June 28, 2019

DCM Shriram Limited: Ratings reaffirmed; Outlook revised to Positive , Rated amount enhanced

Summary of rating action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	179.29	616.78	[ICRA]AA reaffirmed; Outlook revised to Positive from Stable
Fund based Limits	870.00	1120.00	[ICRA]AA reaffirmed; Outlook revised to Positive
Non-fund-based Limits	686.00	800.00	[ICRA]A1+ reaffirmed
Commercial Paper	800.00	800.00	[ICRA]A1+ reaffirmed
Fixed Deposit Programme	40.00	40.00	MAA+ reaffirmed; Outlook revised to Positive from Stable
Unallocated	449.71	0.00	-
Total	**3025.00**	**3376.78**	

*Instrument details are provided in Annexure-1

Rationale

The revision in the outlook factors in the healthy ramp up in the capacity utilisation of expanded caustic soda capacity at Kota in FY2019, the successful commissioning and ramp up of the 332 TPD caustic soda capacity at Bharuch in April 2019, robust profitability of the chlor-alkali segment, forward integration in the sugar segment with the successful ramp up of the 150 kld distillery commissioned in January 2018, strong financial risk profile characterised by comfortable coverage and capitalisation indicators (Total debt/OPBDITA of 1.2 times as of March 31, 2019 and interest coverage of 11.8 times for FY2019) and robust liquidity position of the company. The ratings continue to factor in the diversified business profile of the company, high operating efficiency of the chlor-alkali division and low-cost coal-based captive power generation facilities at the Kota (Rajasthan) and Bharuch (Gujarat) plants. Despite undertaking large capex, the liquidity position of the company continues to remain robust owing to healthy cash accruals generated by the chlor-alkali division resulting in large un-utilised bank limits and healthy cash balance at the end of FY2019.

The ratings, however, are constrained by the cyclical nature of sugar, chlor-alkali and poly-vinyl chloride (PVC) businesses, sensitivity of chemicals and PVC businesses' profitability to exchange fluctuations and import duty levels. The ratings also factor in the weak profitability from sugar sales being witnessed since Q4 FY2018 which is expected to continue in FY2020. However, with the forward integration into production of ethanol owing to the successful ramp-up of 150kld distillery and setting up of the co-gen power plant, the company has been able to mitigate the cyclicality of the sugar business to some extent. Going forward, the setting up of another 200 kld distillery, the commissioning of which is scheduled for Q3 FY2020 is expected to further reduce the volatility in the profitability of the sugar segment. The ratings also take into consideration the vulnerability of profitability of the fertiliser and farm solutions divisions to regulatory policies and delays in subsidy receipts and agro-climatic risks. The bioseed division is working capital intensive and research intensive, apart from its exposure to agro-climatic risks. The ratings also factor in the project execution risks for the significant capex (~Rs.1642 crore in FY2020 and FY2021) being undertaken by the company for setting up a 200 kld distillery at Ajbapur (UP), caustic soda capacity expansion by 700TPD at Bharuch, PVC capacity expansion at Kota by 40 TPD, a 66MW power plant at Kota and a 120 MW captive power plant at Bharuch. The coverage and capitalisation indicators of the company are expected to remain healthy despite large capex owing to healthy cash accruals from the caustic soda segment and the sale of ethanol produced by the existing 150 kld and the upcoming 200 kld distillery. Any large debt-funded capex plans leading to material deterioration in capitalisation and credit metrics would be a key rating sensitivity. Besides, material fall in the profitability of the sugar and/or the caustic soda segments will also remain key rating sensitivities.

Outlook: Positive

ICRA expects the scale and profits to improve going forward as the company expands is caustic soda and distillery capacity. With a positive outlook for the caustic soda segment and focus of GoI on the Ethanol blending program, DCM should witness improvement in cash generation going forward. With healthy cash generation expected, ICRA believes the credit profile of the entity will improve going forward.

The outlook may be revised to Stable if the performance of the caustic soda segment and/or sugar segment is weaker than ICRA's expectations. If there are significant cost/time over run in the current capex program and/or any large debt funded capex that would lead to material deterioration of the credit metrics of the company the outlook could be revised to Stable

Key rating drivers

Credit strengths

Diversified business profile with benefits derived from integration: DCM Shriram has a diversified business profile with presence across chlor-alkali, PVC, sugar, urea, agri-inputs like Bioseeds, agro-chemical trading, fenesta and cement segment. DCM Shriram has two plants located at Kota (Rajasthan) and Bharuch (Gujarat) with both plants having access to low cost coal-based power through captive power plants. The Kota plant is an integrated facility manufacturing caustic soda, chlorine, PVC, cement and urea. The integrated nature of operation ensures company's competitiveness in the chemicals and the PVC segment. It also allows the company to decide on the basket of products to be produced resulting in maximisation of earnings per unit of power produced.

High operating efficiency of chlor-alkali division and low-cost coal-based captive power generation facility at Kota (Rajasthan) and Bharuch (Gujarat) plants: DCM's chlor-alkali operations at Kota (498 TPD) and Bharuch (1343 TPD) are supported by 209 MW coal based captive power capacity. The production of caustic soda is an energy intensive process and DCM's access to low cost power favourably impacts its costs structure and thus results in healthy profitability from the segment.

