Pennar Industries Limited (Revised)

August 21, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term Bank Facilities	358.75	**CARE A; Stable (Single A; Outlook: Stable)**	**Revised from CARE A; Positive (Single A ; Outlook: Positive)**
Short term Bank Facilities	317.50	**CARE A1 (A One)**	**Reaffirmed**
Long term Bank Facilities (Proposed)	165.00	**CARE A; Stable (Single A; Outlook: Stable)**	**Assigned**
Short term Bank Facilities (Proposed)	8.00	**CARE A1 (A One)**	**Assigned**
Long-term/Short-term Bank Facilities (Proposed)	312.50	**CARE A; Stable/ CARE A1 (Single A; Outlook: Stable/ A One)**	**Assigned**
Total	**1161.75 (Rs. One Thousand One Hundred and Sixty One Crore and Seventy five lakhs only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the enhanced 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 also take into account further improvement in revenues albeit decline in profitability margins during FY19. The ratings are, however, constrained by risks associated with volatility in raw material price, limited pricing flexibility, 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: Stable

The revision in outlook from 'Positive' to 'Stable' is on account of the company not being able to improve its margins as envisaged from its diversified product portfolio and optimization of the capital expenditure and operational expenditure. CARE envisages the margins of the company to remain stable going forward.

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. Subsequently, as per the NCLT order pronounced on May 08, 2019 the subsidiaries namely Pennar Engineered building Systems Limited and Pennar Enviro Limited have been amalgamated with PIL.

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

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

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.

Improvement in total operating income albeit decline in profitability margins during FY19:

PIL registered y-o-y revenue growth of 22% in total operating income during FY19 (to Rs. 2159.85 crore) over FY18 at consolidated level. Despite increase in the TOI of the company, the PBILDT levels deteriorated primarily on account of increase in raw material expenses and inability of the company to pass through the increased expenses to customers completely. The PBILDT margin of the company deteriorated from 11.91% in FY18 to 9.26% in FY19 while the PAT margin of the company also declined from 5.10% in FY18 to 3.09% in FY19.

As per published results for Q1FY20, the company has reported TOI of Rs.541.36 crore and PAT of Rs.16.61 crore which represent a y-o-y growth of 16.05% and 15.43% respectively over Q1FY19. The PBILDT margin remained at 10.19% for the quarter.

Satisfactory financial and liquidity position: The capital structure of the company has been satisfactory as on March 31, 2018 and March 31, 2019, 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.

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 four years ended FY19. 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 87.27% during last 12 months ended June 2019.

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:

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. Hence, the consolidated financials of the three entities have been considered till FY19. Subsequently, as per the NCLT order pronounced on May 08, 2019 the subsidiaries (PEBSL and PEL) have been amalgamated with PIL and hence, the standalone financials of PIL for Q1FY20 represent the financials of all the three entities together.

Applicable Criteria

[Criteria on assigning Outlook and Credit Watch to Credit Ratings]
[Rating Methodology: Factoring Linkages in Ratings]
[CARE's Policy on Default Recognition]
[Criteria for Short Term Instruments]
[Rating Methodology - 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).

Subsequently, as per the NCLT order pronounced on May 08, 2019 the subsidiaries namely Pennar engineered Building Systems Limited and Pennar Enviro Limited have been amalgamated with PIL.

Brief Financials – Consolidated (Rs. Crore) –	FY18 (A)	FY19 (A)
Total operating income	1774.31	2,159.85
PBILDT	211.34	199.91
PAT	90.49	66.66
Overall gearing (times)	0.97	NA
Interest coverage (times)	3.15	2.66

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
Fund-based - LT-Cash Credit	-	-	-	200.00	CARE A; Stable
Fund-based - LT-Term Loan	-	-	March 2024	158.75	CARE A; Stable
Non-fund-based - ST-BG/LC	-	-	-	237.50	CARE A1
Non-fund-based - ST-BG/LC	-	-	-	80.00	CARE A1
Fund-based - LT-Cash Credit	-	-	-	150.00	CARE A; Stable
Fund-based - LT-Term	-	-	-	15.00	CARE A; Stable

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Loan					
Non-fund-based - ST-Letter of credit	-	-	-	7.00	CARE A1
Non-fund-based - LT/ ST-BG/LC	-	-	-	290.00	CARE A; Stable / CARE A1
Non-fund-based - ST-Forward Contract	-	-	-	1.00	CARE A1
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	22.50	CARE A; Stable / 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 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.	Fund-based - LT-Cash Credit	LT	200.00	CARE A; Stable	-	1)CARE A; Positive (13-Feb-19) 2)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)
2.	Fund-based - LT-Term Loan	LT	158.75	CARE A; Stable	-	1)CARE A; Positive (13-Feb-19) 2)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)
3.	Non-fund-based - ST-BG/LC	ST	237.50	CARE A1	-	1)CARE A1 (13-Feb-19) 2)CARE A1 (31-Dec-18)	1)CARE A1 (08-Jan-18)	1)CARE A1 (21-Feb-17) 2)CARE A1 (11-Jan-17)
4.	Non-fund-based - ST-BG/LC	ST	80.00	CARE A1	-	1)CARE A1 (13-Feb-19) 2)CARE A1 (31-Dec-18)	1)CARE A1 (08-Jan-18)	1)CARE A1 (21-Feb-17) 2)CARE A1 (11-Jan-17)
5.	Fund-based - LT-Cash Credit	LT	150.00	CARE A; Stable	-	-	-	-
6.	Fund-based - LT-Term Loan	LT	15.00	CARE A; Stable	-	-	-	-
7.	Non-fund-based - ST-Letter of credit	ST	7.00	CARE A1	-	-	-	-
8.	Non-fund-based - LT/ ST-BG/LC	LT/ST	290.00	CARE A; Stable / CARE A1	-	-	-	-

9.	Non-fund-based - ST-Forward Contract	ST	1.00	CARE A1	-	-	-	-
10.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	22.50	CARE A; Stable / CARE A1	-	-	-	-

***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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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.