Press Release

Himadri Speciality Chemical Ltd

March 28, 2017

Rating

Instrument	**Amount**	**Rating**	**Rating Action**
Commercial Paper *(carved out of the tied-up fund based working capital limits of the company)*	Rs.25.00 crores	IVR A1+ (pronounced IVR A one plus)	Assigned

Details of Instrument are in Annexure 1

Infomerics Valuation and Rating Pvt. Ltd. has assigned IVR A1+ (pronounced IVR A one plus) rating to the proposed Rs.25.00 crores Commercial Paper Programme of Himadri Speciality Chemical Ltd. (HSCL). The CPs are likely to have a maximum tenor of 365 days. Instruments with this rating are considered to have very strong degree of safety regarding timely payment of financial obligations. Such instruments carry lowest credit risk.

Detailed Rationale

The aforesaid rating derives strength from the long presence of the company, its leadership position in Coal Tar Pitch market with about 70% share & prominent position in carbon black industry, having satisfactory client base in both domestic as well as in international market, satisfactory EBIDTA margin on consistent basis, improving profitability & cash accruals and comfortable capital structure. The rating also factors in dependence of the company on the fortunes of aluminium & tyre industries, raw material price volatility, exposure to foreign exchange fluctuation risk, high working capital intensity and book loss in the last two years. Ability of the company to continue earning modest level of EBIDTA margin & cash accruals leveraging on the increasing business potential, manage the forex fluctuation risk prudently and efficient working capital management are the key rating sensitivities.

List of Key Rating Drivers

- Long presence.
- Leadership position in Coal Tar Pitch market and prominent presence in Carbon Black market.
- Satisfactory client base.
- Satisfactory EBIDTA margin on consistent basis.
- Improving profitability & cash accruals after incurring book loss in the last two years
- Comfortable capital structure.
- Dependence on the fortunes of aluminium & tyre industries.
- Raw material price volatility.
- Exposure to foreign exchange fluctuation risk.
- High working capital intensity.

Detailed Description of Key Rating Drivers

Rating Strengths

Long presence

The company was incorporated way back in 1987 with coal tar distillation plant at Howrah, West Bengal. Over the years, the company has grown itself as the largest player in the coal tar pitch industry, besides diversifying into other products – major being carbon black. Currently, the company has eight units located across the country.

Leadership position in Coal Tar Pitch market and prominent presence in Carbon Black market

At present, HSCL is the major player in manufacturing of Coal Tar Pitch (CTP), having 70% market share. The company has also made a prominent presence in the domestic Carbon Black industry. The CTP is used majorly in aluminium, graphite electrodes and long war head missiles; whereas, carbon black finds applications mainly in tyre and rubber industries. HSCL has developed Impregnating Pitch and Mesophase Pitch and advanced carbon materials used in electrodes and lithium ion batteries. Till date, HSCL is the only company globally, outside Japan, to manufacture these products.

Satisfactory client base

HSCL has good client base both in domestic and international market. Some of the well-known domestic clients are Hindalco Industries, Mahan Aluminium, MRF Ltd and Vedanta Ltd. The company exports to more than 10 countries including Egypt, China, Poland, Indonesia and Bangladesh.

Satisfactory EBITDA margin on consistent basis

The company continued to earn a satisfactory level of EBIDTA margin over the years and the same also witnessed improvement in the recent past. This has been mainly due to higher level of production driven by capacity ramp up by the aluminium giants leading to better absorption of overheads, its dominant position in the CTP market commanding better price and foraying in speciality grade carbon black products yielding higher margin. In 9MFY17 (refers to the period from April 01 to December 31), EBIDTA witnessed a phenomenal increase on the back of better product pricing & higher capacity utilisation, among others.

Improving profitability & cash accruals after incurring book loss in the last two years

Increasing level of EBIDTA had contributed to higher level of accruals in FY16 (refers to the period from April 01 to March 31) and 9MFY17. However, the PAT got adversely impacted during the last three financial years (including FY16) due to significant level of foreign exchange fluctuation loss pertaining to its outstanding foreign currency loan. The dollar movement which the company had witnessed during the aforesaid period was erratic and unprecedented. However, the significant portion of such foreign exchange fluctuation loss was due to mark-to-market adjustment not entailing any cash loss. Notwithstanding this, the company has significantly reduced its foreign currency borrowing gradually and, currently, the same is about 20% of the total loan portfolio as compared to the peak level of 90% in the past. Further, the company has hedged its entire foreign exchange exposure. Increase in export is also providing higher natural hedging.

