

November 29, 2022

## Himadri Speciality Chemical Limited: Ratings reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund based – Term loan	162.30	115.00	[ICRA]A+(Stable); reaffirmed
Long-term– Fund based	290.00	320.00	[ICRA]A+(Stable); reaffirmed
Long-term unallocated limits	239.56	70.86	[ICRA]A+(Stable); reaffirmed
Long-term/short-term – Non-fund based	644.00	780.0	[ICRA]A+(Stable)/[ICRA]A1; reaffirmed
Long term/short term – Fund based/non-fund based	480.00	530.0	[ICRA]A+(Stable)/[ICRA]A1; reaffirmed
Commercial paper	300.00	300.00	[ICRA]A1; reaffirmed
<b>Total</b>	<b>2,115.86</b>	<b>2,115.86</b>	

\*Instrument details are provided in Annexure-I

### Rationale

The reaffirmation of the ratings continues to factor in Himadri Speciality Chemical Limited's (HSCL) long track record, large scale and the backward integrated nature of manufacturing operations. Further, HSCL has strong market position in domestic coal tar pitch (CTP) and carbon black (CB) businesses with established relationships with customers and suppliers. The ratings also favourably factor in the diversified products of the company, which find usage in the aluminium, graphite, dyes, tyres, paints and other chemical-related product manufacturing industries.

ICRA notes that the company's 5-lakh-metric-tonne-per-annum (MTPA) coal tar distillation plant is the largest in India that produces CTP of various grades and naphthalene for further processing into sulphonated naphthalene formaldehyde (SNF) and is integrated with CB manufacturing lines and a 20-MW power plant. The company's capital structure is comfortable and is likely to remain so with expected strong cash accruals from the business and allotment of share warrants. However, any large capex would remain a key monitorable and ICRA will continue to monitor the developments in this regard.

In August 2022, HSCL allotted 7.25 crore share warrants at a price of Rs. 70 each on preferential basis, aggregating to Rs 507.85 crore, to the company's promoter/promoter group and certain identified non-promoter persons/entity. Each warrant, so allotted, is convertible into or exchangeable for one fully paid-up equity share of the HSCL, within 18 months from the date of allotment of warrants.

The ratings are, however, constrained by the moderation in HSCL's debt protection metrics due to the decline in its operating margins in FY2022 and FY2021 owing to reduced spreads between raw material costs and end-product realisations. While a sequential improvement in EBITDA/MT in the last three quarters ended Q2 FY2023 improved the OPM in H1 FY2023, it remains subdued at 8.9% (5.9% in FY2022). The company's ability to improve its operating profits through an improvement in the EBITDA/MT contribution and increase in the production of specialty carbon black remains a key rating monitorable.

The ratings remain constrained by the cyclical nature in the company's user industries viz. aluminium and steel manufacturing, foreign exchange fluctuation risk and the weak financial position of its overseas subsidiaries.

ICRA further notes that as per HSCL's disclosure, two promoter groups of the Company entered into the Family Settlement Agreement to inter alia, amicably settling all past issues between them. Pursuant to the realignment, Mr. Anurag Choudhary as its Managing Director and CEO will continue to manage and control the Company and the other promoter group will cease to hold any right in the management and/or control in the Company.

The Stable outlook on the long-term rating reflects ICRA's expectations that HSCL will continue to benefit from its established track record, large scale of operations and a healthy demand outlook for its products.

## Key rating drivers and their description

### Credit strengths

**Large scale of integrated operations** – HSCL’s scale of operation is large and integrated, starting from coal tar distillation to manufacturing of various carbon-based products and power generation. The company has achieved total sales volume of 205,731 MT in H1 FY2023 and 371,974 MMT in FY2022 compared to 341,931 MMT in FY2021.

**Dominant status as operator of the single-largest coal tar distillation unit in India** – HSCL operates the largest coal tar distillation plant in India. The company enjoys competitive advantage due to its large scale of operations compared to other entities in the business.

**Strong market position in domestic coal tar pitch and carbon black businesses** – The company has a strong market position in the domestic coal tar pitch and carbon black businesses with established relationships with its customers and suppliers. It has the largest market share in the coal tar pitch business and has the third-largest market share in the carbon black business<sup>1</sup>. Further, it has an established track record of more than two decades in CTP manufacturing and more than a decade in CB manufacturing.

