ICRA

January 29, 2021

Ultramarine and Pigments Ltd: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – Fund-based	7.50	7.50	[ICRA]A+(Stable); reaffirmed
Short-term – Non-fund based	6.00	6.00	[ICRA]A1+; reaffirmed
Long-term – Unallocated	1.50	1.50	[ICRA]A+(Stable); reaffirmed
Total	**15.00**	**15.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation takes into consideration the experience of the promoters and Ultramarine and Pigments Ltd's (UPL) track record as an established manufacturer of ultramarine blue pigments and a range of surfactants. The company's financial risk profile continues to remain healthy as reflected by strong liquidity position and comfortable capital structure as on March 31, 2020 on account of sustained cash accruals and low external funding. Its profitability continued to improve in FY2020 and H1 FY2021 primarily due to improved profitability in its ITES and pigment segments. Further, the ratings factor in UPL's strategic equity investments in Thirumalai Chemicals Ltd, which provides financial flexibility.

The ratings, however, continue to remain constrained by the company's moderate scale of operations in both of its key business segments – pigments and surfactants, and product concentration risk in the pigments segments with presence predominantly in a single product line – ultramarine blue. UPL's revenue growth has been stagnant in FY2020 and had declined in H1 FY2021 on account of the economic slowdown and the pandemic-led lockdown. Nonetheless, with the new capacity addition in surfactant segment, the scale in that segment is expected to improve over the medium term. Also, managing volatility in raw material prices is a key challenge for the company owing to the stiff competition in the surfactant segment.

The Stable outlook on the rating reflects ICRA's opinion that UPL will continue to benefit from the extensive experience of its promoters, strong market position in pigments as well as surfactant segments and its healthy financial profile.

Key rating drivers and their description

Credit strengths

Established presence in ultramarine blue pigments industry – UPL commenced operations in 1961 and is currently one of the largest manufacturers of ultramarine blue pigment in India. Ultramarine blue pigment has diverse application with high-grade pigments used in industries such as plastics, paints, coatings, cosmetics, foods, detergents, etc. The lower grade pigments are primarily used for whitewashing and laundry applications. With significant presence in export markets, in addition to the established customer base in the domestic market, the segment has limited geographical and customer concentrations risks.

Established presence and long-standing customer relationship in surfactant industry – UPL is among the key suppliers of surfactants to detergent manufacturers, including some of the large multinational FMCG players, in South India. The company has been catering to these large FMCG participants over the years and its established relationship has aided in maintaining steady growth in revenues in this segment.

Strong liquidity position and low reliance on external debt – The company maintains a conservative capital structure policy with any capital expenditure being predominantly funded by internal accruals in the past. It had availed term loan during FY2020 to fund the capex, which resulted in marginal increase in capital structure. Nonetheless, the gearing remained robust at 0.1 times as on September 30, 2020. In addition, with significant cash accruals over the years, UPL had a healthy liquidity position with cash and cash equivalents of around Rs. 67.3 crore as on September 30, 2020. In addition, the company has fund-based facilities totalling to Rs. 7.5 crore, which remain largely unutilised. These factors provide comfort on the financial flexibility of the company. UPL also has 19.97% strategic shareholding in Thirumalai Chemicals Ltd, with the investment valued around Rs. 156.1 crore as on September 30, 2020.

Healthy profitability and strong coverage metrics – The company has maintained its operating margins at healthy levels of over 20% since FY2018. The operating margins further improved in FY2020, supported by higher revenue from ITES segment, which grew by 13% during the period. Despite a decline in revenue from ITES segment in H1 FY2021, its profitability remained healthy, backed by favourable realisation in pigment segments. The coverage indicators have moderated due to increase in financial expense since FY2020. Nonetheless, the same remained healthy with interest coverage, Total Debt/OPBDITA and DSCR at 68.8 times, 0.4 times and 61.7 times in FY2020 against 119.1 times, 0.0 times and 100.0 times in FY2019.

Credit challenges

Moderate scale of operations and high product concentration – The company has a moderate scale of operations in both the pigment and surfactant segments, resulting in limited operational flexibility. UPL's operation in the pigment segment is characterised by low product diversification and competition from entrenched global players. Its revenue in this segment is primarily dependent on ultramarine blue pigments with limited revenue from other pigments. While the company is making efforts to develop new products, successful induction and market development for such products, resulting in meaningful diversification of revenue streams, remains to be seen.

Similarly, low value addition in the surfactant segment, moderate scale of operations and intense competition restrict the pricing flexibility for the company. However, with the new capacity addition in the surfactant segment, which had commenced production from January 2020, the scale in that segment is expected to improve over the near-term. The end-user product for the segment – detergents – is a consumer commodity with low demand growth. Hence its scope for improving scale of operations and profitability remain limited, despite increasing preference of its products. These apart, ICRA notes the project risk arising out of the proposed capital expansion in its wholly-owned subsidiary. UPL's ability to successfully commission the project and increase its scale and revenues remains to be seen.

