

## Fairchem Organics Limited

August 20, 2021

### Ratings

Facilities	Amount (Rs. crore)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	74.64 (Reduced from 80.91)	CARE A+; Stable (Single A Plus; Outlook: Stable)	Revised from CARE A; Stable (Single A; Outlook: Stable)
Long Term / Short Term Bank Facilities	2.50	CARE A+; Stable / CARE A1+ (Single A Plus; Outlook: Stable / A One Plus)	Revised from CARE A; Stable / CARE A1 (Single A; Outlook: Stable / A One)
Total Facilities	77.14 (Rs. Seventy-Seven Crore and Fourteen Lakhs Only)		

*Details of facilities in Annexure-1*

### Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Fairchem Organics Ltd. (FOL) factors in healthy growth in its scale of operations over last three years ended FY21 (FY refers to the period from April 1 to March 31) and Q1FY22 with healthy profitability which is expected to be continue in FY22 as well supported by capacity addition. Further, growth will be backed by development of value-added products including new variant of Linoleic acid catering to the requirement of paint industry. The rating revision also factors in further improvement in its already comfortable capital structure and debt coverage indicators.

The ratings continue to derive strength from its experienced and resourceful promoters, long standing operational track record of the business of manufacturing of specialty chemicals which has diverse industry applications, leadership position in domestic market for its products and its established relation with reputed customers.

The ratings are, however, constrained on account of FOL's presence in niche market, risk of import substitutability from low-cost Chinese products and susceptibility of profitability to volatile raw material prices and fluctuations in forex rate. The ratings are further constrained due to its exposure to technology obsolescence risk and stringent pollution control norms.

### Rating Sensitivities

#### Positive Factors

- Growth in scale of operations marked by Total Operating Income (TOI) of more than Rs.1000 crore along with earning PBILDT margin of around 18% on a sustained basis
- Diversification of its revenue stream in terms of products as well as reduced dependence on few major customers

#### Negative Factors

- Decline in its scale of operations marked by TOI of less than Rs.400 crore on sustained basis with PBILDT margin of less than 15% on a sustained basis
- Elongation in its operating cycle beyond 100 days affecting its liquidity
- Any large size debt funded capex leading to moderation in its overall gearing beyond 0.60x

### Detailed description of the key rating drivers

#### Key Rating Strengths

#### **Healthy growth in scale of operations in last three years ended FY21 and Q1FY22 along with healthy profitability**

Over the last three years, FOL's total operating income has increased at healthy CAGR of ~23% on account of increased customer base, development of products variants as per customer requirement and increased sales realization. FOL had developed variant of linoleic acid catering to the requirement of paint industry which is the key growth driver in last two years. Further, growth is also supported by continuous capacity additions done by the company in last three years. During FY21, TOI has increased to Rs. Rs.396.80 crore (PY – Rs. 312.74 crore) with increase in sales of Linoleic acid while contribution of dimer acid and nutraceuticals segment in FOL's total revenue has remained stable. Going forward, value addition in couple of fatty acid products and increased penetration in paint industry are expected to drive its growth prospects in near term.

During FY21, profit margins of FOL also remained healthy in line with previous year. It also had a healthy ROCE of around 20-28% during last three years.

During Q1FY22, company has reported TOI of Rs.139.53 crore with healthy PBILDT margin of 23.84% which is a significant growth over Q1FY21 wherein it has reported TOI of Rs.35.09 crore with PBILDT margin of 12.71%. The growth is primarily

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratings.com](http://www.careratings.com) and in other CARE publications.

on account of higher demand of Dimer acid, other newly developed products and limited impact of COVID19 pandemic on operations. However, going forward profitability margin is expected to remain around 17-18%.

***Improvement in capital structure and debt coverage indicators which remained at comfortable level***

As on March 31, 2021, FOL's overall gearing ratio has improved and remained comfortable at 0.34x (PY – 0.53x). Its interest coverage and TD/GCA have also improved to 10.33x (PY- 8.30x) and 1.16x (PY - 1.66x) respectively during FY21.

FOL, had also prepaid one of its term loans in August 2021 and had no debt raising plans in near future as planned capex is to be funded from internal accruals. Thereby, its overall gearing and TOL/TNW is expected to improve further and remain at comfortable level.

***Experienced and resourceful management***

FOL, is a professionally managed company led by one of the promoters, Mr. Nahoosh Jariwala who is the Managing Director and has experience of more than 25 years in chemical manufacturing and trading of various textile products. He looks after the core operations of the company including process optimization, product development, production planning, etc. He is well supported by a qualified second tier management.

As on June 30, 2021, Canada based FIH Mauritius Investment Limited (FMIL) has 66.65% equity stake (increased from 48.75% as on March 31, 2021) in FOL. FMIL is an investment arm of Fairfax India Holdings Corporations (Fairfax India) founded in 2014 by Mr. V. Prem Watsa having diverse investment portfolio with fair value of Rs.24,723 crore in India as on March 31, 2021. The investment portfolio of Fairfax India includes India Infoline Finance Limited (CARE AA; Negative), IIFL Wealth Management Limited (CARE A1+), Bangalore International Airport Limited, Seven Islands Shipping Limited, CSB Bank Limited and Spaisa Capital Limited amongst others.

