

## Pennar Industries Limited

February 13, 2019

### Ratings

Facilities	Amount (Rs. crore)	Rating <sup>1</sup>	Rating Action
Long term Bank Facilities	358.75 (enhanced from 230.00)	<b>CARE A; Positive</b> <b>(Single A; Outlook: Positive)</b>	Reaffirmed
Short term Bank Facilities	317.50 (enhanced from 175.00)	<b>CARE A1</b> <b>(A One)</b>	Reaffirmed
<b>Total Facilities</b>	<b>676.25</b> <b>(Rs. Six Hundred Seventy Six crore</b> <b>and Twenty Five lakh only)</b>		

*Details of instruments/facilities in Annexure-1*

### Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Pennar Industries Limited (PIL) continue to draw strength from experienced promoter group and management team, long track record of operations, wide product range with presence across diversified business segments, reputed and diversified client base, comfortable capital structure & debt coverage metrics and a satisfactory liquidity position. The ratings also take into account improvement in financial performance during FY18 (refers to the period April 1 to March 31) with substantial growth in revenue. The ratings are, however, constrained by risks associated with volatility in raw material price, limited pricing flexibility, moderation in profitability and debt coverage indicators during H1FY19, extension of working capital cycle during FY18 thereby resulting in increased dependence on working capital borrowings (at a consolidated level), capital intensive nature of business with persistent debt funded capex and competition from other players. The ability of the company to improve the profitability and financial position while managing the requirements of expanding scale of operation are the key rating sensitivities.

### Outlook: Positive

The 'Positive' outlook reflects PIL's continuous endeavor to diversify its product portfolio with investments in high margin segments and expected introduction of new range of products resulting in expansion of scale of operation. This along with optimization of the capital expenditure, and operational expenditure associated with requirements of expanding business would drive improvement in credit profile.

### Detailed description of the key rating drivers

#### Key Rating Strengths

**Long track record of the group:** Incorporated in 1975 as a cold rolled steel strips manufacturer, PIL has expanded its business profile with acquisition of related companies, setting up new plants, expansion of existing units and diversifying into value-added products in the engineering & infrastructure segment. Furthermore, it has significantly increased its presence in the pre-engineered business segment and water & environment infrastructure business through its subsidiaries; Pennar Engineered Building Systems Limited (PEBSL) and Pennar Enviro Limited (PEL) respectively.

**Experienced promoter group with strong management team:** The promoters of Pennar group have been in the engineered steel products business for more than four decades. The company is headed by Mr Nrupender Rao (Chairman) and Mr. Aditya Rao (Vice Chairman and MD), who have long presence in the industry. Furthermore, PIL is managed by a professional board comprising 12 directors with all the directors having long-standing industry experience of more than two decades.

**Diversified product range and revenue profile:** PIL has a diversified product portfolio having wide industrial use ranging from automobile, white goods, general engineering, domestic appliances, buildings and construction, railways, solar mounting structure and chemical treatment plants. The revenue profile of PIL is thus diversified with contributions from four major business units viz. Steel Products, Systems & Projects, Tubes and Industrial Components. The company has been gradually diversifying its revenue stream with a view to reduce concentration on the steel and railway vertical and has been consistently making investments in expansion of its product portfolio across different verticals.

**Reputed and diversified client base:** PIL is an established player in the industry and the clientele comprises renowned names in the industrial and manufacturing industry from which the company has been garnering repeat orders. As the products are technical in nature, clients share related designs and the products are manufactured to exclusively cater to their requirements. The clientele includes Ashok Leyland Ltd, Lloyds Insulation Limited, Integral Coach Factory (Perambur), Modern Coach Factory (Rae Bareli), L&T Construction, Hindustan Unilever Ltd, Emerson Climate Technologies Private Ltd, etc.

**Improvement in financial performance during FY18:** PIL registered y-o-y revenue growth of 15% in total operating income during FY18 (to Rs.1774.31 crore) over FY17 at consolidated level. This was backed by increased orders from all major business verticals, with company expanding its product portfolio during the year. In line with increased revenue, PBILDT level improved substantially by 31.2%. However, in terms of margins, there has been a moderate growth (from 10.43% to 11.91%) given the increased overhead of the new product segment/unit at Velchal.

PIL divested its entire stake in its subsidiary; Pennar Renewables Private Ltd. to Greenko group during January 2018 and profit from sale of same also pulled up PAT for FY18.

During H1FY19, PIL registered total operating income of Rs.994.44 crore reflecting a y-o-y growth of about 16.2% over H1FY18. However, subdued profit level and margin of PEBS vertical resulted in decline in PBILDT level (by about 3.8%) and margin from 10.64% in H1FY18 to 8.81% in H1FY19.

**Satisfactory financial and liquidity position:** The capital structure of the company has been satisfactory as on March 31, 2018, with both debt-equity and overall gearing ratio below unity as on the said date. However, there has not been a marked improvement in the financial position despite the significant profit and cash accrual generated and the overall gearing ratio remains at almost the same level since past 3 years.

The liquidity profile has been satisfactory backed by adequate cash generation and free cash/liquid funds maintained, majorly invested in mutual funds. The said funds, however, are not expected to be continued at the same level given the investment plans envisaged. Nevertheless, the short term debt coverage ratio is expected to remain satisfactory at about 15.2x in FY19 and the current ratio also remained moderate at 1.14x as on March 31, 2018.

