December 06, 2022

DCM Shriram Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loan	544.24	744.24	[ICRA]AA+ (Stable); reaffirmed/ assigned
Fund based cash credit	1,069.0	1,069.0	[ICRA]AA+ (Stable); reaffirmed
Non-fund based	800.0	800.0	[ICRA]A1+; reaffirmed
Commercial paper	600.0	600.0	[ICRA]A1+; reaffirmed
Fixed deposit	40.0	40.0	[ICRA]AA+ (Stable); reaffirmed
Unallocated	123.54	23.54	[ICRA]AA+ (Stable)/[ICRA]A1+; reaffirmed
Total	**3,176.78**	**3,276.78**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of the ratings takes into account the diversified business profile of the company and high operating efficiency of the chlor-alkali division wherein DCM is now the second-largest caustic soda manufacturer in the country and has the advantage of low-cost coal-based captive power generation facilities at the Kota (Rajasthan) and Bharuch (Gujarat) plants. The other business segments, namely Shriram Farm Solutions, Fenesta building system, have also demonstrated a steady improvement in performance. The ratings also factor in the healthy financial risk profile of the entity, characterised by stable cash generation, low net leverage (net debt/OPBDITA) levels and strong liquidity, as indicated by the healthy cash balances and large unutilised working capital limits.

The ratings continue to factor in the healthy contribution margins in the chemical division and improvement in the profitability of the Fenesta and Shriram Farm Solutions segments in H1 FY2023. The chemical division's profitability has been aided by elevated realisations of caustic soda, despite rising power costs. PVC realisations have softened owing to the pressure on global demand and excess supply situation, which has impacted the contributions from the PVC segment, but the overall chloro-vinyl profitability remains healthy. These contribution margins are likely to moderate with the moderation in caustic soda realisations. However, the realisations will remain healthy, which can keep the margins stable, going forward. The sugar division witnessed one-time costs in H1, which along with the increase in state-approved price (SAP) for UP, put pressure on profitability. H1 is seasonally weaker for the sugar segment and the profitability is expected to improve, going forward.

Chlorine is a by-product in caustic soda manufacturing and its disposal remains a key concern for the industry as a whole. ICRA notes the proposed downstream integration projects to be set up at the Bharuch complex which will consume a healthy proportion of the chlorine being produced at the facility. The increased captive chlorine consumption is expected to lend stability to caustic soda production and the ECU realisations at the Bharuch complex.

The ratings are constrained by the cyclical nature of the caustic soda, sugar and PVC segments although the company has been working on downstream integration projects to reduce the volatility in earnings. Also, there is significant capex planned in the current fiscal, which will increase the company's reliance on external debt and is likely to moderate the leverage metrics in the medium term, although these are expected to remain comfortable. While ICRA notes that there have been some cost escalations in the capex programmes planned across various business segments from initially envisaged, the long-term viability and integration of these projects in the company's overall operations is likely to benefit the company. However, with the annual cash generation expected to be in the range of Rs. 1,000 to 1,200 crore per year over the medium term, the company's liquidity profile is expected to remain strong, going forward. The company also has the financial flexibility and headroom to raise additional funding, if required, which can augment the company's liquidity position.

ICRA also notes the measures adopted by the company to reduce its carbon footprint. The company is sourcing fuel from alternative fuel sources such as biomass to reduce the dependence on coal and is also setting up a wind solar hybrid renewable power project through an SPV. It is also actively promoting a circular economy in its operations by setting up projects like the recovery of anhydrous sodium sulphate from brine and manufacturing sulphate of potash from distillery ash.

Key rating drivers and their description

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, Fenesta and cement segments. DCM Shriram's energy-intensive businesses is at Kota (Rajasthan) and Bharuch (Gujarat) with both locations 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 operations ensures the company's competitiveness in the chemical and PVC segments. 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 (1345 TPD) are supported by a 225-MW coal-based captive power capacity. The company is in the process of commissioning a 120-MW power plant at its Bharuch facility which will lead to significant cost savings in the caustic soda segment. The production of caustic soda is an energy-intensive process and DCM's access to low-cost power favourably impacts its cost structure, resulting in healthy profitability from the segment. However, as of now, high coal prices have impacted the cost-dynamics of the captive power plant and the company is suitably reducing its dependence on coal and finding green alternatives to reduce its carbon footprint and procure less cost power.

