May 21, 2020

# Mehta Petro Refineries Ltd: Rating reaffirmed; rated amount enhanced

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Non-fund based limits | 75.00 | 80.00 | [ICRA]A3; Reaffirmed |
| Fund-based sub-limits# | (45.00) | (70.00) | [ICRA]BBB- (Negative) / [ICRA]A3; Reaffirmed |
| Non-fund based sub-limits# | (60.00) | (25.00) | [ICRA]BBB- (Negative) / [ICRA]A3; Reaffirmed |
| Unallocated limits | 15.00 | 30.00 | [ICRA]BBB- (Negative) / [ICRA]A3; Reaffirmed |
| **Total** | 90.00 | 110.00 | |

*#Total utilisation of fund based and non-fund based sublimits should not exceed Rs. 80.00 crore*
**Instrument details are provided in Annexure-1*

## Rationale

The reaffirmation of ratings with Negative outlook reflects the unfavourable business environment for Mehta Petro Refineries Ltd (MPRL) due to the Covid-19 pandemic-driven disruptions in the company's business from the nationwide lockdown and restricted movements. Any longer-than-anticipated stretch in the lockdown period or the pace at which normal business activities resume can severely impact MPRL's scale and profitability in the current year. Thus, ICRA will continue to closely monitor the developments related to the Covid-19 pandemic. Further, the ratings remain constrained by the exposure of the company's profitability to fluctuations in raw material consumption costs. The same is evident from the steep decline in its operating margin to 4.59% in FY2019 from 8.08% in FY2018, led by a sharp increase in raw material cost, given its linkage to volatile crude oil prices. This, along with the currency fluctuation, keeps its profitability under check due to considerable imports, although the risk is partly mitigated by MRPL's forex hedging policies. Moreover, stiff competition in the market from several domestic and international players limits its ability to pass on price fluctuation, which in turn limits the company's margin flexibility.

The ratings, however, favourably factor in the extensive track record of MPRL's promoters in the aromatic and de-aromatic solvent industry and its reputed and diversified customer base attributable to multiple product applications across diverse sectors. The ratings note the healthy revenue growth over the past few years, primarily driven by increase in volume sales. However, in the current year, the company's ability to ramp up its production activities after the cease of the lockdown period and ability to swiftly recoup the lockdown period losses remains to be seen.

## Key rating drivers and their description

## Credit strengths

**Extensive experience of promoters in aromatic and de-aromatic solvents industry –** Mr. Vinod Mehta and Mr. Paresh Mehta are the MRPL's key promoters and have an experience of more than three decades in the same business sector. Over the years, the promoters have established relationships with various key intermediaries and end-customers to scale up business. Their extensive experience will guide the company's future growth.

**Diversified revenue profile, established association with reputed customers across various segments –** MPRL's revenues are primarily derived from the domestic market, driven by the paint, print, resins, pigment, pesticides and insecticides sectors. These segments account for ~60-70% of the total sales. The company achieves sizeable revenues from sectors such as paper, drilling fluids, coating and several other industries. Diversified product portfolio catering to several industries helps the company to adapt to the changing market conditions. This also mitigates the sector-specific risks to a certain extent. Further, MPRL has a well-diversified customer portfolio with its top five customers accounting for around 12-25% of the total sales during the last three years. Moreover, most of its customers enjoy an enduring relationship with the company, resulting in repeat orders.

**Comfortable capital structure –** MRPL's debt profile primarily consists of working capital loans and unsecured loans from promoters and their family members (~15% of the total loans) as on March 31, 2019. The capital structure stood at comfortable level as indicated by a gearing of 1.02 times as on March 31, 2019. Further, the capital structure remains comfortable with gearing of around 0.79 times as on March 31, 2020 based on the key provisional financial numbers shared by the company.

