ICRA

March 25, 2022

Deepak Nitrite Limited: Ratings reaffirmed to [ICRA]AA(Positive)/[ICRA]A1+ ; outlook revised to Positive from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Term Loan	150.00	-	-
Long-term Fund-based Limits	300.00	300.00	[ICRA]AA(Positive); reaffirmed; outlook revised to Positive from Stable
Short Term Non-fund Based Limits	170.00	170.00	[ICRA]A1+; reaffirmed
Long/Short Term Fund-based and Non-fund Based Limits	200.00	20.00	[ICRA]AA(Positive)/[CRA]A1+; reaffirmed; outlook revised to Positive from Stable
Long-term/Short Term Unallocated Limits	127.00	-	-
Short -term – Commercial Paper	200.00	200.00	[ICRA]A1+; reaffirmed
Total	**1,147.00**	**690.00**	

**Instrument details are provided in Annexure-1*

Rationale

While arriving at the ratings, ICRA has taken a consolidated view of Deepak Nitrite Limited (DNL) and its subsidiary Deepak Phenolics Limited (DPL) due to their managerial, operational and financial linkages.

The reaffirmation of the ratings considers the continued improvement in the consolidated financial profile of the company in FY2021 and 9M FY2022 despite Covid-19-led disruptions, supported by a healthy performance in basic intermediates, performance products and the phenolics segment (under DPL), although the fines and specialty segment witnessed some margin contraction due to higher raw material prices. ICRA also notes that the consolidated entity continued to witness reduction in debt to ~Rs. 292.7 crore as on December 31, 2021 compared with Rs. 577.5 crore as on March 31, 2021, driven by prepayments, leading to healthy improvement in capital structure and coverage indicators.

The revision in the outlook from Stable to Positive reflects ICRA's expectation that the consolidated entity's credit profile will continue to benefit from improvement in financial performance in the near to medium term, aided by some of the initiatives taken to save costs and completion of capacity expansion of products like iso propyl alcohol (IPA).

The ratings continue to take into account the long operating track record of the company in the chemical industry, its diversified product mix and exposure to diversified end-user industries. ICRA notes the company's leading market position in most of its product segments across domestic and global markets. The ratings also continue to factor in DNL's multi-purpose manufacturing facility with significant backward and forward integration linkages that provide flexibility in the product mix to suit changing market requirements. ICRA also notes DNL's technical expertise to handle complex and hazardous chemical processes like nitration, hydrogenation and diazotisation.

The ratings are, however, constrained by the exposure of the company's profitability to the volatility in raw material prices, though the same is reduced in certain products through formula-linked price contracts. The rating is also constrained by the high dependence of DPL's profitability on the volatile crack-spreads, which in turn is linked to the volatility in the price of feedstock and finished products. The ratings also factor in execution and market risks associated with a capex of Rs. 1,400-1,450 crore to be incurred over FY2022-FY2024 towards capacity expansion of some existing products, new product addition and backward integration and cost saving measures. ICRA also notes that the company may raise ~Rs. 2,000 crore through a QIP, although the plans are in an incipient stage and the quantum of the fund raise and its use is not yet finalised. The development on this front remains a key monitorable.

Key rating drivers and their description

Credit strengths

Long operating history and established position in global chemical intermediates industry - DNL has been operating in the chemical industry for nearly five decades. Over the years, the company has become a market leader in the domestic market for inorganic intermediates (sodium nitrite and sodium nitrate), nitro toluenes and fuel additives. It is also among the top three global players for xylidines, cumidines and oximes. DPL, a 100% subsidiary of DNL, commissioned its phenol and acetone plant in November 2018, and since the commissioning of its IPA plant in April 2020, DPL has witnessed significant improvement in scale and profitability. Further, with the brownfield expansion of IPA getting commissioned in December 2021, the total capacity of IPA has been doubled. The domestic demand for phenol and acetone far exceeds domestic production currently. Moreover, with limited domestic competition, DPL has been able to garner a significant market share in the domestic market

Diversified product profile mitigates cyclicality risks in different segments - While the company started with a limited portfolio of low-value bulk chemicals, it has grown its product portfolio to include high-value speciality chemicals for multiple end-user applications. Currently, it has a product portfolio of over 100 products (including its derivatives). The company has also added pharma intermediaries and more agro-chemical products to its portfolio over the years. The regular introduction of new products has helped DNL to mitigate the cyclicality risk related to a particular product segment.

