September 04, 2017

National Fertilizers Limited

Summary of rated instruments

Instrument*	Rated Amount (Rs. crore)	Rating Action
Long Term-CC Limits	4000.00	[ICRA]AA(Stable) reaffirmed
Term Loan	788.00 (reduced from Rs 1600.39 crore earlier)	[ICRA]AA(Stable) reaffirmed
Short term- Non Fund Based facilities	1500.00 (increased from Rs. 1325.00 crore earlier)	[ICRA]A1+ reaffirmed
Commercial Paper^	4000.00	[ICRA]A1+ reaffirmed
Short Term limits-Unallocated	637.39 (increased from nil)	[ICRA]A1+ reaffirmed
NCD	Rs 40.16 crore	[ICRA]AA(Stable) withdrawn

**Instrument details are provided in Annexure-1*
^ CP programme has been carved out of the long term fund based facilities and total utilization of CP and ICD combined should not exceed the sanctioned limits for long term fund based facilities

Rating action
ICRA has reaffirmed the rating of [ICRA]AA (pronounced ICRA double A)[1] for Rs. 4000 crore long term fund based facilities and the Rs. 788 crore term loans (reduced from Rs. 1600.39 crore earlier) of National Fertilizers Limited (NFL). The rating of [ICRA]A1+ (pronounced ICRA A one plus)[2] has been reaffirmed for Rs. 1500 crore short term non-fund based limits (increased from Rs. 1325 crore earlier), Rs. 637.39 unallocated short term loans (increased from nil earlier) and Rs. 4000 crore commercial paper programme of NFL. ICRA has also withdrawn the rating of [ICRA]AA(Stable) for the Rs. 40.16 crore NCD programme of NFL. The outlook on the long-term rating is Stable.

Rationale
The ratings factor in the company's established position as the second largest manufacturer of urea in India with a share of over 16% of the total domestic capacity and 13% market share, stable cash flow from urea operations, increasing contribution from industrial products & traded goods, the large sovereign ownership and management strength resulting in strong financial flexibility, as reflected by the company's proven ability to raise funds at competitive rates. Besides, the fact that almost the entire debt of the company is backed by receivables from the Government of India leads to low risks from the credit perspective. The ratings also factor in the company's leading market position in markets in northern and central India due to proximity of plants to key markets and healthy operating efficiency of the plants post the feedstock conversion program undertaken in FY2013, with healthy capacity utilisation levels and energy efficiency vis-a-vis the pre-set norms. While gas pooling has rationalised gas prices, the New Urea Policy 2015 has incentivised production beyond re-assessed capacity thereby aiding the margins of the company. Besides, increase in IPP based cap on realisation for production beyond RAC also aided profitability in FY2017. In FY2017, NFL achieved its highest ever urea production of 3.81MMT. The company also scaled up its portfolio of traded fertilizer mainly di-ammonium phosphate (DAP), bentonite sulphur along with industrial products like nitric acid, ammonium nitrate, odium Nitrate/

[1] *100 lakh = 1 crore = 10 million*
[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

Nitrite etc. which aided profitability during FY2017. However, increase in employee costs owing to wage revision and higher marketing expense on account of higher discounts etc. nearly offset the increase in profitability during the year.

The ratings also factor in the vulnerability of profitability to regulatory policies and agro-climatic conditions, sensitivity of cash flows to delays in subsidy receipts by the GoI, which result in elevated debt levels and interest costs for the company and the modest financial risk profile of the company characterised by high gearing and modest coverage indicators. However a favourable policy environment and reduction in debt levels (owing to lower outstanding subsidy receivables from GoI over the year) along with change in borrowing mix resulted in reduction in interest costs and improvement in profitability in FY2017 which should sustain going forward given the weak outlook for gas prices and reduction in subsidy for NPK fertilizers. During FY2017, GoI amended the policy linked to realisations for production of urea beyond RAC and increased the IPP Linked cap by nearly $15/MT which improved contributions for production beyond RAC. Department of Fertilisers was also given autonomy in a scenario of further decline in international urea prices. These steps should protect domestic urea production beyond RAC.

ICRA notes that NFL has planned a capex of nearly Rs. 2000 crore over next two to three years which includes the energy efficiency capex related to NUP-2015, setting up of a Di-Nitrogen Tetroxide manufacturing plant at Vijaipur-I, extension of height of prilling towers along with the maintenance capex. As per the NUP 2015, these plants need to reduce their energy consumption levels to 6.5 Gcal/MT by FY2019. In order to achieve energy norms pursuant to NUP-2015, NFL will be incurring a capex of around Rs. 700 crore for Nangal, Bhatinda and Panipat, and another Rs. 220 crore for Vijaipur-I & II. The capex will funded mostly by debt. The returns from the energy saving projects will remain contingent on government policy/support, which is yet to be clarified, and will remain a key rating sensitivity going forward. NFL is also setting up a Di-Nitrogen Tetroxide plant at its Vijaipur complex, which will supply exclusively to ISRO and is expected to be commissioned by FY2020.

