March 31, 2023

Deepak Nitrite Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based limits	300.00	-	-
Short-term non-fund based limits	170.00	-	-
Long/Short-term fund-based and non-fund based limits	20.00	490.00	[ICRA]AA(Positive)/[CRA]A1+; reaffirmed
Short-term – Commercial paper	200.00	200.00	[ICRA]A1+; reaffirmed
Total	**690.00**	**690.00**	

**Instrument details are provided in Annexure-I*

Rationale

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

The reaffirmation of the ratings considers the healthy consolidated financial profile of the company, supported by strong performance across segments, although there has been some moderation in the profitability because of higher raw material costs and reduction in crack spreads. ICRA notes that the consolidated entity continued to witness reduction in debt to ~Rs. 109.6 crore as on December 31, 2022 compared with Rs. 300.7 crore as on March 31, 2022, driven by prepayments, leading to a healthy improvement in the capital structure and coverage indicators.

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 the 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 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. 2,500-2,600 crore to be incurred over FY2024-FY2026 towards capacity expansion of some existing products, new product addition, backward integration and cost saving measures. However, ICRA notes that the capex pertains to several smaller projects (under rated entities/subsidiaries/JV), with the execution phased out during the period, which will mitigate the risk to some extent. The development on this front remains a key monitorable.

The positive outlook 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 initiatives such as backward integration and cost saving measures and the successful commissioning of the planned projects.

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 a 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. At present, 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 financial profile – DNL, on a consolidated basis, reported a significant growth in revenue in FY2022 at Rs. 6,821.3 crore (P.Y. Rs. 4365.2 crore) and OPBITDA at Rs. 1,625.7 crore (P.Y. Rs. 1,257.5 crore), driven by higher realisations and capacity utilisation across the phenolics and advanced intermediates segments. However, the OPM moderated to 23.8% in FY2022 from 28.8% in FY2021, impacted by higher input costs. In 9M FY2023, on a consolidated basis, DNL's operating income grew to Rs. 6,010.7 crore, driven by higher realisations which mitigated the moderation in volumes caused by a fire accident at the Nandesari plant. With healthy cash accruals, the company has reduced its debt levels, leading to an improvement in the coverage metrics. In FY2022, on a consolidated basis, the interest coverage and DSCR increased to 44.7 and 14.9 times, respectively, compared with 16.3 and 7.3 times, respectively, in FY2021. The total debt/OPBITDA declined to 0.18 times as on March 31, 2022 compared with 0.46 times as on March 31, 2021. Further, as on December 31, 2022, the total debt/OPBITDA further declined to 0.10 times.

Healthy operations at DPL– DPL's phenol-acetone plant showed a capacity utilisation of over 140% in 9M FY2023, resulting in healthy revenue and cash flow generation for DNL on a consolidated basis. However, the profitability moderated due to the reduced crack spreads during 9M FY2023, but remains healthy. Also, since the operationalisation of its IPA plant in April 2020, DPL has been able to reap the benefits of 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 the 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 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.

Large capex planned over the medium term, exposing to the execution risks - On a consolidated basis, the company incurred ~Rs. 175-crore capex in FY2022 and ~Rs. 300-crore capex in 9M FY2023 to add new products, expand the capacity of the existing products and for backward integration. The company, on a consolidated basis, is expected to incur around Rs. 2,500-2,600 crore capex over FY2024-2026 for regular maintenance, backward integration and expansion of its existing products which will improve the sustainability of the operations over the medium to longer term. The capex also includes the investment in the sodium nitrate plant in Oman. Further, the capex is not for a single project but several projects, which will be staggered over this period and each unit will be monetised/commence operation, even while capex on others might be going on. 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.

Liquidity position: Strong

At a consolidated level, DNL's liquidity position remains strong with healthy annual cash flow from operations at Rs. 782.9 crore in FY2022 and Rs. 421.4 crore in 9M FY2023. The Group's free cash balance and liquid investments were at ~Rs. 381.3 crore as on December 31, 2022. DNL also has a sanctioned fund-based working capital facility of Rs. 320 crore as on December 31, 2022 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. 580 crore as on December 31, 2022, the average utilisation of which was 47% in the form of non-fund based limits over the past 12 months. The company has ~Rs. 13 crore scheduled long-term repayment obligations for the existing debt in FY2024 and FY2025. The company has plans for capex/investment in JVs over the next few years, for which ~Rs. 1,100-1,1200 crore will be incurred in FY2024 and FY2025 each, to be funded through a mix of debt and internal accruals, although the debt funding is expected to be moderate.

Rating sensitivities

Positive factors – The ratings can be upgraded if the company is able to sustain healthy revenue growth and profitability on a consolidated basis, backed by a change in the product mix towards more value-added products and successful commissioning of a major share of the planned projects.

Negative factors – 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 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 considered the consolidated financials of Deepak Nitrite Limited (please refer to Annexure II for details of entities consolidated)

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 two segments— advanced intermediates and phenolics segment. 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 FY2022, DNL, on a consolidated basis, reported a net profit of Rs. 1,066.6 crore on an operating income of Rs. 6,802.2 crore compared with a net profit of Rs. 775.8 crore on an operating income of Rs. 4,361.3 crore in FY2021.

Key financial indicators (audited)

DNL Consolidated	FY2021	FY2022	9M FY2023*
Operating income	**4365.2**	**6821.3**	**6010.7**
PAT	775.8	1066.6	618.1
OPBDIT/OI	28.8%	23.8%	15.7%
PAT/OI	17.8%	15.6%	10.3%
Total outside liabilities/Tangible net worth (times)	0.52	0.33	0.25
Total debt/OPBDIT (times)	0.46	0.18	0.10
Interest coverage (times)	16.3	44.7	46.3

*PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore, *Provisional*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)					Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding as on Dec 31, 2022 (Rs. crore)	Date & rating in FY2023		Date & rating in FY2022		Date & rating in FY2021	Date & rating in FY2020
					Mar 31, 2023	Jun 13, 2022	Mar 25, 2022	Mar 26, 2021	Jun 17, 2020	Aug 22, 2019
1	Term loans	Long-term	-	-	-	-	-	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)
2	Fund-based limits	Long-term	-	-	-	[ICRA]AA (Positive)	[ICRA]AA (Positive)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- (Stable)
3	Non-fund based limits	Short term	-	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Fund and non-fund based limits	Long term/ Short term	490.00	-	[ICRA]AA (Positive)/ [ICRA]A1+	[ICRA]AA (Positive)/ [ICRA]A1+	[ICRA]AA (Positive)/ [ICRA]A1+	[ICRA]AA (Stable)/ [ICRA]A1+	[ICRA]AA (Positive)/ [ICRA]A1+	[ICRA]AA- (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/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 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 I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Fund and non-fund based limits**	NA	NA	-	490.00	[ICRA]AA(Positive)/[ICRA]A1+
Unplaced	**Commercial paper**	NA	NA	7-365 days	200.00	[ICRA]A1

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

Company Name	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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