Parsa Kente Collieries Limited

April 03, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long term / Short term Bank Facilities*	385.00	**CARE BBB; Stable / CARE A3+ [Triple B; Outlook: Stable / A Three Plus]**	Reaffirmed*
Total	**385.00 (Rupees Three Hundred and Eighty Five Crore Only)**		

**Reclassification of outstanding long term rating in to long term/short term ratings;*
Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings continue to derive strength from the strong parentage of Parsa Kente Collieries Ltd. [PKCL; being a 74% JV of Adani Enterprises Ltd (AEL; rated CARE A; Stable / CARE A1)], financial support extended by AEL, extensive experience of Adani group in the energy value chain, gradual ramp-up in the scale of mining operations of Parsa East & Kente Basin (PEKB) Coal Block by AEL which also acts as the Mine Developer and Operator (MDO) for the coal block, economically viable source of coal for Rajasthan Rajya Vidyut Utpadan Nigam Ltd. (RVUNL) to whom the coal block is allocated and presence of a pass-through payment mechanism for receipts from RVUNL towards mining fees and reimbursements; with PKCL retaining a fixed 4% of mining fees with itself.

The rating is, however, constrained on account of below average financial risk profile of PKCL's sole counterparty i.e. RVUNL, working capital intensive nature of its operations, moderation in profitability during FY18, leveraged capital structure due to its low capital base and regulatory risk associated with any cancellation of forest clearance granted to RVUNL for Parsa Kente Coal Block with the matter being currently sub-judice.

Ability of PKCL to effectively manage its working capital requirement, timely receipt of payment from RVUNL and stable operations of its power plants for which this coal block is allocated, achievement of envisaged ramp-up of mining operations by AEL along with need based financial support from AEL are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Strong promoter group with diversified business operations

PKCL is a JV company between AEL and RVUNL with AEL holding 74% and RVUNL holding 26% equity. The primary sponsor i.e. AEL is the flagship company of Adani Group. Incorporated in 1993, AEL is being chaired by Mr. Gautam Adani. AEL, on a standalone basis, has mainly coal trading, coal Mine Developer & Operator (MDO) and power trading businesses, whereas, Adani Group as a whole is engaged in diversified areas of businesses and operates in a range of sectors, primarily energy including coal mining, power generation and transmission, port operations, logistics, oil and gas exploration and city gas distribution. Group is also involved in agro-processing & storage and commodities trading.

Economically viable source of coal for RVUNL

As per the terms of contractual arrangement, PKCL has agreed to supply mined coal from the Parsa Kente coal block to RVUNL at a pre-defined rate of mining fees plus transportation cost & taxes at actuals. The rate of mining fees is escalable linked to Wholesale Price Index (WPI) & Consumer Price Index (CPI) on a yearly basis. The rate of mining fees which is currently being charged by PKCL to RVUNL is lower compared to the prevailing price being charged by Coal India Ltd. (CIL) for similar grade of coal. Accordingly, it is the most economical source of coal for generation of power by RVUNL which substantiates the continuation of this business arrangement for a reasonably long period of time.

Presence of a pass-through payment mechanism for receipts from RVUNL

Since the coal block is now operational, PKCL's current role is to primarily facilitate the payment flow from RVUNL to all involved parties and manage the payment receipt risk from RVUNL. PKCL recognizes only the mining fees as its total operating income whereas the entire charges receivable from RVUNL (including Railway freight, Road freight along with Duties & Taxes) is accounted as receivables in its books. Also, the payables of PKCL comprises of payments to be made to AEL viz. Railway freight and 96% of the total Mining fees (as PKCL retains a fixed 4% of the total mining fees with itself as its income for services rendered by it). Hence, the operations of PKCL are largely in the form of a facilitator. For any delay in receipt of payment from RVUNL, it has flexibility of delaying payment to AEL.

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[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

Ramp-up of mining operations at PEKB Coal Block by AEL as per the Coal Mining Services Agreement (CMSA) during 9MFY19

The revenue of PKCL is dependent on successful ramp-up of the coal mining operations at Parsa Kente Coal Block by AEL. Total quantity of coal mined during FY17 and FY18 was lower at 7.33 MMT and 7.05 MMT as against the minimum required coal mining quantity of 8.65 MMT and 10.50 MMT respectively primarily due to transportation bottlenecks wherein there was delay in completion of one stretch of 37 km railway corridor from the mines to the nearest rail-head by another Adani group company. However, as per company management, the said rail corridor was completed by end FY18 which has consequently resulted in growth in coal dispatch volume to 8.44 MMT during 9MFY19 which is in line with the annual committed volume of FY19.