Multi-purpose manufacturing facility, with significant backward and forward integration linkages - The company's production facilities include processes that allow vertical integration for most products, leading to significant cost savings. Also, its facilities are designed to provide flexibility to change the product mix to suit the market requirements.

Healthy improvement in financial profile – DNL, on a consolidated basis, reported a significant growth in revenue and operating profitability in FY2021 at Rs. 4,361.3 crore (P.Y. Rs. 4,229.7 crore) and 28.7% (P.Y. 24.5%), respectively, driven by a solid growth trajectory in phenolics followed by an improvement in the FNS segment which mitigated the decreased volumes in other segments. While the average realisations from performance products declined in FY2021, the impact was partly mitigated by higher margins in the FNS and phenolics segments. In 9M FY2022, on a consolidated basis, DNL's operating income grew to Rs. 4,929.8 crore, driven by the phenolics segment and higher realisations. With healthy cash accruals, the company has reduced its debt levels by pre-paying ~Rs. 287 crore debt at DPL in 9M FY2022. As a result, the total debt/OPBITDA improved to less than 0.2 times in 9M FY2022 from 0.5 times in FY2021.

Healthy ramp-up of phenolics and IPA operations at DPL– DPL's phenol-acetone plant showed a capacity utilisation of over 125% in 9M FY2022 despite the second wave of the pandemic in Q1 FY2022, resulting in healthy revenue and cash flow generation for DNL on a consolidated basis. Also, since the operationalisation of its IPA plant in April 2020, DPL has been able to reap the benefits from the sharp increase in demand for IPA during the pandemic. With IPA 2 getting commissioned in December 2021, the total capacity of IPA has been doubled to 60,000 MTPA. With timely commissioning, DPL has been able to sell its products in the domestic and global markets while generating healthy cash flows.

Credit challenges

Profitability exposed to volatility in raw material prices; formula-linked price contracts mitigate risk in some segments - Prices of a few of the company's key products are linked to the movement of crude oil prices. The change in price levels, however, varies across product categories and is not commensurate with the change in crude price due to formula-linked pricing. Also, the prices of certain key products, such as sodium nitrite, TFMAP, OBA and DASDA, which formed about 45% of DNL's standalone sales in FY2021 in 9M FY2022 are delinked from the movement in crude oil prices. Under the phenolics segment, the prices of phenol and acetone are cyclical and volatile and the profitability of the project is exposed to the movement in crack spreads between the final products and the feedstock. The movements in the spread are partly governed by crude oil prices and partly by the global demand-supply balance of phenol and acetone.

Capex planned over the near to medium term - On a consolidated basis, the company incurred ~Rs. 200-crore capex in FY2021 to add new products and expand the capacity of existing products. The company, on a consolidated basis, now has a capex of Rs. 1,400-1,450 crore to be incurred over FY2022-FY2024 towards expansion projects across all segments and addition of downstream products in the phenolics segment. Such sizeable capex plans expose the company to execution and market risks, although this is mitigated to some extent by the track record of the company in completing its past projects, including the phenol-acetone project under DPL. Additionally, the company may raise ~Rs. ,2000 crore through a QIP, although the plans are in incipient stage and the quantum of fund raise and its use is not yet finalised. The development on this front remains a key monitorable.

Liquidity position: Strong

At a consolidated level, DNL's liquidity position remains strong with healthy annual fund flow from operations at Rs. 933.5 crore in FY2021 and Rs. 902.3 crore in 9MFY2022. The Group's surplus free cash and liquid investments were at ~Rs. 200.1 crore as on December 31, 2021. DNL also has a sanctioned fund-based working capital facility of Rs. 320 crore as on December 31, 2021 at a standalone level, the average utilisation of which remained negligible over the past 12 months. DPL also has a sanctioned interchangeable working capital limit of Rs. 480 crore as on December 31, 2021, the average utilisation of which was 47% in the form of non-fund based limits over the past 12 months. The liquidity position is supported by healthy pre-payment of the term loans during 9M FY2022 which reduces the future repayment obligations of the consolidated entity (Rs. 287.6 crore outstanding as on December 31, 2021). DNL, on a consolidated basis, has repayment obligations of Rs. 67.2 crore in FY2023.

