Kutch Chemical Industries Limited

April 07, 2021

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	288.88 (Reduced from 479.16)	CARE A; Stable (Single A; Outlook: Stable)	Revised from CARE A-; Stable (Single A Minus; Outlook: Stable)
Long Term / Short Term Bank Facilities	191.25 (Enhanced from 116.00)	CARE A; Stable / CARE A1 (Single A; Outlook: Stable / A One)	Revised from CARE A-; Stable / CARE A2+ (Single A Minus; Outlook: Stable / A Two Plus)
Short Term Bank Facilities	242.25 (Enhanced from 144.00)	CARE A1 (A One)	Revised from CARE A2+ (A Two Plus)
Total Facilities	722.38 (Rs. Seven Hundred Twenty-Two Crore and Thirty-Eight Lakh Only)		

Details of instruments/ facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

Owing to the operational, financial and managerial linkages between Kutch Chemical Industries Limited (KCIL) and Panoli Intermediates (India) Private Limited (PIIPL), CARE has taken a combined analytical view of these two companies, referred hereafter as Kutch Panoli Group (KPG).

The revision in the ratings assigned to the bank facilities of KPG is on account of significant improvement in its profitability during FY20 (FY refers to the period from April 1 to March 31) and 9MFY21 along with improvement in its capital structure and debt coverage indicators. The revision in ratings also factor completion and subsequent stabilization of two of its major projects related to Caustic Soda and Sulphuric Acid leading to addition of new products as well as better integration and operational synergies contributing to improvement in profitability. The ratings continue to derive strength from its experienced promoters, established track record in chemical industry with diversified product portfolio, established clientele and adequate liquidity.

The ratings, however, continue to remain constrained by its moderate capital structure, susceptibility of its profitability to volatile raw material prices and foreign exchange fluctuation risk and regulatory risk pertaining to adherence to the stringent pollution control and environmental compliance norms.

Rating Sensitivities

Positive Factors

- Significant volume driven growth in scale of operations of KPG with combined total operating income (TOI) of more than Rs.3,500 crore and profit before interest, lease, depreciation and tax (PBILDT) margin of over 25% on a sustained basis.
- Improvement in overall gearing below 0.50 times and Total Debt/gross cash accruals (GCA) below 1.50 times on a sustained basis.

Negative Factors

- Decline in sales volume with combined TOI below Rs.1,500 crore and PBILDT margin falling below 15% on sustained basis.
- Deterioration in its debt coverage indicators with interest coverage falling below 5 times and total debt to gross cash accruals (TD/GCA) increasing beyond 3 times on sustained basis.
- Return on capital employed (ROCE) falling below 15% on sustained basis.

Detailed description of the key rating drivers

Key Rating Strengths

Significant improvement in profitability and debt coverage indicators during FY20 and 9MFY21 with stable operations

On combined basis, KPG had reported significant improvement in its profitability during FY20 over FY19 marked by PBILDT margin of 22.46% in FY20 (FY19: 15.50%) which further improved to 30.50% in 9MFY21 on the back of addition of new products with completion and stabilization of Sulphuric Acid plant in PIIPL and Caustic Soda plant in KCIL which also resulted

[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

in better operational synergies with Oleum, Sulphuric Acid, chlorine and Caustic lye being used as raw material for many products manufactured by KPG. This coupled with better raw material cost management with declining trend of crude oil derivatives and healthy demand from end user industries supported the improvement in its profitability and cash accruals. Overall GCA grew by 52% to Rs.333.40 crore in FY20 as compared to Rs.219.76 crore in FY19. Consequently, its debt coverage indicators, too, witnessed improvement with PBILDT Interest coverage of above 10 times and TD/GCA of around 2.30 times (annualized) during 9MFY21.
Also, there was overall growth in its sales volume during FY20. However, the TOI of KPG declined marginally from Rs.2134.60 crore during FY19 to Rs.1897.72 crore during FY20 on the back of decline in the sales realization of its products due to decline in the raw material prices (as majority of its raw material are crude based).
Impact of Covid-19
Plant operations of KPG remained closed from March 23, 2020 to April 13, 2020 due to nationwide lockdown to control the spread of Covid 19 pandemic. Plant operations restarted from April 13, 2020 and gradually scaled up. Further, KPG had not availed the moratorium on the repayment of its bank facilities.
For the 9MFY21 period, as per provisional results, KPG had reported TOI of Rs.1505.30 crore with healthy PBILDT margin of 30.50% on the back of moderation in raw material prices along with contribution from the caustic soda plant.

