March 11, 2024

Neogen Chemicals Limited: Ratings downgraded to [ICRA]A-(Stable)/[ICRA]A2

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based limit – Term loan	254.00	254.00	[ICRA]A-(Stable); downgraded from [ICRA]A (Stable)
Long-term fund-based limit – Cash credit	260.00	260.00	[ICRA]A-(Stable); downgraded from [ICRA]A (Stable)
Short-term fund/non-fund - based limit – Others	175.00	69.61	[ICRA]A2; downgraded from [ICRA]A2+
Short-term non-fund based – Other	32.30	137.69	[ICRA]A2; downgraded from [ICRA]A2+
Long term/ Short term unallocated Limits	3.70	3.70	[ICRA]A-(Stable)/[ICRA]A2; downgraded from [ICRA]A(Stable)/ [ICRA]A2+
Total	**725.00**	**725.00**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings downgrade factors in the expected moderation in the credit profile of Neogen Chemicals Limited (NCL) owing to the significant debt-funded capex announced for the battery chemical segment and the continued elevated working capital intensity for the company. NCL plans to manufacture Li-ion battery electrolyte salts and electrolytes with a total capital outlay of Rs. 1,450-1,500 crore to be incurred over the course of FY2024 to FY2026. Under the first phase, electrolyte salt capacity of 2500 MTPA and electrolyte capacity of 2000 MTPA will come online in FY2024 & FY2025. The rest of the capacities (30,000 MTPA of electrolyte and 3000 MTPA of electrolyte salts) are expected to be commissioned by December 2025 under the second phase. A major portion of the capex is being funded using long-tenor debt, which will result in significant debt uptake by the company over the course of FY2025-FY2026. Moreover, NCL's elevated working capital intensity in standalone operations has also kept the working capital debt higher than ICRA's expectation. Hence, the overall credit profile (including Neogen Ionics Limited) is expected to moderate over FY2025 and FY2026. However, the long tenor of the loan with debt servicing moratorium for the construction period and the ballooning repayments thereafter provide comfort as the ramp up in cash flows will match the debt servicing requirements. The company, nevertheless, remains exposed to the risks pertaining to project execution and ramp up of the capacity.

ICRA expects NCL to benefit from the experience of its promoters in lithiation and bromination/fluorination chemistries due to their synergy with the production of battery electrolytes and electrolyte salts. However, manufacturing battery chemicals is a new line of business for the company and this industry is at a nascent stage in the country. So, the ramp up of the facilities, once production starts, will remain a key monitorable.

ICRA also notes that NCL has entered into an agreement with Mitsubishi Ionics Solutions Corporation (MUIS) to acquire its lithium electrolyte production technology. MUIS is a JV between Mitsubishi Chemical Corporation (MCC) and UBE Corporation and is a group company of The Mitsubishi Chemical Group, one of the leading manufacturers of electrolytes used in lithium-ion batteries. Given the established track record of MUIS in electrolyte manufacturing, ICRA expects the technology licence to enable quicker approvals for NCL from the battery manufacturers. NCL had also acquired BuLi Chemicals Limited in April 2023 for Rs. 19.25 crore which will allow the company to expand its offering in the pharmaceutical and agrochemical space.

The ratings are constrained by the project execution risk posed by the newly announced capex, elevated working capital intensity and exposure to forex risk. The ratings are also constrained by the exposure of the chemical business to regulatory risks emanating from changes in Government restrictions and the expected moderation in the company's credit profile because of the significant debt to be taken up by the company.

The Stable outlook on the long-term rating reflects ICRA's expectation that the company will continue to benefit from the experience of the promoters in the lithiation and bromination processes as well as the tie-up with MUIS which will enable timely execution of the project and faster approvals for the battery business, thereby supporting the company's cash flows.

Key rating drivers and their description

Credit strengths

Extensive experience of promoters and established market position in bromine and lithium compound segment – NCL has a track record of 30 years in manufacturing bromine and lithium-based specialty chemicals, catering to industries like pharmaceuticals, agro-chemicals and engineering chemicals. The promoters are technocrats with extensive experience in the chemical industry.

Diverse product portfolio and R&D capabilities – The company has in-house R&D capabilities for new products/process development. This has helped the company to have a diversified product profile, although they are bromine and lithium-based derivatives. In terms of end-user industry concentration, the pharma sector accounts for 50-60% of sales, followed by agrochemicals, while the remaining sales are driven by other industries. However, the customer concentration remains moderate, with the top 5 customers accounting for 21-22% of the sales in FY2023 and H1 FY2024.