ICRA also notes that the company is a joint venture partner (26% stake) for the Ramagundam urea project. Given the significant capital outlay for the project, the equity investment for the project will lead to cash outflows from NFL in the medium term. By end of august 2017, NFL has contributed nearly Rs 219 crore out of the total Rs 342 crore of equity contribution to be made. Returns on the equity investment for NFL may remain weak in the initial years after project execution, while the significant debt undertaken for the project is being repaid, although the company's urea market share will improve. Besides, such highly capital intensive project entails significant project execution risks, although the risk is limited for NFL to the extent of its share in the JV.

Key rating drivers

Credit strengths

- **Second largest urea manufacturing capacity; third in market share in urea:** With nearly 3.57 MMT of urea production capacity NFL is second only to IFFCO in the country. The Company has been able to maintain healthy capacity utilisation levels for all its plants and stands third in market share (~13%) for sales of urea in the country after IFFCO and KRIBHCO (KRIBHCO along with KSFL). NFL has a vast marketing network comprising of dealers, cooperative societies and institutional agencies spread over 17 states in India. The company sells its urea through a network of 2,000 dealers, state marketing federations and cooperative societies. Sales through these institutions have increased through cooperatives and markfeds rather than through private dealers in recent years.
- **Large sovereign ownership and the resulting strong financial flexibility; proven ability to raise funds at competitive rates due to parentage and management strength:** NFL benefits from the large GoI ownership, 74.71% presently, as it is able to raise funds at very competitive rates aiding its profitability as interest charges remain low.
- **Favourable demand-supply scenario of urea in India; though urea sales declined 7% during FY2017 owing to neem coating and weak monsoons in parts of the country, the demand remains healthy:** Nearly 19% of urea was imported in FY2017 owing to the gap in supply demand for urea. With significant price differential between urea and non-urea fertilisers, the demand for urea remains robust. With significant import dependence for urea the demand for indigenously produced urea remains favourable.
- **Improving product mix with increasing share of contribution from Traded Goods and Industrial products:** NFL has been expanding its industrial product portfolio leading to increasing contribution of the same to profitability. The company has successfully ventured in trading of imported and domestic fertilisers and other traded goods in FY2017 and which has aided to the profitability of the company. The change in product mix overtime will result in lower dependence on urea for profitability. NFL is also setting up a Di-Nitrogen Tetroxide plant for ISRO, which will also increase profitability once production begins in FY2020.
- **Healthy operating efficiency of the plants post the Ammonia Feedstock conversion Project (AFCP) capex programme:** Post the feedstock conversion project undertaken for Nangal, Bhatinda and Panipat in FY2013, the energy efficiency against pre-set norms and the capacity utilisation for the plants has remained healthy and has aided profitability of the company.

Credit weaknesses

- **Vulnerability of profitability to agro-climatic conditions, regulatory risks and seasonality of the fertiliser business:** Agriculture sector in India remains vulnerable to the vagaries of monsoon as the area under irrigation remains low which exposes fertiliser sector's sales and profitability to volatility. The sector being highly regulated also remains vulnerable to changes in the regulations by GoI.
- **Sensitivity of cash flows to delays in subsidy receipts from GoI; delays in subsidy flows from GoI have led to high interest costs and adversely impacted profitability in recent years:** Subsidy inflow from GoI had remained outstanding for nearly 5-6 months during last few years which has impacted the cash flows of the fertiliser companies. In order to fund the delay in subsidy receipts companies have to avail working capital borrowings leading to large interest costs which impact profitability of the companies.
- **Investments to meet NUP-2015 norms may not be remunerative and may lead to weakening of credit metrics unless GoI provides support:** NFL plans to incur a capex of around Rs. 950 crore for all its five plants to achieve pre-set norms under NUP-2015 from FY2019 onwards. The returns from

the energy saving projects will remain contingent on government policy/support which is yet to be clarified.

- **Moderate financial risk profile characterised by high gearing levels on account of the feedstock conversion project:** NFL had undertaken feedstock conversion project for its three plants at Nangal, Bhatinda and Panipat which had been funded largely through debt. As a result the gearing levels and other credit metrics had remained weak owing to delay in receipt of capital subsidy in FY2015 and FY2016. However, since then capital subsidy receipts have improved which has resulted in repayment of term loans and moderation in gearing.

