Phillips Carbon Black Ltd

September 23, 2020

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Long Term Bank Facilities	550	CARE AA-; Stable (Double A Minus; Outlook: Stable)	Reaffirmed
Long Term/ Short Term Bank Facilities	1850	CARE AA-; Stable/ CARE A1+ (Double A Minus; Outlook: Stable/A One Plus)	Reaffirmed
Total	**2400 (Rs. Two thousand four hundred crore only)**		
Commercial Paper Issue	500 (Rs. Five Hundred Crore Only)	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to Phillips Carbon Black Limited (PCBL) continue to derive strength from it being a part of the established RP-Sanjiv Goenka Group, leadership position of the company in the domestic carbon black industry with satisfactory track record of operations, strategic location of the plants, strong presence in the export market, steady source of revenue from the power segment and comfortable capital structure and debt coverage indicators.

The ratings also factor in the moderation in operating margin in FY20 (refers to period April 1 to March 30) due to decrease in realisations on the back of slowdown in the major end user automobile industry, though the company could maintain sales volumes during the period.

The ratings also take note of the substantial decline in sales and profitability in Q1FY21 on account of the Covid-19 induced lockdown and slow-down during the period. While the production was impacted in April and May 2020, the capacity utilisation of various plants improved in June 2020. Nonetheless, it remained significantly low compared to the previous year and thus the total revenue is expected to be impacted materially in the full year, given the volume decline till date. Consequently, absolute profits and cash accruals will also be impacted despite various cost reduction initiatives undertaken by the company. However, given the conservative capital structure, the debt protection metrics and liquidity position of the company are expected to remain healthy. CARE expects gradual increase in demand leading to increase in sales volumes and PCBL's cash flows to remain comfortable relative to its debt service obligations, going forward.

The ratings continue to remain constrained by the risk of volatility in raw material and finished goods prices, stringent pollution norms for the industry, cyclicality in the industry due to dependence on the fortunes of tyre industry and threat of imports of carbon black. The ratings also take into account the implementation and stabilisation risks associated with the expansion projects being undertaken by the company.

Key Rating Sensitivities

Positive Factors

- Ability of the company to maintain PBILDT margin (>=18%) and PAT margin (>=10%) on a sustained basis.

Negative Factors

- Deterioration in overall gearing (>0.70x) and/or debt coverage indicators- TD/GCA (>4x) and interest coverage (< 6x) on a sustained basis.
- Sharp deviation in envisaged sales volumes or contribution having a significant bearing on the company's performance.
- Any regulatory change having the potential to materially impact the company's performance.
- Significant deterioration in liquidity profile.

Detailed description of the key rating drivers

Key Rating Strengths

Strong promoter group, satisfactory track record of operations with leadership position in the domestic carbon black segment

PCBL is a part of RP-Sanjiv Goenka Group of Kolkata which has interests across diverse business segments such as power & natural resources, infrastructure, retail and media & entertainment apart from carbon black. The other major companies of the group include CESC Limited (rated CARE AA; Stable/CARE A1+), Haldia Energy Limited (CARE AA-; Stable/CARE A1+) Saregama India Ltd (rated CARE A+; Stable/CARE A1+) and Noida Power Company Ltd.

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

PCBL commenced its operations from 1962 and has acquired a leadership position in the domestic carbon black industry with its installed capacity gradually increasing from 14,000 mtpa to 571,000 mtpa.

Strong presence in the export market

PCBL is the largest exporter of carbon black from India having presence in more than 40 countries, though majority of exports are to south-east Asian countries. The contribution of exports to sales increased from about 24% of sales volumes to about 29% of sales volumes in FY20.

Strategic location of the plant

PCBL's units are situated in different parts of India, close to the ports {for imports of Carbon Black feedstock (CBFS) and exports of carbon black} and near major tyre manufacturing plants. Its location facilitates PCBL in optimizing transportation cost.

Steady source of revenue from the power segment

PCBL has captive power plants aggregating to 76 MW at its manufacturing facilities. Power produced over and above the captive requirement is sold by PCBL and adds to the overall contribution per ton of carbon black produced. In FY20, while the power segment contributed to only 2.67% of PCBL's operating income (as against 2.76% in FY19), its contribution to overall PBIT (before un-allocable expense) was significant at around 17.47% in FY20 (14.96% in FY19). PCBL does not have any Power Purchase Agreement for off-take of power; however it enters into medium term agreements for the same. Also, a large part of the power is sold to group company, CESC Limited.

Healthy financial risk profile, albeit, moderation in operating profitability in FY20 and Q1FY21

The total operating income (TOI) decreased by about 8% y-o-y in FY20 on account of decrease in realizations of carbon black at the back of lower crude oil prices (driver of prices of raw material CBFS and thereby finished goods), even when sales volumes saw marginal increase. The y-o-y operating profit margin witnessed moderation from 18.27% in FY19 to 15.59% in FY20, due to decline in spreads owing to slow down in the auto sector which led to de-growth in the tyre production in the year. However, it continued to remain healthy.

