Press Release

Haldia Petrochemicals Limited

December 21, 2017

Rating

Instrument / Facility	Amount (Rs. Crores)	Ratings	Rating Action
Commercial Paper (by earmarking fund based working capital bank limit)	100.00	IVR A1+ (IVR A One Plus)	Assigned

Details of facility are in Annexure 1

Detailed Rationale

The rating of Haldia Petrochemicals Limited (HPL) derives comfort from its strong promoters & experienced management team, locational advantage of its plant, steady raw material sourcing arrangements, healthy debt protection parameters and its strong liquidity position majorly supported by its improved financial performance in FY17 (FY refers to the period April 01 to March 31) and H1FY18 (refers to the period April 01 to September 30). The rating is further underpinned by HPL's dominant position in Eastern India for polymer products, its state-of-the art plant and positive demand outlook for the petrochemical industry in India. The rating also takes into account the vulnerability of profitability of the company to volatile input prices & significant fiscal incidence, exposure to foreign exchange fluctuation risk, receding draft level at the Haldia port and generally cyclical nature of the petrochemical industry. Profitability, gearing level and any debt laden greenfield/brownfield capex are the key rating sensitivities.

List of Key Rating Drivers

- Strong promoters and an experienced management team.
- Locational advantage.
- Steady raw material sourcing arrangements.
- Dominant position in Eastern India for polymer products.
- Improved financial performance in FY17 and H1FY18.
- Strong liquidity position.
- Healthy debt protection parameters.
- Positive demand outlook for the petrochemical industry in India.

- Vulnerability of profitability to volatile input prices and significant fiscal incidence.
- Exposure to foreign exchange fluctuation risk.
- Receding draft level at the Haldia port.
- Cyclical nature of the petrochemical industry.

Detailed Description of Key Rating Drivers

Key Rating Strengths:

Strong promoters and an experienced management team

The Chatterjee Group (TCG) and Government of West Bengal (GoWB), through West Bengal Industrial Development Corporation Limited (WBIDC), are the current major shareholders of HPL with TCG having the controlling stake (~55% as on September 30, 2017). Dr. Purnendu Chatterjee led TCG, founded in 1989, is a premiere private equity firm with investments and operations spanning several continents and industries. Dr. Chatterjee (a B.Tech from IIT Kharagpur and PhD from University of California, Berkeley) was associated with internationally reputed names like Mckinsey, Soros Fund Management and served as an Investment advisor to entities in the Quantum Group of Funds for over 13 years. In this role, Dr. Chatterjee has handled investments of over $3 billion across the world. TCG has made various investments in India in sectors like financial services, IT services, pharmaceuticals & life science and real estates. Other major companies of TCG operating in India are, TCG Lifesciences Private Limited, Clininvent Research Private Limited and TCG Digital. Further, TCG acquired controlling stake (90.4%) in Materials Chemicals and Performance Intermediaries Private Limited (MCPI), an Indian subsidiary of Mitsubishi Chemical Corporation (MCC), in November, 2016. MCPI is the second-largest producer of Purified Terephthalic Acid (PTA) in India with an installed capacity of 1.27 mtpa located at Haldia, West Bengal.

HPL is also managed by a team of highly qualified & experienced professionals under the guidance of a 12 member Board of Directors comprising representatives from TCG, GoWB and the term lenders along with independent directors.

Locational advantage

The manufacturing facility of the company, a state-of-the art plant, is located at Haldia, West Bengal, being close to the Haldia port. HPL majorly imports (around 70 - 75%) of its naphtha requirements from Middle East counties and also exports its finished products through the Haldia port. Proximity (about 7 Km) of the plant to the Haldia port is translated in low logistic expenses for the company, thereby providing a business competitiveness.

Steady raw material sourcing arrangements

HPL has long term sourcing arrangements through annual term contract with its major suppliers both in India and overseas for almost 75% of its naphtha requirement. The quantity of naphtha to be procured, delivery period and premium over market price to be charged as fixed by Median of Platts Arabian Gulf (MOPAG) is guided by the said annual contracts. HPL procures the balance requirements on spot basis mainly from domestic oil majors. Existence of fixed quantity naphtha procurement contracts ensures steady sourcing of raw materials.

Dominant position in Eastern India for polymer products

HPL, being the sole petrochemical manufacturer in the eastern part of the country, enjoys a leading position in the eastern and north eastern regions of the country.