**Comfortable capital structure** – The capital structure continues to be comfortable, indicated by a gearing of 0.6 times and TOL/TNW of 0.9 times as on September 30, 2022, though the same has moderated in the last two years. The rising input cost has increased the working capital requirement, resulting in higher utilisation of working capital limits and moderation in capital structure. However, with expected strong cash accruals from the business and allotment of warrants, the company’s capital structure is likely to remain comfortable, going forward.

### Credit challenges

**Subdued profitability and debt coverage indicators** – The operating profitability and debt protection metrics were subdued in FY2021 and FY2022 due to a decline in operating margins owing to the reduced spreads between raw material costs and end-product realisations. While a sequential improvement in EBITDA/MT in the last three quarters ended Q2 FY2023 has improved the OPM in H1 FY2023, it remains subdued at 8.9% (5.9% in FY2022). HSCL’s coverage indicators remain subdued, indicated by total debt/OPBDIT of 3.5 times, interest coverage of 5.8 times and NCA/total debt of 15.4% in H1 FY2023 due to subdued OPM and higher working capital borrowing. Further, the company’s RoCE continued to be low in FY2022 and H1 FY2023.

The company’s ability to improve its operating profits through an improvement in the EBITDA/MT contribution and increase in the production of specialty carbon black remains a key rating monitorable.

**Exposed to business cycles** – More than 50% of HSCL’s sales volume are derived from the cyclical aluminium and graphite electrode industries, which expose its cash flows to business cycles. This results in variations in return indicators. Stability in business returns at a healthy level is a key rating sensitivity.

**Exposed to foreign exchange fluctuation risk** – The major raw material for CTP manufacturing is coal tar. For manufacturing CB, HSCL uses a mix of CBFS and carbon black oil (CBO). CBFS is a crude oil derivative and is mainly imported, exposing HSCL to forex risk. The risk is mitigated to a certain extent as it follows a hedging policy and derives revenue through exports, providing a natural hedge to an extent. However, HSCL continues to be net importer.

**Weak overseas subsidiaries** – The financial position of HSCL’s overseas subsidiaries are weak, which resulted in the company writing off a sizeable investment in these subsidiaries in FY2020.

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<sup>1</sup> HSCL -Investor Presentation and Media Release Q2 FY2023

## Environmental and social risks

Given the safety and environmental health-related concerns associated with chemicals, the industry is exposed to the risk of tightening regulatory norms for production, handling, disposal, and transportation of chemical products. Further, in the event of accidents, the litigation risks and the liabilities for clean-up could be high. While HSCL has a demonstrated track record of running its operations safely, the nature of the risk (being low frequency--high impact) weighs on its rating.

Further, operating responsibly is an imperative and instances of non-compliance with the environmental, health, and safety norms could have an adverse impact on the local community which could manifest in the form of protests, constraining the ability to operate or expand capacity. HSCL hasn't experienced/ reported any incidents suggestive of safety lapses in its manufacturing facilities over the past several years and its ability to maintain the manufacturing controls would be a monitorable.

## Liquidity position: Adequate

HSCL's liquidity is adequate with an average utilisation of 69% of its fund-based working capital limits against the drawing power in the last 12 months ended September 2022. The company has an annual debt repayment obligation of Rs. 39 crore in FY2023 and Rs. 45 crore in FY2024, which can be comfortably met through internal accruals. Given its limited long-term debt repayment obligations, along with no major debt-funded capex planned in the near to medium term, the company's overall liquidity position is likely to be adequate.

## Rating sensitivities

**Positive factors** – The ratings may be upgraded if a sustained improvement in EBDITA/MT and sales volumes results in healthy operating margins and improves the scale. A specific credit metric which may lead to an upgrade includes total debt/OPBDITA of less than 1.5 times on a sustained basis.

**Negative factors** – Pressure on the ratings could arise if a decline in volumes/margins and cash flows adversely impacts HSCL's financial metrics. A large debt-funded capital expenditure adversely affecting the company's financial metrics may also result in a downgrade. A specific credit metric which may lead to a downgrade includes interest coverage of less than 5 times on a sustained basis.

## Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Entities in the Chemical Industry</a> <a href="#">Consolidation and Rating Approach</a>
Parent/Group support	Not Applicable
Consolidation/Standalone	The ratings are based on the consolidated financial profile of the company. As on March 31, 2022, the company had one operating overseas subsidiary and one stepdown subsidiary, which have been enlisted in Annexure 2. Given the accumulated losses in the books of the subsidiaries, HSCL wrote off its investments in these companies in FY2020.

## About the company

HSCL is an integrated manufacturer of various carbon-based products starting from coal tar. The company operates a 5,00,000-MTPA coal tar distillation unit in West Bengal. Various distillates of the plant are used to manufacture coal tar pitch (CTP), various types of carbon blacks (CB), sodium naphthalene formaldehyde (SNF) and other advanced carbon-based materials. The coal tar distillation unit is the single-largest such facility in India and the company commands a leading position in the domestic CTP and CB markets.

## Key financial indicators

Consolidated	FY2021	FY2022	H1 FY2023*
<b>Operating income</b>	1,680.8	2,792.3	2,105.6
<b>PAT</b>	47.3	39.1	74.4
<b>OPBDIT/OI</b>	7.9%	5.9%	8.9%
<b>PAT/OI</b>	2.8%	1.4%	3.5%
<b>Total outside liabilities/Tangible net worth (times)</b>	0.6	0.9	0.9
<b>Total debt/OPBDIT (times)</b>	5.5	3.6	3.5
<b>Interest coverage (times)</b>	4.0	4.6	5.8

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; Total assets and net worth exclude revaluation reserves; Note: Amount in Rs. crore; All calculations are as per ICRA Research; \* Provisional

**Status of non-cooperation with previous CRA:** Not applicable

**Any other information:** None

## Rating history for past three years

Instrument	Type	Current rating (FY2023)		Chronology of rating history for the past 3 years					
		Amount rated (Rs. crore)	Amount outstanding (Rs. crore) as on Sep 30, 2022	Date & rating in FY2023	Date & rating in FY2022		Date & rating in FY2021		Date & rating in FY2020
				Nov 29, 2022	Nov 23, 2021	Aug 24, 2021	Oct 23, 2020	Oct 5, 2020	Oct 14, 2019
1 <b>Term loans</b>	Long-term	115.0	115.0	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	
2 <b>Fund-based bank facilities</b>	Long-term	320.0	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	
3 <b>Non-fund based bank facilities</b>	Long-term and short term	780.0	-	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]AA- (Negative)/ [ICRA]A1+	[ICRA]AA- (Negative)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	
4 <b>Fund based/ Non-fund based bank facilities</b>	Long-term and short term	530.0	-	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	-	-	-	
5 <b>Commercial paper</b>	Short Term	300.0	-	[ICRA]A1	[ICRA]A1	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	
6 <b>Unallocated</b>	Long-term	70.86	-	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]AA- (Negative)	-	-	
7 <b>Non-convertible debenture</b>	Long-Term	-	-	-	-	[ICRA]AA- (Negative) Withdrawn	[ICRA]AA- (Negative)	[ICRA]AA- (Stable)	

## Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term Fund-based – Term Loan	Simple
Fund Based	Simple
Non Fund Based	Very Simple
Fund based/Non-fund based	Simple/ Very Simple

Commercial Paper	Very 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 I: Instrument details**

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan-I	Oct 2020	NA	Sep 2024	65.0	[ICRA]A+(Stable)
NA	Term Loan-II	Sep 2021	NA	Sep 2026	50.0	[ICRA]A+(Stable)
NA	Fund based working capital	NA	NA	NA	320.0	[ICRA]A+(Stable)
NA	Non-Fund based working capital	NA	NA	NA	780.0	[ICRA]A+(Stable)/[ICRA]A1
NA	Fund based/Non-fund based working capital	NA	NA	NA	530.0	[ICRA]A+(Stable)/[ICRA]A1
*	Commercial paper	NA	NA	NA	300.0	[ICRA]A1
NA	Unallocated limits	NA	NA	NA	70.86	[ICRA]A+(Stable)

Source: Company; \* Not placed as on September 30, 2022

**Annexure II: List of entities considered for consolidated analysis**

Company Name	HSCL Ownership	Consolidation Approach
Himadri Speciality Chemical Limited	100.00% (rated entity)	Full Consolidation
AAT Global Limited	100.0%	Full Consolidation
Shandong Dawn Himadri Chemical Industry Limited	94.0%	Full Consolidation

Source: HSCL annual report

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