September 15, 2020

Vasant Chemicals Private Limited: Upgraded to [ICRA]BBB (Positive)/[ICRA]A3+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-Term Fund based – CC/OD	30.50	36.50	[ICRA]BBB (Positive); Upgraded from [ICRA]BBB- (Positive)
Long-Term Fund based – Term Loan	1.80	7.70	
Short-Term Fund based	1.23	1.23	[ICRA]A3+; Upgraded from [ICRA]A3
Short-Term Non Fund based	6.25	6.25	
Long-Term - Unallocated limits	40.22	6.32	[ICRA]BBB (Positive)/A3+; Upgraded from [ICRA]BBB- (Positive)/A3
Total	**80.00**	**58.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings upgrade factors in Vasant Chemical Private Limited's (VCPL) strong revenue growth of ~25% in FY2020 on the back of healthy volume growth for its key products and ramp-up in sales of new products launched in FY2019. Although the revenue growth is likely to be muted for FY2021 owing to the impact of the Covid-19 pandemic, the improvement in operating profitability margins is expected to be sustained at above 20% levels in FY2021 on account of increased share of catalyst chemicals segment, which generate relatively high margins. Further, the operating profit margins improved to20.8% in FY2020 from 18.5% in FY2019 owing to cost efficiencies and economies of scale. The ratings also consider its improved debt coverage indicators with interest coverage of 9.09 times, Total Debt/OPBITDA of 1.29 times and NCA/TD of 57% in FY2020. The ratings continue to draw comfort from the promoters' experience of more than three decades in the speciality chemicals industry and its reputed customer profile, which reduces the counterparty credit risk. The ratings note VCPL's long-term supply agreements with key customers, which protect the gross margins to an extent as they provide for price variations arising out of volatility in raw materials prices and exchange rate fluctuations.

The ratings, however, continue to be constrained by VCPL's moderate scale of operations, high product concentration risk with top three products accounting for ~58% of its revenues and the high customer concentration risk with the top five customers accounting for ~79% of the revenues in FY2020. This is mitigated by the strong credit profile of clients, repeat orders and long-term supply agreements. The ratings also consider the moderate working capital intensity of the business due to high debtors and inventory levels, although the company witnessed an improvement in its liquidity position as reflected by decrease in average working capital limit utilisation during the past twelve months on the back of improved cash flows.

The Positive outlook on [ICRA]BBB rating reflects ICRA's opinion that VCPL is expected to maintain its healthy profitability margins while sustaining its comfortable debt coverage metrics and return indicators.

Key rating drivers and their description

Credit strengths

Established track record in chemicals industry – VCPL has an established track record of more than three decades in the chemicals industry. It was previously involved in manufacturing dye intermediates with the unit being sold to Deepak Nitrite Ltd in 2004. VCPL started manufacturing speciality chemicals and pharmaceutical intermediates in 2004 and has two manufacturing units in Jeedimetla, Hyderabad and Atchutapuram, Andhra Pradesh.

Healthy growth in revenues and profitability in FY2020 – The operating income (OI) increased to Rs. 169.76 crore in FY2020 from Rs. 135.43 crore in FY2019, driven by an increase in orders for the company's existing products and ramp-up in sales of new products, which were launched in FY2019. VCPL's operating profitability witnessed a healthy improvement over the last two years to 20.75% in FY2020 from 11.72% in FY2018, supported by improved absorption of fixed costs given the increase in scale of operations and rationalisation of production costs. The revenue growth is expected to be muted for FY2021 owing to the impact of the Covid-19 pandemic. However, the improvement in operating profitability margins is likely to be sustained at above 20% levels in FY2021 on the back of increased share of catalyst chemicals segment, which generate relatively high margins.

Comfortable financial risk profile – The company's financial risk profile is comfortable with gearing of 0.67 times as on March 31, 2020, which decreased from 1.05 times as on March 31, 2018 owing to healthy accretion to reserves and repayment of term loans. Increased operating profits during the past two years resulted in improved coverage indicators with interest coverage of 9.09 times, Total Debt/OPBITDA of 1.26 times and NCA/Total Debt of 58% in FY2020.The debt coverage metrics are expected to remain comfortable in the medium term.

Reputed clientele reduces counterparty credit risk – VCPL's customer profile remains strong comprising reputed players in the chemical and pharmaceutical industry including Unilever Plc UK, Catexel Limited, Lambson Ltd, Malladi Drugs and Pharmaceuticals Limited, Dr. Reddy's Laboratories, Henkel AG & Company, etc. The established relationship with customers has resulted in repeat orders over the years and mitigates the counterparty credit risk.