Stagnant top line in FY2020 and decline in revenue in H1 FY2021 – In FY2020, the pigments and surfactant segments witnessed a marginal decline in revenue due to reduction in sales volume and price realisation, respectively. Further, loss of sales in Q4 FY2020 on account of the lockdown impacted the sales volume. However, the decline in manufactured segment was offset by revenue from ITES segment, which grew by 13% in FY2020, resulting in a stagnant top line during the year. In H1 FY2021, the manufacturing and ITES revenue dipped on a YoY basis by 5% and 31%, respectively, driven by the lockdown and economic slowdown. With recovery in demand witnessed since Q3 FY2021 and commencement of operation in the new surfactant plant from Q4 FY2021, the full-year manufacturing sales revenue is likely to be in line with the previous year, while the ITES segment revenue is expected to moderate.

Vulnerability of profitability to any adverse fluctuation in raw material prices and forex – UPL's operating margins remain exposed to raw material price fluctuation. Any adverse movement in the price of raw materials, especially in the surfactant segment, could have an adverse impact on the profitability, considering the limited ability to pass on the price hike owing to the stiff competition. The operations are also exposed to the forex fluctuation risk. However, the same is mitigated partly by presence of exports operating as a natural hedge and forex hedging.

Liquidity position: Strong

The company has external term loan of Rs. 31.0 crore as on September 30, 2020, of which Rs. 2.1 crore is expected to be repaid in FY2022. Its free cash flows have primarily remained positive, resulting in positive cash accretion, which has been invested in mutual funds. The liquidity position remains **strong** with cash and liquid investment of Rs. 48.6 crore as on March 31, 2020 and Rs. 67.3 crore as on September 30, 2020. It also has comfortable buffer in working capital limits (Rs. 7.5 crore) from the banks, which remain unutilised.

Rating sensitivities

Positive factors – ICRA may upgrade the ratings if there is a significant improvement in the scale of operations, supported by the product diversifications, while maintaining a healthy capital structure, coverage indicators.

Negative factors – Downward pressure on the ratings could emerge if there is a sustained decline in the revenue and profitability or a stretch in the working capital cycle, which along with the planned debt-funded capex, results in the weakening of the credit profile. Specific credit metrics that may lead to a downgrade include TD/OPBDITA more than 1.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Chemical Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on consolidated financial profile of the company. The details of consolidation is provided in Annexure 2.

About the company

Established in 1960, Ultramarine & Pigments has its manufacturing facilities at Ambattur, Chennai and Ranipet in North Arcot, Tamil Nadu. It is one of the major manufacturers of ultramarine blue pigments and surfactants in India. The company also manufactures detergent powder/liquid (under the brand name OOB) and other inorganic pigments in smaller scale. Besides, it has an ITeS/BPO division with specialisation primarily in content management, publishing, hospital billing services, etc. UPL also earns small revenue from its windmill division. It has a capacity 6,000 MTPA in the pigments segment and 68,000 MTPA in the surfactant segment. The company incorporated a wholly-owned subsidiary, Ultramarine Speciality Chemicals Limited, in December 2019 to expand its pigment production segment. The production facility is expected to be set up in FY2022-FY2023.

Key financial indicators (audited)

UPL Consolidated	FY2019	FY2020	6M FY2021*
Operating Income (Rs. crore)	306.9	306.2	143.3
PAT (Rs. crore)	56.5	62.0	27.2
OPBDIT/OI (%)	23.5%	24.8%	28.7%
RoCE (%)	17.7%	22.6%	20.9%
Total Outside Liabilities/Tangible Net Worth (times)	0.1	0.3	0.2
Total Debt/OPBDIT (times)	0.0	0.4	0.4
Interest Coverage (times)	119.1	68.8	108.1
DSCR (times)	100.0	61.7	22.3

**Published provisional 6M FY2021 results*

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); DSCR: (PBIT + Mat Credit Entitlements - Fair Value Gains through P&L - Non-cash Extraordinary Gain/Loss)/(Interest + Repayments made during the Year)

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Sep 30, 2020 (Rs. crore)	Date & Rating in	Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
					Jan 29, 2021	Jul 31, 2019	-	Jan 11, 2018
1	Cash credit facility	Long-term	7.50	0.0	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	-	**[ICRA]A+ (Stable)**
2	Non-fund based facility	Short-term	6.00	-	**[ICRA]A1+**	**[ICRA]A1+**	-	**[ICRA]A1**
3	Unallocated facility	Long-term	1.50	-	**[ICRA]A+ (Stable)**	**[ICRA]A+ (Stable)**	-	**[ICRA]A+ (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 click here

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Cash credit facility	NA	NA	NA	7.50	[ICRA]A+ (Stable)
NA	Non-fund based facility	NA	NA	NA	6.00	[ICRA]A1+
NA	Unallocated facility	NA	NA	NA	1.50	[ICRA]A+ (Stable)

Source: *UPL*

Annexure-2: List of entities considered for consolidated analysis

Company Name	UPL Ownership	Consolidation Approach
Ultramarine Speciality Chemicals Limited	100.00%	Full Consolidation

Source: *UPL annual report FY2020*

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About ICRA Limited:

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