

April 15, 2020 <sup>Revised</sup>

## Zuari Agro Chemicals Limited: Ratings upgraded

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	260.00	260.00	[ICRA]B (Stable); Upgraded from [ICRA]D
Long Term Fund Based	1000.00	1000.00	[ICRA]B (Stable); Upgraded from [ICRA]D
Long Term un-allocated limits	465.00	465.00	[ICRA]B (Stable); Upgraded from [ICRA]D
Short Term non-fund-based limits	1980.00	1980.00	[ICRA]A4; Upgraded from [ICRA]D
Short Term un-allocated	510.00	510.00	[ICRA]A4; Upgraded from [ICRA]D
Compulsorily convertible Debentures (CCD)	400.40	400.40	[ICRA]B (Stable); Upgraded from [ICRA]D
<b>Total</b>	<b>4615.40</b>	<b>4615.40</b>	

\*Instrument details are provided in Annexure-1

### Rationale

The ratings upgrade factors in account of regularisation of payment of debt obligations by Zuari Agro Chemicals Limited (ZACL) for a period of more than three months and operationalisation of the urea plant. After delaying payments for the Letter of Credits (LCs) beginning in April 2019, the company was unable to meet several of its debt obligations over the next eight months. However, the company had been regular in meeting all its debt obligations since the beginning of January 2020. The company was able to meet its dues by utilising nearly Rs. 274 crore of unsecured loans provided by the promoters, the release of the subsidy by GoI and collections from the market. The Company's plants remained shut for most of FY2020, with urea plants being operationalised in January 2020. Earlier, the gas supplier i.e. GAIL (India) Limited (GAIL, rated [ICRA]AAA(Stable)/[ICRA]A1+) had cut gas supplies as ZACL was unable to pay GAIL its dues for supply of natural gas. However, ZACL and GAIL entered into an arrangement whereby the urea subsidy would be deposited in an escrow account from which GAIL will be paid out its dues. As a result of this arrangement, GAIL has resumed gas supply leading to ZACL's plants becoming operational in January 2020. The NPK plants are expected to be operationalised towards the end of Q1 FY2021.. ICRA also takes note of the expected sale of 30% stake in Zuari Farm Hub Limited (ZFHL), a wholly owned subsidiary of ZACL to which the assets of Specialty fertilisers, retail, Crop protection & Cropcare business of ZACL have been transferred in March 2020. With the stake sale expected to be completed in Q1 FY2021, the proceeds from the stake sale will be used for deleveraging of the balance sheet of ZACL. Besides, there are other monetisation plans in progress including land parcel sale, possible sale of the fertiliser assets of ZACL which are expected to be completed over a period of next one year and would aid in deleveraging the balance sheet of the company. ICRA also notes that the company's plans for a about Rs 400 crore rights issue have been put on hold following weak market conditions.

The ratings continue to factor in the long and established track record of the company in the fertiliser and agri-business, strong market position in the states of Maharashtra & Karnataka, diversified product portfolio including urea, phosphatic and potassic fertiliser and favorable demand outlook for the fertiliser sector given the scarcity of nutrients in the soil.

The ratings are constrained by the weak financial risk profile of the company, vulnerability of profitability to agro-climatic conditions, intermittent plant operations due to liquidity issues, high-working capital intensity and exposure to foreign currency fluctuations given the company imports a substantial portion of its raw material and traded goods. With the urea plant remaining shut during most of FY2020 and NPK plant running at significantly low capacity utilisation, the company posted significant cash loss of Rs. 571 crore in 9M FY2020 which has weakened the liquidity position and the financial risk profile significantly. Going forward, the monetisation of company's assets will be imperative for improving the financial risk profile. The working capital intensity of fertiliser operations tend to remain high owing to the delay in the subsidy receipt from GoI resulting in the reliance on working capital borrowings to meet the cash flow mismatches and keeps the credit profile subdued. The company also stands exposed to foreign currency volatility as it imports a significant portion of its raw material particularly for phosphatic fertilisers and also for the trading operations in the absence of hedging.

The outlook on the rating is "Stable" given the expectation that urea operations will remain stable in the current fiscal and with asset monetisation plans in progress the company should be able to meet its debt servicing obligations in the upcoming fiscal.

## Key rating drivers and their description

### Credit strengths

**Established track record of the company in fertiliser and other agri-businesses-** ZACL has had an established track record in the fertiliser and other agri-business since 1967. ZACL through its subsidiaries and joint ventures is engaged in manufacturing of fertilisers, seeds, and other agri-inputs.

