



Finolex Industries Limited

RATING HISTORY

Original amount	Amount Outstanding	Maturity Date	Rating Outstanding	Previous Ratings	
			May 2008	Sep 2006	February 2006
Rs. 0.75 billion Non-convertible debentures	Rs 0.75 billion	November 2009	LAA	LAA	LAA
Rs. 1.53 billion Non-convertible debentures	Nil		-	LAA	-

ICRA has reaffirmed the LAA rating assigned to Finolex Industries Limited (FIL)'s Rs. 0.75 bn NCD program. The LAA rating assigned to the Rs 1.53 billion NCD programme has been withdrawn as the company has not placed the instrument. The LAA rating reflects FIL's leading and established market position in Poly Vinyl Chloride (PVC) pipes and PVC resins, the buoyant demand for PVC products in India from irrigation and construction segments and high financial flexibility. FIL is setting up an imported coal based captive power plant of capacity 43 MW at Ratnagiri at a cost of around Rs. 2 billion, which should also aid its profitability since the cost of power generation is expected to be cheaper than grid power, besides providing uninterrupted supply. However, the rating is constrained by the commodity nature of FIL's business and the volatility of the spreads between Ethylene Dichloride (EDC)/Ethylene/Vinyl Chloride Monomer (VCM), and PVC. While the company has its own jetty which improves its operational flexibility and cost of procuring raw material, the same is not an all weather facility thereby accentuating the volatility of its profitability. Besides, profitability may be impacted if the duty differential between PVC and its feedstocks/intermediates are further reduced.

FIL is the second largest player in the domestic PVC market, with a capacity of 260,000 tpa and largest player in the PVC pipes. India continues to remain a PVC deficit market, with strong demand growth from pipes & fittings segment (accounts for nearly 70% of PVC sales in India) and absence of any major capacity expansion. Irrigation and Construction segments are the major users of PVC pipes & fittings in the domestic market, which have been growing at a robust pace in the recent past due to Central and State's allocation of funds for irrigation projects and boom in construction business. FIL commands strong brand equity, which enables it to command a price premium on its pipes relative to the industry. PVC pipe business also allows the company to captively consume one third of its PVC resins, which provides greater stability to its cash flows. Going forward, ICRA expects the demand outlook for PVC and PVC pipes to be favourable due to thrust on irrigation infrastructure and current lower penetration levels in India.

FIL's PVC business remains vulnerable to movement in prices of PVC and its intermediates EDC/Ethylene/VCM given its limited backward integration. International PVC prices have firmed up over the last two years against the backdrop

of higher feedstock costs and favourable demand outlook. New capacities in China (which is the largest producer of PVC globally) based on the calcium carbide route, have witnessed increase in production costs due to rising coal prices. As a result, the spread between PVC and EDC/Ethylene prices have increased significantly over the last two years. However, around 50% of FIL's PVC capacity (commissioned in 2006) is based on VCM route, which offers lower value addition. As a result, the company's operating margins have remained subdued even in a scenario of rising PVC - EDC/Ethylene spreads. FIL's profitability has also been tempered by a series of import duty cuts in the recent past. Going forward, FIL's profitability will be vulnerable to any further reduction in the import duty differential between PVC and its intermediates (Current Basic Import Duty: PVC & Ethylene: 5%, EDC and VCM: 2%). Govt has levied anti dumping duty on PVC imports from few suppliers/countries in January 2008, which has also buoyed up the domestic PVC realisation.

FIL's pipes business has a higher Return on Capital employed (RoCE) (30% in 9M FY 08) as compared to the PVC division (15% in 9M FY 08) due to low capital intensity although operating margins remain lower.



Overall, the margins for pipes division have depicted higher stability than PVC, which has fluctuated in line with global prices. FIL is undertaking an expansion of its Pipes division which will increase its capacity from 70,000 MT to 1,00,000 MT by 30,000 MT.

FIL is setting up a captive coal based power plant of 43MW at a capex of Rs 2 billion to cater to its power requirements of PVC plant at Ratnagiri. About 50% of the power will be used to meet its captive requirements; rest will be sold to MSEB/ PTC. The project is behind schedule by around 12 months due to delays in the mobilisation of labour by the contractors. Although coal prices have increased significantly since the project was envisaged, ICRA expects the project to be profitable because of the savings that would accrue from the substitution of costlier MSEB power and higher steam credit.