Healthy cash accruals from chloro-vinyl division due to higher volumes post expansion and rise in caustic soda and chlorine prices: DCM has undertaken successive capacity expansions in the caustic soda segment over the last couple of years. In FY2019, DCM expanded the caustic soda capacity at Kota by 168 TPD and in April 2019 at Bharuch by 332 TPD taking the total caustic soda capacity to 1841 TPD. The capacity ramp up of the expanded capacities has been healthy leading to healthy growth in cash accruals from the segment. Caustic soda volumes witnessed 9% YoY growth in FY2019 and the PBIT of the segment increased to Rs. 910.4 crore in FY2019 as against Rs. 723.7 crore in FY2018. ECU realisations have remained healthy for the company driven by firm caustic soda prices and positive chlorine prices. With India replacing China for a part of the supplies of chlorine derivatives, domestic chlorine prices have remained reasonable providing tailwinds to the overall profitability.

Setting up of 150 kld distillery and another 200 kld distillery going forward to mitigate the cyclicality of sugar segment: DCM Shriram commissioned a 150 kld distillery in January 2018 at its Hariawan sugar facility and the sales of ethanol commenced in April 2018. The distillery has witnessed healthy rampup during FY2019 and provided significant support to the performance of the sugar segment. The company is in the process of setting up another 200kld distillery at Ajbapur (UP), which is expected to be commissioned in Q3 FY2020. The distillery operations will provide stability to the earnings of the sugar segment which remains vulnerable to the volatility in the sugar prices and to cane pricing. Company had also commissioned a 30 MW co-gen power plant at Hariawan facility. Profitability from the power sales will also mitigate the volatility in the earnings of the sugar segment to some extent.

Robust capital structure and liquidity driven by healthy cash accruals and large unutilised bank limits: The capital structure of the company has remained robust, characterised by low gearing and leverage, healthy interest coverage and liquidity resulting from large unutilised bank limits despite undertaking significant capex. Owing to the significant capex and an increase in the working capital requirements for the sugar and urea segment, the overall debt levels witnessed an increase by the end of FY2019. The total debt increased to Rs. 1,610.1 crore at the end of FY2019 vis-à-vis Rs. 755.6 crore at the end of FY2018. The gearing of the company increased to 0.5x at the end of FY2019 vis-à-vis 0.2x at the end of FY2018. The Total Debt/OPBDITA increased to 1.2x in FY2019 from 0.7x in FY2018. Interest coverage ratio moderated to 11.8x in FY2019 from 12.6x in FY2018 owing to an increase in the interest outgo during the year. Though the credit metrics have moderated in FY2019, they continue to remain robust.

Credit challenges

Cyclical nature of sugar, chemicals and polyvinyl chloride (PVC) businesses: Sugar industry is a cyclical industry wherein the input price i.e. cane price is set by government while the realisations are market driven. The realisations are driven by the sugar production, inventory and demand levels while raw material availability is exposed to agro-climatic risks. The chemicals and PVC businesses are also exposed to the vagaries of currency fluctuations and duty structures apart from cyclicality associated with global and domestic supply-demand balance

Weakness in the sugar segment expected in the near term partially mitigated by the commissioning of 150 kld distillery, co-gen power sales and upcoming 200 kld distillery: The performance of the sugar segment continues to witness headwinds form sugar sales driven by record sugar production in India leading to subdued sugar prices. In SY2019, sugar production is expected to be around 30.7 MMT while domestic consumption is expected to be around 25.8 MMT. With an opening stock of around 10.8 MMT and excess production of 4.5 MMT in SY2019, the surplus sugar available will remain significant. While GoI has taken several steps to support sugar prices, the economics of sugar sales remain weak in the country.

Pressure on the profitability of Bio-seed segment: The performance of the bio-seed segment has remained weak for past few years owing to price control by the government on Bt Cotton in India and losses in the international operations. The performance continues to remain weak and was impacted by ~Rs. 13 crore write-off in FY2019 related to slow moving inventory and debtors.

Investment to meet target energy consumption norm for urea segment may not be remunerative: The energy norm applicable for DCM's urea unit under NUP-2015 were to be revised downward from April 1, 2018 onwards. However, deferment of the same by two years has allowed the company to continue with the current energy savings for additional two years. Meeting the new target energy consumption norm may require material investments which may not generate meaningful returns. Currently, the company uses coal to generate power which is more cost efficient (cost of coal being only about half of gas) vis-à-vis alternates even though it is less energy efficient. Thus, even after meeting the target energy consumption, there may not be any savings in subsidy. DCM is yet to finalise the capex and timelines for implementation of energy savings schemes pending decision of the government.

