July 11, 2017

The Andhra Petrochemicals Limited

Summary of rated instruments

Instrument	Amount in Rs Crore[1]	Rating Action
Term Loans	58.90 (revised from 70.12)	[ICRA]BB- reaffirmed; outlook revised from Negative to Stable
Cash Credit	35.00	[ICRA]BB- reaffirmed; outlook revised from Negative to Stable
Unallocated	18.65 (revised from 7.43)	[ICRA]BB- reaffirmed; outlook revised from Negative to Stable
Non Fund Based	2.00	[ICRA]A4 reaffirmed
Total	**114.55**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the long-term rating outstanding on the Rs. 58.90 crore term loans (revised from Rs. 70.12 crore), Rs. 35.00 crore cash credit facility and Rs. 18.65 crore (revised from Rs. 7.43 crore) unallocated facilities of The Andhra Petrochemicals Limited (APL or the company) at [ICRA]BB- (pronounced ICRA double B minus)2.. ICRA has also reaffirmed the short-term rating outstanding on the Rs. 2.00 crore non-fund based facilities at [ICRA]A4 (pronounced ICRA A four). The outlook on the long term rating has been revised from Negative to Stable

Rationale

The revision in outlook from negative to stable considers the continuous improvement in profitability of the Company during FY2017 and in the current fiscal and expected benefits from the implementation of goods and service tax (GST) in the form of input tax credit on naphtha (a key raw material) and LSHS (a fuel), which was earlier not available. However, the ratings remain constrained on account of subdued pace of recovery in financial performance during FY2017, with modest decline in revenue (~2% YoY decline) and while operating margin witnessed improvement from -3.5% in the preceding fiscal to 3.9%, it remained inadequate to absorb the fixed costs and the company continued to report losses with net margin of -2.2% (PY -7.2%). The company continued to witness pricing pressure, despite imposition of anti dumping duty (ADD) on import of 2-EH and NBA from several countries in March/April 2016 due to several factors including (a) increase in imports from countries not covered under the ADD ruling, (b) increase in direct import of DOP[3], which impacted the demand from the end user segment of the company and (c) some increase in import of substitute products like 2-PH and INA[4]. The subdued pricing environment again forced the company to undertake a production shutdown for nearly 73 days during H1 FY2017 and ~11 days during Q3 FY2017, when prices became un-remunerative and due to the impact of

[1] *100 lakh = 1 crore = 10 million*

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

[3] Di-Octyl Phthalate

[4] 2 Propyl Heptanol and Iso Nonyl Alcohol

de-monetisation respectively. The overall capacity utilization stood at 82% during FY2017 compared to 79% in the preceding fiscal. The pressure on pricing during this period was on account of global over supply on the back of supply increase in last few years. However since the second half of the fiscal, there has been gradual improvement in pricing aided by some supply correction for factors like closure due to environmental scrutiny, force majeure events and extended maintenance shutdown. This has eased the pressure on pricing for APL also to some extent in the current fiscal. Further, ICRA notes that the company is also exploring several options to improve production efficiency, have flexibility to change the product mix and reduce power costs. The quantum and timeliness of the benefits accruing from the above mentioned factors remain a rating sensitivity factor.

Due to lack of integration benefits and being a standalone petrochemical producer; the Company's margins are susceptible to spreads between the oxo-alcohols and the feedstock, import duty differentials and foreign exchange rates, leading to volatility and cyclicality of profitability; and is exposed to threat of cheaper imports from countries which are currently not covered under the anti dumping duty. However ICRA notes that currently investigation against countries which are not covered under the ADD ruling issues in March/April 2016 is on and further investigation against DOP imports have also been initiated based on complaint of domestic DOP manufacturers and any potential increase in ADD coverage for these segments should be a positive for APL.

ICRA also takes note of prudent steps taken by the company to mitigate liquidity pressure and prevent any default in the last few years since the HPCL accident by getting the repayments rescheduled for the existing loans. A significant part of these loans had been prepaid prior to the accident . The company had also tied up working capital term loans/corporate loans with moratorium period to tide over the pressure during the stabilization phase. Further, the liquidity position was also aided by continued support from the parent Andhra Sugar Limited (rated [ICRA]A+/stable/[ICRA]A1+) in the form of interest bearing unsecured loans; partial receipt of insurance claims and funds raised from partial divestment of investments (in FY2017). However, due to slower pace of margin recovery post stabilization of raw material supply since FY2016 , the comfort provided by the steps taken have eroded to some extent and with high repayment obligations in the current fiscal, in the absence of sufficient improvement in profitability and cash flows, the company may require further support from the Group/refinancing of loans to meet debt servicing obligations on time.

