

September 03, 2020

Haldia Petrochemicals Limited: Long Term rating revised to [ICRA]A+(Stable); short term rating reaffirmed; NCD rating withdrawn

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term Limits- Term Loans	3,068.00	3,068.00	[ICRA]A+(Stable); downgraded from [ICRA]AA-(Negative)
Long-term Limits-Fund-based	381.00	381.00	[ICRA]A+(Stable); downgraded from [ICRA]AA-(Negative)
Short-term Limits- Non-fund Based Limits	1606.00	1606.00	[ICRA]A1+; reaffirmed
Long-term/Short-term Unallocated	5003.00	5003.00	[ICRA]A+ (Stable); downgraded from [ICRA]AA-(Negative)/[ICRA]A1+; reaffirmed;
Proposed NCD Programme	1,000.00	0.00	[ICRA]A+(Stable); downgraded from [ICRA]AA-(Negative); withdrawn
Issuer Rating ¹	-	-	[ICRA]A+(Stable); downgraded from [ICRA]AA-(Negative)
Short Term – Commercial Paper programme	100.00	100.00	[ICRA]A1+; reaffirmed
Long Term-Non fund based	4000.00	4000.00	[ICRA]A+(Stable); downgraded from [ICRA]AA-(Negative)
Total	15,158.00	14,158.00	

*Instrument details are provided in Annexure-1

Rationale

The rating revision factors in the anticipated adverse impact on the key credit metrics of Haldia Petrochemicals Limited's (HPL) due to the proposed acquisition of ~7% additional equity stake in the technology division of McDermott International Inc (MDR) from Rhone Capital for a consideration of \$70-75 million apart from existing ~57% equity stake acquired in June 2020 for ~\$690 million. The acquisition of the additional 7% stake is expected to be funded by debt of ~\$ 53 million and the balance from the existing cash balances of HPL. The debt of \$ 53 million would be raised at the level of the Netherlands subsidiary i.e. HPL Technology BV (HTS) backed by an SBLC from an Indian bank and would be serviced from the cash flows of HPL over a 10 years period in the form of further investment in HTS, akin to the arrangement followed for the acquisition of the 57% stake. Additionally, the company plans to incur an expenditure of Rs 230 crore on setting up of a R&D facility over FY2021 and FY2022 and incur a capital expenditure of Rs 530 crore in FY2021 which would adversely impact the cash levels of the company thereby impacting the debt metrics on a net debt basis.

In June 2020, HPL in a JV with private equity Rhone Capital acquired the technology division of MDR for an enterprise value of ~\$2.668 billion. MDR hived off its technology business (Target) into a separate SPV which was put up for sale under Chapter XI as per the US Bankruptcy Laws. The acquisition concluded at the bid value of \$ 2.668 billion, was funded as a Leveraged Buyout with target company level (Lummus Technologies) debt of \$ 1.5 billion and the balanced funded with a

¹With effect from September 1, 2017, ICRA has aligned the symbols and the definitions of ratings pertaining to the Issuer Rating Scale with that of the Long-Term Rating Scale. The change in the symbol is not to be construed as a change in the credit rating. Please refer to ICRA's website for more details

combination of equity and debt. HPL had acquired 57% equity stake for ~\$690 million while the balance 43% was acquired by Rhone Capital. With the acquisition of the additional 7% stake the total outgo for the acquisition has increased to \$ 765 million funded through debt of ~\$ 565 million and cash of \$ 200 million out of the existing cash balances of HPL. The \$1.5 billion debt raised at Lummus Technologies is with no recourse to the shareholders, besides which it has a \$ 175 million revolving credit facility. The FCTL of \$565 million raised at the level of HTS backed by an SBLC from an Indian bank will be serviced from the cash flows of HPL over a period of 10 years in the form of further investment in HTS. Notwithstanding the impressive credentials of Lummus Technology division of MDR, the acquisition has significantly reduced the cash reserves and increased the long-term debt to be serviced by HPL even though the company hopes to realise substantial synergies over the medium to long term. ICRA has not consolidated the financials of Lummus Technologies while arriving at the ratings of HPL and hence not considered any incremental support to be provided by the latter to the former. Accordingly, the ability of Lummus Technologies to service the \$1.5 billion debt on its books remains a key monitorable and any support extended by HPL to the target company for shortfall in debt servicing will be a key rating sensitivity.

