Rating Rationale

Arjun Chemicals Pvt. Ltd.

2 May 2019

Brickwork Ratings assigns BWR BB-/A4 for the Bank Loan Facilities of Rs. 51.42 Crores of Arjun Chemicals Pvt. Ltd (ACPL or 'the Company')

Particulars

Facility	Amount (Rs. Crs)	Tenure	Rating*
Fund based Fund Based Working Capital Standby Line of Credit Term Loan	23.00 4.00 8.42	**Long Term**	**BWR BB-** (Pronounced as BWR Double B Minus) (Outlook: Stable)
Non Fund Based Letter of Credit Bank Guarantee	15.00 1.00	**Short Term**	**BWR A4** (Pronounced as BWR A Four)
Total	51.42	**Rupees Fifty One Crores and Forty Two Lakhs Only**	

*Please refer to BWR website www.brickworkratings.com/ for definition of the ratings .
Annexure-I provides details of bank loan facilities

Ratings assigned

Rationale/Description of Key Rating Drivers/Rating sensitivities:

BWR has principally relied upon the audited financials of the Company upto FY18, provisionals for 6MFY19, projections for FY19, publicly available information and information/clarifications provided by the management.

The ratings factor the established track record of operations and experience of the promoters in paper sizing chemicals business. However, the ratings are constrained by the significant investments/loans and advances made in loss making group companies (~ Rs.63 Crs as on 31 Mar 2018) and substantial contingent liabilities (mainly corporate guarantees aggregating to ~Rs 69 Crs to group companies), which adversely impact the financial flexibility, cash flows and credit profile of the company. The statutory auditors have made certain comments/qualifications on the inadequate provision made by the company for diminution in value of investments extended to such group companies and the fact that the aggregate exposure to such group/associate companies exceeds 159% of the net worth of the company. The ratings are also constrained by the low profitability, vulnerability of profitability to volatility in raw material prices and forex rates, working capital intensive nature of operations and the intensely competitive and fragmented paper and pulp industry.

Going forward, the company's ability to increase its scale of operations, improve profitability, significantly reduce intra group investments, effectively manage its working capital and strengthen its credit profile shall be the key rating sensitivities.

Key Rating Drivers

Credit Strengths:

Established track record and experience of the promoter in paper sizing chemical industry:
The company has a track record of nearly three decades, having begun its operations in 1990 in the paper chemicals segment. The management team is well experienced and the company has established relationships with its customers and suppliers. ACPL is the flagship company of Chennai based Arjun group, which has diversified product portfolio in the paper industry under different entities such as paper manufacturing, capital goods etc.

Established customer base:
The company's client profile comprises large and mid sized players in the paper manufacturing industry pan India. APCL's sales are well diversified geographically and the company has long-standing relationships with its customers for nearly two decades which ensures repeat business.

Credit Risks:

Subdued financial risk profile: ACPL reported total operating income of Rs. 124.90 Crs and a PAT of Rs. 4.05 Crs in FY18 as against total operating income Rs.124.18 crs and PAT of Rs. 5.20 crs in FY17. Net profit of the company is low and declined in FY18 to Rs 4.05 Crs in FY18 as against Rs 5.20 Crs in FY17. Interest coverage was 1.55 times as on 31 Mar 2018, declined from 2.01 times as on 31 Mar 2017. Gearing was low at 0.84 times as on 31 Mar 2018.

Vulnerability to change in raw material prices and forex rates:
ACPL's margins are primarily affected by fluctuations in sizing and retention chemical prices which are the major raw materials. Further, since a major part of the raw material requirement is met through imports (nearly 81% in FY18), the company is exposed to fluctuations in foreign currency exchange rates. However, the risk is mitigated through derivative contracts.

Significant contingent liabilities and diminution in value of investments extended to group companies:

ACPL has significant contingent liabilities of Rs 68.90 Crs and investment/advances/unsecured loans extended to its group companies of Rs.62.86 crore as on 31 Mar 2018. The two group companies (Arjun Health and Hygiene Pvt Ltd and Arjun Pulp and Paper (India) Pvt Ltd) in which ACPL has major exposure, have significant accumulated losses resulting in erosion of their net worth. The auditors' comments on the erosion in the net worth of these companies, absence of cash flows etc indicate that there are strong possibilities of further erosion in the carrying value of such investments, thus further weakening the credit profile of the company. The statutory auditors have commented that the company has not made any provision for diminution in carrying value of such investments. As such, the company's credit profile is adversely impacted and significant reduction in such exposure remains a key rating sensitivity.

Limited product mix and fragmented paper and pulp industry:

The products portfolio is restricted to sizing chemicals (alkyl ketene dimer and cationic rosin emulsion) and specialty chemicals, which have limited market size. The company's growth is dependent on the growth of paper and pulp industry, which is fragmented and intensely competitive in nature.

Working capital intensive nature of operations:

Working capital intensity is high owing to high inventory and receivable days owing to the nature of business. ACPL has reported inventory of 93 days and receivable days of 101 days as on 31 Mar 2018. High delivery lead time for raw materials due to imports results in high inventory days.

