

June 17, 2020

Deepak Nitrite Limited: Rating reaffirmed at [ICRA]AA-/A1+; Outlook revised to Positive

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term loans	277.00	277.00	[ICRA]AA- reaffirmed; outlook revised to Positive from Stable
Fund based limits	300.00	300.00	[ICRA]AA- reaffirmed; outlook revised to Positive from Stable
Non-fund based limits	170.00	170.00	[ICRA]A1+ reaffirmed
Fund and Non-Fund Based limits	200.00	200.00	[ICRA]AA-/A1+ reaffirmed; outlook revised to Positive from Stable
Commercial Paper	200.00	200.00	[ICRA]A1+ reaffirmed
Total	1,147.00	1,147.00	

*Instrument details are provided in Annexure-1

Rationale

The rating reaffirmation and revision in outlook to Positive takes into account the continued improvement in the financial profile of Deepak Nitrite Limited (DNL) characterised by healthy growth in revenue and profitability and improvement in the debt coverage indicators in FY2020. ICRA notes that this improvement has been aided by the sustained healthy performance of its erstwhile profitable business segments—viz. Basic Chemicals (BC) and Fine and Specialty Chemicals (FNS), as well as a strong turnaround in its Performance Products (PP) segment, given the steep increase in realisations. While there could be some moderation in the profits in FY2021 as volumes may be impacted by the extended lockdown and realisations moderate, ICRA believes that DNL should retain a portion of the gains on account of its increased market share, which will sustainably strengthen its credit metrics. Additionally, the rating also factors in the healthy ramp-up of operations at the company's phenol and acetone plant as well as the operationalisation of the isopropyl alcohol (IPA) plant under its wholly-owned subsidiary, Deepak Phenolics Limited (DPL), which is expected to translate into healthy cash accruals for DNL on a consolidated basis.

The rating continues to take into account the long operating track record of the company in the chemical industry, its diversified product mix as well as exposure to diversified end-user industries. ICRA notes the leading market position enjoyed by the company in most of its product segments across domestic as well as global markets. The rating continues to factor DNL's multi-purpose manufacturing facility with significant backward and forward integration linkages that provide flexibility over the product mix to suit changing market requirements. ICRA also notes DNL's technical expertise to handle complex and hazardous chemical processes like nitration, hydrogenation and diazotisation.

The rating is, however, constrained by the exposure of the company's profitability to volatility in the raw material prices, though the same is reduced in certain products through formula-linked price contracts. The rating also factors in capex of ~Rs. 375-425 crore for capacity expansion planned in the current fiscal at DNL and DPL. Part of the same, however, may be deferred to FY2022, given the recent Covid-19 pandemic. The rating also factors in the high borrowing at a consolidated level given the debt taken at DPL to fund the phenol-acetone project. However, healthy profitability and cash accruals are expected to help maintain the debt coverage metrics at sound levels.

Key rating drivers and their description

Credit strengths

Long operating history and established track record in the global chemical intermediates industry - DNL has been operating in the chemical industry for nearly five decades. Over the years, the company has grown to become a market leader in the domestic market for inorganic intermediates (sodium nitrite and sodium nitrate), nitro toluenes and fuel additives. It is also among the top three global players for xylidines, cumidines and oximes.

Diversified product profile mitigating risk associated with cyclicalities in different product segments - While the company started with a limited portfolio of low-value bulk chemicals like sodium nitrite and sodium nitrate, it has grown its product portfolio to include high-value speciality chemicals for multiple end-user applications. Currently, it has a product portfolio of over 100 products (including its derivatives). The company has also added pharma intermediaries and more agro-chemical products to its portfolio over the years. The regular introduction of new products has helped DNL to mitigate the cyclicalities risk related to a particular product segment.

Multi-purpose manufacturing facility, with significant backward and forward integration linkages - The company's production facilities include processes that allow vertical integration for most products, leading to significant cost savings. Also, its facilities are designed to provide flexibility to change the product mix to suit market requirements.

Improvement in financial profile driven by turnaround of performance products - DNL reported a significant growth in revenue and operating profitability in FY2020, driven by a turnaround in the PP segment even as BC and FNS product segments continued to demonstrate a healthy performance. The average realisations for diamino stilbene disulfonic acid (DASDA) and optical brightening agent (OBA) increased by over 150% and 50% YoY, respectively, in FY2020, resulting in unprecedented profitability in the PP segment for DNL.

Healthy ramp-up of operations at DPL; successful commissioning of IPA plant – DPL's phenol-acetone plant showcased close to 100% capacity utilisation in FY2020, resulting in healthy revenue and cash flow generation for DNL on a consolidated basis. DPL also commissioned an IPA plant in April 2020. IPA is extensively used as a sanitiser, and with the Covid-19 pandemic, the global demand for IPA peaked. This resulted in the realisations more than doubling since March 2020. With timely commissioning, DPL has been able to sell its product in the domestic and global markets, while generating healthy cash flows.

Credit challenges

Profitability exposed to volatility in raw material prices, although the same is reduced in certain products through formula-linked price contracts - Prices of few of company's key products are linked to the movement of crude oil prices. The change in price levels, however, varies across product categories and is not commensurate with the change in crude price due to formula-linked pricing. Also, the prices of certain key products, such as sodium nitrite, TFMAP, OBA and DASDA, which formed about 40% of DNL's standalone sales in FY2020, are delinked from movement in crude oil prices.