Furthermore, profits in FY19 were exceptionally high due to increased demand from the tyre segment leading to supply shortages and therefore higher margin in the non-tyre segment. Despite de-growth in the domestic market in FY20, PCBL had been able to maintain sales volumes due to increased international presence.

In Q1FY21, the TOI had decreased y-o-y by 61% due to lower production and sales volumes, as a consequence of lock down and Covid-19 induced slowdown. On account of decline in sales volumes and under-absorption of fixed costs, the PBILDT margin also deteriorated to 9.99% in Q1FY21 as against 16.29% in Q1FY20. Though the overall revenue and profitability is likely to be impacted in FY21, the performance is expected to improve from Q2FY21 with relaxations in lockdown conditions and gradual increase in demand leading to increase in sales volumes.

Comfortable capital structure and debt protection metrics of the company

Overall gearing was comfortable and marginally improved from 0.54x as on March 31, 2019 to 0.51x (0.44x, excluding the impact of lease accounting) as on March 31, 2020 on account of lower year end borrowings and repayment of term debt. Total Debt to Gross Cash Accruals (TDGCA), barring the impact of lease liabilities improved as on March 31, 2020 against that on March 31, 2019 and was a little under 2x. Even with the ongoing capex and proposed term loans, the capital structure is expected to remain comfortable.

With moderation in operating margin in FY20, PBILDT interest coverage ratio deteriorated from 17.55x in FY19 to 11.04x in FY20. However, it continued to remain comfortable. In Q1FY21, inspite of substantial decline in profitability, the interest coverage remained above 3x.

Key Rating Weaknesses

Profitability susceptible to volatility in raw material prices, partially mitigated through the pricing formulae

CBFS is the key raw-material for CB, accounting for around 80% of cost of sales in FY20. CBFS is a derivative product of crude oil refining having strong correlation with crude oil prices and exhibits volatility. However, a significant portion of the sales of PCBL is to the tyre segment which operates as per pricing formulae, thereby reducing volatility in profits, if sales volumes are maintained.

Dependence on the fortunes of tyre industry

A major portion of PCBL's revenue is from sale of carbon black to tyre manufacturers, in line with the overall application of carbon black produced across the globe. More than 70% of the product is used for tyre manufacturing. This leads to PCBL's dependence on the fortunes of the tyre industry which in turn is dependent on the cyclical auto industry. Although more than 60% of the overall tyre market is the replacement market, slowdown in the auto segment not only affects the present OEM sales but also has the potential to impact the growth in the future replacement market. However, PCBL has also been increasing its presence in the specialty black range catering to diversified industries- paints, inks, plastics, etc. It also operates a R&D centre in Palej and Belgium where one of the objectives is to grow its portfolio in the specialty black segment.

Project risk in the form of ongoing and recently completed projects
PCBL had completed the capacity expansion of carbon Black in its Mundra unit by 56,000 MT in Q4FY19. Its ongoing speciality black project at Palej of Rs.230 crore funded through a mix of debt and equity is in advanced stage of progress and its commencement has been deferred to the end of FY21. The company has already spent Rs.177 crore on the project till July 2020.
This apart, PCBL also has a plan to set-up a green-field project of capacity of 1,50,000 MTPA for a total cost of Rs.600 crore in Tamil Nadu. However, the company has proposed to calibrate its capex plans against the demand scenario for carbon black.
Given the amount of investments and the slow-down in the end user industry there exists project execution, stabilization and marketing risks. Further, return indicators are also expected to be impacted in the medium term.

Stringent pollution norms for the major industry segments
The Central Pollution Control Board (CPCB) regulates the general standards for emission or discharge of environmental pollutants of carbon chemical industry. Presently, PCBL is adhering to the pollution norms of CPCB and all its plants are zero-discharge facility.

Threat of imports of carbon black
Anti-dumping duty (ADD) is applicable till November 2020 at around USD 397/MT on import of carbon black from China and at differential rates upon import from other countries. Imports of carbon black had increased in FY19 due to increase in demand from the tyre industry in India which has again reduced in FY20 on the back of slowdown in the auto sector.
China accounts for a significant portion of the world carbon black production and majorly produces carbon black through the Carbon Black Oil (CBO)/ Coal Tar route. Even though, currently production from coal tar route is not as competitive as compared through the CBFS route given the wide gap between the current prices of CBFS and CBO, it is seen that imports from China continued to constitute a significant part of carbon black imported into India despite anti-dumping duties being in place. A part of it is due to advance license with tyre companies which allow for duty free imports. Continuation of ADD post November 2020 is a rating monitorable.