Completion and Stabilization of the caustic soda plant and sulphuric acid project resulting in better integration and operational synergies
KCIL completed the green-field project of setting up of Caustic-Chlorine plant of 505 (tons per day) TPD along with 60 MW coal based captive power plant (CPP). Commercial operations of the plant began from January 26, 2020. The aggregate cost of project was Rs.911 crore (including taxes and duties – Rs.785 crore excluding taxes and duties) which was funded through Rs.373 crore of term loan crore (as against sanctioned term loan of Rs.500 crore) and balance from internal accruals and promoter contribution. The plant got stabilized in 9MFY21 and operated with capacity utilization of 80% despite disruption in initial month due to Covid 19. For 9MFY21 period, KCIL reported sales of Rs.171.11 crore from sale of caustic soda (flakes and lyes) along with Rs.10.71 crore from sale of chlorine and Rs.22.08 crore from Hydrogen. Further, KCIL has significant capacities for manufacturing various Chlorine based downstream products which partially lower its chlorine disposal problem. Currently (in February – March 2021) caustic soda plant is operating at ~95-100% of its capacity and KCIL is using 10-15% of Caustic Soda and 60-70% of Chlorine captively.
PIIPL had completed its major green-field project for manufacturing of sulphuric acid (600 TPD) and Thionyl Chloride (135 TPD) in May 2018 whose full year benefit was witnessed from FY20 onwards. Oleum and Sulphuric acid are used in manufacturing of H acid while Thionyl Chloride is used in manufacturing of Vinyl Sulphone (VS) whereas the steam produced during this process is used in various manufacturing processes resulting in better integration and operational synergies. Sulphuric Acid group contributed around Rs.100 crore to it TOI in FY20.

Experienced and resourceful promoters
Both companies of KPG (KCIL and PIIPL) are established and owned by Goyal family. Mr. Shiv Lal Goyal, along with his four brothers Mr. Kailash Goyal, Mr. Jaiprakash Goyal, Mr. Surendra Goyal and Mr. Vijendra Goyal look after strategic decisions as well as overall operations of the companies. Promoters have rich experience and vast knowledge about the product, process and market of various speciality chemicals. Further, top management is assisted by a team of well qualified and experienced professionals having long standing exposure in the same industry. Promoters are also resourceful and have supported the operations of the company as and when required through infusion of unsecured loan which has increased from Rs.329.48 crore as on March 31, 2019 to Rs.397.73 crore as on March 31, 2020.

Established track record with integrated operations in chemical industry and diversified product portfolio and established clientele
PIIPL has an operational track record of more than 20 years while KCIL has more than 15 years of operational track record reflecting long track record of the group in chemical industry. Over the years, the group has focused on backward integration, improvement of process efficiency, better waste management and increased captive power generation. The operations are well integrated with wide product base enabling the company to optimally utilize its large manufacturing facility which insulate it from the inherent cyclicality in demand for various products to some extent and impart better cost control over key inputs. KPG had setup 12.50 MW coal-based power plant and 5.50 MW of windmill to meet majority of its power for captive consumption. Further, KCIL had also set-up 60 MW of coal based CPP for its chlor-alkali plant which was operationalized during January 2020.
KPG has diversified product portfolio which includes various benzene derivatives (chlorination, nitration, hydrogenation products), sulphuric acid and sulphuric based products (Oleum, Chloro Sulphonic Acid), Chlorine derivatives (Thionyl Chloride, Chlorinated Parafin Wax) and dye intermediates (H Acid and VS). During FY20, KPG has added new products viz. Caustic Soda/Lye, Sodium Nitrite to its product portfolio. These products are manufactured from basic chemicals/crude derivatives

and have wide application in agro chemicals, dye intermediates, pharmaceutical, paints and textile industries among others. It has ability to produce various variants from its manufacturing facility as per the prevailing demand. KPG has long standing association with prominent chemical manufacturers in domestic market and has established customer and supplier base.

Liquidity: Adequate

KPG had adequate liquidity marked by low utilization of its working capital limits, moderate liquidity ratios and moderate debt repayment of Rs.94 crore as compared to its envisaged healthy annual cash accruals of around Rs.350-400 crore. Further, group has capex plan of ~Rs.180-200 crore per year over next 2 years which is envisaged to be entirely funded from its cash accruals and promoter contribution. Cash flow from operations remained healthy at Rs.246.98 crore during FY20 as compared to Rs.260.01 crore during FY19. Avg. fund based working capital utilization remained low at 43% for past 12 months ended December 31, 2020 providing cushion in terms of availability of unutilized working capital limits. Current ratio and quick ratios, however, remained moderate at 1.25x and 0.92x respectively as on March 31, 2020. It had free cash and bank balance of Rs.15.69 crore as on March 31, 2020.

