Press Release

Phillips Carbon Black Ltd.

January 31, 2018

Rating

Instrument/Facility	Amount (Rs. Crores)	Rating	Rating Action
Term Loan (Present Outstanding)	4.52	IVR AA-/Stable Outlook (IVR Double A minus with Stable Outlook)	Revised from IVRA+/Stable (IVR Single A plus with Stable Outlook)
Total	**4.52**		

Details of Facility are in Annexure 1

Detailed Rationale

The rating revision factors in improving operational efficiency and increasing focus towards high margin product segment by the company resulting in improvement in profitability parameters and higher cash accruals and consequential improvement in debt coverage indicators of the company. The aforesaid rating continues to derive comfort from established position of the group and vast experience of the management team, leadership position and its long presence in the carbon black segment, strategic location of plants, captive power plants at all manufacturing locations providing operational efficiency, established clientele both in domestic & overseas arena and comfortable liquidity position. The rating is however, constrained by the susceptibility to volatility in margins due to variation in raw material price, dependence on the demand of carbon black to fortunes of tyre industry and associated risks with implementation of proposed projects. The aforesaid rating also takes cognisance of emission risk due to polluting nature of the products and threat of imported carbon black & tyres. Ability of the company to maintain its profitability and successful implementation of the proposed projects without unduly impacting its gearing levels are the key rating sensitivities.

List of Key Rating Drivers

- Established position of the group and experienced management team

- Leading position and long presence in Carbon Black segment

- Strategic location of plants
- Captive power plants at all manufacturing locations providing operational efficiency
- Established clientele
- Increasing focus towards high margin product segments
- Improving profitability parameters
- Comfortable and improving debt protection indicators
- Comfortable liquidity position
- Susceptibility to volatility in margins due to variation in raw material price
- Dependence on the fortunes of tyre industry
- Associated risks with implementation of proposed projects, but success would augment its leadership position in the industry

Detailed Description of Key Rating Drivers

Established position of the group and experienced management team

Phillips Carbon Black Ltd. (PCBL), incorporated in 1960, is one of the major entities of the Kolkata-based RP-Sanjeev Goenka Group. The RP-Sanjeev Goenka group is one of the leading industrial houses of the country with interest in power generation & distribution, coal, carbon black, retailing, entertainment and BPO business with CESC Ltd. being the flagship company. Other major companies of the group are CESC Infrastructure Ltd, Firstsource Solutions, Haldia Energy and Spencer Retail. PCBL has highly qualified and experienced management team.

Leading position and long presence in Carbon Black segment

PCBL has been in the carbon black industry since 1960. It is one of the India's oldest and largest carbon black producers. PCBL offers comprehensive portfolio of Carbon Black for rubber applications and Specialty Black for non-rubber applications across plastics, fibre, pipes, inks & coatings, wire & cable and other niche industries globally.

Its entry in speciality black segment is a relatively recent phenomenon. It manufactures over 50 different grades of carbon black and is also a major exporter.

Strategic location of plants

PCBL has its plants located in Durgapur (W.B.), Palej&Mundra (Gujarat) and Kochi (Kerala). PCBL has a strategic advantage vis-à-vis its competitors as most of its units are situated close to the ports and to the major tyre manufacturing plants (which are primarily the end users of carbon black). Around 80% of the raw material consumed by PCBL is imported and exports comprise around 20% of sales. Hence, the strategic location of the plant provides the company with both time and cost advantage in terms of logistics and supply chain management.

Captive power plants at all manufacturing locations providing operational efficiency

PCBL has captive power plants at all the manufacturing locations using a by-product, i.e, waste gas (tail gas) derived during the production of carbon black, to generate power. PCBL's income profile comprises income from two segments, i.e. carbon black and power. The power generation process involves recovery and utilisation of such gas, entailing no cost. Approximately 35% of power generated by PCBL is being used to meet captive requirement, while balance 65% is sold to grid. This alternative revenue stream acts as a modest buffer for the company thereby improving operational efficiency.