In recent years, the company has incurred capex to add capacities, including a new plant in Dahej, where additional expansion is underway. This will enable the company to add new products in existing end-user industries as well as new segments like lithium-ion battery manufacturers, with high growth potential. A timely completion of the lithium-ion battery project and scaling up of the operations will be the key monitorables. The company has also been increasing its custom synthesis manufacturing business in recent years and the segment is expected to grow, going forward, providing diversification benefits.

Credit challenges

High working capital intensity – The company's operations are working capital intensive with NWC/OI in the range of 50-70% in the last five years. The working capital intensity is elevated due to the high inventory requirements as it manufactures a large number of products with multiple stages of processing. The company may also maintain a high raw material inventory for certain products, which may have high volatility or availability issues. The company is trying to moderate its working capital intensity and the developments will be monitored.

Exposure to foreign exchange and raw material price volatility – NCL largely imports its raw material which exposes the company to foreign currency fluctuations. However, nearly 40-50% of the revenue is derived from exports, providing a natural hedge to an extent. NCL's operating profitability also remains susceptible to the volatility in key raw material prices. However, due to the value-added nature of the products, the company has been able to pass on the input cost fluctuations to an extent, which mitigates the risk. The company also has established relationship with suppliers which mitigates the availability risk to some extent.

Exposed to projection execution risk due to significant capex in battery chemical business - NCL has announced a capex of Rs 1,450-1,500 crore to set up the lithium electrolyte manufacturing capacity under its newly floated subsidiary, Neogen Ionics Limited. In phase 1, NCL is a setting up electrolyte salt capacity of 2,500 MTPA, of which one section of 400-MTPA capacity has commenced trial production and the remaining section is under final testing and is expected to be commissioned in FY2025. Phase 1 also entails setting up of electrolyte capacity of 2,000 MTPA, production and sales of which are expected to commence from Q1 FY2025. In phase 2, NCL will be setting up a greenfield facility with electrolyte salt capacity of 3,000 MTPA and electrolyte capacity of 30,000 MTPA. These facilities are expected to come online by December 2025. Given the large size of the capex and a relatively nascent stage of the industry in the country, the company will remain exposed to project execution risks as well as the risk associated with ramp up of the capacity.

Moderation in financial risk profile – NCL plans to fund the Rs. 1,450-1,500-crore battery chemical capex using a mix of debt and equity, wherein debt will comprise 70-75% of the project cost. Over the next 2 years, Rs. 1,000-1,100-crore is expected to come on NCL's books, which will significantly moderate the leverage and coverage indicators. While ICRA derives comfort from the expected long tenor with moratorium for the construction period, the financial profile is expected to remain subdued in the near to medium term.

Environmental and social risk

Neogen, being a chemical company, requires various statutory and regulatory permits, licences and approvals to run its operations, including environmental clearance. Many of these approvals are granted for a limited duration and must be periodically renewed. They can even be revoked in the event of non-compliance and lead to penalties and incarceration. However, Neogen has placed keen focus on compliance with EHS (environment, health and safety) standards. This is validated through the ISO certifications that Neogen holds. Further, the Dahej SEZ plant has been GMP (Good Manufacturing Practices) certified by SGS. The facility operates a zero-liquid discharge system.

The company's exposure to social risks mainly pertains to safe operations and remaining compliant with all environmental regulations to ensure the safety of the employees and the community in the vicinity of its manufacturing units. As per the disclosures, the company has safety equipment in place at its units and follows employee safety norms with stringent standards

ICRA does not expect the environmental and social risks to have any major impact on the company's credit profile in the near to medium term.

Liquidity position: Adequate

The company's liquidity position is expected to remain adequate, supported by the equity raised recently, part of which has been utilised to fund the working capital requirements and meet the equity commitment for the battery business capex. The debt tie-up for the upcoming capex is at advanced stages and, once approved, will enable the company to meet its capex requirements. The overall cash accruals of Rs. 70-80 crore p.a., going forward, remain more than adequate to meet the debt repayments of Rs. 40-50 crore per annum. Thus, the overall liquidity position of the company will remain adequate. NCL also has fund-based working capital limits of Rs. 360 crore with an average utilisation of 78% in the 12-month period ended January 2024.

