Phillips Carbon Black Limited

February 08, 2018

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	554.00 (reduced form 618.00)	**CARE AA-; Stable (Double A Minus; Outlook: Stable)**	**Revised from CARE A+; Stable (Single A Plus; Outlook: Stable)**
Long/Short Term Bank Facilities	1,850.00	**CARE AA-; Stable/CARE A1+ (Double A Minus; Outlook: Stable/A One Plus)**	**Revised from CARE A+; Stable/CARE A1+ (Single A Plus; Outlook: Stable/A One Plus)**
Total Facilities	**2404.00 (Rs. Twenty Thousand Four Hundred and Four crore only)**		
Commercial Paper (CP) issue*	500.0 (Rs. Five Hundred crore only)	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

**The aggregate of CP and other working capital borrowings should be within the sanctioned working capital limits of the company.*

Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities of Phillips Carbon Black Limited (PCBL) takes into account consistent improvement in the financial and operating performance of the company in FY17 (refers to the period April 01 to March 31) and 9MFY18 marked by improvement in the capacity utilisation along with improvement in the debt protection metrics of the company along with increase in contribution (sales volume) of specialty carbon in FY17 & 9MFY18 leading to better margins during the aforesaid period. The revision also takes into account the favorable demand outlook for the domestic carbon black industry backed by increased demand scenario from domestic tyre industry.

The rating further derives strength from strong promoter group (RP-Sanjiv Goenka) and satisfactory track record of operations, leadership position in the domestic carbon black industry, strategic location of the plant, steady source of revenue from power segment, strong export presence, improvement in the capital structure and hedging of net foreign exposure. The above strengths are, however, partially offset by risk of volatility of raw material prices, foreign exchange fluctuation risk, stringent pollution norms for the industry and cyclicality in the industry due to dependence on the fortune of the tyre industry, which is mitigated with increase in sale of specialty black product. The rating also takes into account the green-field project undertaken by the company for which the financial closure is yet to be achieved.

Going forward, ability of the company to continue to improve the product mix and trend in crude oil price would remain the key rating sensitivities. Further completion of the on-going brownfield project and achieve financial closure for the Greenfield expansion and project completion timeline would also be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Group support & satisfactory track record

PCBL is a part of RP-Sanjiv Goenka Group of Kolkata. The other major companies of the group are CESC, Firstsource Solutions Ltd, Saregama India, Noida Power, Spencer's Retails, etc. RP-Sanjiv Goenka Group has interests across diverse business segments such as power & natural resources, infrastructure, carbon black, retail, and media & entertainment. The total turnover of the group was Rs.15,626 crore in FY17. PCBL has a highly qualified and experienced employee pool having large experience in their related field.

Strategic location of the plant

CBFS, CBO and carbon black are bulk products and therefore, transportation is a major issue. PCBL has a strategic advantage vis-à-vis its competitors as its units are situated at different parts of India, close to the ports and major tyre manufacturing plants. Its location facilitates PCBL in optimizing transportation cost.

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

Steady source of revenue from the power segment

PCBL has captive power plants aggregating to 76 MW at all its manufacturing facilities. Power production over and above its captive requirements are sold to the respective state grids; thus providing a steady source of revenue. During FY17, power sales accounted for 4-5% of total operating income during FY16 & FY17.

Strong export presence

PCBL is the seventh largest CB producer in the world and the largest exporter of CB from India. The company's export revenue was Rs.431.56 crore in FY17 (Rs.466.96 crore in FY16). Though PCBL's export realization is well below the domestic market prices, it continues to focus on the export market in anticipation of higher demand from US & Europe markets. Going forward, with increase in investment in tyre industry and demand abroad and reduction in export from China, PCBL expects significant amount of revenue generation from exports (mainly South East Asia).

Increased competitiveness of Indian CB manufacturers over Chinese counterparts on account of raw material cost and continued imposition of anti-dumping duty

The CB production in China is mainly based on carbon black oil (CBO - which is derived out of processing of waste obtained from coke oven batteries during steel production process), whereas domestic manufacturers produces mainly through CBFS. The CB imports from China has restricted to a great extent in the past two years due to a) increasing spread between CBFS and CBO on the back of closure of few plants in China on the back of environmental concerns and higher usage of CBO for other purposes and b) imposition of high anti-dumping duty in November 2015. This coupled with forced and increasing demand from Chinese automotive industry has improved the competitiveness of domestic CB manufacturers.

Improvement in the financial and operational performance in FY17 & 9MFY18 and improvement in the debt protection metrics

Financial performance of PCBL was marked by improvement in the profitability and debt protection metrics of the company quarter on quarter in FY17. The same performance was replicated by PCBL from Q1FY18 to Q3FY18. The improvement in the margins was on account of increase in volume sales of speciality carbon has also gone up from 4,700 MT in FY16 to 8,300 MT in FY17 coupled with high CB production in FY17 vis-à-vis FY16 leading to higher absorption of fixed cost. The increase in CB production was on account of higher demand from tyre manufacturers.

