Thirumalai Chemicals Limited

October 03, 2018

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Long term; Fund based facilities	208.2	[ICRA]A+ (Stable); assigned
Short term; Non fund based facilities	407.4	[ICRA]A1+; assigned
Long term / Short term; Unallocated	9.4	[ICRA]A+ (Stable) / [ICRA]A1+; assigned
Total	**625.0**	

Rating action

ICRA has assigned a long term rating of [ICRA]A+ (pronounced ICRA A plus) to the Rs 208.2 crore fund based bank facilities and a short term rating of [ICRA]A1+ (pronounced ICRA A one plus) to the Rs. 407.4 crore non fund based bank facilities of Thirumalai Chemicals Limited ("TCL"/"the company"). ICRA has also assigned a long term / short term rating of [ICRA]A+ / [ICRA]A1+ to the Rs 9.4 crore proposed facilities of TCL. The outlook on the long term rating is Stable.

Rationale

The assigned ratings reflect the established track record and market position of TCL in the Phthalic Anhydride (PAN) market. ICRA takes note of the strong revenue growth and margin improvement witnessed in recent years aided by healthy demand, favourable PAN-Orthoxylene (OX) spreads and reduction in production lead time undertaken by the company. Further, the turnaround witnessed in the operations of the Malaysian subsidiary – Optimistic Organic SDN BHD (OOSB) – driven by a shift to cheaper raw material, capacity expansion and increase in realisations of Maleic Anhydride (MAN) have also supported the improvement in performance of the consolidated entity. The healthy cash accruals in last two years, have led to improvement in capital structure and coverage indicators. The ratings further factor in the increasing contribution from the downstream derivative products such as esters and Food acids which has lent significant diversity to demand and revenues.

The ratings also factor in the ongoing capacity expenditure programme being incurred by the company towards modernisation of the existing facilities, increasing established capacities and setting up of a greenfield PAN plant in Dahej, Gujarat. The modernization capex will aid in improving cost structure and TCL's ability to withstand volatility in PAN-OX spreads, whereas the increased capacity would aid in maintaining its market position. The scheduled capex programme is being funded entirely out of internal accruals which provides further comfort on the rating. Nonetheless, any large debt funded capital expenditure remains a rating sensitivity factor.

The ratings are, however, constrained by the susceptibility of the financial performance to volatility in PAN-OX spreads, which are dependent on crude price levels; cyclicality in demand from end user industries and competition from imports. While ICRA notes that the PAN-OX spreads have been favourable in recent years due to tight supply in the Asian markets; with recent increase in the crude oil prices, the company might see a moderation in the margin levels, from the peak witnessed in FY 2018, and an increase in the working capital requirements. Further, the domestic industry also remains vulnerable to changes in duty structure and the competition from imports may intensify, as some of the trade protection benefits enjoyed by the industry in past few years may not be renewed. Nonetheless, ICRA notes that the company's ability to withstand the above-mentioned risks are better, compared to earlier downturns due to improved financial risk profile and other initiatives taken by the company.

Outlook: Stable

ICRA believes TCL's credit profile will remain healthy supported by the product demand, established market position, and healthy capital structure. The outlook may be revised to 'Positive' if there is significant improvement in cash accruals of the company following sustained high profitability. The outlook may be revised to 'Negative' if TCL's financial profile weakens due to lower cash accruals on account of significant drop in margins or if debt-funded capex or stretch in working capital cycle, leads to pressure on capital structure.

Key rating drivers

Credit strengths

Established operating track record and market position in the Phthalic Anhydride (PAN) industry – TCL is the second largest player with a significant market share in the domestic phthalic anhydride industry, which is in effect a duopoly. The company has established relationships with clients in the key end user industries such as plasticizers, paints and pigments having been in operation for more than three decades. TCL also has a longstanding relationship with Reliance Industries Limited, the supplier of raw material – Orthoxylene (OX), and operates on an assured offtake model.

Sharp increase in the profitability post 2016 – TCL's PAN profitability is directly dependant on the spread between the prices of PAN and OX given that OX makes up ~80% of production cost. Orthoxylene being a crude derivative, prices have declined in line with the sharp reduction in the crude prices in the last two years. The PAN prices, however, have remained high given the moderately strong demand from end use markets such as plasticizers & paints as well as the tight supply of the product in Asia following closure of some capacities in China's recent environment protection drive. Hence, the PAN-OX spread had widened substantially from 2016 resulting in healthy operating profitability in FY 2017 and FY 2018.

Diversification into other related chemicals; turnaround of Malaysian operations – The company produces phthalate esters and food acids, which are downstream derivatives, and the contribution of these products have grown over the years given the improving demand in the market. Maleic Anhydride (MAN) operations at the Malaysian subsidiary, OOSB, have also turned around driven by increase in capacity utilisation and the product realisations. With an increasing revenue and profit share of these products, the business risk of TCL stands moderately diversified.

Healthy financial risk profile– Cash flows at the TCL's standalone operations have been healthy resulting in repayment of all availed borrowings and the company was debt-free in FY 2017 and FY 2018. At the consolidated level, the debt levels are marginal compared to the net worth and the debt at the Malaysian subsidiary is expected to be serviced out of its own cash flows given the improved profitability. The debt coverage metrics have also remained robust given the very low interest and financing charges

Expansion/modernization of capacity of various product lines – The company is in the midst of a large capital expenditure programme wherein the Ranipet PAN plant is being modernised, the derivatives capacity is being enhanced; and a greenfield PAN / derivatives project is being set up in Dahej, Gujarat. These initiatives would aid the company in maintaining its market position and also improve its competitiveness, given that the greenfield project location is proximate to the supplier, majority of existing customers and a potentially large export market, the Middle East. The scheduled capex is being entirely funded out of the internal accruals and hence the capital structure will continue to remain healthy.