Apart from the aforementioned acquisition the company also proposes to acquire 2,158 acres of industrial land in Cuddalore, Tamil Nadu under the liquidation of Nagarjuna Oil Corporation Limited (NOCL) for a consideration of Rs 600 crore. The proposed acquisition and investment, although in a phased manner and subject to milestones, will lead to depletion of cash reserves even as the petrochemical cycle is weak leading to lower tolling margins and cash accruals. ICRA also notes that HPL has been investing in subsidiaries and extending short term loans and advances to group companies, with the current total exposure at Rs. 1325 crore (excluding the recent acquisition). Of this, the company has invested about \$175 million in HPL Global, its trading subsidiary at Singapore to enable paper and physical trade with large counterparties and better commodity risk management; however, of this amount about \$90 million has been extended to group companies as security deposit and loans and advances. Any further material increase in loans and advances to group companies including Lummus Technologies remains a key rating sensitivity.

The ratings of the company are also constrained owing to weaker than expected performance in FY2019 and FY2020; and subdued industry outlook owing to which tolling margins are expected to remain weak over the medium term. Additionally, the company's plant had to be shut down for almost a month due to the COVID-19 pandemic from March 2020 to April 2020, though the performance has improved in June and July 2020 owing to lifting of lockdown. Besides, the company incurred large inventory losses at FY2020 end owing to the sharp decline in naphtha and product prices. Accordingly, the operating profits declined to ~Rs 871 crore in FY2020 (as per provisional standalone numbers) from Rs 1603 crore in FY2019. Apart from the impact on capacity utilisation in FY2021 due to shutdown of plant during April 2020, the demand for the company's products is expected to remain weak in the near term due to the Covid-19 pandemic. Going forward, ethylene over capacity and downcycle in margins are projected through 2023; propylene market is tighter than ethylene but new 'on-purpose capacity' could lead to mild downcycle through 2023. Accordingly tolling margins are projected to remain ranged over the near to medium term.

ICRA notes that the company has signed non-binding MoUs with the state governments of Andhra Pradesh and Odisha for setting up refinery-cum-petrochemical complexes. Though the investments in any of the afore mentioned projects would be large however these plans are as yet preliminary and accordingly, ICRA has not factored in any large long-term acquisitions/investments by HPL (other than MDR's technology division and NOCL land). ICRA will review the ratings if the company was to embark on large debt funded projects that impacts its financial profile.

The revised ratings continue to factor in HPL's demonstrated track record in the petrochemicals business, the strength of its promoter, and its leading market position in the eastern Indian market for polymers. Its locational advantages in servicing eastern India and Asian exports demand, along with a favourable outlook for polymers demand in India over the long-term from several end-users are other rating comforts. The ratings also consider the cyclicity inherent in the petrochemicals business and the vulnerability of its profitability to the changes in import duty levels and the Rupee-Dollar

movement. However, the pricing of HPL's key raw materials and finished products is largely based on import parity, limiting the impact of forex fluctuations on its overall profits.

The Stable outlook on the long-term rating of HPL reflects ICRA's belief that the company will continue to benefit from its dominant position in the petrochemicals sector in East India.

Key rating drivers and their description

Credit strengths

Demonstrated track record in the petrochemicals business, with established customers - The domestic polyolefins market has major participants—namely, Reliance Industries Ltd., HPL, Indian Oil Corporation Limited, GAIL India, OPAL, HPCL Mittal Energy Limited, Mangalore Refinery and Petrochemicals Limited wherein, HPL has maintained its niche position through its high-quality focus.

Dominant market position in eastern India and logistical advantage in exporting to East Asian region - HPL has enjoyed a strong market position in eastern and northern India and sells most of its products in the high netback regions of these markets. Additionally, owing to the location of its Haldia Plant, the company enjoys logistical advantage in exporting to the East Asian geography.

Favourable outlook for polyolefins demand in India - The domestic per capita consumption as well as absolute consumption of commodity polymers are expected to show secular growth due to various economic and demographic factors such as increase in urban population and rise in per capita income. Notwithstanding increasing concerns over single-use plastics and weakness in demand owing to the Covid-19 pandemic, which will curtail growth rate for polymers, ICRA expects the domestic consumption of commodity polymers to grow at a CAGR of 7-8% over the long term.