However, operations of KPG are working capital intensive in nature, as it is required to maintain inventory of raw material for 40-45 days and of finished goods for 15-20 days while collection period ranges from 70-90 days leading to gross current assets days of 178 days in FY20 (FY19: 143 days). Operating cycle elongated from 68 days during FY19 to 95 days during FY20 due to increase in the inventory as well as receivables days during FY20.

Key Rating Weaknesses

Improvement in capital structure; albeit it remained at moderate level

On a combined level, KPG's overall gearing has exhibited an improving trend from 1.40x as on March 31, 2019 to 1.21x as on March 31, 2020 and further to 0.91x as on December 31, 2020. However, it remained at moderate level due to recent conclusion of its debt funded capex whose benefits would accrue over the next 1-3 years. Total debt (including LC backed creditors) of KPG had increased from Rs.877.60 crore as on March 31, 2019 to Rs.1053.82 crore as on March 31, 2020 due to debt funded capex (caustic soda plant) undertaken in KCIL. KCIL had availed new term loan of Rs.373 crore for the said project (as compared to sanctioned term loan of Rs.500 crore). Historically, KPG had shown low reliance on bank debt and as on March 31, 2020 out of its total debt around 38% is in the form of unsecured loan from related party and promoters.

Susceptibility of profitability to volatile raw material price and foreign exchange fluctuation risk

Benzene as well as Sulphur are the main raw materials used by KPG which are crude oil derivatives and their prices are driven by the international demand-supply dynamics and remains volatile which makes the profitability of KPG susceptible to any adverse change in crude oil price. Further, KPG is a net importer with total export sales of Rs.185.68 crore during FY20 (FY19: 193.83 crore) as compared with import of Rs.239.98 crore during FY20 (FY19: Rs.293.49 crore). In the absence of any active hedging policy, any adverse movement in exchange rate can affect its profitability.

Regulatory risk pertaining to environmental norms and strict adherence to pollution control norms

Chemical industry is regulated by stringent regulatory and pollution control norms which companies need to strictly adhere to. Continued compliance with these stringent pollution control norms is essential for the un-interrupted operation of KPG. Further, companies have to regularly up-grade and invest in line with evolving regulatory requirements. Any changes in the regulatory norms or non-compliances can affect the operation of KPG.

Stable outlook for chemicals industry; albeit caustic soda industry witnessing declining pricing trend

China, which has dominant position in the chemical sector, has tightened environmental standards, resulting in the closure/shifting of its manufacturing capacities. Further, increased compliances as well as labour costs and the COVID-19 pandemic have aggravated the situation further with companies around the globe looking for alternative sources. However, threat of imports from China continues due to its very large capacities. The Indian speciality chemical sector is expected to witness stable growth on the back of favourable government policy, realigning global supply chain and stable demand from end user industries.

For caustic soda industry, as per data from CMIE, the imports of caustic soda after plunging by 50% in FY19 on y-o-y basis has again grown by around 49% on y-o-y basis in FY20. As against 4-7% production growth recorded in the preceding three years ended FY20, growth slowed to about 2% in FY20. This has also led manufacturers to cut prices and hence prices of caustic soda lye and flakes plunged by around 20% in FY20 on y-o-y basis and further reduced during 9MFY21. Significant imports from countries having surplus capacities like China, Iran, Turkey, US, Russia, etc have also kept prices under pressure. In order to help domestic manufacturers, Alkalies Manufacturers Association of India (AMAI) has sought a level playing field from the government by way of increase in customs duty on caustic soda imports, a GST structure for electricity taxes and the imposition of export duty on salt. Further, Directorate General of Trade Remedies via Ministry of Commerce and Industry, has initiated the anti-dumping duty investigation concerning imports of caustic soda origination in and exported from Japan, Iran, Qatar and Oman vide its notification dated December 17, 2020 post non-renewal of anti-dumping duty on imports which expired in November 2020. The outlook for the domestic chlor-alkali industry is likely to remain stable in the long-term, mainly on account of expectation of gradual recovery in demand from its key end-use industries like pharmaceuticals, agrochemicals, alumina, organic chemicals, etc.