EBIDTA per tonne has improved in the last three years (FY15-FY17) on the back of commencement of specialty black business. The significant decline in interest costs (incl. hedging costs) in FY17 over FY16 due to efficient working capital management along with repayment of term debt obligation had led to substantial improvement in PAT margin to 3.60% in FY17 (0.89% in FY16).

In 9MFY18 (refers to the period April 01 to December 31), PCBL reported PAT of Rs.155.53 crore (PAT of Rs.36.87 crore in 9MFY17) on a total operating income of Rs.1802.63 crore (Rs.1382.54 crore). The operating margin of the company further improved and stood at 17.25% in 9MFY18 vis-à-vis 10.88% in 9MFY17 on the back of higher sale of specialty black products. The PAT margin also improved on the back of higher PBILT level coupled with decline in the capital charges; primarily interest cost.

Improvement in capital structure and debt protection metrics of the company

Long term debt equity ratio improved to 0.19x as on March 31, 2017 from 0.31x as on Mar.31, 2017. Overall gearing ratio also improved to 0.67x from 1.04x as on the aforesaid dates in view of decline in long term borrowings out of scheduled repayment and short term borrowings due to reduced working capital requirement.

The interest coverage ratio of the company also improved and stood at 3.67x in FY17 vis-à-vis 1.88x in FY16 on the back of increase in operating profit coupled with decline in interest cost of the company. Total debt to GCA and Total debt to PBILDT also improved and stood at 0.73x & 3.99x respectively as on March 31, 2017 vis-à-vis 11.11x & 5.38x as on March 31, 2016. The improvement was on account of decline in debt levels and increase in PBILDT and GCA level of the company in FY17 vis-à-vis FY16.

Improved demand outlook for carbon black (CB)

The Global carbon black industry operated at an improved estimated capacity utilization of 80% in FY17 against the demand supply imbalance created by huge capacity base installed in China. However, exports from China declined in the International market in 2017, due to loosing on competitive advantage over raw material cost, which it had enjoyed during recent years and also due to government crackdown on fragmented Carbon Black capacities to enforce stringent environment norms.

The key user industry of carbon black is tyre which is expected to grow due to improving demand from both domestic and export market. Global tyre manufacturers are planning to further invest around USD 22 billion in ramping up the capacity during the period 2016-2021. CB application for tyre manufacturing accounts for more than half of its total market size.

With high correlation of tyre, auto and carbon black, shows positive relationship among the three segments.
Non-tyre applications of CB include ink, paints, conveyor belts, etc. Though PCBL is gradually reducing its dependence on the tyre industry & diversifying itself towards non-tyre segment, the tyre segment continues to be the major contributor.
Carbon black market is witnessing increased penetration of specialty carbon black which provides sharp colour and enhanced conductivity, viscosity and UV protection. Demand for carbon black in paints and coatings and inks are expected to show an increase over the next five years. Demand for non-rubber applications that mainly use specialty blacks will display significant increase.

Key Rating Weaknesses

Volatility in raw material & finished goods prices

CBFS and CBO are the key raw-material for CB, accounting for around 78% of cost of sales in FY17. CBFS is a derivative product of crude oil refining and its price has a fair degree of co-relation with international crude oil price. CBO is a derivative of coal tar which is a by-product in the process of converting coking coal to coke (used for steel production). As indigenous CBFS/CBO do not meet the quality requirements (in terms of carbon content), PCBL uses imported CBFS. The prices of CBFS & CBO are highly volatile in nature as it is linked to volatile crude oil price and steel industry dynamics.
However, around 75-80% of PCBL's sales are determined using a pricing formula, which takes into account changes in oil prices and the Rupee –Dollar (US$) exchange rate.
The company maintains around 40 days of raw material inventory & around 5 days of finished goods inventory. So accordingly, if there is a fall in the raw material prices, the company might incur inventory losses which could impact the profitability of the company.

Foreign currency fluctuation risks

PCBL sourced 85% of its raw material requirement (CBFS, CBO, LDO, Tar oil) through imports and it exported around 23% of its gross sales. From October 2014 onwards the company has started to completely hedge its net forex exposure reducing the volatility in forex fluctuations risks to an extent. PCBL has reported forex gain of Rs.18.68 crore in FY17 as against forex gain of Rs.21.27 crore in FY16.

Future capex plan

PCBL has proposed to increase the capacity by 80,000 MTPA (including 32,000 MTPA of high margin specialty segment) at its existing plants at Palej and Mundhra, Gujarat. The total project cost is estimated to be Rs.320 crore and the same is expected to be financed in the D/E ratio of 0.78:1 (funded out of debt of Rs.140 crore and internal accruals of Rs.180 crore). The project is expected to be completed in phases by FY19. The company has done an expenditure of around Rs.70 crore on the project till date.
PCBL has undertaken a green-field project for a capacity of 1,20,000 MTPA for total cost of Rs.480 crore. The project is proposed to be financed in the D/E ratio of 2.33:1. Financial closure is yet to be achieved.
With majority of Specialty black being served (around 92%) by imports, PCBL has plans to raise the capacity of specialty black in the company to 56,000 MTPA from present 24,000 MTPA by FY20. The gross margin of Specialty black is around 4-5 times of the normal carbon black margin. The addition of the specialty carbon would lead to improvement in the operating margins of the company in the projected period.