Established clientele

PCBL has strong network of local distributors and channel partners across several countries. PCBL exports its products to over 30 countries across five continents. PCBL’s clientele includes global leaders in the tyre industry such as Bridgestone Corporation and Goodyear Tire & Rubber Company, as well as leading Indian tyre manufacturers like MRF, Ceat, J. K. Tyres, Apollo Tyres, Bridgestone India and Goodyear India.

Increasing focus towards high margin product segments

The company is consciously focusing on enhancing the portfolio of premium products, like manufacturing of high performance, high margin grade carbon black for rubber applications and speciality black for non-rubber applications. The gross margin in case of specialty black is almost 3.5 times the margin for carbon black segment. During FY17, income from non-rubber products formed 9% of total volume, but contributed to 20% of EBITDA. This strategic focus of the company towards high margin products is also expected to support the company to maintain good margins, going forward.

Improving profitability parameters

The profitability margins of the company have been majorly improving majorly on quarter-to-quarter basis over the last two years. EBITDA margin improved from 11.71% in FY16 to 16.18% in FY17 on account of higher capacity utilisation (94% in FY17 as against 81% in FY16), increasing sales volume for premium products and higher profitability from power. Higher EBIDTA level with lower interest cost due to repayment of debt resulted in significant improvement in PAT margin from 0.88% in FY16 to 3.57% in FY17. The PAT margin further improved to 8.37% in H1FY18 (from 2.47% in H1FY17). Given the positive outlook for the automobile industry in India and the resultant increase in demand of tyres, PCBL expects that the capacity utilisation would remain high, going forward, and thus, its expanded capacities will also be well utilised. The summarised position of profitability and gross cash accruals over the last seven quarters is tabulated below:

Ratios	**Q4FY16**	**Q1FY17**	**Q2FY17**	**Q3FY17**	**Q4FY17**	**Q1FY18**	**Q2FY18**
EBITDA Margin (%)	10.77	14.90	14.50	14.84	15.05	16.70	16.81
PAT Margin (%)	0.60	2.21	2.71	3.94	5.14	8.29	8.50
Gross Cash Accrual (Rs. Crore)	18.25	24.60	27.75	34.37	43.25	63.41	66.00

Comfortable and improving debt protection indicators

PCBL repaid a substantial portion of its long term debt and contained the working capital borrowings by virtue of its strong cash flow from operations which resulted in considerable improvement in overall gearing from 1.83 as on March 31, 2016 to 1.17 as on March 31, 2017. Long term debt-equity ratio also improved from 0.57 as on March 31, 2016 to 0.32 as on March 31, 2017. Total debt to GCA also witnessed mark improvement from 10.51 times in FY16 to 3.99 times in FY17 on account of reduction in overall debt level coupled with almost doubling of the Gross Cash Accruals from Rs.97 crore in FY16 to Rs.190 crore in FY17. Interest coverage also improved from 1.73 times in FY16 to 3.20 times in FY17. With continuing improvement in profitability, the debt coverage metrics are expected to remain healthy, going forward.

Comfortable liquidity position

The average utilisation of working capital bank limit during the year ended December 2017 was very low indicating significant liquidity buffer for the company. This is also evident from the fact that the company has prepaid some of its long term loans due to high level of GCA. Operating cycle also improved to a comfortable level of 27 days in FY17 from 74 days in FY16.

Susceptibility to volatility in margins due to variation in raw material price

Carbon Black Feed Stock, the main raw material, is a downstream product of crude oil refining and its price has a fair degree of co-relation with international crude oil price. PCBL (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. Around 60%-65% of PCBL's sales in terms of volume are to tyre manufacturers. Even in overseas, the pricing formula works for sales to tyre manufacturers pertaining to crude price variation, but with a monthly time lag. In view of the foregoing, PCBL manages to significantly mitigate the raw material price volatility risk.

Although PCBL is exposed to forex fluctuation risk, the same is mitigated by virtue of natural hedging partially (as PCBL is both an importer and an exporter) and the net position is also hedged.