Liquidity Position:

DCM's liquidity position remains robust driven by healthy cash generation from the caustic operations and improving performance of the sugar segment driven by distillery operations and power sales. With nearly Rs. 416 crore of cash balance at the end of FY2019 and large unutilised fund-based limits, company has significant liquidity cushion available to tide over any short-term cash flow mismatches. The debt repayments of the company over the next few years range between Rs. 120-130 crores vis-à-vis the net cash accruals of around Rs. 1000-1100 crore going forward. With expectations of continued healthy performance of the caustic soda segment driven by healthy demand growth coupled with improvement in the earnings from the sugar segment driven by scaling up of the distillery operations and power sales, the liquidity profile is expected to improve in the near term.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for entities in the Chemical industry Rating methodology for rating entities in Sugar industry Rating methodology for entities in the Fertiliser industry
Parent/Group Support	NA
Consolidation / Standalone	The ratings are based on consolidated financials of DCM Shriram Limited

About the company:

DCM Shriram Limited (DCM Shriram) is a diversified company with interests in agri-value chain (urea, sugar, seeds and trading of agri-inputs) and the chloro-vinyl chain (chlor-alkali and PVC). Apart from these, the company is involved in certain other related businesses to take advantage of vertical integration, such as Fenesta Building System (UPVC doors and windows), cement (produced at its integrated Kota plant) and PVC compounding (50:50 JV with Axiall Inc., USA). The company's operations are based out of Kota and Bharuch (for chloro-vinyl value chain) and central Uttar Pradesh (for sugar). In Kota, the company has a fully integrated unit with chlor-alkali, PVC, urea and cement plants and a captive power plant. The company also has a chlor-alkali plant in Bharuch along with a captive power plant. The sugar operations of the company are based in central Uttar Pradesh (UP). The bioseed division of the company is headquartered in Hyderabad. The company is a public limited company with 66.53% of the shareholding being held by the promoter group as of March 31, 2019 post a buyback executed in FY2019, while the rest is held by institutional investors and the public.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	6,900.5	7,801.7
PAT (Rs. crore)	668.7	902.6
OPBDIT/OI (%)	15.2%	17.9%
RoCE (%)	26.5%	31.0%
Total Debt/TNW (times)	0.2	0.5
Total Debt/OPBDIT (times)	0.7	1.2
Interest coverage (times)	12.6	11.8

Source: ICRA estimates; OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work in Progress)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Instrument	Current Rating (FY2020)				Chronology of Rating History for the past 3 years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating	Date & Rating in FY2019	Date & Rating in FY2018	Date & Rating in FY2017	
				June 2019	May 2018	June 2017	May 2016	April 2016
Term Loan	Long Term	616.78	616.78	[ICRA]AA Positive	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
Fund based	Long term	1120.00	-	[ICRA]AA Positive	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)
Non-fund based	Short Term	800.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
Commercial Paper	Short Term	800.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
Fixed Deposit	Medium term	40.00	-	MAA+ (Positive)	MAA+ (Stable)	MAA+ (Stable)	MAA- (Stable)	MAA- (Stable)

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
-	Term Loan-1	October 2016	-	October 2026	54.00	[ICRA]AA (Positive)
-	Term Loan-2	January 2018	-	January 2028	93.00	[ICRA]AA (Positive)
-	Term loan-3	November 2018		June 2024	198.78	[ICRA]AA (Positive)
-	Term loan-4	December 2018	-	March 2020	25.00	[ICRA]AA (Positive)
-	Term loan-5	December 2018	-	December 2024	15.00	[ICRA]AA (Positive)
-	Term loan-6	March 2019	-	March 2029	41.00	[ICRA]AA (Positive)
-	Term loan-7	March 2019	-	March 2029	190.00	[ICRA]AA (Positive)
-	Cash Credit		-		1120.00	[ICRA]AA (Positive)
-	Non-fund based	-	-	-	800.00	[ICRA]A1+
-	Commercial Paper	-	-	7-365 days	800.00	[ICRA]A1+
-	Fixed Deposit	-	-	-	40.00	MAA+ (Positive)

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
DCM Shriram Credit & Investments Limited	100.00%	Full Consolidation
Bioseed India Limited	100.00%	Full Consolidation
DCM Shriram Infrastructure Limited	100.00%	Full Consolidation
Fenesta India Limited	100.00%	Full Consolidation
Shri Ganpati Fertilizers Limited	81.41%	Full Consolidation
Hariyali Rural Ventures Limited	100.00%	Full Consolidation
DCM Shriram Aqua Foods Limited	100.00%	Full Consolidation
Shriram Bioseed Ventures Limited	100.00%	Full Consolidation
Bioseeds Limited	100.00%	Full Consolidation
Bioseeds Holdings PTE Limited	100.00%	Full Consolidation
Bioseed Research Phillipiness Inc.	100.00%	Full Consolidation
Bioseed Vietnam Limited	100.00%	Full Consolidation
PT Shriram Seed Indonesia	95.00%	Full Consolidation
PT Shriram Genetics Indonesia	49.00%	Full Consolidation
Shriram Bioseed (Thailand) Limited	99.99%	Full Consolidation
Bioseed Research USA Inc.	100.00%	Full Consolidation

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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.

For more information, visit www.icra.in

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