Value-added projects to improve returns from the business over the long-term - Pursuant to the SPA signed between the West Bengal government and TCG Group and upon payment of the first tranche of Rs 653 crore in December 31, 2015 to West Bengal Industrial Development Corporation, the change of management was effectuated. Under the new management, HPL set up a Butene-1 plant (under its subsidiary) with a capex of about Rs 300 crore and a pygas de-sulfurisation project at a capex of about Rs. 105 crore. Commercial production from the Butene-1 plant commenced from March 2019 and from the Pygas de-sulfurisation plant in September 2019. In addition to the afore mentioned projects, the company has planned a project to change the fuel of two boilers from Naphtha & CBFS to coal. The capex for the project is estimated at Rs 360 crore. The project is estimated to be completed by the Q4 of CY2020 and would have short payback period owing to the substantial savings in power cost that would accrue to the company. While the capex plans would entail project execution risks, nevertheless these are largely mitigated by the experience of the company in executing large and complex projects

Significant improvement in the liquidity position following robust cash accruals from operations since it restarted from January 2015 - After restarting its operations in January 2015, the company has performed significantly well. However, the operating profitability declined in FY2019 (due to plant shutdowns and a fire incident) and FY2020 (due to low tolling margins, inventory losses and plant shutdowns). Accordingly, the operating margin declined to 8.7% in FY2020 (based on provisional and unaudited numbers) from 15.5% in FY2019 and 22.9% in FY2018. The net cash accruals of the company was ~Rs 617 crore in FY2020 (based on standalone provisional numbers) and Rs 1415 crore in FY2019 as against a net cash accruals of ~Rs 1943 crore in FY2018. ICRA also notes that HPL booked accrued income of Rs 393.5 crore in FY2019 and ~Rs 200 crore in FY2020 basis the West Bengal Incentive scheme and as agreed between TCG and WBIDC under share purchase agreement in 2015, however, the recovery of the same might be delayed given the tenuous fiscal position of the latter. The cash and cash equivalents declined from Rs 4673.3 crore as at FY2018 end to ~Rs 2000 crore as at August FY2020 end

owing to increase in net working capital intensity, capex undertaken, prepayment of debt, part payment for acquisition of MDR's technology division and investments in group companies.

Credit challenges

Large debt funded acquisitions of the technology division of Mc Dermott and land parcel of Nagarjuna Oil as well as advances to other group companies leading to deterioration in debt metrics – The proposed acquisition of MDR's technology division and land of NOCL apart from the advances extended to other group companies would reduce the cash reserves and increase the debt of HPL leading to significant deterioration of its debt metrics going forward.

Olefin cycle expected to remain weak in the near to medium term - The global operating rates of ethylene plants had peaked in CY2017; however, the industry is now passing through a phase of capacity investment. Owing to supply overhang, ethylene over capacity and downcycle in margins are projected through 2023. Nonetheless, the propylene market is tighter than ethylene but new 'on-purpose capacity' could lead to a mild downcycle through 2023. Accordingly, tolling margins for all types of crackers are expected to remain subdued and below their last 10-year averages over the medium term owing to a supply overhang, demand slowdown and more intense competition.

Vulnerability of profitability to cyclical inherent in the business, import duty levels and exchange fluctuations -Despite the current healthy cash accruals of the company, the profitability remains vulnerable to cyclical inherent in the petrochemical business, import duty levels and exchange fluctuations.

Operational risks emanating from draft levels at Haldia port, through which HPL imports naphtha; sustainability of cost structure will also be sensitive to the ability of the company to run its plant without significant downturns -The company is dependent on the draft at the Haldia port, owing to which HPL unloads cargo from the mother vessel to a daughter vessel at the Vizag port and both the mother and daughter vessels with relatively lower weight are unloaded at the Haldia port. However, with the draft level stabilising off late, the risk emanating from receding draft has been offset to some extent. While the high capacity utilisation has resulted in cost efficiencies in manufacturing expenses and better fixed cost absorption in the past, any material decline in the capacity utilisation would adversely impact the cost structure of the company.

Liquidity position: Adequate

The company has large cash reserves (~Rs 2000 crore in mid-August 2020) aided by healthy tolling margins and high capacity utilisation of its plant in the last few years. Accordingly, the liquidity position of the company is expected to remain adequate supported by healthy cash accruals and cash and liquid investments, which would be sufficient to meet the annual debt repayment obligations (including repayment of preference share) of ~ Rs 534 and capex plans of ~Rs 530 crore in FY2021.

Rating sensitivities

Positive triggers – An upgrade in ratings is unlikely in the near to medium term however deleveraging of the balance sheet leading to net debt/OPBDITA (including debt for acquisition) below 1.75 times on a sustained basis could lead to an upgrade.

Negative triggers – The ratings of HPL may be downgraded if net debt/OPBITDA (including debt for acquisition) exceeds 3.5 times on a sustained basis. Additionally, any material funding support to group companies including Lummus Technologies or any large acquisitions could also be a scenario for downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Chemical Industry
Parent/Group Support	NA
Consolidation/Standalone	The rating is based on consolidated financial statements of the rated entity.