The ratings however continue to favourably consider the sole producer status of APL in the Indian oxo-alcohol market with APL catering to 35-40% of the domestic oxo-alcohol demand (at normalized production level); and the optimistic long-term domestic demand outlook for various end-use sectors of oxo-alcohols. The ratings also consider the healthy capital structure of the company, aided by profits generated in the past and prepayment of term loans (prior to HPCL accident) and low working capital intensity. ICRA also draws comfort from the benefits accruing to APL as part of the Andhra Sugars Group, which has an established track record over the past six decades.

Key rating drivers

Credit strengths

- Sole producer of oxo-alcohols (2-ethyl hexanol, n-butanol, iso-butanol) in India with an estimated market share of 35-40% (at full capacity utilisation), with imports catering to the remaining domestic demand
- Favourable long-term domestic demand outlook for various end-use sectors of oxo-alcohols such as plasticisers
- Promoted by Andhra Sugars Limited; the GGroup has around six decades of operating history
- Implementation of GST will provide benefits due to additional input tax credits, which were not available earlier

Credit weaknesses

- Standalone petrochemical producer without integration benefits; margins dependent on spreads between oxo-alcohols and its feedstocks, and are hence volatile and cyclical
- Margins also susceptible to import duty differentials and forex rates, as prices are linked to international ones
- Revenues and margins are vulnerable to cheaper imports from countries like Saudi Arabia, the USA, Russia, EU, where the local players enjoy the advantage of lower cost of feedstock either due to backward integration with refineries or due to usage of natural gas. While the Directorate General of Anti Dumping and Allied Duties (DGAD) has imposed Anti Dumping Duty (ADD) on imports from several large importing countries in March/April 2016, the pressure on pricing from imports have continued due to increase in imports of from countries not covered under the ruling and direct import of DOP, which is the end user of oxo-alcohols.
- High dependence on a single feedstock supplier makes it vulnerable to force majeure event risk leading to a disruption of operations, as witnessed in FY2014 and FY2015. However, the supply has been largely regular since FY2016.
- Significant deterioration in financial performance post HPCL accident and subsequent subdued recovery in last few years due to adverse market conditions have adversely impacted the debt protection metrics. While the liquidity was supported to an extent by steps taken by the Company, which includes term loan re-schedulement, availing new corporate /working capital loans with moratorium period and continued support from Group entities, the slower pace of recovery has reduced the comfort and with high repayment obligations in near term, inadequate recovery in margins may necessitate additional support from the Group/refinancing of loans to timely meet debt repayment obligations.

Description of key rating drivers

Andhra Petrochemicals Limited is the sole producer of oxo-alcohols in India and has been operational for more than three decades. A part of the reputed Andhra Sugars Group, which has long operational track record of six decades, the company can cater to ~35-40% of domestic demand when operating at full capacity. The company’s products are mainly used by domestic manufacturers of DOP, which is used as plasticisers in manufacturing of PVC. The long term demand potential for PVC in India remains favourable.

APL is a standalone manufacturer without backward integration benefits and is dependent on a single source – HPCL for supply of key feedstock propylene. Additionally, the usage of naphtha compared to natural gas used by other international manufacturers, puts it at a relative cost disadvantage. This exposes the company’s sales and margin to volatility in global prices and spread between product and feedstock prices, intense competition from imports, changes in duty structure and import pattern of end user segments and substitute products. The company's operations were severely impacted in FY2014 and FY2015, due to feedstock supply disruption following a fire at HPCL's refinery. Subsequently, while the feedstock supply was restored and stabilized by FY2016, the company's operations were impacted by pricing pressure arising from cheaper imports, which impacted the recovery during the year as the Company had to undertake shutdown during periods of un-remunerative pricing. Based on company's petition and subsequent investigation, the DGAD imposed ADD on imports of 2-EH and NBA from several countries in March/April 2016. However, despite these measures the recovery remained subdued during FY2017 due to several factors including increase in imports from companies not covered under the ADD ruling, increase in direct imports of DOP and substitute products, due to which company had to undertake periodic shutdowns.