Improved financial performance in FY17 and H1FY18

HPL has the history of having incurred cash loss leading to liquidity stress and delay in the debt servicing in the past which got compounded due to long-drawn differences between TCG and GoWB regarding the ownership and management control. However, in September 2014, GoWB agreed to offload its entire equity stake in tranches and transfer the management control to TCG. Under the management control of TCG, post debt restructuring in January 2015, the financial performance of the company improved significantly with robust profit and cash accruals driven by substantial improvement in spread between finished products (Polymers) and main raw material (Naphtha) coupled with high level of capacity utilisation in FY16 and FY17. Total operating income on a consolidated basis witnessed a marginal y-o-y increase of about 1.6% in FY17 due to almost full utilisation of its capacity and relatively stable polymer prices during the period. However, HPL earned a robust level of EBIDTA of Rs.2672.10 crores in FY16 and Rs.3406.83 crores in FY17 with healthy

EBIDTA margin of 26.15% in FY16 and 32.82% in FY17. The decent level of EBITDA margin was mainly driven by decline in naphtha prices vis-à-vis relatively stable finished goods prices during the aforesaid period. The PAT significantly improved from Rs.119.75 crores in FY16 to Rs.863.29 crores in FY17. During the first half of the current financial year (HY1FY18), HPL posted a PBT of Rs.292 crores on net sales of Rs.4884 crores. HPL is executing projects to set up a 30KT Butene-1 manufacturing facility and a Py Gas Desulphurization facility within the existing plant premises at Haldia at an envisaged cost of ~Rs.298 crores and ~Rs.105 crores respectively, being funded through internal accruals only. These facilities are expected to be operational from September 2018 which is likely to have a consequential positive impact on EBIDTA in near to medium term. However, the profit margins of the company are likely to be dampened a bit in near term due to an increasing trend in the Naphtha prices.

Strong liquidity position

The liquidity position of HPL is highly comfortable with its robust cash and liquid investment balance (including accrued interest) aggregating about Rs.5583 crores (including free investments in mutual funds of Rs.2996 crores and free cash and bank balance of Rs.192 crores) as on November 30, 2017. This is attributable to healthy cash generation since recommencement of its operations from February, 2015 and release of earmarked investments & fixed deposits due to reduction in outstanding guarantee level.

Healthy debt protection parameters

The debt protection parameters of the company became healthy in the last two years and improved noticeably in FY17 over FY16. The interest coverage ratio improved from 3.59x in FY16 to 5.41x in FY17 and Total debt to GCA from 2.61x in FY16 to 1.72x in FY17. Long-term Debt to EBIDTA also remained comfortable at 1.32x in FY17. Further, HPL generated a robust cash accrual of Rs.2929.93 crores in FY17 and prepaid loans aggregating to Rs.456 crores during FY17 and further Rs.33 crores during the current year (till November 30, 2017).

Positive demand outlook for the petrochemical industry in India

The outlook for petrochemical industry in India is positive in the medium to long term as domestic per capita consumption of petrochemical derivatives is much lower than that of world level, indicating a strong potential for substantial growth. Further, increasing use of polymer based products in different industries, higher presence of traditional materials leading to higher opportunities for substitution, insignificant size of the industry in comparison to major global peers and expected higher GDP growth, rising urbanisation and per capita income levels are expected to auger well for the industry.

Key Rating Weaknesses

Vulnerability of profitability to volatile input prices and significant fiscal incidence

Naphtha forms around 80-90% of HPL’s cost of production. Being a crude derivative, Naphtha prices are subject to volatility with a consequential impact on its profitability. Further, the company needs to maintain an inventory of about 30-45 days for smooth running of its operation, besides requiring a lead time of around 20-25 days. Hence, the company is also exposed to inventory writing down in case of adverse movement of prices of Naptha. Apart from this, the prices of polymers (finished products) are also driven by the import parity prices; therefore, any negative fluctuation can tamper the profitability. However, fluctuation in Naphtha prices is generally passed on to the end consumers in a steady state of operations. Also, duty differentials on import of Naphtha and Polyolefin Polymer (finished goods) play significant role in determining the profitability of HPL. Any adverse movement in import duty structure (lowering of the duty differential) may restrict the competitiveness of the company and tamper the profitability. However, post Goods and Service Tax (GST) implementation in India in July, 2017, HPL is gradually increasing its Naphtha procurement from domestic sources to mitigate any eventuality. Further, majority of its chemical products are exported which entitles the company for duty free import of raw material.

