January 19, 2024

Talcher Fertilizers Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based – Term loan	9,560.00	9,560.00	[ICRA]A- (Stable); reaffirmed
Total	**9,560.00**	**9,560.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating of Talcher Fertilizers Limited (TFL) continues to take into account its strong parentage - Coal India Limited, GAIL (India) Limited {GAIL, [ICRA]AAA(Stable)/[ICRA]A1+} and Rashtriya Chemical & Fertilisers Limited {RCF, [ICRA]AA (Stable)/[ICRA]A1+}, and a positive demand-supply outlook for urea in the country. TFL is setting up a 1.27-MMTPA urea plant with coal gasification technology. The project holds strategic importance for the Government of India (GoI) as it would pave the way for utilising the coal gasification technology to produce fuels, chemicals and polymers using large reserves of indigenous coal that may face demand headwinds from other sectors over the long term due to climate change related concerns.

The total project outlay is currently estimated at ~Rs. 13,277 crore, which is likely to face cost and time overruns . The quantum of the cost escalation, the funding pattern and the revised commissioning date is yet to be finalised. Given the high capex and new technology being implemented for urea production, the DoF has formulated a policy assuring a 12% post-tax internal rate of return (IRR), thus assuring healthy profitability and comfortable debt servicing. While the detailed contours of the policy will be defined closer to the commissioning of the project, the policy will ensure a 12% post-tax equity IRR. The project was originally scheduled to be commissioned by June 2024, but is likely to face some delays due to the pandemic and some changes in the scope of the project, which will result in cost and time overruns. ICRA expects the sponsors to fund the project adequately by infusing the requisite amount of additional equity. Till October 2023, around 51% of the project was complete, funded through a sizeable proportion of equity, thereby leading to lower interest during construction.

The rating is, however, constrained by the high technological risk of operating the plant successfully with domestic coal that has high ash content, though the company plans to mitigate the risk by adopting a state-of-the-art technology and blending the feedstock with petcoke. The project also remains exposed to implementation risks owing to its large size and the relatively nascent stage as of now, although the risk is partly mitigated by the lump sum turnkey (LSTK) mode of contract execution being adopted on a fixed price and fixed tenure basis.

The rating also factors in the vulnerability of the fertiliser sector's profitability and cash flows to regulatory policies, timely payment of subsidy by the GoI and agro-climatic conditions. ICRA also notes that the LSTK contractor is a Chinese company and the project execution may witness challenges due to geo-political issues, though there have been no such issues as of now. Given the strategic importance of the project to the GoI, this project should get the requisite support for timely execution.

The outlook on the rating is Stable as ICRA expects the project execution to benefit from the strong track record of the promoters in executing large-sized projects successfully over the years and the experience of the LSTK contractors in executing similar projects in the past, and the cash flow support the project is likely to witness with 12% assured equity IRR.

Key rating drivers and their description

Credit strengths

Strategic importance of project to GoI - TFL's plant is the first unit to implement the shell coal gasification process (SCGP) to use Indian coal with high ash content. The project holds strategic importance for the Government of India (GoI) as its successful implementation would pave the way for utilising the coal gasification technology to produce fuels, chemicals and polymers using the large reserves of indigenous coal that may face demand headwinds from other sectors over the long term due to climate change related concerns.

Favourable demand-supply scenario for urea in India - Domestic demand for urea continues to rise at a steady pace, growing at ~2.9% per annum to 35.7 MMT in FY2023 from 19.2 MMT in FY2000. As a result, India's dependence on imported urea has increased significantly, reaching around 17% in 7M FY2024. Post the announcement of the New Urea Investment Policy2012 (NIP-2012), Chambal Fertilisers & Chemicals Limited (CFCL, rated [ICRA]A1+) commissioned a 1.27-MMTPA urea plant in January 2019. Two new plants - one by Ramagundam Fertilisers & Chemicals Limited (RFCL) and the other by Matix Fertilisers & Chemicals Limited (MFCL) - of 1.27 MMTPA capacity each were commissioned in FY2022. Hindustan Urvarak & Rasayan Limited (HURL) commissioned three other plants of 1.27 MMTPA capacity each in FY2022 and FY2023.

With TFL's plant slated to be commissioned in FY2025 (likely to be delayed), the import dependence will be kept under check, even as imports had spiked in years of high demand. Thus, the demand-supply scenario remains favourable for urea in the country, also supported by the significant price differential between urea and phosphatic/potassic fertilisers. Even in a potential surplus scenario for domestic urea, ICRA expects the offtake from the project to be optimal, given its strategic importance to the GoI and the locational advantage.

Strong promoter profile; sponsor support by promoters provides comfort - TFL's promoters include CIL, GAIL and RCF which have strong credit profiles and operational experience in handling coal mining, gas processing and fertiliser manufacturing & marketing. The promoters will also be providing a sponsor support undertaking (SSU) to the lenders to fund any cost overruns through equity or post approval by the lenders in the target debt:equity ratio. At present, several personnel have been appointed by the promoters at managerial and operational positions. The current Managing Director has been appointed by RCF, while the Director Finance has been brought in by CIL. The board of the company also comprises senior managers from the promoters with two each from CIL, GAIL and RCF to have a closer oversight over the execution of the project.