**Diversified product portfolio including urea, DAP and NPK complexes as well as traded products-** ZACL is engaged in manufacturing of urea as well as DAP/NPK fertilisers at its Goa manufacturing facility along with water soluble fertilisers (WSF) and Single Super Phosphate (SSP) manufactured at other plants of the company. It also undertakes trading of various fertilisers to provide wide range of agri products to the farmers. ZACL also benefits from access to the DAP/NPK fertilisers manufactured by its JV Paradeep Phosphate Limited (PPL).

**Favourable long-term demand outlook for fertilisers in India due to scarcity of nutrients in the soil-** Indian soil remains deficient in nutrient content which has resulted in lower agri-productivity. With increasing population, the demand for food will increase which will make productivity improvement imperative for the agri sector. Thus, the demand outlook for fertilisers remains positive in India.

**Strong marketing network and leading market position in Karnataka and Maharashtra-** ZACL caters to the southern and western part of India and enjoys leading market position in Karnataka and Maharashtra. ZACL along with PPL enjoy a major part of the DAP/NPK market in south –western part of India and a strong marketing network.

### Credit challenges

**Weak financial risk profile following significant losses in FY2020 following extended plant shutdowns and delay in asset monetisation and equity raising plans-** Capital structure of the company has weakened since demerger from Zuari Industries Limited. Low capitalisation, high debt due to subsidy receivable driven working capital borrowings along with weak core profitability over the past few years has resulted in weak capital structure. Going forward the debt funded capex

will keep the capital structure subdued unless equity infusion is completed in a timely manner by the company. The issues mentioned in heading are not discussed in para

**Intermittent plant operations due to weak liquidity position-** ZACL’s plants have been operational intermittently for most of FY2020. Urea plants were shut for most of FY2020 and came online in January 2020. ZACL’s NPK plant has been running only one train for most of FY2020 but is currently under shutdown. The company was not able to run its plants owing to liquidity issues. Going forward the NPK plants are expected to come online but the overall capacity utilisation is expected to remain low.

**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 to volatility as well. The sector being highly regulated also remains vulnerable to changes in the regulations by Gol.

**Being a substantial importer, exposed to currency fluctuations though risk is partially mitigated by hedging policy-** ZACL imports its entire requirement of phosphoric acid, ammonia and MOP for production of DAP/NPK fertiliser which exposes it to foreign exchange risks. The risk is however partly mitigated as the company leaves very small amount of its foreign exchange exposure as unhedged.

**High working capital intensity due to subsidy delays and high trade receivables resulting in high borrowings-** As the subsidy receivables from Gol continue to remain outstanding for as long as 4-5 months working capital borrowings to fund the receivables keep the borrowing levels elevated. The high receivable days also lead to high working capital intensity for the business and high interest costs for the company impacting profitability.

### Liquidity position: Stretched

ZACL’s liquidity remains stretched given the weak cash inflows from operations as the plants had been operational intermittently. The urea plants are expected to remain operational given the tie-up with GAIL (India) Limited to provide natural gas in lieu of first claim on receipt of subsidy receivables. Additionally, the dependence on the subsidy inflow from Gol, which is usually delayed, will keep the liquidity position subdued. Given that the Gol’s finances will be constrained due to the ongoing novel coronavirus (COVID-19) pandemic, any abnormal delay in the subsidy payments may adversely affect the liquidity position of the company.

### Rating sensitivities

**Positive trigger-** Faster than expected completion of asset monetization plans resulting in deleveraging of the balance sheet and improvement in the financial risk profile

**Negative trigger-** Deterioration in the liquidity profile of the company putting pressure on the debt servicing capabilities of the company

### Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Fertiliser sector</a>
Parent	NA
Standalone	The ratings are based on the Standalone financials of the company

## About the company:

Zuari Agro Chemicals Limited (erstwhile Zuari Holdings Limited) constitutes the fertiliser operations of the Adventz Group following the demerger of Zuari Industries Limited (ZIL). It is also the holding company for the other agri-business operations of the Adventz Group. The group has interests in agri-inputs, engineering, infrastructure, real estate, consumer durables and services sectors. It was a part of the erstwhile K.K. Birla Group. In April 2011, the Bombay High Court (Goa bench) approved the demerger of ZIL's fertiliser business into Zuari Holdings Limited (later renamed as ZAFL), while the residual entity ZIL (later renamed as Zuari Global Limited) retained the non-fertiliser business operations and investments. The demerger scheme was applicable w.e.f July 1, 2012.

