October 16, 2020

Gujarat Narmada Valley Fertilizers and Chemicals Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based Facilities	1,425.00	1,425.00	[ICRA]AA+(Stable); reaffirmed
Long-term/Short-term Fund-based	75.00	75.00	[ICRA]AA+(Stable)/[ICRA]A1+; reaffirmed
Non-fund Based Facilities	825.00	825.00	[ICRA]A1+; reaffirmed
Long-term/Short-term Non-fund Based	75.00	75.00	[ICRA]AA+(Stable)/[ICRA]A1+; reaffirmed
Commercial Paper Programme	1,000.00	1,000.00	[ICRA]A1+; reaffirmed
Total	**3,400.00**	**3,400.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation factors in the established market position of Gujarat Narmada Valley Fertilizers and Chemicals Limited (GNFC) in the fertilisers business (with its fertiliszer brand Narmada being well-entrenched within the farmer community especially in Gujarat) and market leadership in the chemical business for products including acetic acid, aniline and toluene di-isocyanate (TDI). The ratings consider its diversified chemicals product portfolio with vertical-integration benefits and the stable demand outlook for key chemicals. Moreover, GNFC has improved its energy efficiency for its urea plants in FY2020 with 6.16Gcal/MT from 6.30 Gcal/MT in FY2019, meeting the pre-set norms specified under the New Urea policy-2015 (NUP-2015), which would reduce its under-recoveries. The ratings also take into account the company's robust financial risk profile characterised by comfortable coverage indicators and capital structure in the absence of term debt. ICRA notes its healthy financial flexibility by virtue of the sovereign ownership and access to debt markets at competitive rates. Further, GNFC has unutilised working capital limits and surplus cash strengthening its liquidity profile.

However, the ratings remain constrained by the continuing losses in the fertiliser business (expected in Q4 FY2020 due to one-time recognition of subsidy income). ICRA notes that the chemical segment is facing pricing pressures, which has impacted the profitability. Nonetheless, with likely revival in chemical prices, its margins should improve over the long term on account of the competitive advantage that GNFC holds in the domestic market. The ratings are constrained by the vulnerability of the fertiliser division's profitability to regulatory policies and agro-climatic risks, commodity price risk associated with its chemicals business and the vulnerability of its cost structure to fluctuation in prices of gas, which is consumed in both the chemicals and non-urea fertilisers businesses. The company has moderate-sized chemical and efficiency improvement projects in the pipeline, which would entail funding, execution and market risks.

Moreover, on December 27, 2019, GNFC received a demand notice from the Department of Telecommunication (DoT) for payment of Rs. 15,020 crore of statutory dues in connection with V-SAT & ISP licenses held by the Company. However, it was not a party to the litigation and has represented to the DoT about non-applicability of the Supreme Court Judgement to GNFC. Recently, the Supreme Court directed DoT to reconsider the demand raised on public sector undertakings (PSUs), which are not in business of mobile services to the general public. As on date, there is uncertainty as to the amount and timing of any potential payment by GNFC. While the incidence of a significant amount of dues is less likely, ICRA will continue to monitor the developments in this regard.

The Stable outlook on the [ICRA]AA+ rating reflects ICRA's opinion that GNFC's operations will remain steady, driven by its strong portfolio of chemicals, sovereign ownership and healthy demand indicators.

Key rating drivers and their description

Credit strengths

Healthy financial risk profile characterised by low gearing and comfortable coverage indicators – Despite a moderation in the chemical segment's profitability, the company's capital structure and coverage indicators remained comfortable because of no term debt outstanding as of March 2020 end. GNFC had outstanding working capital debt of Rs. 233 crore (mainly as special banking arrangement against its subsidy receivables) and the remaining debt was availed to provide advances provident fund (PF) trust, since it has surrendered its own PF trust to the Central PF in March 2020. GNFC has repaid the entire short-term debt of Rs. 600 crore through sale of securities held for the PF trust. Further, the company had surplus cash of Rs. 190 crore as of March 2020 end. Accordingly, the gearing remained low at 0.16 times, while its coverage metrics remained comfortable in FY2020 with OPBDIT/I&F of 112 times, NCA/Debt of 57% and Total Debt/OPBDIT of 1.5 times.