Exposure to foreign exchange fluctuation risk

The profitability of the company is also susceptible to foreign exchange fluctuations as majority of the raw materials are imported. However, HPL, being an exporter, enjoys a natural hedging to an extent and uses forward contracts to reduce the risk of foreign exchange fluctuations. Further, polymer prices are linked to international price movements thereby enabling the company to mitigate foreign exchange fluctuation risk partially.

Receding draft level in Haldia port

Receding draft level in the Haldia port is a matter of concern for HPL as majority of its raw materials are imported and around 17-18% of its sales are in the form of exports to many East Asian countries. Currently, HPL is using the Vizag port (raw material imported at Vizag and then transferred to Haldia port in small ships) to mitigate the risk to an extent; however, entailing higher transportation charges. While the recent signs of stabilisation of draft level at Haldia are likely to be a matter of comfort, the company is also considering alternative options like feasibility of feedstock pipeline from Dhamra / Paradeep port and/or using upcoming Tajpur deep-water port close to Haldia.

Cyclical nature of the petrochemical industry

The global petrochemical industry has been inherently cyclical and is sensitive to changes in supply and demand, caused by political and economic factors. The international petrochemical markets have witnessed volatility in prices and profit margins driven by limited supply, on one hand, and expansion in production capacity, on the other. The profitability in the petrochemical industry is affected by the worldwide level of demand along with vigorous price competition. Further, there is a high degree of correlation between the economic growth and the growth in polymer consumption.

Analytical Approach and Applicable Criteria:

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation (Non-financial Sector)

About the Company

HPL is one of largest (4th) domestic polyolefin manufacturers in India. It manufactures polymer products like Linear Low Density Polyethylene (LLDPE), High Density Polyethylene (HDPE), Polypropylene (PP) and Chemicals (Viz. Benzene, Butadiene, Cyclopentane, C4 Hydrogenated (LPG), Pyrolysis Gasoline (Py Gas), Motor-Spirit and Carbon Black Feed stocks (CBFS)) at its naphtha cracker unit (capacity of 670,000 MTPA of Ethylene and 335,000 MTPA of Propylene). HPL also owns a 116 MW naphtha based captive power plant (CPP) at its facility. CBFS is also used in the CPP as fuel alternative to naphtha due to its cost effectiveness. Naphtha based petrochemical complex (spread across 1119 acres) of the company, located in Haldia, West Bengal (125 km from Kolkata) was commissioned in 2000 and started operation from 2001. HPL has two subsidiaries, Haldia Riverside Estate Limited (HREL) and HPL Global PTE Limited (HPGL). HREL is engaged in the real estate activities and maintaining the Haldia township for HPL employees. HPGL is a Singapore-based entity which is yet to become operational to act as a commission agent for procurement of materials for HPL and other group companies.

Financials (Consolidated)

(Rs. Crores)

For the year ended* / As On	**31-03-2016**	**31-03-2017**
	Audited	**Audited**
Total Operating Income	10218.72	10381.73
EBITDA	2672.10	3406.83
PAT	119.75	863.38
Total Debt	5263.69	5045.51
Tangible Net worth	3765.56	6065.79
EBITDA Margin (%)	26.15	32.82
PAT Margin (%)	1.16	8.09
Overall Gearing Ratio (x)	1.40	0.83

*Classification as per Infomerics' standards

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Nil

Rating History for last three years:

Sr. No.	**Name of Instrument/Facilities**	**Current Rating (Year 2017-18)**			**Rating History for the past 3 years**		
		Type	**Amount outstanding (Rs. crore)**	**Rating**	**Date(s) & Rating (s) assigned in 2016-17**	**Date(s) & Rating(s) assigned in 2015-16**	**Date(s) & Rating(s) assigned in 2014-15**
1.	Commercial Paper	Short Term	100	IVR A1+ (IVR A One Plus)	-	--	--

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 accredited by Reserve Bank of India. It 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.

Annexure 1: Details of Facilities

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility (Rs. Crore)	Rating Assigned
Commercial Paper	-	-	-	100.00	IVR A1 + (IVR A One Plus)