  Significant increase in gas costs may dent profitability for production beyond RAC; recent policy measures may however protect production beyond RAC: Contribution from production beyond RAC directly depends on the international urea prices and the gas costs. In case there is significant increase in gas costs the contribution from production beyond RAC may witness downward pressure. However, recent policy measures by GoI to increase IPP based cap for production beyond RAC and autonomy to DoF in safeguarding production beyond RAC by taking steps as deemed necessary should act as a safeguard for the domestic urea industry.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:
Corporate Credit Rating Methodology
Rating Methodology for fertiliser industry
Commercial paper rating methodology

About the company:

Incorporated in 1974, National Fertilizers Limited (NFL) is a public sector, Mini Ratna undertaking, primarily engaged in the manufacture of urea. The company's operations are spread across five units, one each in Nangal and Bhatinda (Punjab), and Panipat (Haryana), and two units at Vijaipur (MP). NFL commenced operations by setting up two FO/LSHS based urea units at Bathinda (Punjab) and Panipat (Haryana) in 1979. Subsequently, as part of the reorganisation of public sector fertiliser companies, the Nangal (Punjab) unit of Fertilizer Corporation of India (FCI) came under the NFL fold. The company set up another urea plant at Vijaipur (Vijaipur-I), Madhya Pradesh in 1988 when the Hazira-Vijaipur-Jagdishpur (HVJ) gas transmission pipeline was set up. NFL undertook brownfield expansion of the Vijaipur plant (Vijaipur-II) in 1997. The Vijaipur units are gas-based, with the Vijaipur-II plant having dual feedstock ability (naphtha and gas). The other three units earlier used Furnace oil (FO) as feedstock, though they have now been converted to gas as mandated by the GoI.

NFL has a combined urea production capacity of 3.57 MMTPA as on date (increased from 3.21 MMTPA prior to FY2013), making it the second largest producer of urea in the country. The GoI divested 7.64% holdings in NFL bringing down its stake to 90% in July 2013 to meet the norms laid down by the SEBI for public sector undertakings. GoI further reduced its stake by 15% in August 2017 through an Offer for Sale (OFS).

While ~88% of the company's revenues come from urea, it manufactures / trades in other products such as bio-fertilisers, trading and bulk industrial products such as Nitric Acid, Ammonium nitrate, Sodium Nitrate / Nitrite, Anhydrous Ammonia, etc. The traded products include city compost, certified seeds, agrochemicals and other chemical fertilisers like Muriate of Potash (MOP), DAP, etc.

In FY2017, the company reported net profit of Rs. 208 crore on an operating income of Rs. 7,624 crore against net profit of Rs. 198 crore on an operating income of Rs. 7,771 crore in FY2016.

Key Financial Indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	7771	7624
PAT (Rs. crore)	198	208
OPBDIT/ OI (%)	7.1%	7.4%
RoCE (%)	6.1%	7.5%
Total Debt/ TNW (times)	6124	4135
Total Debt/ OPBDIT (times)	10.9	7.3
Interest coverage (times)	2.4	3.0
NWC/ OI (%)	48%	25%

OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress);
NWC: Net Working Capital

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No.	**Instrument**	**Current Rating (FY2018)**			**Chronology of Rating History for the past 3 years**		
		Type	**Amount Rated (Rs. crore)**	**Date & Rating**	**Date & Rating in FY2017**		**Date & Rating in FY2016**
				Sept 2017	**September 2016**	**July 2016**	**August 2015**
1	Term Loan	Long Term	788.0	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable) assigned
2	Fund based limits*	Long term	4,000	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA (Stable) assigned
3	Non-fund based limits	Short term	1500	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+ assigned
4	Commercial Paper*	Short Term	4000	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+ assigned
5	Unallocated	Short term	637.39	[ICRA]A1+		[ICRA]A1+	
6	NCD	Long Term	40.16	[ICRA]AA (Stable) withdrawn	[ICRA]AA (Stable)	[ICRA]AA (Stable)	-

Complexity level of the rated instrument:
ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1
<u>Instrument Details</u>

ISIN No	Instrument	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
-	Term Loan-1	June 2010	10.40%	March 2018	578.00	[ICRA]AA(Stable)
-	Term Loan-2	January 2016	-	September 2020	210	[ICRA]AA(Stable)
-	Fund Based- Long Term facilities*	-	-	-	4000.00	[ICRA]AA(Stable)
-	Non Fund Based- Short Term facilities	-	-	-	1500.00	[ICRA]A1+
-	Commercial Paper*	-	-	-	4000.00	[ICRA]A1+
-	Unallocated- Short Term	-	-	-	637.39	[ICRA]A1+
INE870D07035	NCD	September 2011	9.42%	September 2016		[ICRA]AA(Stable) withdrawn

Source: The company
** CP programme has been carved out of the long term fund based facilities and total utilization of CP and ICD combined should not exceed the sanctioned limits for long term fund based facilities*

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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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