

Premier Explosives Limited

November 12, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount(Rs. crore)	Current Rated Amount(Rs. crore)	Rating Action
Long-term Fund based -Term Loan	25.25	23.00	[ICRA]A (Stable); reaffirmed
Long-term Fund based -Term Loan – sub limit	(6.00)	0.00	-
Long-term Fund based	21.00	34.00	[ICRA]A (Stable); reaffirmed
Long-term Fund based – sub limit	(10.00)	(15.00)	[ICRA]A (Stable); reaffirmed
Long-term/ Short Term fund based	10.00	10.00	[ICRA]A (Stable)/ [ICRA]A1; reaffirmed
Short-term Fund based - sub limit	(46.00)	(64.00)	[ICRA]A1; reaffirmed
Short-term Non-Fund based	164.00	230.00	[ICRA]A1; reaffirmed;
Short-term Non-Fund based - sub limit	(45.00)	(100.00)	[ICRA]A1; reaffirmed;
Long-term/ Short-term Proposed facilities	78.00	1.25	[ICRA]A (Stable)/ [ICRA]A1; reaffirmed
Total	298.25	298.25	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the [ICRA]A (pronounced ICRA A)¹ rating outstanding on the Rs. 23.00 crore² term loan facilities, the Rs. 34.00 crore long-term fund-based facilities and the Rs. 15.00 crore long-term fund-based sublimit facilities of Premier Explosives Limited (PEL/the company). ICRA has also reaffirmed the [ICRA]A1 (pronounced ICRA A one) rating outstanding on the Rs. 230.00 crore short-term non-fund-based facilities, the Rs. 64.00 crore short-term fund-based facilities (sublimit) and the Rs. 100.00 crore short-term non-fund-based facilities (sublimit) of the company. ICRA has also reaffirmed the [ICRA]A (pronounced ICRA A)/[ICRA]A1 (pronounced ICRA A one) ratings for the Rs. 10.00 crore long-term/short-term fund-based facilities and the Rs. 1.25 crore long-term/short-term proposed facilities of the company. The outlook on the long-term rating is 'stable'.

Rationale

The reaffirmation of ratings takes into accounts PEL's conservative debt levels at Rs. 39.5 crore, its comfortable capital structure at 0.2 times (net gearing at 0.04 times) and the company's adequate liquidity by virtue of cash balances to the tune of Rs. 31.5 crore as on September 30, 2018 and average fund based working capital utilisation of 59% between July 2017 to June 2018. The ratings also positively factor in the company's marquee clientele comprising of Northern Coalfields Limited (NCL, subsidiary of Coal India Limited), The Singareni Collieries Company Limited (SCCL), Bharat Dynamics Limited (BDL) and Indian Space Research Organisation (ISRO) to name a few, with repeat orders from most customers. Also, PEL is one of the two private players supplying explosives for defence.

However, the ratings are constrained by the decline in PEL's margins in FY2018 and H1 FY2019. The company's operating margin had declined by 470 bps to 8.1% during FY2018 and further to 7.2% in H1 FY2019 primarily on account of lower

¹ For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

² 100 lakh = 1 crore = 10 million

margins from the commercial explosives segment where PEL absorbed the intermediary hikes in ammonium nitrate prices in H2 FY2018 and Q1 FY2019. Also, the company made provisions for expected credit loss of about Rs. 1.9 crore in FY2018 and 0.6 crore in H1 FY2019 which had further dwindled the margins. However, ICRA takes note of the improved margins of 9.7% OPM (operating profit margin) and 4.4% NPM (net profit margin) in Q2 FY2019, compared to 5.0% OPM and 1.5% NPM in Q1 FY2019. PEL's working capital cycle has also stretched in FY2018 and H1 FY2019, with increase in receivables following higher debtor days for defence supplies. As a result, PEL's working capital intensity has stretched to over 30% during these periods. While the company's scale of operations remains modest, PEL has further witnessed a marginal decline of 1.9% in revenues in H1 FY2019. The company remains exposed to the intense price competition in the commercial explosives segment due to fragmented industry structure, commoditised nature of the products in the trade segment and tender-based order procurement with Government entities, although PEL witnessed relatively lower competition in defence. Also, PEL continues to derive ~65% of its revenues from the cyclical mining/ infrastructure industries and about 65% of its revenues from the top five customers, exposing it to associated risks.

The company has a healthy order book position of Rs. 270 crore as on September 30, 2018, to be executed over the next 12-18 months. While this provides revenue visibility, the impact of various strategic initiatives such as pruning low-margin products, on revenues, remains to be seen. There has been an increased focus on the defence segment which is likely to improve the margins in the medium term. ICRA will continue to monitor PEL's profit margins and any downward trend from Q2 FY2019 levels, would be a key rating sensitivity. With increase in proportion of the defence business, PEL's receivables are likely to increase going forward. The ability of the company to manage its working capital requirements without strain on borrowings/cash flows would be critical.

