

April 14, 2022

National Fertilizers Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term-Fund Based Limits	4000.0	4000.0	[ICRA]AA-(Stable); reaffirmed
Term Loans	1,044.0	1,044.0	[ICRA]AA-(Stable); reaffirmed
Short Term-Non-Fund Based Facilities	3000.0	3000.0	[ICRA]A1+; reaffirmed
Commercial Paper^	4000.0	4000.0	[ICRA]A1+; reaffirmed
Total	8044.0	8044.0	

*Instrument details are provided in Annexure-1; the commercial paper program is carved out of the fund-based limits of the company

Rationale

The reaffirmation of the ratings for the credit lines of National Fertilizers Limited (NFL) factor in the leadership position in the fertiliser industry, improvement in the receivables cycle of the company owing to timely release of subsidy by the GoI in FY2022 and expectation of the same continuing in the future as well. The ratings also factor in the low demand risk for urea, healthy contribution from the sale of traded and industrial products, exceptional financial flexibility arising out of strategic importance to Government of India (GoI) and the large sovereign ownership. NFL's profitability moderated in 9M FY2022 owing to the losses posted in the urea segment, although the same was partially tempered by the increase in the profitability from the trading and industrial products segment. Urea operations posted losses as the actual energy consumption remained higher than the normative energy norms under the New Urea Policy-2015 (NUP-2015) as the implementation of Energy Savings Scheme (ESS) were delayed for all the plants. The ESS for all the units have been implemented in FY2022 and the energy consumption for all the plants is expected to remain lower than the normative norms thus aiding the profitability of the urea segment going forward. The trading portfolio also witnessed significant improvement in the profitability as periodic subsidy revisions under the Nutrient Based Subsidy (NBS) scheme undertaken by the Government of India (GoI) during the course of FY2022 supported improvement in the contribution levels. Thus, despite the decline in sales volume, the segment profitability witnessed improvement. The profitability of the segment in FY2023 hinges on the level of the subsidy rates to be announced under the NBS scheme for FY2023. ICRA expects GoI to announce the subsidy rates which will allow the company to make profit in line with the long-term trend. The industrial products segment has also witnessed significant uptick in profitability driven by higher sales volume and increased profitability on ammonium nitrate and nitric acid. The realization for ammonium nitrate had been on an uptrend since August 2020 post the Beirut blast and lower production in Europe amid elevated natural gas/ammonia prices while nitric acid prices have also firmed up driven by the increased input costs globally. As a result, NFL's contribution on sale of these products increased owing to access to relatively lower cost natural gas. Going forward, planned expansion of nitric acid capacity and setting up of agrochemical formulation plant should support NFL's profitability. The subsidy receipt from GoI remained timely in FY2022 post the clearance of the subsidy backlog in FY2021 which kept the working capital borrowings and the associated interest expense low during the year. As a result, the capitalization and coverage metrics remained better than last few years although lower operating profitability in FY2022 partially tempered the impact of improved subsidy inflow. The exceptional financial flexibility displayed by NFL in raising funds from the capital markets at short notice and highly competitive rates emanates from the large sovereign ownership and strategic importance for the GoI in ensuring the adequate fertiliser supply. NFL has PAN India Distribution and Sales network with three plants located in the most intensive fertilizers consuming states i.e. Punjab and Haryana.

NFL's main product i.e. urea faces low demand risk given the significant import dependence to meet the domestic demand. Despite planned capacity additions to the tune of ~6.4 MMTPA over the next 15 months, the import dependence for urea will remain significant leading to low demand risk for domestic urea manufacturers.

The ratings are constrained by the vulnerability of the profitability of the sector to the regulatory policies governing the sector formulated by the GoI. The downward revision in the energy norms as well as removal of the floor of Rs. 2300/MT on the fixed costs has resulted in lower profitability for urea operations for the entire urea industry. The profitability of the phosphatic fertilizer sellers depends on the NBS rates announced by the GoI which remains a key driver of the profitability of the P&K segment. The performance of the fertilizer sector also remains vulnerable to the vagaries of the monsoon as nearly 55% of the arable land is dependent on monsoons for irrigation. A weak monsoon for couple of seasons can severely impact the agricultural activity in a region and also impact the fertilizer offtake. The performance of the fertilizer sector also remains vulnerable to the timeliness of the subsidy from the GoI as significant delays lead to increase in working capital borrowings and associated interest costs.