As per Coal Mining and Delivery Agreement (CMDA), PKCL was required to supply certain minimum quantity of coal every year to RVUNL's plant. However, because of delay in completion of the stretch of railway line, RVUNL floated tender for road transportation of coal for this stretch and the same was facilitated by PKCL. Consequently, till March 2018 no penalty on account of any short supply has been levied by RVUNL on PKCL. Going forward, achievement of minimum required coal supply to RVUNL and RVUNL's future stance on any short supply of coal shall be a key monitorable.

Key Rating Weaknesses

Leveraged capital structure primarily due to its nature of business

As per the arrangement, PKCL passes on all the payments received from RVUNL except 4% of the mining fees, with which it services its interest obligations. Accordingly, build-up of its net-worth is very minimal. Also, till FY15, PKCL was fully passing on the delayed payment charges received from RVUNL to AEL since it had no working capital limit sanctioned initially. However, subsequently, PKCL has availed working capital limit of Rs.100 crore during FY16 to make timely payment to AEL. In order to meet its increasing working capital requirement and timely payment to AEL, PKCL has enhanced its working capital limit to Rs.185 crore from banks as on March 31, 2017. With the ramp up in the scale of mining operations upon completion of the railway corridor, PKCL has further enhanced its working capital limits by Rs.200 crore thereby taking its total sanctioned working capital limits to Rs.385 crore as on March 31, 2018.

As on March 31, 2018, PKCL had outstanding unsecured loan of Rs.80.34 crore [PY: Rs.151.29 crore] from group companies out of which Rs.60 crore is subordinated to its bank borrowings and are considered as 'quasi equity' (as per sanction stipulation of bank). Capital structure of PKCL, though improved as of end-FY18 mainly upon repayment of USL, has remained weak with overall gearing recorded at 2.03 times as on March 31, 2018. However, upon availment of higher working capital limits & rise in un-subordinated loans from AEL, its overall gearing has again moderated as on December 31, 2018.

Below average credit risk profile of the counterparty

Parsa Kente Coal Block has been allocated to RVUNL to meet the coal requirements of its thermal power stations in Rajasthan viz. Chhabra Phase II and Kalisindh. RVUNL, the only counter-party for PKCL, has a below average credit risk profile. Financial risk profile of RVUNL had weakened during FY15 and FY16 upon disallowance of some cost by Rajasthan Electricity Regulatory Commission (RERC), however it has shown improvement in FY17 and has continued to improve in FY18 also with PAT margin of 6.09% [PY:2.41%] and interest coverage of 1.70 times [PY:1.65 times] during FY18. RVUNL, being a Government of Rajasthan (GoR) entity, has not defaulted in its payments to AEL till now; although payments have been received with delay beyond normal credit period. However, RVUNL is liable to pay delayed payment charges as per the terms of the agreement. RVUNL has paid PKCL a sum of Rs. 33 crore as delayed payment charges during FY18 as compared to Rs.53 crore during FY17.

Moderation in profitability during FY18

PKCL has recorded total operating income of Rs.842.91 crore during FY18 [P.Y:Rs.768.55 crore] primarily driven by increase in coal mining fees. On the other hand volume of coal mining dispatch to RVUNL witnessed a decline due to non-availability of railway line for partial stretch and bad road conditions for surface transportation.

Profitability has declined with PBILDT and PAT margin at 3.35% and 0.29% respectively during FY18 compared to 4.72% and 0.80% respectively in FY17 due to lower volume of coal dispatch, write-off of prior period income of Rs.5.70 crore after the adverse order of Hon'ble High Court of Rajasthan dated Feb 28, 2018 w.r.to escalation benefits for disputed base price of coal for the period of FY14 to FY17 and higher legal and professional expenses of Rs.3.00 crore towards the proceedings of the court in this matter.