Credit challenges

Presence in commodity chemical industry limits pricing flexibility – Limited product differentiation and large volumes of inter-regional trade of PAN has resulted in TCL's realisations being influenced by the overall demand – supply dynamics in the region. The key end user industries of the product are plasticizers, paints & pigments, which are further mainly used in the construction and automobile sectors and hence the demand is based on broader economic conditions. With regards to supply, the market dynamics change significantly based on the production and consumption in key markets such as China, Korea and South East Asia. Hence, even though TCL has long / medium term contracts with a large number of its customers, the product realisations are volatile.

Increased competitive intensity due to higher volumes of imports – Imports of PAN into India increased from 52,350 MT in FY 2015 to 1,30,440 MT in FY 2018 (Source: DGFT) mainly driven by the increase in consumption which is higher than the production of the domestic industry. The increase in imports was in spite of the in-place Anti-Dumping Duties (ADD) imposed in the year 2012 on producers from countries like Korea and Taiwan. In September 2018, the Director General of Trade Remedies has recommended discontinuation of the ADD and this could result in increase of imports in the long term.

Though Indian manufacturers are currently competitive when compared to the prices of the other Asian exporters, any sudden change in the consumption trends in other countries in the region would result in more import volumes into India and impact PAN pricing and margins. Hence the business remains susceptible to any significant regulatory changes.

Raw material price volatility impacts product demand and margins – The prices of orthoxylene have remained highly volatile in the past, being a crude derivative. The demand for the company's products as well as its working capital intensity would be impacted during periods when crude oil prices rule high. With crude prices trending up again in 2018 and with the significant depreciation witnessed in the rupee, the overall PAN-OX spread can be expected to moderate; albeit, still remaining healthy at an absolute level. The company has, however, rationalised its production lead time and inventory management which will aid in passing on OX price changes onwards to its customers thereby protecting its margins.

Project risks with regards to the new capacities being set up – TCL's large ongoing capital expenditure is towards enhancing production capacities of various products. Timely commissioning of these projects, without major cost overruns, and early stabilisation of the capacities would be critical to achieve growth. The company also has significant capacity expansion plans in the long term; the nature and funding plan for the same would determine the long term 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:

TCL started its operations in 1976 in Ranipet in Tamil Nadu as a single product petrochemical company manufacturing Phthalic Anhydride, with a production capacity of 6000 TPA. The company is part of the Thirumalai group, which has business interests in chemicals, surfactants, pigments and education. Over the years, the company has expanded the PAN manufacturing capacity to ~145000 TPA and has also added other products to its portfolio, which includes food additives like Malic Acid and Fumaric Acid; PAN derivatives like Di-ethyl Phthlate (DEP) and Pthalimide (PID) etc. and caters to customers in construction, auto, paint, food, personal care and pharma industries. The company has developed low energy process, which enables it to meet ~90% of its power requirements through waste heat recovery.

The company also has a Maleic Anhydride manufacturing facility in Malaysia under its step-down subsidiary, Optimistic Organic Sdn. Bhd. (OOSB).

The company, on a standalone basis, reported an operating income of Rs 1,011.6 crore and net profit of Rs 144.0 crore in FY 2018 as against operating income of Rs 857.2 crore and a net profit of Rs 74.1 crore in FY 2017.

Key financial indicators (audited)

Consolidated	FY 2017	FY 2018
Operating Income (Rs. crore)	1,028.5	1,312.0
PAT (Rs. crore)	70.7	170.4
OPBDIT/ OI (%)	15.6%	22.6%
RoCE (%)	27.8%	48.2%
Total Debt/ TNW (times)	0.15	0.09
Total Debt/ OPBDIT (times)	0.38	0.17
Interest coverage (times)	9.60	23.10

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 Oct 2018	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016
1	Fund based facilities	Long Term	208.2*	-	[ICRA]A+ (Stable)	-	-	-
2	Fund based facilities	Long Term	407.4*	-	[ICRA]A1+	-	-	-
3	Unallocated	Long Term / Short Term	9.4	-	[ICRA]A+ (Stable) / [ICRA]A1+	-	-	-

*Partial interchangeability between fund based and non fund based facilities

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	Cash Credit	-	-	-	208.2	[ICRA]A+ (Stable)
NA	Non fund based facilities (LC / BG)	-	-	-	407.4	[ICRA]A1+
NA	Unallocated	-	-	-	9.4	[ICRA]A+ (Stable) / [ICRA]A1+

Source: TCL

ANALYST CONTACTS

K.Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Sai Krishna
+91 44 4596 4304
sai.krishna@icraindia.com

Raghunath.T
+91 44 4596 4304
raghunath.t@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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.

For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 6606 9999

© Copyright, 2018 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. ICRA ratings are subject to a process of surveillance, which may lead to revision in ratings. An ICRA rating is a symbolic indicator of ICRA's current opinion on the relative capability of the issuer concerned to timely service debts and obligations, with reference to the instrument rated. Please visit our website www.icra.in 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, including the rated issuer. ICRA however has not conducted any audit of the rated issuer or of the information provided by it. While 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. Also, ICRA or any of its group companies may have provided services other than rating to the issuer rated. 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