Prospects

Ability to complete the on-going brownfield project and achieve financial closure and project completion timeline for the green-field project and improvement in the product mix would be the key rating sensitivities. Given the strong brand image, sound financial and liquidity position, PCBL is well placed to complete the on-going and future capex plan to retain its market position.

Analytical approach:

Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Financial ratios – Non-Financial Sector
Criteria for Short Term Instruments

CARE's methodology for manufacturing companies

About the Company

PCBL, incorporated in 1960, is engaged in the manufacturing & sale of carbon black, which is used in tyre & other rubber products. It is the leading producer of Carbon Black (CB) in the country (37% market share) and seventh largest in the world, with an installed capacity of 4,72,000 MTPA. Post de-bottlenecking, the capacity has increased to 5,02,000 MTPA (CB-4,78,000 MTPA; Speciality Black:24,000 MTPA) from December 2017. PCBL produces around 56 grades of CB spread across tyre rubber black, non-tyre rubber black and speciality black.

Further, PCBL also has captive power plants (CPP) at all its locations (aggregate capacity of 76 MW). The company also produces and sells excess electric power generated from the low calorific value off gas which is generated in the process of manufacturing of Carbon Black. Sale of surplus power to grid provides a steady alternative revenue stream. PCBL is managed under the stewardship of Kolkata-based RP–Sanjiv Goenka group.

Financials of Phillips Carbon Black Limited

Brief Financials (Rs. crore)	FY16 (A)	FY17 (A)
Total operating income	1894.53	1930.29
PBILDT	200.98	289.43
PAT	16.91	69.52
Overall gearing (times)	1.04	0.67
Interest coverage (times)	1.88	3.67

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. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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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	-	-	-	550.00	CARE AA-; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	1498.30	CARE AA-; Stable / CARE A1+
Term Loan-Long Term	-	-	Dec-20	4.00	CARE AA-; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	351.70	CARE AA-; Stable / CARE A1+
Commercial Paper	-	-	-	450.00	CARE A1+
Commercial Paper	-	-	-	50.00	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 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Commercial Paper	ST	50.00	CARE A1+	1)CARE A1+ (21-Jun-17)	1)CARE A1+ (09-Dec-16) 2)CARE A1+ (07-Sep-16) 3)CARE A1+ (11-Jul-16)	1)CARE A1 (20-Aug-15)	1)CARE A1 (05-Jan-15)
2.	Fund-based - LT-Cash Credit	LT	550.00	CARE AA-; Stable	1)CARE A+; Stable (21-Jun-17)	1)CARE A; Positive (09-Dec-16) 2)CARE A (07-Sep-16) 3)CARE A (11-Jul-16)	1)CARE A (20-Aug-15)	1)CARE A (05-Jan-15)
3.	Non-fund-based - LT/ ST-BG/LC	LT/ST	1498.30	CARE AA-; Stable / CARE A1+	1)CARE A+; Stable / CARE A1+ (21-Jun-17)	1)CARE A; Positive / CARE A1+ (09-Dec-16) 2)CARE A / CARE A1+ (07-Sep-16) 3)CARE A / CARE A1+ (11-Jul-16)	1)CARE A / CARE A1 (20-Aug-15)	1)CARE A / CARE A1 (05-Jan-15)
4.	Term Loan-Long Term	LT	4.00	CARE AA-; Stable	1)CARE A+; Stable (21-Jun-17)	1)CARE A; Positive (09-Dec-16) 2)CARE A (07-Sep-16) 3)CARE A (11-Jul-16)	1)CARE A (20-Aug-15)	1)CARE A (05-Jan-15)
5.	Non-fund-based - LT/ ST-BG/LC	LT/ST	351.70	CARE AA-; Stable / CARE A1+	1)CARE A+; Stable / CARE A1+ (21-Jun-17)	1)CARE A; Positive / CARE A1+ (09-Dec-16) 2)CARE A / CARE A1+ (07-Sep-16) 3)CARE A / CARE A1+ (11-Jul-16)	1)CARE A / CARE A1 (20-Aug-15)	1)CARE A / CARE A1 (05-Jan-15)
6.	Commercial Paper	ST	450.00	CARE A1+	1)CARE A1+ (21-Jun-17)	1)CARE A1+ (09-Dec-16) 2)CARE A1+ (07-Sep-16) 3)CARE A1+ (11-Jul-16)	1)CARE A1 (20-Aug-15)	1)CARE A1 (09-Mar-15)

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