Regulatory risk associated with any cancellation of forest clearance of Parsa Kente Coal Block in the future

An appeal had been filed before the National Green Tribunal (NGT), New Delhi against grant of forest clearance to RVUNL in respect of Para East and Kente Basin Coal block. NGT vide its order had passed direction for setting aside of forest clearance, remanding back the case to Ministry of Environment and Forests (MoEF) and directed stoppage of work at the mine site. Against the above order of NGT, RVUNL has filed appeal before H'ble Supreme Court of India which has given stay over the order of NGT. Appeal filed by RVUNL before the H'ble Supreme Court of India is pending for adjudication. Any adverse outcome w.r.to cancellation of environment clearance for the block may result in disruption of operations.

However, as per terms of Coal Mining and Delivery Agreement (CMDA), PKCL shall be entitled to recover the capital cost incurred for the block from RVUNL in case of cancellation of the block.

Liquidity analysis

As per its business model, PKCL is required to make upfront payment towards reimbursable expenditure whereas it receives the same from RVUNL with some time lag which essentially leads to working capital intensive nature of its operations and with increasing scale of its operations, its working capital intensity is also increasing. Accordingly, PKCL has got its working capital limits enhanced from Rs.185 crore to Rs.385 crore to take care of any delay in payment by RVUNL. Average utilisation of its fund based working capital limit stood high at ~85% during the trailing 12 months ended January 2019. Although, during FY18, PKCL's operating cycle improved to 61 days from 85 days during FY17 on the back of better payment track record from RVUNL, however, performance in 9MFY19 suggests elongation of operating cycle due to delay in payment from RVUNL. Going forward, with the expected growth in its scale of operations, its working capital requirement is also expected to increase. Accordingly, payment track record from RVUNL would be one of the key rating monitorable.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology – Service Sector Companies
Financial ratios – Non-Financial Sector
Rating Methodology: Factoring Linkages in Ratings

About the Company

The Parsa East and Kente Basin coal blocks in Chhattisgarh (Parsa Kente Coal Block) is allocated by the Ministry of Coal (MoC), Government of India (GoI) to Rajasthan Rajya Vidyut Utpadan Nigam Ltd. (RVUNL) to mainly meet the coal requirement of RVUNL's thermal power plants viz. Chhabra Phase II (500 MW) and Kalisindh (2x600 MW) in Rajasthan. In May 2006, RVUNL had issued a tender to appoint a Joint Venture (JV) partner for development and operation of the coal block, transportation and delivery of the coal to its thermal power stations, through a competitive bidding process. The selection of the successful bidder by RVUNL for development and operation of Parsa Kente Coal Block was based on the quoted price of coal for the first year of mining operations. Based on the quotes received from Adani Enterprises Ltd (AEL) it was awarded the contract by RVUNL.

Subsequently, in accordance with the terms of the bid, Parsa Kente Collieries Ltd. (PKCL) was incorporated on October 16, 2007 as a JV Company between AEL and RVUNL with AEL holding 74% and RVUNL holding 26% equity. The primary objective of PKCL is to manage the mine development and operations of the Parsa Kente Coal Block and delivery of coal to RVUNL's thermal power stations. Subsequently, in July 2008, PKCL entered into a Coal Mining and Delivery Agreement (CMDA) with RVUNL for a period of 30 years. In July 2009, PKCL sub-contracted the Mine Development and Operation (MDO) work to the erstwhile Adani Mining Private Limited (AMPL, which used to be a 100% subsidiary of AEL, however subsequently it was merged with AEL during the business restructuring of the Adani Group w. e. f. April 01, 2015) by way of entering into a Coal Mining Services Agreement (CMSA) for development and operation of Parsa Kente Coal Block and supply of coal to the designated thermal power plants of RVUNL for a period of 30 years, in accordance with the terms of the CMDA. AEL commenced mining operations in FY13 and coal mining volumes are gradually improving.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	768.55	842.91
PBILDT	36.27	28.23
PAT	6.15	2.41
Overall gearing (times)	3.52	2.03
Interest coverage (times)	1.37	1.45

A: Audited

As per 9MFY19 (Prov.) results, PKCL has reported a TOI of Rs.1,063.95 crore with a PBT of Rs.19.65 crore.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

***Note on complexity levels of the rated instrument:** CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Analyst Contact:
Name: Hardik Shah
Tel: 079 – 40265620
Mobile: +91-9898802101
Email: hardik.shah@careratings.com

For detailed Rationale Report and subscription information, please contact us at www.careratings.com

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Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based/Non-fund-based-LT/ST	NA	NA	NA	385.00	CARE BBB; Stable / CARE A3+