Healthy scale of operations of the chlor-alkali business - DCM has undertaken successive capacity expansions in the caustic soda segment over the last couple of years, taking the total caustic soda capacity to 1,843 TPD. DCM is currently the second-largest manufacturer of caustic soda in the country with a competitive cost structure which places it well among its peers in the industry. The company is expanding its capacities and is also setting up chorine and hydrogen downstream integration projects which will lend more stability to the operations and also add value to the downstream products through the manufacturing of epichlorohydrin from chlorine and hydrogen peroxide form hydrogen.

Ramp-up of distillery operations to mitigate cyclicality of sugar segment- DCM Shriram had commissioned two distilleries with a combined capacity of 350 kld on C heavy molasses which have been able to ramp up production at a healthy pace. In FY2022, the company diverted a significant amount of its B-molasses to produce ethanol and thus reduced its sugar production. The distillery operations have further provided stability to the earnings of the sugar segment, which earlier remained vulnerable to the volatility in sugar prices and cane pricing. The company is in the process of expanding its sugar capacity and distillery operations which shall lend further stability to the earnings.

Healthy financial risk profile - The capital structure of the company has remained robust, characterised by low gearing and leverage, healthy interest coverage and liquidity from large unutilised bank limits. The gearing of the company remains comfortable at 0.25x in H1 FY2023 (0.27x at the end of FY2022). With healthy cash and equivalents at around Rs. 1,500 crore at the end of H1 FY2023, the net debt remained negligible. The interest coverage remains strong at 25x in H1 FY2023 (21x in FY2022) . With sizeable capex planned in the near term, the debt levels are expected to increase which is likely to moderate the leverage metrics although the same are expected to remain comfortable.

Credit challenges

Cyclical nature of sugar, chemical and polyvinyl chloride (PVC) businesses – Sugar is a cyclical industry wherein the input price i.e., cane price, is set by the Government while the realisations are market-driven, though with an MSP announced by the Government that provides a minimum base for the selling price. The realisations are driven by sugar production, inventory and demand levels, while the raw material availability is exposed to agro-climatic risks. The chemical and PVC businesses are also exposed to the vagaries of currency fluctuations and duty structures, apart from the cyclicality associated with global and domestic supply-demand balance. However, the company has taken steps to mitigate the volatility in the earnings of the sugar segment by commissioning 350-kld distilleries in the last couple of years, wherein ethanol production has been ramped up significantly.

The company is also undertaking downstream integration projects in the caustic soda segment with planned capex for a 51,000-MTPA epichlorohydrin (ECH) project, aluminium chloride capacity expansion project and a 52,500-MTPA hydrogen peroxide (H_2O_2) plant. These projects are expected to moderate the cyclicality of the caustic soda segment although the offtake of these products and the realisations will remain exposed to commodity cycles.

Significant capex planned in FY2023 - The total outflow of cash towards capex is expected to be around Rs. 2,800 crore in FY2023. The expected capex amounts have increased sharply this year due to high commodity prices and delays due to Covid-related challenges, coupled with changes in scope of some of these projects. The increase in capex has slightly impacted the return on these projects and the payback period has increased for all the projects. Despite the slight increase in the payback period and reduction in returns, the overall returns continue to be healthy and shall benefit the company in the long run. Further, the capex will increase the reliance on external debt, pushing up the net debt/OPBDITA to more than 1x for FY2023, though the same is likely to improve, going forward. The existing cash/investments surplus of ~Rs. 1,500 crore, coupled with an annual internal generation of Rs. 1,000-1,200 crore, will ensure limited reliance on external debt and the debt metrics are expected to remain comfortable.

Environmental and Social Risks

DCM manufactures caustic soda, which results in the production of chlorine as a by-product, the disposal of which remains a key challenge for the industry. The chemical sector in general remains exposed to the risk of tightening regulations for the production, handling and transport of chemical products with regards to safety and environmental impact, remedial measures for pollution and effluent treatment. Additionally, some products can face restrictions/substitution over time due to the hazardous nature and the availability of more environmentally-friendly products. Further, in the event of accidents, the liability for clean-up could be high for certain products. However, ICRA notes the measures adopted by the company to reduce its carbon footprint and water conservation. The company is 11x water positive and ~22% of its total power consumption is green power. The company is sourcing fuel from alternative sources such as biomass to reduce dependence on coal and is also setting up a wind solar hybrid renewable power project through an SPV. It is also promoting a circular economy in its operations by setting up projects like the recovery of anhydrous sodium sulphate from brine and manufacturing sulphate of potash from distillery ash.

