March 16, 2020

The Andhra Petrochemicals Limited: Ratings reaffirmed; outlook revised to Stable from Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based - Term Loans	13.50	13.50	[ICRA]BBB+(Stable); rating reaffirmed and outlook revised to Stable from Positive
Fund-based - Cash Credit	35.00	35.00	[ICRA]BBB+(Stable); rating reaffirmed and outlook revised to Stable from Positive
Long-term Unallocated	43.68	43.68	[ICRA]BBB+(Stable); rating reaffirmed and outlook revised to Stable from Positive
Non-fund Based	2.00	2.00	[ICRA]A2; reaffirmed
Total	**94.18**	**94.18**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in rating outlook from Positive to Stable is on account of the decline in profitability of The Andhra Petrochemicals Limited (APL) in H2 FY2020 due to steep moderation in product – raw material price spread and subdued outlook for recovery in spread in the near term due to global economic slowdown and impact of COVID-19. The company's performance was also impacted by feedstock supply disruption during Q3 FY2020 due to some capex being undertaken by Hindustan Petroleum Corporation Limited (HPCL) and maintenance shutdown undertaken by APL during Q4 FY2020.

The ratings favourably consider APL's sole producer status in the Indian oxo-alcohol market, with it catering to 35-40% of the domestic demand (at normalised production level). ICRA notes the increase in the domestic capacity with Bharat Petroleum Corporation Limited (BPCL) setting up a manufacturing facility for oxo-alcohols. However, given the high domestic demand with a part of incremental production to be used for other downstream use, the impact on APL is expected to be limited. Any additional domestic capacity addition may result in increased competition. Nevertheless, such plans are in incipient stage and not yet firmed up. The ratings factor in the company's healthy capital structure with modest gearing of 0.03 as on December 31, 2019 on the back of scheduled repayments and some prepayments of the outstanding term loans. The capital structure and coverage indicators are expected to remain healthy and witness further improvement over the near to medium term, amid lack of any major debt-funded capacity expansion plans. The rating continues to take comfort from APL being a part of The Andhra Sugars Group and the support received from the parent during times of distress. However, with the improvement in financial performance in the past few fiscals, it has completely repaid the outstanding loans from the Group in FY2019 and the ratings reflect the company's standalone performance.

However, ICRA notes that with lack of integration benefits and APL being a standalone petrochemical producer, its margins remains susceptible to volatility in spreads between oxo-alcohols and feedstock, import duty differentials and foreign exchange rates, leading to volatility and cyclicality of profitability. While the company benefits from trade protection metrics in the form of ADD imposed on several countries for the import of NBA and 2EH, its efforts to increase the coverage has not fructified. Any incremental increase in ADD coverage to other countries for APL's products or substitute products or dioctyl phthalate (DOP)[1] will be a positive development. ICRA notes that dependence on a single supplier (HPCL) for the key raw material, propylene, exposes the company to force majeure risk, as witnessed in the past. Further, any incremental sizeable debt-funded capex may put pressure on its capital structure and coverage indicators and remains a sensitivity factor.

The Stable outlook on the [ICRA]BBB+ rating reflects ICRA's opinion that APL will continue to benefit from its sole producer status in the domestic market, where demand significantly exceeds supply reducing the offtake risk. Its margins may witness pressure in the near term on account of subdued product- feedstock price spreads due to weak global demand. However, the capital structure and coverage indicators are expected to remain healthy.

Key rating drivers and their description

Credit strengths

Sole producer of oxo-alcohols in India; favourable long-term demand outlook for various end-user sectors – APL, the sole producer of oxo-alcohols in India, is operational for more than three decades. The company caters to ~35-40% of the domestic demand when operating at full capacity, while the remaining is met through imports. Its products are mainly used by the domestic manufacturers of DOP, which is used as plasticiser in manufacturing polyvinyl chloride (PVC). The long-term demand potential for PVC in India remains favourable. The market entry of BPCL in FY2020 is expected to have limited impact, given the high domestic demand with a part of the production being used for other downstream use.

Promoted by ASL; around six decades of operating history of Group – APL is a part of the Andhra Sugars Group. The flagship entity, The Andhra Sugars Limited (ASL, rated [ICRA]A+(Positive)/[ICRA]A1+), has around six decades of operating history and a strong credit profile.

Healthy capital structure and coverage indicators – APL's financial profile remains healthy with modest gearing and healthy coverage indicators on the back of modest debt levels. The capital structure and coverage indicators are expected to remain healthy as the outstanding term loans are scheduled to be completely repaid by FY2021 and the company has no major debt-funded capacity expansion plans.

Credit challenges

Standalone petrochemical producer without integration benefits; margins depend on spread between oxo-alcohols and feedstock – APL is a standalone manufacturer without backward-integration benefits. Additionally, the use of naphtha as a feedstock instead of natural gas (used by other international manufacturers) puts the company at a relative cost disadvantage. These shortcomings expose its sales and margin to volatility in global prices (spread between product and feedstock prices), intense competition from imports, changes in duty structure/trade protection measures such as ADD, import pattern of end-user segments and substitute products.