The erstwhile ZIL was promoted in 1967 in financial and technical collaboration between the K.K. Birla Group and the U.S. Steel Corporation to manufacture urea, compound nitrogenous fertilisers and phosphates in Goa. In 1985, ZIL promoted Chambal Fertilisers & Chemicals Limited (CFCL, rated [ICRA]A1+) to produce urea using natural gas at Gadepan, Rajasthan. In 2002, ZIL acquired Paradeep Phosphates Ltd (PPL - rated [ICRA]A(Stable)/[ICRA]A1) through a JV company, as part of the disinvestment process of Gol. PPL manufactures DAP and NPK fertilisers, with its plant located at Paradeep, Orissa. While the equity shareholding of ZIL in PPL is now held by ZAFL (40.225% of entire shareholding of PPL through the JV company), the 13.3% shareholding of ZIL in CFCL continues to be held by ZGL.

## Key financial indicators (audited):

	FY2018	FY2019	9M FY2020*
Operating Income (Rs. crore)	4,650.3	5,131.4	1,880.8
PAT (Rs. crore)	33.1	-211.2	-509.7
OPBDIT/OI (%)	7.4%	2.6%	-14.7%
RoCE (%)	9.9%	4.3%	
Total Outside Liabilities/Tangible Net Worth (times)	6.4	12.2	
Total Debt/OPBDIT (times)	9.2	26.6	
Interest Coverage (times)	1.1	0.3	-0.8
DSCR	0.9	0.4	

Source: ICRA estimates; 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; \* 9M FY2020 results are un-audited

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

## Any other information: None

## Rating history for past three years

	Instrument	Current Rating (FY2021)			Rating History for the Past 3 Years							
		Type	Amount Rated	Amount Outstanding	Rating April 15, 2020	FY2020			FY2019		FY2018	
						15 July 2019	23 May 2019	13 May 2019	22 Feb 2019	10 Aug 2018	25 Sep 2017	16 Aug 2017
1	Fund Based	Long Term	1000.0	-	[ICRA]B (Stable)	[ICRA]D	[ICRA]D	[ICRA]BB (Negative)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
2	Term Loan	Long Term	260.0	260.00	[ICRA]B (Stable)	[ICRA]D	[ICRA]D	[ICRA]BB (Negative)	[ICRA]BBB+ (Negative)	-	-	-
3	Un-allocated	Long Term	465.0	-	[ICRA]B (Stable)	[ICRA]D	[ICRA]D	[ICRA]BB (Negative)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)
4	Compulsorily convertible Debentures	Long Term	400.4	0.00	[ICRA]B (Stable)	[ICRA]D	-	-	-	-	-	-
5	Non-fund based limits	Short Term	1980.0	-	[ICRA]A4	[ICRA]D	[ICRA]D	[ICRA]A4	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
6	Un-allocated	Short term	510.0	-	[ICRA]A4	[ICRA]D	[ICRA]D	[ICRA]A4	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+

Amount in Rs. crore

## 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
-	Term Loan	December 2014	9.6%-11.4%	March 2022	260.00	[ICRA]B (Stable)
-	Fund Based long term	-	-	-	1000.00	[ICRA]B (Stable)
-	Long term Un-allocated limits	-	-	-	465.00	[ICRA]B (Stable)
-	Non-fund-based limits	-	-	-	1980.00	[ICRA]A4
-	Short term unallocated	-	-	-	510.00	[ICRA]A4
-	Compulsorily convertible debentures	-	-	-	400.40	[ICRA]B (Stable)

Source: ZACL

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

Company Name	Ownership	Consolidation Approach
NA		

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**Corrigendum:**

The PR date in Rating history table was corrected from August 10, 2019 to August 10, 2018.

## ANALYST CONTACTS

**K Ravichandran**

+91 44 4596 4301  
[ravichandran@icraindia.com](mailto:ravichandran@icraindia.com)

**Prashant Vasisht**

+91 124 4545 322  
[prashant.vasisht@icraindia.com](mailto:prashant.vasisht@icraindia.com)

**Varun Gogia**

+91 124 4545 373  
[varun.gogia@icraindia.com](mailto:varun.gogia@icraindia.com)

## RELATIONSHIP CONTACT

**L Shivakumar**

+91 22 6114 3406  
[shivakumar@icraindia.com](mailto:shivakumar@icraindia.com)

## MEDIA AND PUBLIC RELATIONS CONTACT

**Ms. Naznin Prodhani**

Tel: +91 124 4545 860  
[communications@icraindia.com](mailto:communications@icraindia.com)

## Helpline for business queries:

+ 91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

[info@icraindia.com](mailto:info@icraindia.com)

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## ICRA Limited

### Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: [info@icraindia.com](mailto:info@icraindia.com)

Website: [www.icra.in](http://www.icra.in)

### Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

### Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 020 6606 9999

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