NFL is a Joint Venture (JV) partner in Ramagundam Fertilisers Corporation Limited (RFCL) which has set up a 1.27 MMTPA urea plant at Ramagundam, Telengana. The plant had faced stabilization issues post its commissioning in March 2021 but has stabilized towards the end of FY2022. The plant is expected to achieve healthy capacity utilization in FY2023 which should enable the company to service its debt obligations comfortably. ICRA notes that NFL has provided a Letter of Comfort (LOC) backing a Rs. 500.0 crore unsecured loan availed by RFCL to meet cash flow mismatches in FY2022. While the LOC does not guarantee the repayment of principle of interest by NFL, any material cash outflow to support RFCL going forward will still remain a key monitorable.

ICRA also takes note of the GoI's intent to offload 20% stake in NFL through an Offer for Sale (OFS) which will bring down the sovereign ownership to 54.71%. While the GoI will continue to hold, majority stake in the company, any change in the philosophy for support to NFL and reduction of the ownership below 50% will remain a key monitorable.

NFL has also been nominated as a JV partner for setting up a 1.27 MMTPA urea unit in Assam at the facility of Brahmaputra Valley Fertiliser Corporation Limited (BVFCL) with an equity contribution of 28%. Currently, NFL had engaged Project Development India Limited (PDIL) for preparation for the techno-Economic Feasibility Report (TEFR). The proposal along with TEFR has been submitted to DoF and the same is under review. ICRA will assess the impact of the investment in the JV on the credit profile of the company as and when the details are finalized.

The Stable outlook on the long-term rating reflects ICRA's opinion that the company will continue to benefit from its leadership position in the fertiliser sector and its strategic importance to GoI.

Key rating drivers and their description

Credit strengths

Second largest urea manufacturer with nearly 16% domestic capacity share; Leading market position in urea, particularly in northern and central India- With nearly 3.57 MMT of urea production capacity, NFL is second only to IFFCO in the country. The company maintains healthy capacity utilisation levels for all its plants and stands second in the market share (~13% in 9M FY2022) for urea sales (including imported urea sold) in the country after IFFCO. NFL has a vast marketing network comprising dealers, cooperative societies and institutional agencies spread over twenty states in India. The company sells its urea through a network of 2,805 dealers, state marketing federations and cooperative societies.

Large sovereign ownership and the resulting strong financial flexibility; proven ability to raise funds at competitive rates due to parentage- 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. NFL has also received support from GoI in the past and ICRA expects GoI to provide support to NFL going forward as well as and when needed. GoI will be offloading 20% stake in NFL through an OFS, although currently no timelines have been specified for the same.

Improving product mix with rising contribution from industrial and other products in profitability- NFL sells ammonium nitrate and nitric acid under its industrial products segment and phosphatic fertilisers, compost, agrochemicals etc. under the trading segment. The company also sells seeds to farmers thus providing a gamut of farm related products. The contribution from the sale of industrial products has improved owing to higher realisations and higher volumes. The contribution from the trading portfolio has also increased over the years due to rising volumes and increase in the contribution margin in FY2021. The company is in the process of expanding its Nitric acid capacity by 270 Metric Ton per Day (MTPD) and also setting up an agrochemical formulation plant both of which are expected to be completed in mid of FY2023. Post the completion of these projects, the contribution from the sale of non-urea products is expected to rise further which will lend stability to the overall profitability of the company.

Favourable demand-supply scenario of urea in India- Import dependence for urea remains in the range of 25%-30% given the inadequate domestic capacity. With a significant price differential between urea and non-urea fertilisers, the demand for urea remains intact and is expected to grow at a stable rate of 1.5%-2% in the near to medium term although the growth/degrowth may move out of this range in few years. Thus, despite planned capacity additions in the range of 3.8 MMTPA over the course of next 6-10 months, the import dependence will remain significant going forward as well.

Expected improvement in urea operations post implementation of energy saving schemes to support cash generation- NFL completed implementation of the ESS schemes to meet the normative energy norms under the NUP-2015 for all its plants in FY2022. While in FY2022, the urea operations posted losses due to higher than normative energy consumption across all its plants, from FY2023 onwards with the actual energy consumption expected to remain lower than the normative norms, the urea operations are expected to witness improved cash generation. The company is also expected to earn healthy contribution on sale of the production beyond the re-assessed capacity which will also support cash generation.

Credit challenges

Vulnerability of profitability of the fertiliser sector to regulatory policies and agro-climatic conditions- The agricultural 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 the GoI.

Sensitivity of cash flows to the timeliness of subsidy release by the GoI- In the past fertiliser companies have witnessed significant cash-flow mismatches owing to the delay in the release of the subsidy by the GoI due to inadequate subsidy budgeting. The subsidy receipt from GoI remained timely in FY2022 post the clearance of the subsidy backlog in FY2021 which kept the working capital borrowings and the associated interest expense low during the year. Going forward the timeliness of the subsidy receipt from the GoI will remain a key monitorable.