Capacity expansion and efficiency improvement capex planned over near term; high borrowing at consolidated level - DNL's borrowing at a consolidated level remain high owing to a long-term debt of Rs. 843 crore as on March 31, 2020 (reduced from Rs. 931 crore as on March 31, 2019), majority of which has been raised at DPL to fund the phenol-acetone project. Further, the company has a planned capex of ~Rs. 375-425 crore for FY2021 for capacity expansion of certain key products and other efficiency improvement capex at DNL and DPL. ICRA notes that some portion of this planned capex has already been incurred in commissioning the IPA plant in April 2020 and some portion may be deferred to FY2022, given the ongoing pandemic.

Liquidity position: Strong

At a consolidated level, DNL's liquidity position remains strong with a healthy annual fund flow from operations of Rs. 583 crore in FY2020 and surplus free cash and liquid investments of Rs. 4 crore as on March 31, 2020. The liquidity position improved in FY2020 with healthy cash accruals, reduction in working capital intensity and no additional equity commitment towards its subsidiary, DPL. DNL also had a sanctioned fund-based working capital facility of Rs. 500 crore as on March 31, 2020, the average utilisation of which remained low at 28% of the drawing power over the past 12 months. Further, DNL has an additional sanctioned loan facility of Rs. 250 crore (Rs. 100 crore drawn and Rs. 30 crore outstanding as on March 31, 2020) from Axis Bank, which can be availed for any capex, if the need arises.

Rating sensitivities

Positive triggers: Sustenance of healthy revenue growth and profit margins resulting in deleveraging of DNL's consolidated balance sheet and improvement in return metrics could lead to a rating upgrade.

Negative triggers: Downward pressure on the ratings may arise if the company faces material weakening in its profitability owing to movements in product prices and/or raw material costs, or undertakes higher-than-expected capex that delays the expected improvement in leverage (Total Debt/OPBDITA) and coverage indicators.

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	For arriving at the ratings, ICRA has considered the consolidated financials of Deepak Nitrite Limited. As on March 31, 2020, the company had two wholly-owned subsidiaries that are enlisted in Annexure-2.

About the company

DNL is the flagship of the Deepak Group, which was incorporated in 1970 by Mr. C.K. Mehta. It began as a fully indigenous sodium nitrite and sodium nitrate manufacturer, before gradually widening its product portfolio over the years. Currently, DNL enjoys a leading market position in most of its products in the domestic as well as global markets. DNL has a portfolio of over 100 products, broadly divided into three segments—BC, FNS and PP. The company has five manufacturing facilities, one each at Nandesari and Dahej in Gujarat, Taloja and Roha in Maharashtra, and at Hyderabad. DNL's growth has also been aided by strategic acquisitions of companies with complementary product lines. In November 2018, the company commissioned its phenol and acetone manufacturing plant at Dahej at a project cost of ~Rs. 1,400 crore under its wholly-owned subsidiary, DPL. DNL infused equity of Rs. 560 crore in the project, 50% of which was in the form of non-cumulative optionally convertible redeemable preference shares.

During FY2020, at a consolidated DNL reported an operating income (OI) of Rs. 4,229.7 crore and profit after tax (PAT) of Rs. 611.0 crore. During FY2019, DNL had reported an OI of Rs. 2,699.9 crore and PAT of Rs. 173.7 crore.

Key financial indicators (consolidated - audited)

	FY2019	FY2020
Operating Income (Rs. crore)	2,699.9	4,229.7
PAT (Rs. crore)	173.7	611.0
OPBDIT/OI (%)	15.8%	24.3%
RoCE (%)	21.7%	37.8%
Total Outside Liabilities/Tangible Net Worth (times)	1.7	1.0
Total Debt/OPBDIT (times)	2.8	1.1
Interest coverage (times)	4.9	8.9
DSCR (times)	1.9	4.9

Source: Deepak Nitrite Limited consolidated financials

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

Instrument	Type	Current Rating (FY2021)			Chronology of Rating History for the past 3 years				
		Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2020	Date & Rating in FY2019		Date & Rating in FY2018	
						17-Jun-2020	22-Aug-2019	18-Mar-2019	01-Oct-2018
1 Term loans	Long term	277.00	30.00	[ICRA]AA-(Positive)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	
2 Fund based limits	Long term	300.00	-	[ICRA]AA-(Positive)	[ICRA]AA-(Stable)	[ICRA]A+(Positive)	[ICRA]A+(Stable)	[ICRA]A+(Stable)	
3 Non-fund based limits	Short term	170.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	
4 Fund and non-fund based limits	Long term/Short term	200.00	-	[ICRA]AA-(Positive)/[ICRA]A1+	[ICRA]AA-(Stable)/[ICRA]A1+	[ICRA]A+(Positive)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+	[ICRA]A+(Stable)/[ICRA]A1+	
5 Commercial paper	Short term	200.00	125.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	

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: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term loans	FY2015	NA	FY2026	277.00	[ICRA]AA-(Positive)
NA	Fund based limits	-	-	-	300.00	[ICRA]AA-(Positive)
NA	Non-fund based limits	-	-	-	170.00	[ICRA]A1+
NA	Fund and non-fund based limits	-	-	-	200.00	[ICRA]AA-Positive)/ [ICRA]A1+
NA	Commercial paper	-	-	7-365 days	200.00	[ICRA]A1+

Source: Deepak Nitrite Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Deepak Phenolics Limited	100.00%	Full consolidation
Deepak Nitrite Corporation Inc., USA	100.00%	Full consolidation

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