Healthy financial flexibility; superior liquidity profile – GNFC's financial flexibility is healthy with access to low-cost funds from the state government financial institutions, given its sovereign ownership. Further, it has a superior liquidity profile due to its unused working credit limits. The company, at present, operates with cash credit limits of Rs. 1,500 crore to further support its liquidity. The average utilisation during the last 12 months that ended in July 2020 remained negligible.

Established track record in both fertiliser and chemical businesses – GNFC has an extensive track record in the manufacturing and marketing of fertilisers such as urea and ammonium nitro phosphate (ANP), industrial chemicals such as TDI, methanol, acetic acid, formic acid and nitric acid. It also trades in fertilisers such as di-ammonium phosphate (DAP) (both imported as well as indigenous), muriate of potash (MOP) ammonium sulphate, and industrial chemicals such as methanol and acetic acid. The contribution of fertilisers to the total revenue was around 43% of the overall sales, while chemicals accounted for around 55% in FY2020. The company also operates an IT-products division and other small segments, which contributed 2% to the total operating income in FY2020.

Strong brand equity in fertiliser business; market leadership in chemical business – GNFC sells its fertilisers under the brand, Narmada, through a number of cooperative societies, dealers and sub-dealers. The company's marketing network, at par with that of the industry leaders, is relatively stronger in Gujarat. With a strong brand equity built over the years, it has been able to sell its entire production, while increasing its share of sales in Gujarat. GNFC sells urea primarily in Gujarat, Madhya Pradesh, Maharashtra, Rajasthan and Uttar Pradesh.

Product diversity and vertical integration help to maintain profitable operations – GNFC's operations are characterised by a high level of vertical integration across its fertilisers and chemical divisions, thereby allowing high value addition and diversification. The company's strength lies in its product diversity and ability to switch among product streams in tune with the market conditions. Accordingly, even under extreme price volatilities for a particular product segment, GNFC was able to maintain profitable operations over the years.

Credit challenges

High dependence on chemical division's profitability for overall net cash accruals– Historically, the fertiliser business has remained a drag in terms of profitability for GNFC. However, in Q4 FY2020, it recognised a one-time fixed cost subsidy income, which was reversed in the previous year. Hence, the fertiliser segment turned profitable in FY2020 with PBIT of ~10%, though the same is expected to reduce in FY2021. The company's profitability has been driven by its chemical division, which also moderated in FY2020.

Vulnerability of chemical division's profitability to fluctuations in natural gas prices and exchange rates, cyclicality, and fall in import duty levels – GNFC's profitability is vulnerable to fluctuations in the prices of industrial chemicals and natural gas. The reduction in duty differential for imported chemicals could impact the company's profitability. Moreover, because of the import parity pricing of these products for domestic sales, GNFC's profit margins remain exposed to adverse fluctuations in the INR-USD exchange rates. Moreover, most of the chemicals witnessed moderation in realisations in FY2020. GNFC's profitability for TDI (major contributor in chemical segment profitability) is dependent upon the spread between the prices of TDI and toluene, among others. The TDI prices started declining from September 2018 and the average realisation remained 40% lower in FY2020 compared to FY2019. This impacted the chemical segment's overall profitability in FY2020. However, TDI prices have been hardening from August 2020 on account of global supply issues. Moreover, there has been levy of anti-dumping duty on aniline from July 2020, which should support domestic realisations. ICRA would continue to monitor the performance of GNFC's key chemical segments and it remains a key monitorable.

Fertiliser business exposed to regulatory and monsoon-related risks – As per the New Urea Policy 2015, urea units in the country are categorised into three groups based on their energy efficiency. Of the three groups, GNFC's unit falls under Group-II (pre-set norms between 6 Gcal/MT and 7 Gcal/MT). The company made losses/small profits in the last few years due to various under-recoveries in subsidy mechanism relating to conversion costs and fixed costs. However, post capex, its energy efficiency level improved to 6.16 Gcal/MT in FY2020 and is expected to remain within the 6.2 Gcal/MT (pre-set norm for GNFC) in FY2021. With improved efficiency, GNFC plans to reduce the under-recoveries. Moreover,the Indian agriculture sector remains vulnerable to the vagaries of monsoon as the area under irrigation remains low, resulting in volatility in sales and profitability of the fertiliser sector.