The company is setting up a Greenfield project at Katepally to manufacture Solid propellants, RDX, Warheads, Mines etc. at an expected cost of Rs.50 crore and is expected to commence its operations by end of FY2019. However, the project is being funded out of equity raised in FY2018 and internal accruals. Also, Andhra Pradesh Industrial Infrastructure Corporation (APIIC) had provisionally allotted about 200 acres of land in Andhra Pradesh to the company for setting up a Greenfield satellite propellant plant. The proposal is still in nascent stages and the amount of capex/funding mode has not been finalised. Any significant debt-funded capex for this project would affect the company's capital structure. ICRA would monitor developments on this front and evaluate the impact as and when further details are available.

Outlook: Stable

ICRA believes that Premier Explosives Limited will continue to benefit from increasing demand for its products from defence segment and its established presence in the commercial explosives space. The higher proportion of defence revenues and pruning of low-margin commercial explosive businesses are likely to aid in margin improvement. In the absence of debt-funded capex and with margin improvement, the debt levels and cash flows are likely to remain healthy. The outlook may be revised to 'positive' if the company witnesses significantly higher-than-expected revenue and profit margins. The outlook may be revised to 'negative' upon further decline in margins/accruals or if there is any significant deterioration in debt levels be it because of stretched receivables and/or debt-funded capex. Key rating drivers

Credit strengths

Comfortable debt levels and adequate liquidity – PEL's debt levels continue to remain low at Rs. 39.5 crore as on Sep 30, 2018. The low debt levels, along with a relatively strong Network (partly from a Qualified Institutional Placement and Preferential allotment of shares and warrants of Rs. 70.3 crore in May 2017), have maintained the comfortable capital structure; PEL's gearing was conservative at 0.2 times as on Sep 30, 2018 (net gearing is at 0.04 times). PEL's interest coverage was also healthy at 3.2 times for H1 FY2019. Further, the company's liquidity position remains healthy,

with cash and bank balances of Rs. 31.5 crore as on September 30, 2018, average fund-based utilization of ~59% against sanctioned limits and 51% of drawing power for July 2017-June 2018.

Reputed client profile in the commercial explosives business; PEL continues to be one of the two private suppliers in defence - The company has been present in the commercial explosives business for over three decades and is one of the well-known players in the space. PEL continues to have marquee clients in the mining, cement and infrastructure industries such as Northern Coalfields Limited (subsidiary of Coal India Limited), The Singareni Collieries Company Limited and Neyveli Lignite Corporation Limited to name a few and has history of repeat orders from these clients. Further, PEL is one among the two private players supplying chemicals/explosives for defence and stands to benefit from its technological expertise in the defence space (as can be see through recent order wins).

Healthy order book position – The company has a healthy order book position of Rs. 270 crore as on September 30, 2018, to be executed over the next 12-18 months. While this provides revenue visibility, the impact of various strategic initiatives such as pruning low-margin segments, on revenues, remains to be seen.

Increasing focus on defence and higher-margin products in commercial explosives likely to improve margins over the medium term – PEL has strategically shifted its focus towards the margin-accretive defence segment. Defence revenues have grown at a 5-year CAGR (Compounded Annual Growth Rate) of 27% during FY2018. The company is also focussing on increasing margins from the commercial explosives segments, by concentrating on the high-margin products and pruning the low margin ones, the results of which are evident in Q2 FY2019. As a combination effect of these, PEL's margins are likely to improve over the near to medium term.

Credit challenges

Decline in profit margins YoY in FY2018 and H1 FY2019 – The company's operating margin had declined by 470 bps to 8.1% during FY2018 and further to 7.2% in H1 FY2019 primarily on account of lower margins from the commercial explosives segment where PEL absorbed the intermediary hikes in ammonium nitrate prices in H2 FY2018 and Q1 FY2019. Also, the company made provisions for expected credit loss of about Rs. 1.9 crore in FY2018 and 0.6 crore in H1 FY2019 which had further dwindled the margins. However, ICRA takes note of the improved margins of 9.7% OPM and 4.4% NPM in Q2 FY2019, compared to 5.0% OPM and 1.5% NPM in Q1 FY2019, with increase in share of margin accretive defence revenues and relatively stable ammonium nitrate prices. PEL's margins are likely to improve going forward as discussed above. ICRA will continue to monitor PEL's profit margins and any downward trend from Q2 FY2019 levels, would be a key rating sensitivity.

Stretched working capital cycle - The company's debtor days have increased from 70-80 days in FY2014-FY2017 to 120-140 during FY2018 and H1 FY2019, due to elongated receipts for defence supplies. This has deteriorated the working capital intensity to over 30% during FY2018 and H1 FY2019. However, ICRA draws comfort from PEL's working capital utilization, which has remained at <60% during Oct 2017 to Sep 2018. With increase in proportion of the defence business, PEL's receivables are likely to increase going forward. The ability of the company to manage its working capital requirements without strain on borrowings/cash flows, remains to be seen.

Intense price competition in the commercial explosives segment; however relatively lower competition in defence – The commercial explosives space remains highly competitive because of the fragmented industry structure, commoditised nature of the products in the trade segment and tender-based order procurement with Government entities. PEL's revenues declined by 1.9% on YoY basis in H1 FY2019, while its margins also dropped 180 bps YoY partly on account of the competition. However, in defence, the company is one of the two private players supplying explosives currently and as a result, faces relatively low competition.