Liquidity: Strong
PCBL has not opted for moratorium from its banks in terms of the Covid-19 Regulatory Package of RBI. The company's cash accruals even with anticipated moderation in FY21 and commitment for capital expenditure are expected to be sufficient to meet its balance scheduled repayment obligations. Further, the company has calibrated plans for its greenfield project of Rs.600 crore with the demand scenario and does not plan on incurring any significant expenditure against it in FY21 unless there is sufficient cash generation. PCBL had free cash and liquid investments of Rs.36 crore (parked in mutual funds) as on August 26, 2020. The average utilisation of working capital limits of Rs.550 crore was moderate at about 60% in the last 12 months ended August 2020. Apart from liquidity being supported by buffer available in fund based working capital limits, the company also enjoys financial flexibility by virtue of it being part of RP-SG group. Furthermore, the company is in the advanced stages of raising a term loan to meet the current year capital expenditure requirement which would provide support to the liquidity.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning Outlook & Credit watch to Credit Ratings
CARE's Policy of Default Recognition
Criteria for Short Term Instruments
Financial ratios - Non Financial Sector
Rating Methodology- Consolidation & Factoring Linkages in Ratings
Rating Methodology-Manufacturing Companies
Liquidity indicators- Non-financial sector entities

About the Company
PCBL, incorporated in 1960, is engaged in the manufacturing and sale of carbon black, which is mainly used in tyre and other rubber products. The company also produces specialty carbon blacks which are used as pigmenting, UV stabilizing and conductive agents in a variety of common and specialty products, including plastics, printing & packaging and coatings. PCBL is the largest producer of carbon black in the country and one of the largest players in the world, with an installed capacity of 5,71,000 MTPA of carbon black. It also has captive power plants (CPP) at all its locations (aggregate capacity of 76 MW). The company sells excess power generated. Its plants are located at Durgapur (West Bengal),

Mundra (Gujarat), Palej (Gujarat) and Kochi (Kerala). PCBL is managed under the stewardship of Kolkata-based RP–Sanjiv Goenka group.

Brief Financials (Rs. crore)- Standalone	**FY19 (A)**	**FY20 (A)**
Total operating income	3533.31	3250.49
PBILDT	645.42	506.86
PAT	388.53	283.49
Overall gearing (times)	0.54	0.51
Interest coverage (times)	17.55	11.04

A: Audited

Status of non-cooperation with other CRA: Not applicable

Any other information: Not Applicable

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

Annexure-1: Details of 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	-	-	-	1275.00	CARE AA-; Stable / CARE A1+
Non-fund-based - LT/ ST-BG/LC	-	-	-	575.00	CARE AA-; Stable / CARE A1+
Commercial Paper-Commercial Paper (Standalone)	-	-	7-364 days	450.00	CARE A1+
Commercial Paper-Commercial Paper (Standalone)	-	-	7-364 days	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 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.	Commercial Paper-Commercial Paper (Standalone)	ST	50.00	CARE A1+	1)CARE A1+ (02-Jun-20)	1)CARE A1+ (18-Feb-20)	1)CARE A1+ (26-Dec-18)	1)CARE A1+ (08-Feb-18) 2)CARE A1+ (21-Jun-17)
2.	Fund-based - LT-Cash Credit	LT	550.00	CARE AA-; Stable	-	1)CARE AA-; Stable (18-Feb-20)	1)CARE AA-; Positive (26-Dec-18)	1)CARE AA-; Stable (08-Feb-18) 2)CARE A+; Stable (21-Jun-17)
3.	Non-fund-based - LT/ ST-BG/LC	LT/ST	1275.00	CARE AA-; Stable / CARE A1+	-	1)CARE AA-; Stable / CARE A1+ (18-Feb-20)	1)CARE AA-; Positive / CARE A1+ (26-Dec-18)	1)CARE AA-; Stable / CARE A1+ (08-Feb-18) 2)CARE A+; Stable / CARE A1+ (21-Jun-17)
4.	Term Loan-Long Term	LT	-	-	-	-	1)Withdrawn (26-Dec-18)	1)CARE AA-; Stable (08-Feb-18) 2)CARE A+; Stable (21-Jun-17)
5.	Non-fund-based - LT/ ST-BG/LC	LT/ST	575.00	CARE AA-; Stable / CARE A1+	-	1)CARE AA-; Stable / CARE A1+ (18-Feb-20)	1)CARE AA-; Positive / CARE A1+ (26-Dec-18)	1)CARE AA-; Stable / CARE A1+ (08-Feb-18) 2)CARE A+; Stable / CARE A1+ (21-Jun-17)
6.	Commercial Paper-Commercial Paper (Standalone)	ST	450.00	CARE A1+	1)CARE A1+ (02-Jun-20)	1)CARE A1+ (18-Feb-20)	1)CARE A1+ (26-Dec-18)	1)CARE A1+ (08-Feb-18) 2)CARE A1+ (21-Jun-17)

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

Annexure 4- Complexity of various instruments rated for this Company

Sr. No.	Name of the Instrument	Complexity Level
1.	Commercial Paper-Commercial Paper (Standalone)	Simple
2.	Fund-based - LT-Cash Credit	Simple
3.	Non-fund-based - LT/ 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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