Analytical Approach: Combined

Combined analytical approach has been taken for the credit assessment of KCIL and PIIPL as both companies; referred to as Kutch-Panoli Group (KPG), have common promoters and both companies are engaged in manufacturing of speciality chemicals and dyes intermediates. Also, there is fungibility of cash flows and both companies have provided cross guarantees for bank facilities availed by them.

APPLICABLE CRITERIA:

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology: Consolidation
Rating Methodology - manufacturing companies
Financial ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities

About the company/group

Incorporated in June 2002, KCIL (CIN: U24114DL2002PLC115757) is a closely held public limited company promoted by the Goyal family based out of Gujarat. KCIL is engaged in the manufacturing of wide range of specialty chemicals viz. Benzene derivatives such as mono chloro benzene (MCB), ortho dichloro benzene (ODCB), para dichloro benzene (PDCB) etc., dye intermediates (Vinyl Sulphone) and Sulphur based chemicals. Benzene is one of the key hydrocarbons which finds application in agrochemicals, pharmaceuticals, dyes & pigments, paint industry, etc. In January 2020, KCIL had completed greenfield Chlor-Alkali project having manufacturing capacity of 505 MTPD (metric ton per day) of caustic soda coupled with captive coal-based power plant of 60 Megawatt (MW).

Its group company, PIIPL is also engaged in the manufacturing of benzene derivatives such as MCB, Para Nitro Chloro Benzene (PNCB), Ortho Nitor Chloro Benzene (ONCB) etc., dye intermediates and other inorganic chemicals at its manufacturing facilities located at Nandesari (Vadodara) and Jhagadia (Bharuch). KCIL and PIIPL are together referred to as Kutch-Panoli group (KPG).

Brief Financials (Rs. Crore)-Combined (KPG)	FY19 (UA)	FY20 (UA)	9MFY21 (UA)
Total Operating Income	2134.60	1897.72	1505.30
PBILDT	330.83	426.29	459.13
PAT	158.15	244.63	* 248.59
Overall Gearing (times)	1.40	1.21	0.91
Interest Coverage (times)	13.14	10.45	10.48

**assuming income tax rate of 25.17%*
A: Audited;
UA-Un-audited (Financials are combined by analytical team on basis of line by line addition and netting off inter group transactions)

Brief Financials (Rs. Crore)-Standalone (KCIL)	FY19 (A)	FY20 (A)	9MFY21 (UA)
Total Operating Income	1103.63	892.46	844.40
PBILDT	145.46	224.00	251.74
PAT	74.77	112.56	121.74
Overall Gearing (times)	1.82	1.83	1.43
Interest Coverage (times)	12.26	7.82	7.23

A: Audited; UA-Un-audited

Status of non-cooperation with previous CRA:

CRISIL has suspended ratings assigned to the bank facilities of KCIL vide press release dated March 27, 2015 on account of non-cooperation by KCIL with CRISIL's efforts to undertake a review of the rating outstanding.

Any other information: Not Applicable

Rating History (Last three years): Please refer Annexure-2

Covenants of rated instruments/facility: Not Applicable

Complexity level of various instruments rated for this company: Please refer Annexure-3.

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based-LT/ST	-	-	-	191.25	CARE A; Stable / CARE A1
Fund-based - LT-Term Loan	-	-	June 2024	288.88	CARE A; Stable
Non-fund-based - ST-BG/LC	-	-	-	217.25	CARE A1
Fund-based - ST-Bills discounting/ Bills purchasing	-	-	-	25.00	CARE A1

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based-LT/ST	LT/ST	191.25	CARE A; Stable / CARE A1	1)CARE A-; Stable / CARE A2+ (06-Apr-20)	-	1)CARE A-; Stable / CARE A2+ (25-Jan-19)	-
2.	Fund-based - LT-Term Loan	LT	288.88	CARE A; Stable	1)CARE A-; Stable (06-Apr-20)	-	1)CARE A-; Stable (25-Jan-19)	-
3.	Non-fund-based - ST-BG/LC	ST	217.25	CARE A1	1)CARE A2+ (06-Apr-20)	-	1)CARE A2+ (25-Jan-19)	-
4.	Fund-based - ST-Bills discounting/ Bills purchasing	ST	25.00	CARE A1	1)CARE A2+ (06-Apr-20)	-	1)CARE A2+ (25-Jan-19)	-

Annexure 3: Complexity level of various instruments rated for this Company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Term Loan	Simple
2.	Fund-based - ST-Bills discounting/ Bills purchasing	Simple
3.	Fund-based-LT/ST	Simple
4.	Non-fund-based - ST-BG/LC	Simple

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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