The global product prices and spreads have witnessed some improvement in recent months, which coupled with implementation of GST and execution of several cost control measures being explored by the company, should aid in improvement in profitability of the Company. However, the quantum of improvement and timeliness of the benefits remains to be seen and is a sensitivity factor. Due to the significant deterioration in financial performance post HPCL accident and subsequent slow recovery, the company's debt protection metrics have weakened. While, the liquidity pressure was partly mitigated by steps undertaken by the company post the HPCL accident including getting the debt repayment rescheduled, support from Andhra Sugars Group, availing additional debt with moratorium period during the expected stabilization phase, partial receipt of insurance claim and partial divestment of investment (in FY2017), the comfort has reduced due to slow pace of recovery. With high repayment obligations in the near term, in the absence of adequate recovery in margins due to above mentioned factors, the company may need additional support from the Group/refinancing to meet its repayment obligations.

Table 1

Key Financial Indicators	**FY16**	**FY17**
Operating income (Crores)	335.7	328.9
PAT (Crores)	-24.1	-7.4
OPBDIT/ OI (%)	-3.5%	3.9%
RoCE (%)	-5.4%	2.0%
Total Debt/ TNW (times)	0.8	1.0
Total Debt/ OPBDIT (times)	-8.2	8.7
Interest coverage (times)	-0.9	0.8
NWC/ OI (%)	8.2%	12.5%

Source: APL and ICRA Research

Analytical approach

For arriving at the ratings, ICRA has applied its rating methodology as indicated below.

Links to applicable criteria

Corporate Credit Rating Methodology
Rating Methodology for Entities in the Chemical Industry

About the company

The Andhra Petrochemicals Limited (APL) was promoted by The Andhra Sugars Limited (ASL) and incorporated on April 18, 1984. It is currently the sole producer of oxo-alcohols in India with a capacity to manufacture 73,000 tonnes per annum (tpa) of oxo-alcohols. The product mix includes 2 ethyl hexanol (2EH), n-butanol (NB) and iso-butanol (IB). APL's oxo-alcohol manufacturing capacity currently caters to about 35-40% of the Indian market, with imports accounting for the rest. Oxo-alcohols are primarily used as one of the raw materials for manufacturing polyvinyl chloride (PVC) plasticisers. APL commenced operations in February 1994. APL's factory is located adjacent to Hindustan Petroleum Corporation Limited's (HPCL) Vishakhapatnam refinery and APL has entered into a long term contract with the latter for procurement of propylene, which is the key raw material in the manufacturing process.

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years

Table

S. No.	Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. Crore)	Date & Rating	Date & Rating in FY2016	Date & Rating in FY2015			Date & Rating in FY2014
				July 2017	March 2016	March 2015	Sep 2014	May 2014	Nov 2013
1	Fund Based – Cash Credit	Long Term	35.00	**[ICRA]BB- (Stable)**	**[ICRA]BB- (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BBB- (Negative)**	**[ICRA]BBB+ (Negative)**
2	Term Loans	Long Term	58.90	**[ICRA]BB- (Stable)**	**[ICRA]BB- (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BBB- (Negative)**	**[ICRA]BBB+ (Negative)**
3	Unallocated	Long Term	18.65	**[ICRA]BB- (Stable)**	**[ICRA]BB- (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BB+ (Negative)**	**[ICRA]BBB- (Negative)**	**[ICRA]BBB+ (Negative)**
4	Non Fund Based – LC/BG	Short Term	2.00	**[ICRA] A4**	**[ICRA] A4**	**[ICRA]A4+**	**[ICRA]A4+**	**[ICRA]A3**	**[ICRA]A2**

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

Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
Consortium Project Term Loan	FY2008 and FY2009*	-	October 2017	11.15	[ICRA]BB-(Stable)
Corporate Loan	February 2016	-	January 2017	10.0	[ICRA]BB-(Stable)
Consortium Working Capital Term Loans	FY2015^	-	March 2021	37.75	[ICRA]BB-(Stable)
Long Term Unallocated				18.5	[ICRA]BB-(Stable)
Cash Credit				35.00	[ICRA]BB-(Stable)
Non Fund Based				2.00	[ICRA]A4

Source: Andhra Petrochemicals Limited; ^Consortium partners sanctioned the loans during FY2015 on different dates; * Consortium partners sanctioned the loans during FY2008 and FY2009 on different dates

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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.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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