Dependence on the fortunes of tyre industry

The demand for carbon black is a derived demand of the tyre industry. The demand in the tyre industry is dependent on the growth in automobile sector & replacement demand for tyres and is cyclical in nature. However, the company has been gradually foraying into speciality grade carbon black segment thereby diversifying into non-tyre and non-rubber products to insulate itself from the aforesaid dependence.

Associated risks with implementation of proposed projects, but success would augment its leadership position in the industry

PCBL is expanding capacities in Gujarat. It is building additional capacity at two locations – 48,000 MT at Mundra and 32,000 MT at Palej for Hard line Carbon Black and Specialty Carbon Black respectively. The estimated total project cost is Rs.300 crores, of which around Rs.140 crore is proposed to be funded through debt and balance through internal accruals. The financial closure has already been achieved, besides the company having obtained all the requisite approvals. The company has, so far, spent Rs.70 crore on this project. The entire project implementation is proposed to be completed by March, 2019.

PCBL has also projected to come up with a new plant with an expected 1,20,000 tone capacity in South India wherein the aggregate project cost is estimated to be around Rs.480 crore. The project is the project is likely to be funded through a mix of debt and internal accruals. The expansion is projected to commence in FY19 and to complete by March 2020. However, the project is at a drawing board stage, as of now.

As the company is resorting to internal accruals for funding the project mainly on the back of increasing level of accruals, this is not expected to materially impact the financial risk profile of the company. However, as the proposed expansion is significant, successful and timely commissioning of the same is likely to be critical for the company. At the same time, it would help PCBL in augmenting its leadership position in the industry.

Analytical Approach & Applicable Criteria

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation (Non-Financial Sector)

About the Company

PCBL, incorporated in 1960, belongs to the Kolkata-based RP-SanjeevGoenka group. The RP-SanjeevGoenka group is one of the leading industrial houses of the country with interest in power generation & distribution, coal, carbon black, retailing, entertainment and BPO business with CESC Ltd. being the flagship company. PCBL offers a comprehensive portfolio of Carbon Black for rubber applications and Specialty Black for non-rubber applications across plastics, fibre, pipes, inks & coatings, wire & cable and other niche industries. It is India's oldest carbon black (CB) producer with an aggregate installed capacity of 4,72,000 MTPA encompassing its four plants across the country. PCBL has captive power plants at all of its manufacturing locations. Its clientele includes global leaders in the tyre industry such as Bridgestone Corporation and Goodyear Tire & Rubber Company, as well as leading Indian tyre manufacturers like MRF, Ceat, J. K. Tyres, Apollo Tyres, Bridgestone India and Goodyear India.

Financials

(Rs. Crores)

For the year ended / Rs. Crs	**31-03-2016**	**31-03-2017**
	Audited	**Audited**
Total Operating Income	1894.1	1927.0
EBITDA	221.8	311.7
PAT	16.9	69.5
Total Debt	1023.5	758.2
Networth (*)	559.2	646.9
Ratios		
a. EBITDA Margin	11.71	16.18
b. PAT Margin	0.88	3.57
c. Overall Gearing ratio	1.83	1.17

** After netting of the effect of Rs.479 crore (net) on account of fair valuation of fixed assets under IND AS which was included under the head "Reserves & Surplus" in the balance sheet as on the aforesaid dates.*

Note: Classification of financial numbers is as per Infomerics' standards

Status of non-cooperation with previous CRA: Not applicable

Any other information:N.A

Disclosure:

Rating History for last three years:

S. 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.	Outstanding Term Loan	Long Term Loan	4.52	IVR AA-/Stable Outlook (IVR Double A minus with Stable Outlook)	IVRA+/Stable (IVR Single A plus with Stable Outlook), March 24, 2017 (Rs.50 crores)	--	--

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.

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Annexure 1: Details of Facility

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility(Rs. Crores)	Rating Assigned/ Outlook
Term Loan (Present Outstanding)	February, 2014	10%	December 2020	4.52	IVR AA-/Stable Outlook