FIL's topline grew moderately during 2003-05 (CAGR of 10%), however declined in 2005-06, due to a sharp decline in PVC realizations and lower PVC volumes (partly due to plant shut down). The company also suffered from stocking higher cost EDC during monsoon, which followed

by crash in PVC prices led to pressure on FIL's margins in 2005-06. Subsequently, the turnover & profits have increased following volume growth from PVC capacity expansion and higher realizations in FY07 and FY08. Although PVC prices increased sharply in FY07 and FY08, the operating margins remained low as the expanded PVC production was through the lower margin VCM route. However, the company's RoCE has improved over the last two years due to lower capital intensity (of VCM based capacity) and higher capacity utilisation. FIL has significant liquid investments primarily in mutual funds, which impart financial flexibility. As a result, the net debt remained low at 0.58 times as on 31-Mar-07.

Going forward, FIL's turnover is expected to grow steadily due to capacity expansion in PVC pipes and steady demand growth in PVC. Although profitability would continue to remain vulnerable to PVC-EDC/Ethylene and VCM spreads, the profitability is expected to improve on the back of cost savings from the captive power plant. Overall, improved profitability and financial flexibility should keep FIL's risk profile

favourable. The company also holds 78 acres of land in Pune, which it is planning to either sell outright or develop it to a special economic zone (SEZ) (by equity contribution through land holding). A sale of land could improve FIL's capital structure and provide financial flexibility for funding its future projects.

Company profile:

FIL was set up in 1981 by Mr. P.P Chhabria as a PVC pipe manufacturing company. The company backward integrated into manufacturing of PVC resins in 1994. FIL is the largest manufacturer of PVC pipes and the second largest player in PVC resin market. Large part of FIL's operations is located in Ratnagiri, where it has its PVC resin (Installed capacity of 260,000 tpa) and pipe capacity (54,000 tpa) and a jetty to import its raw materials. The company also has small pipe manufacturing facility (20,000 tpa) in Pune. In 2006-07, FIL reported net sales of Rs 10.12 bn and net profits of Rs. 0.70 bn. In the nine months ended December 2007, FIL reported net sales of Rs.9.66 bn and net profits of Rs. 0.70 bn

March 2007

KEY FINANCIALS

Particulars	FY 2008	FY 2007	FY 2006	FY 2005
Period in Months	9	12	12	12
Net Sales	9.66	10.12	7.18	8.19
Operating Income	9.66	10.27	7.36	8.39
Operating Profit before Depreciation, Interest and Tax	0.99	1.26	0.99	1.72
Profit after Tax	0.70	0.70	0.42	0.96
Equity Capital	-	1.24	1.24	1.24
Tangible Net Worth	-	5.29	5.04	5.05
Operating Profit before Depreciation, Interest and Tax/ Operating Income	10.25%	12.30%	13.43%	20.49%
Profit after Tax/Operating Income	7.25%	6.80%	5.75%	11.44%
Profit before Interest and Tax/(Total Debt + Net Tangible Worth)	-	10.02%	8.23%	15.04%
Operating Profit before Depreciation, Interest and Tax/Interest & Financial Charges (Times)	5.95	9.20	3.89	14.00
Net Cash Accruals/Total Debt	-	16%	9%	18%
Total Debt/Net Worth (Times)	-	0.91	1.04	1.10
Total Debt/(Net Worth + Deferred Tax Liability) (Times)	-	0.76	0.86	0.91

Note: Amounts in Rs. Billion



For further details please contact:

Mr. L. Shivakumar, 91-22-24331046/53

Mr. Anjan Ghosh, 91-22-24331046/53

Mr. K. Ravichandran, 91-44-24333293

© Copyright, 2008, ICRA Limited. All Rights Reserved.

Contents may be used freely with due acknowledgement to ICRA

ICRA ratings should not be treated as recommendation to buy, sell or hold the rated debt instruments. The ICRA ratings are subject to a process of surveillance which may lead to a revision in ratings. Please visit our website (www.icra.in, www.icraratings.com) or contact any ICRA office for the latest information on ICRA ratings outstanding. All information contained herein has been obtained by ICRA from sources believed by it to be accurate and reliable. Although reasonable care has been taken to ensure that the information herein is true, such information is provided 'as is' without any warranty of any kind, and ICRA in particular, makes no representation or warranty, express or implied, as to the accuracy, timeliness or completeness of any such information. All information contained herein must be construed solely as statements of opinion and ICRA shall not be liable for any losses incurred by users from any use of this publication or its contents