#### Key Rating Weaknesses

**Risk associated with volatility in raw material prices:** The raw material cost is the major cost component and accounted for 70-75% of the total cost of sales in the last three years ended FY18. The input prices being highly volatile subjects the profitability to risk associated with adverse movement of prices.

**Capital intensive nature of business with persistent debt funded capex:** The Company's business nature is capital intensive and hence to maintain market position, PIL has been continuously investing in expansion of its product base across different segments. However, all the capital expenditure plans are majorly debt funded and hence the term debt position of the company has been similar over the years. This in turn has resulted in moderation in debt coverage parameters and return ratios with Total debt/GCA at 4.50x in FY18; although improved from 6.95x in FY17. The debt level is expected to further increase going forward and thus, the ability of the company to optimize the debt level and improve the capital structure remains important from credit perspective. In FY18, the company completed capex of approx. Rs.100 crore and for FY19 too, it has undertaken capex of Rs.100.0 crore being funded through debt of Rs.75.0 crore and balance through internal accruals.

**Extended operating cycle with growing dependence on working capital borrowings:** PIL operates in a working capital intensive industry also marked by high inventory level as the company has to stock the raw material due to volatility associated with input prices mainly at PEBSL level. The operating cycle of the company extended to 82 days during FY18 (from 50 days in FY17). Further, there is growing dependence on working capital borrowings majorly to fund the operations at recently completed Velchal plant and other expansion capex undertaken. The working capital utilization has been on the higher side with average utilization of about 85% during last 12 months.

**High competition from major players:** The engineering segment is a highly competitive and low margin business with competition from large integrated steel manufacturers. However, the industry growth prospects are stable with significant railway budget announced, growth in renewable energy segment and improvement in the automobile industry.

#### Analytical approach: Consolidated

CARE in its analysis has considered the consolidated business and financial risk profiles of Pennar Industries Ltd. and its subsidiaries; Pennar Engineered Building Systems Limited (PEBSL), Pennar Enviro Limited (PEL), and Pennar Global INC, together referred to as Pennar group, as the entities are linked through a parent-subsidiary relationship and collectively have management, business & financial linkages.

#### Applicable Criteria

[Criteria on assigning Outlook to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Rating Methodology: Factoring Linkages in Ratings](#)

[Criteria for Short Term Instruments](#)

[CARE's methodology for Manufacturing Companies](#)

[Financial ratios – Non-Financial Sector](#)

### About the Company

Pennar Industries Limited (PIL), incorporated in 1975, is engaged in manufacturing of cold rolled steel strips (installed capacity of 110,000 MT) and engineered steel products, majorly cold rolled formed sections (installed capacity of 144,200 MT) at its manufacturing facilities spread across six places in South India. PIL is particularly focused on the value-added engineered products segment and the business is divided into four major verticals; Steel Products (cold rolled steel strips, building products and formed sections), Systems and Projects (Railways and Solar module mounting systems (MMS) components), Industrial Components (general Engineering and Automotive components) and Tubes (Electric Resistant Welded, and Cold Drawn Tubes).

During FY18, the company sold its entire stake in the subsidiary; PRPL, to Hyderabad based Greenko group. The company has also announced merger of its subsidiaries; PEBSL and PEL with itself, and the proposed scheme of amalgamation has been approved by the requisite majority equity shareholders of the Company (including public shareholders). The same is expected to be completed before March 31, 2019. Hence, in the interim period, the company continues to extend corporate guarantee to the bank facilities of the said subsidiaries.

Brief Financials (Rs. Crore) – PIL Consolidated	FY17 (A)	FY18 (A)
Total operating income	1542.89	1774.31
PBILDT	160.93	211.34
PAT	49.78	90.49
Overall gearing (times)	1.01	0.97
Interest coverage (times)	2.62	3.15

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

**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](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications.

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In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

**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
Fund-based - LT-Cash Credit	-	-	-	200.00	CARE A; Positive
Fund-based - LT-Term Loan	-	-	March 2024	158.75	CARE A; Positive
Non-fund-based - ST-BG/LC	-	-	-	237.50	CARE A1
Non-fund-based - ST-BG/LC	-	-	-	80.00	CARE A1

**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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Cash Credit	LT	200.00	CARE A; Positive	1)CARE A; Positive (31-Dec-18)	1)CARE A; Positive (08-Jan-18)	1)CARE A; Positive (21-Feb-17) 2)CARE A; Positive (11-Jan-17)	1)CARE A (08-Dec-15)
2.	Fund-based - LT-Term Loan	LT	158.75	CARE A; Positive	1)CARE A; Positive (31-Dec-18)	1)CARE A; Positive (08-Jan-18)	1)CARE A; Positive (21-Feb-17) 2)CARE A; Positive (11-Jan-17)	1)CARE A (08-Dec-15)
3.	Non-fund-based - ST-BG/LC	ST	237.50	CARE A1	1)CARE A1 (31-Dec-18)	1)CARE A1 (08-Jan-18)	1)CARE A1 (21-Feb-17) 2)CARE A1 (11-Jan-17)	1)CARE A1 (08-Dec-15)
4.	Non-fund-based - ST-BG/LC	ST	80.00	CARE A1	1)CARE A1 (31-Dec-18)	1)CARE A1 (08-Jan-18)	1)CARE A1 (21-Feb-17) 2)CARE A1 (11-Jan-17)	1)CARE A1 (08-Dec-15)

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