Modest scale of operations; high segment and customer concentration risks – Although PEL’s revenues grew at a healthy rate of 19.4% (5-year CAGR), the company’s scale of operations continues to be modest at Rs. 265.9 crore for FY2018. Further, in H1 FY2019, the company’s revenues witnessed a marginal decline of 1.9% to Rs. 113.0 crore primarily on account of subdued growth in the commercial explosives space.

PEL continues to derive ~65% of its revenues from the cyclical mining/ infrastructure industries and the remaining ~35% from the relatively uniform defence segment. While the segment concentration has reduced marginally from previous levels, the company still remains vulnerable to downturns in the mining/infrastructure space. Also, the company’s customer concentration with its top five customers remains high at 65% of revenues in H1 FY2019. The high customer concentration exposes PEL to revenue risks in the event of order slowdown from the customers, loss of clients to competition or decline in average realizations from these customers.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

[Rating Methodology for Entities in the Chemical Industry](#)

About the company:

Incorporated in 1980, PEL is primarily engaged in manufacture and sale of industrial explosives in India to established players like Northern Coalfields Limited (subsidiary of Coal India Limited), The Singareni Collieries Company Limited and Neyveli Lignite Corporation Limited. The company also has minimal exports. Further, PEL is also engaged in design, development and manufacture of solid propellants for Indian defence, in addition to operation and maintenance (O&M) services of solid propellant plants at the Sriharikota Centre of Indian Space Research Organization (ISRO) and Solid Fuel Complex at Jagdalpur under the umbrella of Defence Research and Development Organisation (DRDO). Sale of industrial explosives constituted ~63% of PEL’s revenues while revenues from defence supplies and operation and maintenance (O&M) services were around 28% and 9% of revenues respectively in H1 FY2019.

PEL has two subsidiaries - Premier Wire Products Limited (80% stake) and PELNEXT Defence Systems (100% stake). While Premier Wire Products Limited is into manufacturing of Galvanised Iron (GI) wires used in detonators, PELNEXT Defence Systems is established for manufacturing ammunition for Indian defence. PEL has also incorporated a joint venture with the Kalyani Group in April 2015, under the name BF Premier Energy Systems Private Limited for manufacturing defence products; however, this venture is yet to commence operations.

Key financial indicators (audited)

	FY2017	FY2018
Operating Income (Rs. crore)	230.3	265.9
PAT (Rs. crore)	14.8	8.7
OPBDIT/OI (%)	12.8%	8.1%
RoCE (%)	20.9%	9.2%
Total Debt/TNW (times)	0.3	0.2
Total Debt/OPBDIT (times)	1.3	2.1
Interest coverage (times)	6.7	4.0

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)			Chronology of Rating History for the Past 3 Years			
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016	
				November 2018	January 2018	February 2017	February 2016	
1	Term Loan 1	10.50	10.50	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	
2	Term Loan 2	12.50	0.0	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	
3	Fund based	34.00		[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	
4	Fund based sublimit	(15.00)		[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	-	
5	Fund based	10.00		[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	-	-	
6	Fund based sublimit	(64.00)		[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+	
7	Non-Fund based	230.00		[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+	
8	Non-Fund based sublimit	(100.00)		[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A2+	
9	Proposed facilities	1.25		[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	-	-	
10	Proposed facilities	-		-	-	[ICRA]A (Stable)	[ICRA]A- (Stable)	
11	Term Loan sublimit	-		[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A- (Stable)	

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
NA	Term Loan 1	Sep 2016	-	Sep 2022	10.50	[ICRA]A (Stable)
NA	Term Loan 2	Oct 2018	-	NA*	12.50	[ICRA]A (Stable)
NA	Cash Credit	-	-	-	30.00	[ICRA]A (Stable)
NA	Cash Credit sublimit	-	-	-	(15.00)	[ICRA]A (Stable)
NA	Bank Guarantee	-	-	-	230.00	[ICRA]A1
NA	Letter of Credit	-	-	-	(50.00)	[ICRA]A1
NA	Bank Guarantee sublimit	-	-	-	(20.00)	[ICRA]A1
NA	Standby Letter of Credit	-	-	-	4.00	[ICRA]A1
NA	EPC/ PCFC/ FBD/ BD/ EBR sub limit	-	-	-	(9.00)	[ICRA]A1
NA	WCDL sublimit	-	-	-	(15.00)	[ICRA]A1
NA	PCFC/ PSFC/ PC – INR/ EBD sub limit	-	-	-	(10.00)	[ICRA]A1
NA	FCNR (B) sub limit	-	-	-	(30.00)	[ICRA]A1
NA	Inland Letter of Credit/ Foreign Letter of Credit	-	-	-	(30.00)	[ICRA]A1
NA	Cash Credit/ WCDL	-	-	-	10.00	[ICRA]A (Stable)/ [ICRA]A1
NA	Proposed Facilities	-	-	-	1.25	[ICRA]A (Stable)/ [ICRA]A1

Source: Premier Explosives Limited; * - Yet to be availed

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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