About the company

Haldia Petrochemicals Limited (HPL) was set up as a joint venture (JV) between the Dr Purnendu Chatterjee-led Chatterjee Petrochem (Mauritius) and the Government of West Bengal (GoWB), With the sale of 52 crore shares by GoWB in tranches, the majority shareholding as well as the management control of the JV is now with the Chatterjee Group (TCG). HPL manufactures commodity polymers like high-density polyethylene (HDPE), linear low-density polyethylene (LLDPE), and polypropylene (PP), as well as chemicals/fuels like benzene and butadiene with intermediates sourced from a naphtha cracker (capacity: 700 KTA of ethylene) at Haldia, West Bengal. The company is the fourth largest player in the domestic polyolefins market after Reliance Industries Limited Indian Oil Corporation and ONGC Petro Additions Limited.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	9761.8	10698.6
PAT (Rs. crore)	102.4	-309.5
OPBDIT/OI (%)	22.9%	15.5%
RoCE (%)	3.3%	-0.5%
Total Outside Liabilities/Tangible Net Worth (times)	0.4	0.4
Total Debt/OPBDIT (times)	2.0	2.2
Interest Coverage (times)	3.9	3.7

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Amount Rated	Amount Outstanding	Rating (FY2021)		Rating History for the Past 3 Years									
				3-Sept-2020	24-June - 2020	FY2020			FY2019		FY2018				
						13-Dec-2019	16-Sep-2019	12-April-2019	31-Aug-2018	23-Feb-2018	25-Jan-2018	4-Dec-2017	30-June-2017	8-May-2017	
1	Long Term-Proposed NCD Programme	1000.0	-	[ICRA]A+(Stable); withdrawn	[ICRA]AA-(Negative)	[ICRA]AA@	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA-(Stable)	-	-	-	-
2	Long Term Limits-Term Loans	3068.00	3,068.00	[ICRA]A+(Stable)	[ICRA]AA-(Negative)	[ICRA]AA@	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)
3	Long-term Limits-Fund-based	381.00	-	[ICRA]A+(Stable)	[ICRA]AA-(Negative)	[ICRA]AA@	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)
4	Short-term Limits-Non-fund Based Limits	1606.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+@	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Long-term/Short-term Unallocated	5003.00	-	[ICRA]A+(Stable)/[ICRA]A1+	[ICRA]AA-(Negative)/[ICRA]A1+	[ICRA]AA@/[ICRA]A1+@	[ICRA]AA (Negative)/[ICRA]A1+	[ICRA]AA (Stable)/[ICRA]A1+	[ICRA]AA (Stable)/[ICRA]A1+	[ICRA]AA (Stable)/[ICRA]A1+	[ICRA]AA-(Stable)/[ICRA]A1+	[ICRA]AA-(Stable)/[ICRA]A1+	[ICRA]A+(Positive)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+
6	Issuer Rating	-	-	[ICRA]A+(Stable)	[ICRA]AA-(Negative)	[ICRA]AA@	[ICRA]AA (Negative)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)
7	Short Term-Commercial Paper Programme	100.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+@	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	-
8	Long Term Non Fund Based	4000.00	-	[ICRA]A+(Stable)	[ICRA]AA-(Negative)	-	-	-	-	-	-	-	-	-	-

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 [click here](#)

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long Term Limits- Proposed NCD programme	-	-	-	1000.00	[ICRA]A+(Stable)
NA	Long Term Limits- Term Loans	January 2015	9%	March 2029	3068.00	[ICRA]A+(Stable)
NA	Long-term Limits-Fund-based	-	-	-	381.00	[ICRA]A+(Stable)
NA	Short-term Limits- Non-fund Based Limits				1606.00	[ICRA]A1+
NA	Long-term/Short-term Unallocated				5003.00	[ICRA]A+(Stable)/ [ICRA]A1+
NA	Issuer Rating				N.A.	[ICRA]A+(Stable)
NA	Short Term – Commercial Paper programme			7-90 days	100.00	[ICRA]A1+
NA	Long Term Limits- Proposed NCD programme	-	-	-	1000.00	[ICRA]A+(Stable); withdrawn
NA	Long Term Non-fund based	-	-	-	4000.00	[ICRA]A+(Stable)

Source: Haldia Petrochemicals Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Haldia Riverside Estates Limited	100.00%	Full consolidation
HPL Go Private Limited	100.00%	Full consolidation
Advanced Performance Material Private Limited	100.00%	Full consolidation
HPL Global Pte limited	100.00%	Full consolidation

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