October 07, 2019

Chowgule and Company Private Limited: Ratings downgraded to [ICRA]A(Stable)/[ICRA]A1; removed from rating watch with negative implications

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	145.00	145.00	[ICRA]A (Stable); downgraded from [ICRA]A+ and removed from rating watch with negative implications
Long-Term Non-Fund Based Limits	135.00	135.00	[ICRA]A (Stable); downgraded from [ICRA]A+ and removed from rating watch with negative implications
Short-Term Fund Based and Non-Fund Based Limits	182.03	182.03	[ICRA]A1; downgraded from [ICRA]A1+ and removed from rating watch with negative implications
Total	**462.03**	**462.03**	

*Instrument details are provided in Annexure-1

Rationale

The revision of ratings takes into account the decline in the profitability and cash accruals of Chowgule and Company Private Limited (CCPL) in FY2019 following the ban-led closure of mining operations in Goa in February 2018. The company's Goa mining operations accounted for 52% of its total revenues (standalone) in FY2018. The loss of revenue from Goa mining along with absorption of certain one-time and recurring fixed costs pertaining to Goa mines has led to erosion of the company's operating profitability thereby weakening its debt coverage metrics and liquidity profile in the last fiscal. Operating losses of Rs. 2.8 crore in FY2019 along with continued support to its subsidiary, Angre Port Private Limited (APPL), has led to a decline in the company's cash balance and liquid investments to Rs. 84.6 crore as of March 31, 2019 from Rs. 184.4 crore as of March 31, 2018. ICRA acknowledges that non-mining businesses of CCPL have a healthy order book and are expected to start contributing significantly from FY2020 to the overall cash flows. However, the actual performance achieved by these businesses, which are in early stages and their ability to generate healthy recurring order flow, remains to be seen.

The ratings, however, draw comfort from CCPL's low-cost mining operations in Karnataka where the company received a ~33% increase in mining allocation limit in late FY2019. CCPL's Karnataka mining operations are generating healthy profits at current iron ore prices. ICRA also notes that the company's other businesses such as shipbuilding and ship repair have been ramping up in the current fiscal on the back of healthy opening order book position. Further, CCPL has restarted its pelletisation operations that had been shut down in 2012 for being unviable at the time. Healthy performance in these non-mining businesses is expected to off-set the impact of halt in the Goa mining operations and lead to an increase in CCPL's scale of operations and profitability in the current fiscal.

The ratings however, take into account the company's vulnerability to volatility in iron ore prices and exchange rates, and susceptibility to any adverse development in the regulatory framework such as changes in government policies regarding increase in royalty rates/export duty or ban on export of fines/lumps. While arriving at the ratings, ICRA has taken note of the debt service reserve account (DSRA) guarantee provided by CCPL[1] for the entire loan tenure of one of its subsidiaries - Angre Port Private Limited (APPL). While the cargo throughput at APPL has increased over the last couple of quarters, it remains low. As a result, cash flow support from CCPL to APPL is expected to continue in the near to medium term. The company has also taken sizeable impairment loss towards its investments in certain group companies holding shipping assets in the last two fiscals; any further impairment loss of sizeable value would be a rating sensitivity.

Key rating drivers

Credit strengths

Strong competitive position in mining – CCPL has a strong position in the mining sector driven by the company's large iron ore reserves in Goa and Karnataka, low-cost operations, and logistical advantage with mines connected to inland waterways. CCPL has mining leases for ten mines at Goa and two mines in Karnataka with ore reserves sufficient for the next 25 years at past production rates.

Long-standing relationship with its key customer – The company has an evergreen contract with Japan-based JFE Holdings Inc. (JFE). CCPL typically sells ~80% of its total production in Goa to JFE guarding the company from uncertainty in demand. The company is mainly selling lower grade ore i.e. less than 58 Fe grade, from Goa since it does not carry any export duty. In the event the mining operations in Goa resume, the company's longstanding relationship with JFE would support healthy ramp up of operations. Further, JFE is the key customer for CCPL's recently restarted palletisation operations.

Expected turnaround in other divisions – The other divisions of CCPL have witnessed a ramp up in operations. The company's shipbuilding division has a firm order book position of ~Rs. 350 crore at present (to be executed within 2-3 years) while its ship repair business (Lavgan Dockyard) has signed contracts with private contractors, rig owners, and the Navy Coast Guard.

Comfortable gearing levels and healthy liquid investments – The company had a comfortable capital structure with gearing of 0.2 time as of March 31, 2019. While the company's cash and cash equivalents balance has declined in FY2019, it remains healthy at Rs. 85 crore as of March 31, 2019.

Credit challenges

Impact on cash flows and profitability from the cancellation of mining leases in Goa – The halt in iron ore mining activity in Goa (w.e.f. March 16, 2018) following the SC order in February 2018 has had an adverse impact on the company's cash flows and profitability. The company reported operating losses of Rs. 2.8 crore in FY2019 due to loss of revenue from Goa operations and absorption of fixed costs pertaining to the Goa mines. However, the company's mining operations in Karnataka and ramp up in non-mining businesses are expected to offset the impact to some extent.

[1] CCPL, Chowgule Industries Private Limited, and Chowgule and Company (Salt) Private Limited have jointly provided the DSRA guarantee on APPL's new term loan

Profits and cash flows vulnerable to volatility in iron ore prices and fluctuations in exchange rates– CCPL's profitability is vulnerable to fluctuations in the international and domestic iron ore prices and deterioration in the iron content of its reserves. Also, majority of CCPL's revenues are denominated in USD or EUR exposing the company's profitability to volatility in exchange rates. However, the company's EUR-denominated imports for its shipbuilding division help in reducing the net forex exposure to some extent.

