor in the extensive experience of the promoters in the petrochemical industry with diverse product offerings, long-standing relationship with reputed clientele and track record of consistently catering to them over the years. The ratings derive strength from the improvement in the liquidity profile of PPL as indicated by substantial improvement in Cash Flow from Operations on the back of strict working capital management. This has also resulted in building up of a liquidity back-up in the form of unencumbered cash and bank balance of Rs. 30.45 crore as on March 31, 2020. Owing to improved working capital management, the dependence on external borrowing was low which improved the leverage as on Mar. 31, 2020.

PPL witnessed substantial reduction in its plant capacity utilization during end of March 2020 till mid of April 2020, as country was under government-imposed lockdown then. Since, PPL also caters to demand of pharmaceuticals segment, the operations commenced from late April 2020 and plant capacity utilization levels reached respectable levels since May 2020. The demand from end user industry also picked up from June 2020 and debtor realization has remained robust during this time. Although, Q1FY20 is expected to be weaker, CARE believes, improved cash flow from prudent working capital management has provided sufficient liquidity cushion to wither the CoVID-19 impact.

The ratings are constrained by the decline in total operating income witnessed in FY20 on a YoY basis on account of subdued demand from end user industries, resulting in lower capacity utilization levels which, coupled with lower realizations on products resulted in a decline in PBILDT margins during the year. However, CARE expects PBILDT margins to improve in FY21 on the back of certain cost rationalization measures adopted by PPL and improved capacity utilization levels of its manufacturing units post resumption of operations after the relaxations of lockdown on account of CoVID-19. With debtor realizations remaining at healthy levels on the back of reputed clientele enjoyed by the company and prudent working capital management practices adopted by it, CARE expects the liquidity profile of PPL to remain comfortable in the near term.

The ratings 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.

Rating sensitivities:

Positive Factors:

- Operating income increasing above Rs.1300 core on sustained basis
- Return on capital employed improving beyond 25% on a sustained basis

Negative Factors:

- Operating profitability declining below 5% on a sustained basis
- Overall gearing increasing above 1.00x on a sustained basis
- Interest coverage deteriorating below 3.00x on a sustained basis

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

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

petrochemical industries etc. Cosmetics industry accounts for the highest share of revenue (24% of revenue in FY20) followed by Inks/coatings (22% of revenue in FY20) and textile (20% of revenue in FY20).

Repeat orders from reputed and diversified clientele
PPL caters to the demand of reputed and a diversified clientele with includes industry majors such as Hubergroup (for Inks), Gulf Oil & Indian Oil Corporation Limited (for lubricants), Dabur India Ltd. (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 with exports accounting for 35%-40% of the total sales.

Subdued demand from end user industry led to decline in sales volume translating into decline in its Total Operating Income
PPL reported 21% decline in its Total Operating Income in FY20 on a YoY basis; the decline was attributed to decline in sales volume of ~20% and dip in sales realizations of ~8% on an average witnessed during the year. Overall slump in the domestic and global markets adversely impacted the total operating income of PPL in FY20. Further, the management had consciously decided to discontinue or reduce business from clients with elongated payment cycles. As such, this led to shrinking of overall volumes during the year. PPL is engaged in the manufacturing of petroleum derivative products with very little value addition and also operates in a highly competitive market thus, leading to low bargaining power with clients. In a weak economic scenario, PPL had to compromise on its realisations to ensure optimum sales volumes.

Robust recovery witnessed post CoVID 19 lockdown
PPL's plants were shut on account of nationwide lockdown imposed due to CoVID -19. However, its Ankleshwar plant commenced operations in early April 2020 as it was supplying to the pharmaceutical sector. The other plants commenced operations from April 20, 2020 after relaxations were announced by GoI. Capacity utilization has picked up as manufacturing units of its end user industries have commenced operations with plants now operating at near 90% capacity utilization levels. Sales have also picked up as manufacturing units of its clients have started operations post lockdown relaxations. Debtor realizations have also been steady during this period. As such, PPL has been able to meet its import payments and other obligations from the realized cash, keep its fund based working capital utilization low and has maintain a comfortable level of cash and bank balance.