Rating sensitivities

Positive factors – ICRA could upgrade NCL's ratings if there is a significant improvement in its cash generation from operations and improvement in working capital intensity, leading to a significant improvement in the credit metrics and liquidity profile. Timely completion of the battery chemical capex without any cost overruns and a successful ramp up of operations will be the key triggers for upgrade.

Negative factors – The ratings may be downgraded if higher-than-expected debt is availed for the upcoming capex, or if there is any significant time/cost overrun in project execution that would moderate the company's credit risk profile and liquidity position. Further, moderation in the company's working capital intensity and/or subdued profitability from the current operations impacting the overall credit metrics will remain a negative trigger.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology - Chemicals
Parent/Group support	Not Applicable

Consolidation/Standalone	For arriving at the ratings, ICRA has consolidated the financials of NCL, projected financials of Neogen Ionics Limited and Buli Chemicals Private Limited

About the company

Neogen Chemicals Ltd. is an over 30-year-old company, specialising in bromine-based compounds, Grignard reagents and inorganic lithium salts. The company was founded by Mr. Haridas Kanani, a chemical engineer from the Indian Institute of Technology (IIT), Mumbai. At present, Dr Harin Kanani, who is also a chemical engineer from IIT, Mumbai, and a PHD holder, runs the day-to-day operations of the company.

Over the years, Neogen has developed several bromine-based intermediates and is a leading manufacturer of these products. Its specialty chemicals are used in pharmaceutical, agro-chemicals, engineering chemicals, electronic chemicals, construction chemicals, aroma chemicals, flavours and fragrances, and other industries. Specialty chemicals are also finding application in lithium-ion battery materials for energy storage and EV application. The company serves across 29 countries (USA, Europe, Japan and Middle East).

At present, they have four plants in Mahape, Vadodarp, Dahej and the recently acquired BuliChem plant in Hyderabad with a combined capacity of 3,600 MTPA for inorganic chemicals and 463 kilolitres of reactor capacity for manufacturing organic chemicals.

Key financial indicators (audited)

	FY2022	FY2023	9M FY24*
Operating income	487.0	686.0	491.0
PAT	44.5	49.9	18.6
OPBDIT/OI	17.8%	16.3%	15.1%
PAT/OI	9.1%	7.3%	3.8%
Total outside liabilities/Tangible net worth (times)	0.9	1.2	
Total debt/OPBDIT (times)	2.8	3.3	
Interest coverage (times)	4.5	3.9	

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

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
					Mar 11,2024	Dec 20, 2022	-	-
1	Long-term fund-based limit – Term loan	Long term	254.00	165.67	[ICRA]A- (Stable)	[ICRA]A(Stable)	-	-
2	Long-term fund-based limit – Cash credit	Long term	260.00	-	[ICRA]A- (Stable)	[ICRA]A(Stable)	-	-
3	Short-term fund/non-fund-based limit – Others	Short term	69.61	-	[ICRA]A2	[ICRA]A2+	-	-
4	Short-term non-fund based – Other	Short term	137.69	-	[ICRA]A2	[ICRA]A2+	-	-
5	Long term/ Short term unallocated Limits	Long term/ Short term	3.70		[ICRA]A- (Stable)/ [ICRA]A2	[ICRA]A(Stable)/ [ICRA]A2+	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term fund-based limit – Term loan	Simple
Long-term fund-based limit – Cash credit	Simple
Short-term fund/non-fund-based limit – Others	Simple
Short-term non-fund based – Other	Simple
Long term/Short term unallocated limits	NA

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	**Long-term fund-based limit – Term loan**	**NA***	**NA**	**FY26 - FY28**	254.00	[ICRA]A-(Stable)
NA	**Long-term fund-based limit – Cash credit**	**NA**	**NA**	**NA**	260.00	[ICRA]A-(Stable)
NA	**Short-term fund/non-fund - based limit – Others**	**NA**	**NA**	**NA**	69.61	[ICRA]A2
NA	**Short-term non-fund based – Other**	**NA**	**NA**	**NA**	137.69	[ICRA]A2
NA	**Long term/Short term unallocated limits**	**NA**	**NA**	**NA**	3.70	[ICRA]A-(Stable)/[ICRA]A2

*Source: Company; *Not available*

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

Annexure II: List of entities considered for consolidated analysis

Firm	Ownership	Consolidation Approach
Dhara Fine Chem Industries	90%	Equity Method
Neogen Ionics Limited*	100%	Full Consolidation
Buli Chemicals India Private Limited	100%	Full Consolidation

**Only projected financials of this entity have been considered in the analysis*

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About ICRA Limited:

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