## Credit challenges

**Pressure on profitability arising from volatile raw material prices and costlier imports due to rupee depreciation, risk amplified by nationwide shutdown amid Covid-19 pandemic –** The company achieved a revenue growth by ~57% to Rs. 277.72 crore in FY2019. However, the profitability, as represented by OPM, declined to 4.59% in FY2019 from 8.08% in FY2018, primarily due to increase in raw material consumption cost aided by an increase in crude oil prices and significant rupee depreciation in FY2019. It reported a moderate growth of ~8% to Rs. 300.00 crore (key provisional number shared by the company) in FY2020, however, profitability on the same remains to be seen amid the raw material prices fluctuations and currency fluctuations in FY2020. Raw materials constitute nearly 80-90% of the total value of MPRL's finished products. Thus, its ability to procure the required raw materials at a competitive price is critical to maintain cost competitiveness, as raw material prices vary with the movement in crude oil prices. Further, MPRL's revenues and earnings are expected to be adversely impacted in Q1 FY2021, owing to the prevalent weak demand conditions given the Covid-19 pandemic. Any longer-than-anticipated stretch in the lockdown period, or the pace at which normal business activities resume, can severely impact the operations and liquidity profile, which will remain key monitorables. MPRL's ability to consistently improve its operating efficiencies and remain cost competitive remains critical.

**Vulnerability to forex risk emanating from significant imports; risk is mitigated to an extent by hedging policy –** The company is exposed to forex risk as it imports of a sizeable portion of key raw materials for its manufacturing. It procured almost 30-50% of its raw material requirements from the international market during the last three years based on the price differentials between domestic and international markets. Escalating import cost due to the rupee depreciation continues to keep profitability metrics under check, although the risk is partly mitigated by MPRL's active forex hedging practice.

**Weakening of coverage indicators due to moderation in operating profitability in FY2019 –** Decrease in operating profits, coupled with an increase in interest and financial expenses due to higher utilisation of working capital as well as increase in bank charges owing to shift in bank led to moderation in interest coverage ratio. The same was indicated by a decline in OPDBITA/Interest and financial charges to 2.36 times in FY2019 from 4.03 times in FY2018. Moreover, the debt protection ratio as depicted by total debt/OPBDITA moderated to 3.41 times as on March 31, 2019 from 2.97 times as on March 31, 2018. The coverage indicators are likely to improve in FY2020 owing to an expected decrease in debt levels and interest cost in FY2020. However, the extent of the same remains to be seen and is a rating monitorable.

**Working capital-intensive nature of business –** Stiff competition in the market leads to a relatively liberal credit period extended to customers against tight payment terms with suppliers. This, along with moderate inventory holding to timely service its customer base results in a working capital-intensive business. MRPL's working capital intensity as represented by NWC/OI stood high at 24.35% as on March 31, 2019.

**Intense competition with limited entry barriers in terms of technology and manufacturing operations –** The low technological complexity and moderate capital investment in setting up a manufacturing plant for aromatic and de-aromatic products resulted in several smaller players setting up operations. Moreover, because of the low product differentiation, price competitiveness remains the key for maintaining and/or increasing its market share and building strong relationships with its end-customers. Stiff competition with the limited entry barriers limits the margin flexibility of the companies in the industry.

## Liquidity position - Adequate

MPRL had outstanding short-term loans of Rs. 0.59 crore on its books as on March 31, 2019 from banks and NBFCs, which will be repaid in FY2020. The average utilisation of working capital limits stood moderate at an average of 57% during the last 15 months that ended in March 2020 and 65% in March 2020. Moderate free cash and cash equivalent of Rs. 2.46 crore as on March 31, 2020, coupled with moderate buffer from unutilised sanctioned working capital limits provide comforts to its liquidity position. In addition, the company is expected to enhance its fund-based and non-fund based working capital limits by Rs. 10.00 crore. Any sizeable debt-funded capex will deteriorate the capital structure and the impending repayments can put pressure on MPRL's liquidity profile. Going forward, in a limited timeframe, its ability to secure timely sanction of additional funds and steady realisation of receivables amid the lockdown will be critical and remains a key monitorable.

## Rating sensitivities

**Positive triggers –** ICRA could change the outlook to Stable, if the company demonstrates a considerable improvement in its capacity utilisation, sustained increase in profitability, along with an improvement in liquidity position. Moreover, adequate buffer from unutilised sanctioned limits and better working capital management with a decrease in working capital intensity will remain favourable for a rating upgrade. Specific credit metrics that may to lead a change in outlook include OPBDITA/Interest and financials charges of above 2.5 times, and Total Debt/ OPBITDA below 3.5 times on a sustained basis.

**Negative triggers –** Negative pressure on the rating would arise in case of prolong impact of the Covid-19 pandemic leads to a decrease in the cash accrual position due to reduction in revenues and/or margins, deterioration in capital structure. Moreover, any significant debt-funded capex or increase in dependency on external debt or stretch in working capital cycle owing to extended credits to customers, leading to a stretch in the liquidity position will remain a negative trigger. Weakening of OPBDITA/Interest and financial charges to below 2.0 times and total debt/OPBDITA to above 4.0 times will lead to a downward pressure on the rating.