Rating sensitivities

Positive factors – The ratings can be upgraded if the company is able to sustain healthy revenue growth and profit margins on a consolidated basis, backed by a change in the product mix towards more value-added products.

Negative factors – Downward pressure on the ratings may arise if the company faces significant decline in its consolidated revenue and profitability on a sustained basis, or undertakes higher-than-expected debt-funded capex that will weaken its credit profile. A specific credit metric that could lead to a rating downgrade is total net debt/OPBITDA >1 on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Chemical Industry Consolidation and Rating Approach
Parent/Group Support	Not Applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has taken a consolidated view of Deepak Nitrite Limited (DNL) and its subsidiary Deepak Phenolics Limited (DPL). As on December 31, 2021, the company had three wholly-owned subsidiaries that are enlisted in Annexure-2.

About the company

DNL is the flagship of the Deepak Group, which was incorporated in 1970 by Mr. C.K. Mehta. It began as a fully indigenous sodium nitrite and sodium nitrate manufacturer, before gradually widening its product portfolio over the years. At present, DNL has a leading market position in most of its products in the domestic and global markets. DNL has a portfolio of over 100 products, broadly divided into three segments— Basic Intermediates, Fine & Specialty Chemicals and Performance Products The company has five manufacturing facilities, one each at Nandesari and Dahej in Gujarat, Taloja and Roha in Maharashtra, and in Hyderabad in Telangana. DNL also has a research and development facility at Nandesari in Gujarat. The company's growth has also been aided by strategic acquisitions of companies with complementary product lines. In November 2018, the company commissioned its phenol and acetone manufacturing plant at Dahej under its wholly-owned subsidiary, DPL.

In FY2021, DNL, on a consolidated basis, reported a net profit of Rs. 775.8 crore on an operating income of Rs. 4,361.3 crore compared with a net profit of Rs. 611.0 crore on an operating income of Rs. 4,229.7 crore in FY2020.

Key financial indicators (audited)

DNL Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	4229.7	4361.3
PAT (Rs. crore)	611.0	775.8
OPBDIT/OI (%)	24.5%	28.7%
PAT/OI (%)	14.4%	17.8%
Total Outside Liabilities/Tangible Net Worth (times)	1.0	0.5
Total Debt/OPBDIT (times)	1.1	0.5
Interest Coverage (times)	8.8	16.2

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on Feb 29, 2022 (Rs. crore)	Date & Rating on	Date & Rating in FY2021		Date & Rating in FY2020	Date & Rating in FY2019	
					March 25, 2022	March 26, 2021	Jun 17, 2020	Aug 22, 2019	Mar 18, 2019	Oct 1, 2018
1	Term Loans	Long-term	-	-	-	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)
2	Fund based limits	Long-term	300.00	-	[ICRA]AA (Positive)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)	[ICRA]A+ (Positive)	[ICRA]A+ (Stable)
3	Non-fund based limits	Short term	170.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Fund and non-fund based limits	Long term/ Short term	20.00	-	[ICRA]AA (Positive)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA- (Positive)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+	[ICRA]A+ (Stable)/ [ICRA]A1+
5	Unallocated limits	Long term/ Short term	-	-	-	[ICRA]AA (Stable)/ [ICRA]A1+	-	-		

6	Commercial papers	Short term	200.00	-	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**	**[ICRA]A1+**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based Limits	Simple
Short Term Non-fund Based Limits	Very Simple
Long/Short Term Fund-based and Non-fund Based Limits	Simple/Very Simple
Short -term – Commercial Paper	Very Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No.	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (RS Crore)	Current Rating and Outlook
NA	Fund based limits	NA	NA	-	300.00	[ICRA]AA(Positive)
NA	Non-fund based limits	NA	NA	-	170.00	[ICRA]A1+
NA	Fund and non-fund based limits	NA	NA	-	20.00	[ICRA]AA(Positive)/[ICRA]A1+
Unplaced	Commercial paper	NA	NA	7-365 days	200.00	[ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	DNL Ownership	Consolidation Approach
Deepak Nitrite Limited	100.00% (rated entity)	Full Consolidation
Deepak Phenolics Limited	100.0%	Full Consolidation
Deepak Nitrite Corporation Inc., USA	100.0%	Full Consolidation
Deepak Chem Tech Limited	100.0%	Full Consolidation

Source: *DNL Annual report*

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About ICRA Limited:

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