Liquidity - Strained:

The company's liquidity position is tight due to substantial exposure to group companies as investments and loans and advances. The company is significantly dependent on external funding to meet the working capital requirements evident from almost full utilisation of working capital facilities over the last six months. Cash and cash equivalents were low at Rs 3.96 Crs as at March 31 2018. Debt repayments are in the range of Rs.4.00 Crs to Rs.5.00 Crs for FY20, which are expected to be serviced from net cash accruals. Effective recovery of the intergroup investments/loans and advances at the earliest is critical for improving the liquidity and financial profile.

Analytical Approach

For arriving at its ratings, BWR has applied its rating methodology as detailed in the Rating Criteria detailed below (hyperlinks provided at the end of this rationale). The Company does not have any subsidiaries.

Rating Outlook: *Stable*

BWR believes ACPL's business risk profile will be maintained over the medium term. The 'Stable' outlook indicates a low likelihood of rating change over the medium term. The outlook may be revised to Positive in case of significant reduction in exposure to group companies and improvement in operational efficiencies, thereby strengthening the financial risk profile. The outlook may be revised to Negative in case of lower than anticipated performance and/or additional support to group entities and/or any additional debt-funded capital expenditure programme, adversely impacting the financial risk profile.

About the Company

ACPL was incorporated in 1990 at Chennai. The company is engaged in the manufacture and sale of paper chemicals such as Alkyl Ketene Dimer, Cationic Rosin Emulsion and various types of chemicals which are used as sizing chemicals in the paper and pulp industry. The company has three manufacturing facilities located at SIPCOT Industrial Complex Ranipet (Tamil Nadu), Vapi (Gujarat) and Samba (Jammu).

Mr. P Chandrasekar is the Chairman of the company and the Arjun group. Mr. P Vasantha Kumar and Mr. Shashikanth Narayamarao are the directors.

Arjun Pulp and Paper India Private Limited, Arjun Health and Hygiene Private Limited, Arjun Technologies India Limited, S. B. Industrial Engineering Private Limited, E & S Technologies Pvt Ltd, Colonial Trading House Pvt Ltd and Arjun Farm Product (India) Pvt Ltd are the other associate companies which are part of the Arjun Group.

Financial Performance

ACPL reported total operating income of Rs.124.90 Crs and Net Profit of Rs 4.05 Crs in FY18 as against total operating income of Rs.124.18 Crs and Net Profit of Rs. 5.20 Crs in FY17. Tangible net worth was Rs. 63.26 Crores as of March 31, 2018. The company has low gearing of 0.84 times as on March 31 2018. Total Debt was around Rs. 53.00 crs as on 31 Mar 2018.

Key financial indicators are given in Annexure II

Rating History for the last three years

S.No	Facility	Current Rating (April 2019)			Rating History		
		Type	Amount (Rs Crs)	Rating	2018	2017	2016
1	Fund based FBWC SLC Term Loan	Long Term	23.00 4.00 8.42	BWR BB- (Pronounced as BWR Double B Minus) (Outlook: Stable)	-	-	-
2	Non Fund Based LC BG	Short Term	15.00 1.00	BWR A4 (Pronounced as BWR A Four)	-	-	-
	Total		**51.42**	**Rupees Fifty One Crores and Forty Two Lakhs Only**			

Status of non-cooperation with previous CRA (if applicable)- NA

Any other information - NA

Hyperlink/Reference to applicable Criteria

- **General Criteria**
- **Approach to Financial Ratios**
- **Manufacturing Companies**
- **Short Term Debt**

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Arjun Chemicals Pvt Ltd

Annexure I:
Details of Bank Facilities

(in Rs Crs)

Facilities	State Bank of India	Axis Bank	Total
Fund Based Working Capital	23.00	-	23.00
Standby Line of Credit	4.00	-	4.00
Term Loan*	5.08	3.34	8.42
Letter of Credit	15.00	-	15.00
Bank Guarantee	1.00	-	1.00
Total	**48.08**	**3.34**	**51.42**

*Term loan outstanding

Annexure II:
Key Financial Indicators

Key Parameters	Units	31 March 2017	31 March 2018
Result Type		**Audited**	**Audited**
Operating Revenue	Rs Cr	124.18	124.90
EBITDA	Rs Cr	12.36	10.37
PAT	Rs Cr	5.20	4.05
Tangible Net worth	Rs Cr	60.19	63.26
Total Debt/Tangible Net worth	Times	0.72	0.84
Current Ratio	Times	1.31	1.33

For print and digital media
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Note on complexity levels of the rated instrument:
BWR complexity levels are meant for educating investors. The BWR complexity levels are available at www.brickworkratings.com/download/ComplexityLevels.pdf Investors queries can be sent to info@brickworkratings.com.

About Brickwork Ratings

Brickwork Ratings (BWR), a SEBI registered Credit Rating Agency, accredited by RBI and empaneled by NSIC, offers Bank Loan, NCD, Commercial Paper, MSME ratings and grading services. NABARD has empaneled Brickwork for MFI and NGO grading. BWR is accredited by IREDA & the Ministry of New and Renewable Energy (MNRE), Government of India. Brickwork Ratings has Canara Bank, a leading public sector bank, as its promoter and strategic partner.
BWR has its corporate office in Bengaluru and a country-wide presence with its offices in Ahmedabad, Chandigarh, Chennai, Hyderabad, Kolkata, Mumbai and New Delhi along with representatives in 150+ locations.

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