Substantial reduction in debt levels owing to prudent working capital management practices led to improvement in leverage indicators as on Mar. 31, 2020
Debt levels for the consolidated entity have reduced considerably from Rs. 412.06 crore as on March 31, 2019 to Rs. 234.59 crore as on March 31, 2020 which led to overall gearing improving from 1.00x as on March 31, 2019 to 0.54x as on March 31, 2020. Reduced working capital borrowing on the back of improvement in collection efficiency as well as better inventory management has resulted in reduced reliance on external debt for working capital needs.
Management has taken cautious approach during last year (FY20) to reduce the sales volume with clients that requires extending higher credit period. Although, this has impacted their ability to grow on sales volumes, same has translated into improved working capital management and lower reliance on external debt.
Better working capital management has also resulted in substantial improvement in cash flow from operations (CFO) with reported CFO after working capital changes being positive Rs. 178.80 crore in FY20 as against a negative figure of Rs. 78.31 crore in FY21. Thus, total debt/ CFO has also shown substantial improvement.

Key Rating Weaknesses
Moderation in profitability indicators in FY20; albeit recovery expected based on cost rationalisation measures
PPL reported weakened operating profit margin for FY20 largely on account of underutilization of capacities on the back of subdued demand. PPL's is engaged in the manufacturing of petroleum derivative products with very little value addition and also operates in a highly competitive market thus, leading to low bargaining power with clients. In a weak economic scenario, PPL had to take a hit on its realisations to ensure optimum sales volumes thus, resulting in a decline in operating profitability. Reduced scale of operations coupled with deterioration in operating profitability adversely impacted ROCE% for PPL during FY20 despite, reduction in overall capital employed.

	FY16	FY17	FY18	FY19	FY20
PBILDT %	6.43	9.30	8.19	8.05	5.61
PAT %	3.34	5.24	4.59	4.08	2.86
RoCE%	14.08	21.68	26.78	19.20	9.24

Decline in operating profit margin is also attributed to decline in sales volume, as previously, management was extending higher credit period which was generating them higher sales volume on same operating overheads. As indicated by management, they have taken cost rationalization measures (under cost heads like freight, manpower and power cost) for reducing their operating overheads and extending lower credit period which would translate into lower utilization of fund based limits and lower finance cost. Results on these rationalization efforts would be visible from FY21 and thus CARE believes, the PBILDT margin is expected to recover to some extent for the full year FY21.

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 quarter of FY20 declining from a high of $66 a barrel in April 2019 to $20 a barrel in March 2020 however, for majority of the year, it hovered in the range of $55 -$66 a barrel. Change in the price of base oil take place with a lag of two months. 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. The company's profit margins remain susceptible to foreign exchange fluctuation risk.

Liquidity: Adequate
Absence of long term debt coupled with moderate average working capital utilization (fund based and non- fund based) at 36.93% for the 12 months ended April 2020 has resulted in comfortable liquidity position of the company. Further, PPL had unencumbered cash balance of Rs. 30.45 crore as on March 31, 2020. Further, improved working capital management has resulted in positive cash flow from operations in FY20. The management made a conscious effort during the year to reduce business from clients where receivable cycle was stretched as well as at reducing inventory holding period which had earlier resulted in blocking of capital in meeting working capital requirements.

Analytical approach: Consolidated.
PPL publishes consolidated wherein, the 100% subsidiary Panol Industries, RMC FZE (Panol; in similar line of business) is consolidated. PPL has extended corporate guarantee for debt availed by Panol, thus, there is legal obligation to support the subsidiary.
Applicable Criteria

Criteria on assigning Outlook and Credit Watch 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: Consolidation & Factoring Linkages in Ratings
CARE's policy on curing period

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 1,80,000 MTPA as on March 31, 2020.
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)	FY19 (A)	FY20 (A)
Total operating income	1,271.83	1,005.91
PBILDT	102.42	56.40
PAT	51.88	28.78
Overall gearing (times)	1.00	0.54
Interest coverage (times)	4.07	3.23

A: Audited

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

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	ISIN	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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Non-fund-based - ST-BG/LC	ST	600.00	CARE A2+	-	1)CARE A2+ (01-Jul-19) 2)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)
2.	Fund-based - LT-Cash Credit	LT	49.00	CARE A-; Stable	-	1)CARE A-; Stable (01-Jul-19) 2)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)

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not available

Annexure 4: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Non-fund-based - ST-BG/LC	Simple

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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