Liquidity position: Adequate

The liquidity position of the company remains adequate given the availability of large working capital borrowing limits and availability of adequate drawing power coupled with large sovereign ownership which yields significant financial flexibility. The timely inflow of subsidy from the GoI in FY2022 and expectations of the same continuing forward will support the liquidity position of the company. The ongoing capex has been funded entirely through long term debt. With the decline in the interest outgo and expected improvement in the cash generation going forward coupled with no major capex plans, NFL's liquidity position remains adequate to meet its near term liabilities.

Rating sensitivities

Positive factors - The rating may be upgraded in a scenario of favorable outcome on the extension of the energy consumption norms for Nangal, Bhatinda and Panipat units. Favorable outcome for the reinstatement of the floor of Rs. 2300/MT of the fixed cost will also be a positive for the entity's rating. Sustained improvement in the credit profile of the company driven by healthy profitability and lower working capital borrowings will be a key positive for the rating.

Negative factors- Deterioration in the working capital cycle leading to receivable days of more than 180 days on a sustained basis may lead to a rating downgrade. Any deterioration in debt metrics owing to any large debt funded capex/investments or weak profitability will also put negative pressure on the ratings of the company. Additionally, reduction in GoI stake below 50%, weakening of the linkages with GoI and/or change in the support philosophy of GoI could lead to a downgrade.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Fertiliser sector Impact of Parent or Group Support on an Issuer's Credit Rating
Parent/Group Support	Parent: Government of India The ratings factor in the parentage from GoI and strategic importance of NFL for GoI given the company is a major fertiliser supplier in the country and ensures lower reliance on imported urea.
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the standalone financials of NFL.

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. These three plants subsequently shifted to natural gas based ammonia production. 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).

NFL has a combined urea production capacity of 3.57 MMTPA as on date, making it the second largest producer of urea in the country. The GoI currently holds 74.71% stake in the company. GoI is looking to divest 20% stake in NFL and through Department of Investment and Public asset management (DIPAM) has invited proposals from legal advisors, merchant bankers and brokers. GoI will be selling 20% stake in the company through an Offer for Sale.

Key financial indicators (audited)

NFL standalone	FY2020	FY2021	9M FY2022*
Operating Income (Rs. crore)	13,130.7	11,905.7	11,414.8
PAT (Rs. crore)	-171.0	249.6	60.0
OPBDIT/OI (%)	6.6%	7.9%	3.5%
PAT/OI (%)	-1.3%	2.1%	0.5%
Total Outside Liabilities/Tangible Net Worth (times)	6.6	2.9	
Total Debt/OPBDIT (times)	9.3	2.0	
Interest Coverage (times)	2.1	3.2	4.2

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation*Unaudited

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	FY2023				Chronology of Rating History for the past 3 years				
		Type	Amount Rated	Amount Outstanding as of Dec 31, 2021	Date & Rating in	FY2022	FY2021	Date & Rating in FY2020		
			(Rs. crore)	(Rs. crore)	14-Apr-22	6-Apr-21	-	27-Mar-20	14-Aug-19	26-Jun-19
1	Long Term-fund based Limit	Long Term	4,000.00	-	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	-	[ICRA]AA-(Stable)	[ICRA]AA (Negative)	[ICRA]AA (Stable)
2	Term Loans	Long term	1,044.00	718.1	[ICRA]AA-(Stable)	[ICRA]AA-(Stable)	-	[ICRA]AA-(Stable)	[ICRA]AA (Negative)	[ICRA]AA (Stable)
3	Short Term-Non Fund Based	Short Term	3,000.00	-	[ICRA]A1+	[ICRA]A1+	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Commercial Paper^	Short Term	4000	0.0	[ICRA]A1+	[ICRA]A1+	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
5	Short Term-Unallocated	Short Term	0.0	0.0	-	-	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

Amount in Rs. crore; ^: The commercial paper program is carved out of the fund-based limits of the company

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term-fund Based	Simple
Term Loans	Simple
Short Term-Non-fund Based	Simple
Commercial Paper	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 analyzing 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, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No.	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (RS Crore)	Current Rating and Outlook
-	Long Term-fund Based	-	-	-	4,000.00	[ICRA]AA- (Stable)
-	Term Loans	Jul-18	-	Mar-30	1,044.00	[ICRA]AA- (Stable)
-	Short Term-Non-fund Based	-	-	-	3,000.00	[ICRA]A1+
Unplaced	Commercial Paper [^]	-	-	-	4000.00	[ICRA]A1+

Source: Company; [^] The commercial paper program is carved out of the fund-based limits of the company

Annexure-2: List of entities considered for consolidated analysis-NA

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