

December 29, 2020

## Panama Petrochem Ltd: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based limits	6.0	6.0	[ICRA]A-(Stable); reaffirmed
Non-fund based limits	73.0	73.0	[ICRA]A2+; reaffirmed
<b>Total</b>	<b>79.00</b>	<b>79.00</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The reaffirmation of ratings reflects the established track record of Panama Petrochem Limited (PPL) in the white oil and allied oils business. The ratings also consider the company's strong customer base and its long-term relationship with reputed companies across multiple industries. The company's product profile is well diversified across various end-user industries such as cosmetics, ink, rubber, textiles, transformer and lubricants, thereby mitigating the risks from slowdown in any particular sector. The ratings also favourably consider the diversified manufacturing presence of the company through four manufacturing units in India that are strategically located to cater to different industrial clients for different kinds of oil. Further, the company also has a manufacturing unit at Ras Al Khaimah, the UAE, under its wholly-owned subsidiary, Panol Industries RMC, which enjoys proximity to the base oil suppliers in West Asia and caters to the demand for its products in the region. There is a healthy diversification of the company's revenues in both domestic and overseas markets with about 40% of its sales coming from exports. The geographical diversification helps mitigate risks from slowdown in a particular market. The ratings also take into account the comfortable capital structure of the company as reflected by its low gearing of 0.1 time as of March 31, 2020 and September 30, 2020 due to decline in short-term debt following lower working capital intensity during the period.

The ratings are, however, constrained by the vulnerability of PPL's profitability to fluctuations in forex rates and base oil prices, which are volatile being crude oil derivatives. The company's operations are also exposed to high competition in the industry from other established players. The profitability in FY2020 was impacted by the demand slowdown in certain sectors accompanied with high competition, resulting in an operating margin of 5.5% over 8.8% in FY2019. However, the company's performance has improved in the current fiscal with an operating margin of 7.2% in H1 FY2021 supported by recovery in demand from key sectors. Additionally, PPL's receivable cycle had stretched over the past two years, but during FY2020 the management reduced business with clients with stretched receivable cycles. Along with a weaker demand environment, this had led to lower sales in FY2020. However, the company is witnessing recovery in demand from various sectors in the current financial year.

ICRA notes that the company's domestic manufacturing operations were temporarily shut down from March 23, 2020 due to the Covid-19 pandemic-related lockdowns. The unit at Ankaleshwar (Gujarat) was allowed to operate from March 28-29, 2020, since the unit manufactures white oil/ petroleum jelly for the pharmaceuticals and cosmetics industries. Gradually, other units resumed operations over the April-June 2020 period. This led to the

company utilising lower capacity levels during Q1 FY2021. Nevertheless, with the easing of lockdowns and improving demand, the capacity utilisation levels recovered to 84% in H1 FY2021. Higher capacity utilisation levels along with certain cost rationalisation measures adopted by PPL have improved the operating margins in Q2 FY2021.

The Stable outlook on the long-term rating reflects ICRA's opinion that PPL will continue to benefit from its established position in the liquid paraffin/white oil business and healthy financial risk profile.

## Key rating drivers and their description

### Credit strengths

**Established track record in white oil and allied oils business** – The company is an established player in the liquid paraffin/white oil business with more than 35 years of experience. The company manufactures over 80 variants of oils, which are used across multiple industries.

**Strong customer profile and geographical diversification of revenues** – The company has a strong customer profile including large international FMCG companies such as Dabur and Marico, and reputed players in the textile, ink and tyre sectors, while enjoying long-term relationships with several of its key clients. The company's customer profile remains well-diversified with its top five customers typically driving 25-30% of its total sales. Further, PPL's portfolio remains well diversified across several industries, thereby mitigating the risks, to an extent, against demand slowdown in any particular sector. PPL's revenues are well-diversified in the domestic and overseas markets. Its exports typically account for 35-40% of its total standalone sales, which are distributed between Africa, East Asia, South America and Europe. The company also operates in West Asia through its subsidiary, Panol Industries RMC. Further, PPL has a diversified presence in India. A geographically diversified revenue base helps mitigate risks against slowdown in any particular market.

**Manufacturing units strategically located to cater to different end-user industries** – PPL has four manufacturing units in India that are strategically located to cater to specific industrial clusters. The company's facility in Talaja, Maharashtra, is located close to the port and is used for most of the company's exports. Further, it has a manufacturing unit at Ras Al Khaimah in the UAE, which has the advantage of being located close to the base oil suppliers in West Asia as well as to PPL's customers in the region.