Mining operations vulnerable to adverse development in regulatory framework –The company's operations remain vulnerable to any adverse development in the regulatory framework for iron ore operations such as changes in the government policies regarding increase in royalty rates/export duty or ban on exports. The company's operations were significantly impacted during the period FY2013-FY2015 due to the ban on mining operations. While the mining activity subsequently resumed, the latest Supreme Court order canceling the licenses for mining iron ore in Goa have once again impacted the operations of the company.

DSRA guarantee provided to APPL - CCPL has provided a guarantee to meet any shortfall in the debt service reserve account (DSRA) for the entire loan tenure of APPL (a direct subsidiary of CCPL after reverse merger of holding company, Chowgule Ports and Infrastructure Limited, with APPL w.e.f. April 1, 2017). CCPL has been providing regular cash support to APPL (~Rs. 13.5 crore in FY2019) since the cargo throughput at the port remains low. However, with APPL refinancing its term loan, the DSRA guarantee is now shared between CCPL and two other group companies - Chowgule Industries Private Limited, and Chowgule and Company (Salt) Private Limited. Further, the cargo throughput at the port has increased over the last couple of quarters leading to an improvement in APPL's financial performance. The same could lower APPL's requirement of cash flow support from CCPL.

Liquidity Position: Adequate

CCPL's liquidity position is **adequate** with healthy cash balances and liquid investments of Rs. 84.6 crore as of March 31, 2019, however, the same has declined from Rs.184.4 crore as of March 31, 2018. The company has repayment obligations of Rs. 97 crore in the period between FY2020 and FY2022. The debt repayment would be met through steady generation of internal accruals. Also, CCPL's support to its subsidiaries is expected to decline going forward. While it would still be required to support its direct subsidiary, APPL, towards debt repayment and payment of interest obligations, APPL's debt servicing obligations have declined owing to the part refinancing of its term loan in March 2019.

Rating Sensitivities

Positive triggers – The ratings could be revised upwards if the Total Debt-to-OPBITDA for CCPL (on a standalone basis) was to fall below 1.5 times and if the ramp up of the non-mining businesses such as shipbuilding, ship repair, and palletisation takes place as anticipated leading to increase in profitability and cash accruals.

Negative triggers – Downward pressure on the ratings could arise if the Total Debt-to-OPBITDA for CCPL (on a standalone basis) was to rise above 2.4 times; in case of higher-than-anticipated funding support to Angre Port Private Limited leading to tightening of CCPL's liquidity position and if the ramp up of the non-mining businesses is slower than anticipated.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Mining Entities
Parent/Group Support	NA
Consolidation / Standalone	For arriving at the ratings, ICRA has considered the standalone financials of Chowgule and Company Private Limited. However, in line with its limited consolidation approach, ICRA has factored in the rated entity's support to its wholly-owned subsidiary, Angre Port Private Limited, for debt servicing and other purposes, if required.

About the company:

Chowgule and Company Private Limited (CCPL) is the flagship company of the Chowgule Group established in 1941 for mining and exports of iron ore in Goa. Over a period, the company has forayed into shipbuilding, manufacturing of material handling equipment, ship repair and has two mining leases in Karnataka. The company also has a 1.8 million tonnes per annum pelletisation plant. CCPL entered the shipping business with the acquisition of a dry bulk carrier in July 2010. The company entered into ship repairs through its step-down subsidiary, Lavgan Dockyard Private Limited, which got merged with CCPL w.e.f. April 1, 2017. CCPL also operates a port at Jaigad through its subsidiary, Angre Port Private Limited.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	428.3	275.6
PAT (Rs. crore)	-83.3	-191.1
OPBDIT/OI (%)	29.9%	-1.0%
RoCE (%)	-5.1%	-11.1%
Total Debt/TNW (times)	0.2	0.2
Total Debt/OPBDIT (times)	2.4	-108.2
Interest coverage (times)	5.2	-0.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

	Instrument	Current Rating (FY2020) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	07-Oct 2019	Chronology of Rating History for the past 3 years: Date & Rating in FY2019 16-Aug 2018	Date & Rating in FY2018 16-Feb 2018	01-June 2017	Date & Rating in FY2017 12-July 2016
1	Term Loan	Long-Term	145.00	67.06	[ICRA]A (Stable)	[ICRA]A+@	[ICRA]A+@	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)
2	Non-Fund Based Limits	Long-Term	135.00	-	[ICRA]A (Stable)	[ICRA]A+@	[ICRA]A+@	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)
3	Fund Based Limits	Short-Term	145.00	-	[ICRA]A1	[ICRA]A1+@	[ICRA]A1+@	[ICRA]A1+	[ICRA]A1+
4	Non-Fund Based Limits	Short-Term	37.03	-	[ICRA]A1	[ICRA]A1+@	[ICRA]A1+@	[ICRA]A1+	[ICRA]A1+

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	July 2015	-	July 2021	145.00	[ICRA]A (Stable)
NA	Long-Term Non-Fund Based Limits	-	-	-	135.00	[ICRA]A (Stable)
NA	Short-Term Non-Fund Based Limits	-	-	-	37.03	[ICRA]A1
NA	Short-Term Fund Based Limits	-	-	-	145.00	[ICRA]A1

Source: Chowgule and Company Private Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Angre Port Private Limited	100.00%	Limited Consolidation

ANALYST CONTACTS

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

Ankit Patel
+91 79 4027 1509
ankit.patel@icraindia.com

Anubha Rustagi
+91 22 6169 3341
anubha.rustagi@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:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

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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) 2556 0194/ 6606 9999