## Analytical approach

| Analytical Approach | Comments |
|---|---|
| Applicable Rating Methodologies | Corporate Rating Methodology<br>Rating methodology for Entities in the Chemical Industry |
| Parent/Group Support | Not applicable |
| Consolidation/Standalone | The rating is based on standalone financial statements of the company |

## About the company

Incorporated in 1993, MRPL manufactures and markets aromatic and de-aromatic products and solvents, which find application in the production of inks, paints, pesticides, papers, resins, coatings, varnishes, pigments, pesticides, adhesives and many other products. The company is promoted and managed by Mr. Vinod Mehta, Mr. Paresh Mehta and their family. The company's manufacturing facilities are at Palghar, Maharashtra, and at Dahej, Gujarat. Palghar has a single processing unit, while Dahej has three processing units. The company's total manufacturing capacity is ~400 KL per day. The Palghar unit accommodates 25 storage tanks, while Dahej accommodates 29 with an aggregate storage capacity of ~5,300 KL.

The company reported a net profit of Rs. 3.93 crore on an operating income (OI) of 277.72 crore as per the FY2019 audited statement, against a net profit of Rs.5.28 crore on an OI of Rs. 177.01 crore as per the FY2018 audited statement.

## Key financial indicators (Audited)

| | FY2018 | FY2019 |
|---|---|---|
| Operating Income (Rs. crore) | 177.01 | 277.72 |
| PAT (Rs. crore) | 5.28 | 3.93 |
| OPBDIT/OI (%) | 8.08% | 4.59% |
| RoCE (%) | 17.62% | 12.83% |
| | | |
| Total Outside Liabilities/Tangible Net Worth (times) | 2.01 | 1.64 |
| Total Debt/OPBDIT (times) | 2.97 | 3.41 |
| Interest Coverage (times) | 4.03 | 2.36 |
| DSCR | 2.67 | 1.81 |

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

| | Instrument | Current Rating (FY2021) | | | | Chronology of Rating History for the past 3 years | | | |
|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount Rated | Amount Outstanding | Rating | Date & Rating in FY2020 | Date & Rating in FY2019 | | Date & Rating in FY2018 |
| | | | | | 21 May - 2020 | 5-Sep-2019 | 14-Dec-2018 | 16-May-2018 | 13-Apr-2017 |
| 1 | Non-fund Based Limits | Short-term | 80.00 | - | [ICRA]A3 | [ICRA]A3 | [ICRA]A3 | [ICRA]A3 | [ICRA]A3 |
| 2 | Fund Based Sub-limits | Long Term & Short Term | (70.00) | - | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 |
| 3 | Non-Fund Based Sub-limits | Long Term & Short Term | (25.00) | - | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 |
| 4 | Unallocated Limits | Long Term & Short Term | 30.00 | - | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Negative) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 |
| 5 | Fund Based Limits | Long Term & Short Term | - | - | - | - | - | [ICRA]BBB- (Stable) / [ICRA]A3 | [ICRA]BBB- (Stable) / [ICRA]A3 |

*Amount in Rs crore*
*#Total utilisation of fund based and non-fund based sublimits should not exceed Rs. 75.00 crore*

## Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

## Annexure-1: Instrument details

| ISIN No | Instrument Name | Date of Issuance / Sanction | Coupon Rate | Maturity Date | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| - | Letter of Credit | - | - | - | 80.00 | [ICRA]A3 |
| - | Fund Based – Cash Credit /WCDL/Sales Invoice discounting/Purchase invoice discounting/ Over draft/ RCRL/ PCFC/PSFC (Sub-limit of LC)* | - | - | - | (70.00) | [ICRA]BBB- (Negative) / [ICRA]A3 |
| - | Non-fund Based – Bank Guarantee and stand by letter of credit (Sub-limit of LC)* | - | - | - | (25.00) | [ICRA]BBB- (Negative) / [ICRA]A3 |
| - | Unallocated Limits | - | - | - | 30.00 | [ICRA]BBB- (Negative) / [ICRA]A3 |

*#Total utilisation of fund based and non-fund based sublimits should not exceed Rs. 80.00 crore*
*Source: Mehta Petro Refineries Limited*

## Annexure-2: List of entities considered for consolidated analysis – NA

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## About ICRA Limited:

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