NA: Not Applicable

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Working Capital Limits	LT	-	-	1)Withdrawn (26-Apr-18)	1)CARE BBB (29-Nov-17)	1)CARE BBB (12-Aug-16)	-
2.	Fund-based/Non-fund-based-LT/ST	LT/ST	385.00	CARE BBB; Stable / CARE A3+	1)CARE BBB; Stable (06-Dec-18) 2)CARE BBB; Stable (26-Apr-18)	1)CARE BBB (29-Nov-17)	1)CARE BBB (12-Aug-16)	-
3.	Fund-based - LT-Working Capital Demand loan	-	-	-	-	1)Withdrawn (29-Nov-17)	1)CARE BBB (12-Aug-16)	-

CONTACT

Head Office Mumbai

Ms. Meenal Sikchi
Cell: + 91 98190 09839
E-mail: meenal.sikchi@careratings.com

Mr. Ankur Sachdeva
Cell: + 91 98196 98985
E-mail: ankur.sachdeva@careratings.com

Ms. Rashmi Narvankar
Cell: + 91 99675 70636
E-mail: rashmi.narvankar@careratings.com

Mr. Saikat Roy
Cell: + 91 98209 98779
E-mail: saikat.roy@careratings.com

CARE Ratings Limited

(Formerly known as Credit Analysis & Research Ltd.)

Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Tel: +91-22-6754 3456 | Fax: +91-22-6754 3457 | E-mail: care@careratings.com

AHMEDABAD
Mr. Deepak Prajapati
32, Titanium, Prahaladnagar Corporate Road,
Satellite, Ahmedabad - 380 015
Cell: +91-9099028864
Tel: +91-79-4026 5656
E-mail: deepak.prajapati@careratings.com

BENGALURU
Mr. V Pradeep Kumar
Unit No. 1101-1102, 11th Floor, Prestige Meridian II,
No. 30, M.G. Road, Bangalore - 560 001.
Cell: +91 98407 54521
Tel: +91-80-4115 0445, 4165 4529
Email: pradeep.kumar@careratings.com

CHANDIGARH
Mr. Anand Jha
SCF No. 54-55,
First Floor, Phase 11,
Sector 65, Mohali - 160062
Chandigarh
Cell: +91 85111-53511/99251-42264
Tel: +91- 0172-490-4000/01
Email: anand.jha@careratings.com

CHENNAI
Mr. V Pradeep Kumar
Unit No. O-509/C, Spencer Plaza, 5th Floor,
No. 769, Anna Salai, Chennai - 600 002.
Cell: +91 98407 54521
Tel: +91-44-2849 7812 / 0811
Email: pradeep.kumar@careratings.com

COIMBATORE
Mr. V Pradeep Kumar
T-3, 3rd Floor, Manchester Square
Puliakulam Road, Coimbatore - 641 037.
Tel: +91-422-4332399 / 4502399
Email: pradeep.kumar@careratings.com

HYDERABAD
Mr. Ramesh Bob
401, Ashoka Scintilla, 3-6-502, Himayat Nagar,
Hyderabad - 500 029.
Cell : + 91 90520 00521
Tel: +91-40-4010 2030
E-mail: ramesh.bob@careratings.com

JAIPUR
Mr. Nikhil Soni
304, Pashupati Akshat Heights, Plot No. D-91,
Madho Singh Road, Near Collectorate Circle,
Bani Park, Jaipur - 302 016.
Cell: +91 – 95490 33222
Tel: +91-141-402 0213 / 14
E-mail: nikhil.soni@careratings.com

KOLKATA
Ms. Priti Agarwal
3rd Floor, Prasad Chambers, (Shagun Mall Bldg.)
10A, Shakespeare Sarani, Kolkata - 700 071.
Cell: +91-98319 67110
Tel: +91-33- 4018 1600
E-mail: priti.agarwal@careratings.com

NEW DELHI
Ms. Swati Agrawal
13th Floor, E-1 Block, Videocon Tower,
Jhandewalan Extension, New Delhi - 110 055.
Cell: +91-98117 45677
Tel: +91-11-4533 3200
E-mail: swati.agrawal@careratings.com

PUNE
Mr.Pratim Banerjee
9th Floor, Pride Kumar Senate,
Plot No. 970, Bhamburda, Senapati Bapat Road,
Shivaji Nagar, Pune - 411 015.
Cell: +91-98361 07331
Tel: +91-20- 4000 9000
E-mail: pratim.banerjee@careratings.com

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