September 01, 2017

The Andhra Petrochemicals Limited

Summary of rated instruments

Instrument	Amount in Rs Crore[1]	Rating Action
Fund Based -Term Loans	58.90	Upgraded from [ICRA]BB- to [ICRA]BB; outlook revised from Stable to Positive
Fund Based-Cash Credit	35.00	Upgraded from [ICRA]BB- to [ICRA]BB; outlook revised from Stable to Positive
Unallocated	18.65	Upgraded from [ICRA]BB- to [ICRA]BB; outlook revised from Stable to Positive
Non Fund Based	2.00	Upgraded from [ICRA]A4 to [ICRA]A4+
Total	**114.55**	

*Instrument details are provided in Annexure-1

Rating action

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

Rationale

The revision in ratings and outlook considers the continued improvement in financial performance of the Company during the current fiscal (till date) aided by improvement in spread between global product prices and raw material on the back of supply correction, continued healthy demand in the domestic market and benefits from the implementation of goods and service tax (GST) from the month of July in the form of input tax credits on naphtha (a key raw material) and L.S.H.S (a fuel), which were earlier not available. The company witnessed 42.3% YoY and 9.6% of sequential revenue growth during Q1 FY2018, aided by improvement in product prices and capacity utilization of ~98% (~86% in Q1 FY2017). The OPM and NPM also improved from 4.6% and -0.7% during Q1 FY2017 and 3.3% and -2.5% during Q4 FY2017 to 5.2% and 0.5% during Q1 FY2018 leading to positive cash accrual of ~Rs. 2.8 crore during the quarter. The performance witnessed further improvement during July 2017 backed by healthy capacity utilization of ~125% and availability of input tax credit under the GST regime leading to healthy increase in cash accruals, of which ~ Rs. 7.6 crore was used for prepayment of one of the term loans. 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. While imposition of ADD on import of 2-EH/NBA in March/April 2016 was meant to address this issue, the company remained exposed to threat of cheaper imports from countries which are currently not covered and further impacted by increase in direct imports of DOP. However, ICRA notes that currently investigation against countries which are not covered under the ADD ruling issued earlier is on and further investigation against DOP imports have also been initiated based on complaint of domestic DOP manufacturers and any potential

[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

increase in ADD coverage for these segments should be a positive for APL. ICRA expects the improvement in financial performance to continue in the current fiscal backed by GST benefits and cost control and efficiency improvement measures being undertaken by the company. However, the pace and quantum of improvement in financial performance and timeliness of additional trade protection measures remain a sensitivity for improvement in company's credit profile and the developments will be monitored.

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 slow pace of margin recovery post stabilization of raw material supply since FY2016 , the comfort provided by the steps taken have eroded to some extent. With high repayment obligations in the current fiscal, it will be critical for the company to sustain the healthy improvement in financial performance witnessed in recent months, as 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 of operations over the past six decades.

Key rating drivers

Credit strengths

- **Sole producer of oxo-alcohols (2-ethyl hexanol, n-butanol, iso-butanol) in India; favourable long term demand outlook for various end user sectors –** APL is the sole producer of oxo-alcohols in India and has been operational for more than three decades. The company can cater to ~35-40% of domestic demand when operating at full capacity, while remaining demand is being met by imports. 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 outlook for PVC in India remains favourable.
- **Promoted by Andhra Sugars Limited; the Group has around six decades of operating history -** APL is part of the Andhra Sugars group, with the flagship entity Andhra Sugars Limited (rated [ICRA]A+(Stable)/[ICRA]A1+) having around six decades of operating history and a strong credit profile.
- **Implementation of GST to provide benefits due to additional input tax credits, which were not available earlier –** The company has started getting input tax credits on naphtha (a key raw material) and LSHS under the GST regime, which was not available earlier for the VAT applicable on these commodities as more than 95% of company's sales were interstate sales. The benefit from these additional tax credits are expected to help company's profitability and improve its competitiveness.

Credit weaknesses

- **Standalone petrochemical producer without integration benefits; margins dependent on spreads between oxo-alcohols and its feedstock, and susceptible to changes in import duties, other trade protection measures and forex rates -** APL is a standalone manufacturer without backward integration benefits and 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, spread between product and feedstock prices, intense competition from imports, changes in duty structure and import pattern of end user segments and substitute products. While, the imposition of ADD on imports of 2EH/NBA from several large importing countries in March/April 2016, did not lead to sufficient improvement in profit margins during FY2017 on account of factors like increase in imports from countries not covered under ADD ruling issued, increase in import of substitute products and direct import of DOP; the pricing and spread has improved in current fiscal on the back of global supply correction. Further, currently investigation against countries which are not covered under the ADD ruling issued earlier 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. Since the prices of products and raw materials are linked to global prices, the margins are also susceptible to volatility in forex rates.
- **High dependence on a single feedstock supplier makes it vulnerable to force majeure event risk leading to a disruption of operations–** APL is dependent on a single source – HPCL for supply of key feedstock propylene. The company's operations were severely impacted in FY2014 and FY2015, due to feedstock supply disruption following a fire at HPCL's refinery. However the supply has been largely regular since FY2016.
- **Debt protection metrics weakened by significant deterioration in financial performance post HPCL accident and subsequent subdued recovery in last few years. However prudent measures and group support have mitigated the impact to some extent. Pace of recovery in financial performance remains critical for improvement in credit profile -** 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 from these measures had reduced due to slower pace of recovery. However the healthy improvement in performance witnessed in current fiscal (till date) and prepayment of one of the term loans is a positive. With high repayment obligations in the near term, it will be critical for the company to sustain the improvement in margin witnessed in recent months as in the absence of adequate recovery in margins due, the company may need additional support from the Group/refinancing to meet its repayment obligations. Hence, the pace of recovery in financial performance and timeliness of materialisation of additional trade protection measures remain a sensitivity factor for improvement in credit profile

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:
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.

In Q1 FY2018, the company reported a net profit of Rs. 0.6 crore on an operating income of Rs. 114.7 crore, as compared to a loss of Rs. 0.5 crore on an operating income of Rs. 80.6 crore during Q1 FY 2017.

Key Financial Indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	335.7	328.9
PAT (Rs. crore)	-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%

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);
NWC: Net Working Capital

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	Date & Rating in FY2016	Date & Rating in FY2015			Date & Rating in FY2014
				Sept 2017	July 2017	Mar 2016	Mar 2015	Sep 2014	May 2014	Nov 2013
1	Fund Based – Cash Credit	Long Term	35.00	[ICRA]BB (Positive)	[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 (Positive)	[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 (Positive)	[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]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

ISIN No	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 2018	11.15	[ICRA]BB(Positive)
	Corporate Loan	February 2016	-	March 2018	10.00	[ICRA]BB(Positive)
	Consortium Working Capital Term Loans	FY2015^	-	January 2021	37.75	[ICRA]BB(Positive)
	Long Term Unallocated				18.65	[ICRA]BB(Positive)
	Cash Credit				35.00	[ICRA]BB(Positive)
	Non Fund Based				2.00	[ICRA]A4+

Source: Andhra Petrochemicals Limited; ^Consortium partners sanctioned the loans during FY2015 on different dates of which the longest tenure loan is maturing on January 2021; * 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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