Contractual agreements with various customers support offtake and escalation clauses support margins – The company has supply agreements with most of its customers accounting for ~81% of total revenues in FY2020, which lends medium-term revenue stability. The agreements with these customers have been periodically renewed over the years reflecting positively on VCPL's track record and established relationship with the customers. Moreover, the contractual agreements protect the gross margins to an extent, as they provide for price variations arising out of volatility in prices of key raw materials and exchange rate fluctuations beyond an agreed variance.

Credit challenges

Moderate scale of operations – Despite healthy ramp-up in sales during the last two years, the scale remains moderate with revenues of Rs. 169.76 crore in FY2020. Further, the revenues are expected to improve over the medium term with proposed expansion of capacity and commercialisation of new products.

High product and customer concentration – VCPL's product concentration continues to remain high with the top three products contributing ~58% of total revenues in FY2020. Also, the company has a high customer concentration with the top five customers accounting for ~79% of total revenues in FY2020. Despite expected commercialisation of new products and addition of new customers, the concentration is likely to remain high in the medium term.

High working capital intensity driven by high debtor and inventory levels – VCPL's working capital intensity stood high at 24% in FY2020 owing to high debtor and inventory levels. The company extends a credit period of 60-90 days to its customers and maintains a stock of key raw materials, which are imported from China. However, its liquidity position improved in the past one year as reflected by decrease in working capital limit utilisation on the back of improved cash flows.

Liquidity position: Adequate

The company's liquidity position is **adequate** and is supported by healthy retained cash flows, unutilised working capital limits and unencumbered cash balances of Rs. 6.10 crore as on March 31, 2020. The average fund-based limit utilisation remained moderate at ~68% during the past twelve months. The company has capex plans of ~Rs. 10 crore and repayment of Rs. 1.88 crore in FY2021 against Rs. 3.80-crore undrawn debt and retained cash flows of more than Rs. 15 crore in FY2021. Further, absence of sizeable debt repayment obligations in the near term is expected to support VCPL's liquidity position.

Rating sensitivities

Positive triggers – ICRA could upgrade VCPL's ratings if it maintains its operating margins along with reduction in product and customer concentration. Specific credit metrics that could lead to a rating upgrade include RoCE greater than 20% on a sustained basis.

Negative triggers – Negative pressure on VCPL's ratings could arise if there is significant degrowth in revenues or profitability margins or deterioration in working capital cycle impacting the company's liquidity position. Specific credit metrics that could lead to a rating downgrade include interest coverage ratio less than 4 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 standalone financial profile of the company

About the company

VCPL was established as a partnership firm by Mr. G. K. B. Chowdhary in 1978 and was later converted into a private limited company in 1988. It was involved in manufacturing dye intermediates till 2004, after which the unit was sold to Deepak Nitrite Ltd, and the company commenced manufacturing speciality chemicals and pharmaceutical intermediates. VCPL's manufacturing units are located in Jeedimetla, Hyderabad and APSEZ, Visakhapatnam.

Key financial indicators

	FY2019	FY2020
Operating Income (Rs. crore)	135.4	169.8
PAT (Rs. Crore)	8.7	18.0
OPBDIT/ OI (%)	18.5%	20.8%
RoCE (%)	16.6%	29.0%
Total Outside Liabilities/Tangible Net Worth (times)	1.6	1.4
Total Debt/ OPBDIT (times)	1.8	1.3
Interest Coverage (times)	6.1	9.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date &Rating in FY2021	Chronology of Rating History for the past 3 years: Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
		Current Rating (FY2021)			15-Sep-2020	19-Jul-2019	-	02-Feb-2018
1	Fund based – CC/OD	Long Term	36.50	NA	[ICRA]BBB (Positive)	[ICRA]BBB- (Positive)	-	[ICRA]BBB- (Stable)
2	Term Loan	Long Term	7.70	7.70	[ICRA]BBB (Positive)	[ICRA]BBB- (Positive)	-	[ICRA]BBB- (Stable)
3	Fund Based	Short Term	1.23	NA	[ICRA]A3+	[ICRA]A3	-	[ICRA]A3
4	Non Fund Based	Short Term	6.25	NA	[ICRA]A3+	[ICRA]A3	-	[ICRA]A3
5	Unallocated Limits	Long Term	6.32	NA	[ICRA]BBB (Positive)/A3+	[ICRA]BBB- (Positive)/A3	-	[ICRA]BBB- (Stable)/A3

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	Fund based – CC/OD	NA	NA	NA	36.50	[ICRA]BBB (Positive)
NA	Term Loan 1	FY2017	NA	FY2022	1.20	[ICRA]BBB (Positive)
NA	Term Loan 2	FY2020	NA	FY2026	6.50	[ICRA]BBB (Positive)
NA	Fund Based	NA	NA	NA	1.23	[ICRA]A3+
NA	Non-fund based	NA	NA	NA	6.25	[ICRA]A3+
NA	Unallocated	NA	NA	NA	6.32	[ICRA]BBB(Positive)/A3+

Source: Vasant Chemicals Private Limited

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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.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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