The import of 2EH/NBA moderated post imposition of ADD imposed in March-April 2016, although the benefits reflected with a lag of one year. However, there are several countries that are not covered under ADD, which had

[1] *2-EH and NBA are used in the manufacturing of DOP*

contributed to an increase in imports. Moreover, the increase in direct imports of DOP or substitute products for 2EH and NBA, has an adverse impact on the domestic demand for oxo-alcohols, as the plasticiser manufacturers are the major consumers. Any potential increase in trade protection coverage to additional countries for 2EH and NBA or imposition of ADD on DOP and substitute products should be favourable for the company.

Vulnerable to force majeure risk with high dependence on single feedstock supplier – APL is dependent on a single source, HPCL, for the supply of its 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 primarily regular since FY2016, except a minor disruption in FY2020 due to planned shutdown undertaken by HPCL.

Liquidity position: Adequate

The company's liquidity profile witnessed improvement over the last few years, aided by improvement in revenue and profitability and consequent reduction in debt levels due to scheduled repayments and some prepayments. Although there has been moderation in profit margin in the current fiscal especially in H2 FY2020, the liquidity profile remains **adequate** due to low repayment obligations, modest capex, cash and liquid investments of ~Rs. 27.2 crore (as of December 2019) and unutilised working capital limits. ICRA takes note of financial flexibility enjoyed by the company with lenders due to being a part of the Andhra Sugars Group.

Rating sensitivities

Positive triggers – ICRA could upgrade the company's rating if it exhibits sustained improvement in profitability, while maintaining healthy capital structure, coverage indicators and working capital intensity.

Negative triggers – Negative pressure on the rating could arise if there is sustained decline in profitability, or if any major debt-funded capital expenditure or a stretch in the working capital cycle, weakens liquidity. The ratings may be downgraded if the ROCE is lower than 13% on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Chemical Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	Ratings are based on standalone financial statements

About the company

The Andhra Petrochemicals Limited, promoted by ASL, was incorporated on April 18, 1984. At present, it is the sole producer of oxo-alcohols in India, with a manufacturing capacity of 73,000 tonne per annum (TPA) of oxo-alcohols. The product mix includes 2EH, n-butanol (NBA) and isobutanol (IBA). At present, APL's oxo-alcohol manufacturing capacity caters to ~35-40% of the Indian market, while the remaining comes from imports. Oxo-alcohol is primarily used as a raw material to manufacture PVC plasticisers. It commenced operations from February 1994. APL's factory is located adjacent to HPCL's Visakhapatnam refinery, with which it has entered into a long-term contract for the procurement of propylene, the key raw material in the manufacturing process.

In FY2019, the company reported a net profit of Rs. 69.8 crore on an operating income (OI) of Rs. 665.9 crore, compared to a net profit of Rs. 46.5 crore on an OI of Rs. 518.2 crore in the previous year. In 9M FY2020, on a provisional basis, it reported a net profit of Rs. 27.3 crore on an OI of Rs. 383.2 crore.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	518.2	665.9
PAT (Rs. crore)	46.5	69.8
OPBDIT/OI (%)	13.1%	16.3%
RoCE (%)	25.7%	42.7%
Total Outside Liabilities/Tangible Net Worth (times)	0.6	0.2
Total Debt/OPBDIT (times)	1.0	0.1
Interest Coverage (times)	5.7	18.4
DSCR	1.6	1.8

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Rating (FY2020)					Rating History for the Past 3 Years				
		Type	Amount Rated	Amount Outstanding	Current Rating	Earlier Rating	FY2019	FY2018			FY2017
					16-Mar-2020	3-Jun-2019	7-Sep-2018	29-Dec-2017	1-Sep-2017	11-Jul-2017	14-Apr-2016
1	Term Loans	Long Term	13.50	7.6	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Positive)	[ICRA]BBB (Positive)	[ICRA]BBB- (Stable)	[ICRA]BB (Positive)	[ICRA]BB- (Stable)	[ICRA]BB- (Negative)
2	Fund-based - Cash Credit	Long Term	35.00	NA	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Positive)	[ICRA]BBB (Positive)	[ICRA]BBB- (Stable)	[ICRA]BB (Positive)	[ICRA]BB- (Stable)	[ICRA]BB- (Negative)
3	Unallocated	Long Term	43.68	NA	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Positive)	[ICRA]BBB (Positive)	[ICRA]BBB- (Stable)	[ICRA]BB (Positive)	[ICRA]BB- (Stable)	[ICRA]BB- (Negative)
4	Non-fund Based - LC/BG	Short Term	2.00	NA	[ICRA]A2	[ICRA]A2	[ICRA]A3+	[ICRA]A3	[ICRA]A4+	[ICRA] A4	[ICRA] A4

Amount in Rs. crore

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Consortium Working Capital Term Loans	FY2015^	-	January 2021	13.50	[ICRA]BBB+(Stable)
NA	Long-term Unallocated				43.68	[ICRA]BBB+(Stable)
NA	Cash Credit				35.00	[ICRA]BBB+(Stable)
NA	Non-fund Based				2.00	[ICRA]A2

^Consortium partners sanctioned the loans in FY2015 on different dates, of which the longest tenure loan is maturing on January 2021;
Source: APL

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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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