Moderate-sized capex plans in pipeline to entail moderate funding, execution and market risks – GNFC is, at present, considering several medium-scale projects at a total project cost of ~Rs. 700 crore, with the execution period likely to be three years from the project commencement. These include ammonia capacity enhancement, TDI reliability improvement, and expansion of formic acid and nitric acid add-on capacities at Bharuch (Gujarat). The other capex plans include scaling up its neem-based FMCG products as well as setting up a 10-MW solar plant.

Liquidity position: Strong

In FY2020, the gross cash flows declined on account of moderation in profitability and increased working capital intensity, which resulted in negative free cash flows. However, GNFC's liquidity position is **strong** due to absence of long-term debt and no repayment obligations, comfortable cash accruals and access to unused bank credit limits of Rs. 1,500 crore. GNFC had a surplus cash of Rs. 189 crore as of March 2020 end, further strengthening its liquidity profile. In terms of commitments, it has capex plans of Rs. 700 crore over the next three-four years. This would primarily be partly funded through internal accruals and partly through external debt. In addition, the company has a healthy financial flexibility to raise debt at low cost from the state government financial institutions.

Rating sensitivities

Positive triggers – ICRA is unlikely to upgrade the ratings in the near term, given the company's business profile consists of loss-making fertiliser operations and its high dependence on the cyclical chemical segment.

Negative triggers – Negative pressure on GNFC's ratings could arise if an extended down-cycle in the prices of its key chemical products results in a weak profitability, or if any major debt-funded capex or sizeable investments leads to significant additional debt, with the Net Debt/OPBDIT ratio exceeding 2.0 times.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology on Fertilisers Rating Methodology on Chemicals
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of GNFC. As on March 31, 2020, GNFC had one subsidiary and one associate,which are enlisted in Annexure-2.

About the company

Promoted jointly by the Government of Gujarat (GoG) and Gujarat State Fertilizers and Chemicals Limited (GSFC), GNFC was incorporated as a public limited company in 1976, with the two promoters cumulatively holding a 41.18% equity stake in it. Subsequently, however, the GoG's entire shareholding was transferred to Gujarat State Investments Limited (GSIL), a GoG undertaking. Based in Bharuch, GNFC mainly manufactures fertilisers such as urea, ANP and calcium ammonium nitrate (CAN), and industrial chemicals such as methanol, acetic acid, aniline, TDI, formic acid and nitric acid. The company also trades in few fertilisers and chemicals. It further provides IT services and solutions covering digital signature certificates (DSCs), e-procurement, e-governance projects, data centres, CCTV surveillance systems etc under the brand name of (n)Code solutions.

Key financial indicators (audited)

	FY2019	FY2020
Operating Income (Rs. Crore)	5,961	5,212
PAT (Rs. Crore)	741	499
OPBDIT/ OI (%)	15.7%	11.4%
RoCE (%)	15.2%	7.2%
Total Debt/ TNW (times)	0.04	0.16
Total Debt/ OPBDIT (times)	0.22	1.45
Interest Coverage (times)	146.2	112.3

Source: GNFC

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2021) Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Rating October 16, 2020	Chronology of Rating History for the past 3 years FY2020 January 27, 2020	FY2020 September 9, 2019	FY2019 August 29, 2018	FY2018 August 16, 2017
1	Long-term Fund-based	Long Term	1,425	-	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA+ (Stable)	[ICRA]AA (Stable)
2	Long-term/Short-term Fund-based	Long Term/Short Term	75	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	-	-
3	Short-term Non-fund Based	Short Term	825	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Long-term/Short-term Non-fund Based	Long Term/Short Term	75	-	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	[ICRA]AA+ (Stable)/ [ICRA]A1+	-	-
5	Commercial Paper	Short Term	1,000	-	[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	Cash Credit	NA	NA	-	1,425	[ICRA]AA+(Stable)
NA	Long-term/Short-term Fund-based	NA	NA	-	75	[ICRA]AA+(Stable)/ [ICRA]A1+
NA	Long-term/Short-term Non-fund Based	NA	NA	-	75	[ICRA]AA+(Stable)/ [ICRA]A1+
NA	Non-fund Based	NA	NA	-	825	[ICRA]A1+
NA	Commercial Paper	NA	NA	-*	1,000	[ICRA]A1+

** as on date, nil commercial paper outstanding*

Source: GNFC

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Gujarat Ncode Solutions Ltd	100.00%	Full Consolidation
Gujarat Green Revolution Co. Ltd	46.87%	Equity Method

Source: GNFC

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About ICRA Limited:

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