Liquidity position: Strong

DCM Shriram's liquidity is strong, given the large cash balances and unutilised working capital limits with expectations of healthy cash accruals. While the company is undertaking a large capex programme with the capex bunching up in FY2023, the cash generation is likely to be comfortable. ICRA expects DCM Shriram to meet its debt repayment obligations comfortably, going forward, as the repayments are comfortable vis-a-vis the cash flow from operations.

Rating sensitivities

Positive factors – The ratings of DCM Shriram Limited is unlikely to be upgraded till the company is able to significantly ramp up its scale of operations and diversify into less commoditised products.

Negative factors – The ratings may be downgraded is the company's net debt/OPBDITA remains above 1.5x for a sustained period owing to weak cash generation. Capex plans/acquisitions resulting in higher debt on the books of the company may also trigger a downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Fertiliser Entities Rating Methodology for Entities in the Chemical Industry Rating Methodology for Entities in the Sugar Industry
Parent/Group support	NA
Consolidation/Standalone	The ratings are based on the consolidated financials of the company. The details of the entities consolidated are given in Annexure-2

About the company

DCM Shriram Limited (DCM Shriram) is a diversified company with interests in the agri-value chain (urea, sugar, seeds and trading of agri-inputs) and 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. The company's operations are based in 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 company's sugar operations are based in central Uttar Pradesh (UP). The bioseed division of the company has its headquarters in Hyderabad. The company is a public limited company with 66.52% of the shareholding being held by the promoter group as on September 30, 2022, while the rest is held by institutional investors and the public.

Key financial indicators (audited)

DCM Shriram Limited, Consolidated	FY2021	FY2022
Operating income (Rs. crore)	8308.2	9627.4
PAT (Rs. crore)	672.3	1066.1
OPBDIT/OI (%)	13.82%	18.62%
PAT/OI (%)	8.09%	11.07%
Total outside liabilities/Tangible net worth (times)	0.7	0.7
Total debt/OPBDIT (times)	1.3	0.8
Interest coverage (times)	9.4	21.0

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	Type	Amount rated (Rs. crore)	Amount outstanding (Rs. crore)	Current rating (FY2023) Date & rating on			Chronology of rating history for the past 3 years		
								Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					06 Dec 2022	30 June 2022	12 May 2022	29 June 2021	6 July 2020	28 Jun 2019
1	Term loan	Long term	744.24	733.44*	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Positive)
2	Fund based cash credit	Long term	1069.00	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Positive)
3	Non-fund based	Short term	800.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Commercial paper	Short term	600.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Fixed deposit	Long term	40.00	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	MAAA (Stable)	MAA+ (Stable)	MAA+ (Positive)
6	Unallocated	Long term/Short term	23.54	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA (Positive)/ [ICRA]A1+

**As on September 30, 2022*

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term loan	Simple
Fund based	Simple
Non-fund based	Simple
Commercial paper	Simple
Fixed deposit	Simple
Unallocated	Not applicable

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 analysing 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 are available on ICRA's website: [Click Here]

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 loans	FY2017-FY2023	-	FY2025-FY2030	744.24	[ICRA]AA+ (Stable)
-	Fund-based cash credit	-	-	-	1069.0	[ICRA]AA+ (Stable)
-	Fixed deposit programme	-	-	-	40.0	[ICRA]AA+ (Stable)
-	Non-fund based	-	-	-	800.0	[ICRA]A1+
Not placed	Commercial paper	-	-	7-360 days	600.0	[ICRA]A1+
	Unallocated	-	-	-	23.54	[ICRA]AA+ (Stable) / [ICRA]A1+

Source: *Company*

Please click here to view details of lender-wise facilities rated by ICRA

Annexure-2: List of entities considered for consolidated analysis

Company Name	DCM Shriram's 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
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 Holdings PTE Limited	100.00%	Full Consolidation
Bioseed Research Philippines Inc.	100.00%	Full Consolidation
Bioseed Research USA Inc.	100.00%	Full Consolidation
Shriram Polytech Limited	100.00%	Full Consolidation

Source: *DCM Shriram Limited*

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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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