**Comfortable capital structure with no long-term debt** – The company has a comfortable capital structure with only short-term debt on its books. PPL has maintained a low gearing of 0.1-0.2 time over the last three to four fiscals, but the same increased to 0.4 time as of March 31, 2019 owing to increase in short-term debt following increase in working capital intensity. Nonetheless, the gearing improved to 0.1 time as on March 31, 2020 and September 30, 2020, supported by lower working capital debt. The company has undertaken consistent capacity expansions across its manufacturing units, all of which have been funded through internal accruals.

## Credit challenges

**Vulnerability of profits to forex fluctuations; sensitivity to base oil prices** – Given the nature of the business, the company remains exposed to the movement in base oil prices, which remain volatile being crude oil derivatives. However, it is able to pass on any significant increase in base oil prices with the provision to set prices on a monthly basis. In case of exposure to forex fluctuations, the company’s exports provide a natural hedge up to 35-40%. For the remaining exposure, it has an active hedging policy to hedge a part of its exposure through forward covers. PPL has faced a contraction in its operating margins in FY2020 owing to the slowdown in demand and intense competition for market share among different players.

**High competition in the industry** - The company’s operations are exposed to high competition from other established players, few of which have bigger scale of operations. ICRA notes low entry barriers and limited product differentiation have led to intense competition in the base oil processing industry. Companies mostly focus on volume, which leads to competitive pricing.

## Liquidity Position: Adequate

PPL’s liquidity is expected to remain **adequate** supported by healthy cash accruals and low utilisation of its working capital limits. Further, it has no long-term debt repayment obligations. The company had positive cash flows from operations and positive retained cash flows in FY2020, with a decline in working capital intensity. The company has incurred capex over the last few fiscals, funded through internal accruals, and has moderate capacity expansion plans. All regular capex and any brownfield expansion capex at the subsidiary level are all expected to be funded through PPL’s internal accruals.

## Rating sensitivities

**Positive triggers** - Increase in scale of operations and improvement in profitability and cash accruals while maintaining moderate working capital intensity could be positive rating triggers. Additionally, ROCE above 20% on sustained basis could also trigger a rating upgrade.

**Negative triggers** - Decline in scale of operations or further decline in profitability with operating margins reaching below 5%, or any stretch in the working capital cycle leading to increase in debt levels and moderation of debt coverage metrics on a consistent basis, could lead to a rating downgrade.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a>
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financial profile of Panama Petrochem Limited. As of March 31, 2020, PPL had a wholly-owned subsidiary, which has been enlisted in Annexure-2.

## About the company

Incorporated in 1982, Panama Petrochem Limited (PPL) is a manufacturer and exporter of over 80 variants of speciality petrochemicals. The company's key products include liquid paraffin oils (white oils), petroleum jelly, ink oil, rubber oil, coning oil, and transformer oil. The company has four manufacturing units in the country, one each at Ankleshwar (Gujarat), Dahej (Gujarat), Taloja (Maharashtra) and Daman. PPL's products are used across several industries, such as printing ink, cosmetics, pharmaceuticals, rubber, resin, engineering and chemicals. PPL also enjoys a manufacturing presence in West Asia through its wholly-owned subsidiary, Panol Industries RMC, FZE, at Ras Al Khaimah, the UAE. PPL has a consolidated manufacturing capacity of 230,000 metric tonne per annum (MTPA).

For the six-month period ending September 30, 2020, PPL reported a profit after tax (PAT) of Rs. 22.2 crore on an operating income (OI) of Rs. 485.1 crore, against a PAT of Rs. 16.0 crore on an OI of Rs. 529.9 crore for the six-month period ending September 30, 2019.

## Key financial indicators

	<b>FY2019 Audited</b>	<b>FY2020 Audited</b>	<b>H1 FY2021 Unaudited</b>
Operating Income (Rs. crore)	1269.3	1002.8	485.1
PAT (Rs. crore)	51.9	28.8	22.2
OPBDIT/ OI (%)	8.8%	5.5%	7.2%
PAT/OI (%)	4.1%	2.9%	4.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.2	0.7	0.7
Total Debt/OPBDIT (times)	1.4	0.9	0.7
Interest Coverage (times)	4.5	3.2	6.9

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

**Any other information: None**

### Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2020	FY2019	FY2018
				30-November-2020	29-December-2020	23-December-2019	-	-
1	Fund based limits	Long Term	6.0	-	[ICRA]A- (Stable)	[ICRA]A- (Stable)	-	-
2	Non-fund based limits	Short Term	73.0	-	[ICRA]A2+	[ICRA]A2+	-	-

Amount in Rs. 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](http://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
NA	Fund based limits	NA	NA	NA	6.0	[ICRA]A- (Stable)
	Non-fund based limits	NA	NA	NA	73.0	[ICRA]A2+

Source: Panama Petrochem Ltd

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

Company Name	Ownership	Consolidation Approach
Panol Industries RMC FZE, UAE	100.0%	Full Consolidation

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