Comfortable capital structure

The capital structure of the company, as reflected by long-term debt-equity ratio and overall gearing, has been comfortable over the last three years and gradually improved with reduction in borrowing level. Long term Debt to EBIDTA has generally been comfortable indicating adequate debt protection coverage.

Rating Weaknesses

Dependence on the fortunes of aluminium & tyre industries.

Major user of CTP (about 75% of total CTP consumption) is aluminium sector which is generally volatile in nature. The slowdown in the commodity sector has an adverse impact on the aluminium industry in the past, besides the impact of rupee depreciation. The demand for carbon black is a derived demand of the tyre industry and hence, its success is highly dependent on the fortunes of the tyre industry which is again directly linked to the success of automobile industry.

Raw material price volatility due to linkage with global crude price

Carbon Black Feed Stock (CBFS), the main raw material for carbon black production, is a downstream product of crude oil refining and its price has a fair degree of co-relation with international crude oil price. HSCL (alongwith other carbon black manufacturers) has however, largely kept itself insulated from the hike in crude price due to a pricing formula (increase in raw material price is passed on quarterly) having been agreed with All India Tyre Manufacturers Association, but with one-quarter time lag.

Exposure to exchange fluctuation risk

The major raw materials, Coal Tar & Pitch for CTP and CBFS for Carbon Black production, are imported due to short supply in the domestic arena and/or cost effectiveness, Besides, the company has outstanding foreign currency loan. All these expose the company to foreign exchange fluctuation risk, although company's resorting to hedging the exposure through forward contracts and natural hedging by way of moderate level of exports act as a buffer. As for CBFS, the pricing formula, as aforesaid, agreed with All India Tyre Manufacturers Association mitigates such risk.

High working capital intensity.

HSCL's operations are working capital intensive due to its high inventory holding period and moderate average receivable collection period. The company enjoys a decent credit period from its suppliers, besides the backing of adequate working capital bank line. Further, a significant portion of its working capital bank line remains unutilised for a major part of the year, providing liquidity buffer in times of stress.

Analytical Approach: Standalone

Applicable Criteria
Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation

About the Company

HSCL, incorporated in 1987 by one Choudhary family of Kolkata, is currently the largest manufacturer of Coal Tar Distillates in India having 70% share in India's coal tar pitch market. The company is also one of the major players in Carbon Black market. It has eight plants, located four in West Bengal and one each in Andhra Pradesh, Gujarat, Chhattisgarh and Odisha. These apart the company has presence in Sulphonated Nepthalene Formaldehyde (SNF) & Poly Carboxylate Ether (PCE) manufacturing. Its aggregate capacity for coal tar distillation is 4 lacs metric tonne (MT) and for carbon black is 1.2 lacs MT. The company has captive power plants for aggregate capacity of 20 MW, besides 2.5 MW wind power generation capacity. During 9MFY17, the company reported a PAT of Rs.50.8 crores on a Total Operating Income of Rs.948.6 crores (as against Net Loss of Rs.12.1 crores and Total Operating Income of Rs.1151.8 crores in FY16)

Status of non-cooperation with previous CRA: Not applicable

Any other information: Nil

Rating History for last three years: Not applicable

Note on complexity levels of the rated instrument: Infomerics has classified instruments rated by it on the basis of complexity and a note thereon is available at www.infomerics.com.

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About Infomerics:
Infomerics commenced rating & grading operations in April 2015 after having spent over 25 years in various segments of financial services. Infomerics is registered with the Securities and Exchange Board of India (SEBI) and is gradually gaining prominence in domestic rating

and/or grading space. Infomerics is striving for positioning itself as the most trusted & credible rating agency in the country and is gradually widening its product portfolio. Company's long experience in varied spectrum of financial services is helping it to fine tune its product offerings to best suit the market.

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Annexure 1: Details of Instrument

Name of Instrument	Date of issuance	Coupon Rate/ IRR	Maturity Date	Size of issuance (Rs Crores)	Rating Assigned/ Outlook
Commercial Paper	Not yet issued	Market driven	Maximum tenor of 365 days	25.00	IVR A1+ (pronounced IVR A one plus)