FSA for entire requirement of coal with CIL provides feedstock security - Coal and petcoke will be the main raw materials to be used in the project. The company has entered into a long term FSA with Coal India Limited for the supply of 3 MMTPA of coal, meeting the entire coal requirement of TFL from one of the coalfields of CIL. With Coal India Limited being one of the promoters, coal availability is not expected to be an issue. The company has also signed a memorandum of understanding (MoU) with Indian Oil Corporation Limited {IOCL, [ICRA]AAA(Stable)/[ICRA]A1+} to source petcoke and the final agreement will be signed closer to the commissioning date.

Policy support from Department of Fertilisers (DoF) assuring 12% equity IRR - Given the high capex and new technology being implemented for urea production, the DoF has formulated a policy assuring a 12% post-tax equity IRR, thus ensuring healthy profitability and comfortable debt servicing. While the policy has been announced by the DoF, the details will be finalised closer to the project commissioning as several engineering and financial parameters would have crystallised by then.

Credit challenges

Project implementation challenges and technology risks - TFL's urea project has a capital outlay of Rs. 13,277 crore which will face some cost escalations and will be implemented over the course of the next five years. Given the large size of the project, it remains vulnerable to execution risks. The project also remains exposed to technological risks as it is the first unit to implement the SCGP technology in India and could face stabilisation/operational issues. The successful implementation of the technology in China and the experience of the LSTK contractor in executing projects of similar scope remain the key mitigants.

Cost overruns may impact project IRR and moderate credit metrics – The urea project by TFL is expected to experience cost overruns primarily due to some change is scope, leading to potential delays in project commissioning. The credit metrics are likely to moderate further as the increased capital outlay will necessitate additional funding.

Vulnerability of profitability to agro-climatic risk and regulatory policies - The profitability of the fertiliser sector remains vulnerable to the regulatory policies of the GoI, including subsidy budgeting and policy formulation. The DoF has formulated a policy for TFL, assuring a 12% post-tax equity IRR which will ensure timely debt servicing and adequate returns for the project.

Agro-climatic risks like weak monsoon also impact the profitability of the fertiliser sector as the industry has to offer higher discounts at such times, given the stressed condition of the end-users.

Moderate financial risk profile - The coverage and capitalisation indicators are expected to remain subdued in the initial phase of operation because of the large capital outlay and significant debt being contracted for the project. However, the long tenure of the repayment (9.75 years) with a 1-year moratorium, post commissioning, provides comfort from a debt servicing perspective.

Liquidity position: Adequate

TFL's liquidity will remain adequate to meet the funding requirements of the project as the entire debt tie-up has been completed, while the equity contribution from the promoters has been timely. The promoters have already provided 65% of their equity contribution by the end of September 2023. While there will be some cost escalations, ICRA expects the promoters to support the project by infusing additional equity as per the requirements.

Rating sensitivities

Positive factors– A rating upgrade looks unlikely in the near term until there is significant progress in project construction and stabilisation.

Negative factors – The rating may be under pressure if material time and/or cost overruns impact the project's returns and debt metrics. Weakening of linkage or deterioration of the credit profile of the sponsors will also weigh on the rating.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Rating Methodology for Fertilizers Corporate Credit Rating Methodology
Parent/Group support	Parent: GAIL (India) Limited (GAIL), Coal India Limited (CIL) and Rashtriya Chemicals & Fertilisers Limited (RCF) The rating takes into account the strength of the promoters and the sponsor support undertaking (SSU) signed with the lenders to fund cost overruns through infusion of equity
Consolidation/Standalone	The rating is based on the projected standalone financials of the company

About the company

Talcher Fertilizers Limited (TFL) is a joint venture of GAIL (India) Limited {GAIL, rated [ICRA]AAA (Stable)/[ICRA]A1+}, Coal India Limited (CIL) and Rashtriya Chemicals & Fertilisers Limited {RCF, rated [ICRA]AA- (Stable)/[ICRA]A1+}, with each having a 31.85% stake, and Fertiliser Corporation of India Limited (FCIL) with a 4.45% stake. The JV was formed to set up a new coal gasification-based urea manufacturing plant at FCIL's Talcher site where a coal-based urea plant existed till 2002. The urea plant being set up at Talcher has a production capacity of 2,200 MTPD ammonia and 3,850 MTPD (1.27 MMTPA) of urea and is based on the coal gasification technology sourced from Shell Eastern Pte Limited (with the technology now acquired by M/S Air Products Limited, USA). Coal (25,29,339 tpa) and petcoke (3,48,480 tpa) are the feedstocks. The company has an in-principle approval for a bridge linkage for coal supply from Coal India Limited till a coal mine is allocated by the Ministry of Coal and operationalised. The total capital outlay for the project is Rs. 13,277 crore which will face some cost escalations and is proposed to be funded in a debt-equity ratio of 72:28 at present. The zero date of the project was October 1, 2019 and the project was expected to be commissioned in 57 months from the zero date i.e. end of June 2024, which is likely to be delayed.

Key financial indicators (audited): **As TFL is a project company, the key financial indicators have not been included**

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as on Sep 30, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021
					Jan 19, 2024	Mar 21, 2023	Dec 14, 2021	Nov 06, 2020
1	**Term loan**	Long term	9560.00	1748.78	**[ICRA]A-(Stable)**	**[ICRA]A-(Stable)**	**[ICRA]A-(Stable)**	-
2	**Proposed term loan**	Long term	--	--	-	-	-	**[ICRA]A-(Stable)**

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based – Term loan	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	**Term Loan**	FY2022	-	FY2035	9560.00	[ICRA]A-(Stable)

Source: Company

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

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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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.

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