***Established track record of operations along with diverse industry application***

FOL had been operating in the specialty chemicals segment for more than two decades where it is into manufacturing niche products having diverse industry applications. The company is primarily engaged in manufacturing of Dimer Acid and Linoleic Acid which find its application in industries like paints, printing ink, polyamides and adhesives. Residue generated during the manufacturing processes is sold to the local soap manufacturers and other industries as a fuel. FOL's product portfolio also includes Mixed Tocopherol Concentrate and Concentrated Sterols under nutraceuticals segment. Over the period, company had been increasing its processing capacity from 10,000 Metric Ton Per Annum (MTPA) in FY11 to 72,000 MTPA in FY20. Despite addition in capacity, the utilizations remained healthy around 80%.

Currently, company is undertaking capex to increase its capacity to 1,20,000 MTPA by end of FY22 in phased manner with part of the enhance capacity to become operational in Q3FY22. The project cost is estimated around Rs.29 crores to be funded from internal accruals.

***Reputed clientele***

FOL has long association with its customers in domestic as well as export markets. FOL has a reputed and diversified clientele including companies like Asian Paints Limited, Uniform Synthetics, Resins & Plastics Limited, Resinova Chemie Limited, BASF Corporation (USA), KENKO Corporation, Archer Daniel Midland Co, Arkema Chemicals India Private Limited, Hubergroup India Private Limited etc. During FY21, top 10 customers contribute around 64% of its TOI during with top customer contributing 41.6% of its TOI reflecting moderate customer concentration. Majority of its clientele enjoy leading position in their respective industry segments and hence credit risk is envisaged to be minimal.

***Leadership position in domestic market creating entry barriers to other players***

Company is enjoying lead position in the industry in terms of acid-based products, Dimer Acid and Linoleic Acid, in India. FOL manufactures its' products through fatty acid [1-1.5% of waste generated during refining of edible oil] which provide it the cost advantage as compared to other players who manufactures these products using raw soft oil or tall oil. The total availability of the fatty acid in India is limited however, over a period of time, company has developed relation with its suppliers and established procurement network to ensure steady supply of raw material. Cost advantage, established procurement network and limited size act as a barrier for other players in the industry.

***Stable demand prospect from industry***

The products manufactured by FOL find application in high growth consumer goods industries like nutraceuticals, paints, printing ink, adhesives, soap manufacturing etc. All these industries are expected to grow at a steady rate in the medium term due to factors such as rising population, increase in disposable income, increase in penetration of e-commerce which increases demand for packaging and printing ink industry and increasing spending on healthcare and nutrition products.

**Liquidity - Strong**

Liquidity of FOL is strong marked by healthy cash accruals against low debt repayment obligations, moderate liquidity ratios and low utilization of fund-based limits. Its current ratio was comfortable at 1.47x as on March 31, 2021. Company

has reported healthy cash flow from operation of Rs.39.42 crore (PY – Rs.31.18 crore). Going forward company is expected to generate strong cash accruals of Rs. 70 - 100 crores against which company has repayment of Rs.25 crores in FY22 (including prepayment of one of its outstanding term loans in August 2021) and low repayment of Rs.2-3 crore thereafter. The average monthly utilization for last twelve months ended July, 2021 stood at ~64%. During FY21, company has availed Guaranteed Emergency Credit Line WCTL of Rs.13.15 crore as the same is available at lower interest rate.

#### **Key Rating Weaknesses**

##### ***Presence in niche market with competition from low cost Chinese products***

The industry size for Dimer acid and Linoleic acid is relatively small compared to the overall size of chemical industry which limits the growth of the company. Further, FOL faces competition from the low-cost products from China especially in Dimer acid. However; FOL has been able to gain significant market share in India with its apt pricing strategy and cost advantages.

##### ***Susceptibility of FOL's profitability to volatile raw material prices and fluctuations in forex rates***

Vegetable oil distillate and acid oil are the main raw materials for FOL. These raw materials are by-products of soya and sunflower oils generated during their refining process. The prices of both these oils have remained volatile and witnessed sharp fluctuations in FY21. FOL's exports comprise around 10% to 15% of its gross sales over past three years; however, major portion of its raw material requirement is procured domestically. Hence, the profitability of FOL is susceptible to volatile agro based raw material prices and forex rates as company does not have any active hedging policy.

##### ***Stringent pollution control norms***

There is stringent pollution control regulation laid down for chemical processing units under the Gujarat Pollution Control Board (GPCB) norms. The company during its production process generates polluted water and air that needs to be treated before their disposal. Compliance with stringent pollution control norms set by the regulatory authorities and any violation in compliance with these norms or any further strengthening of these norms would adversely impact FOL's operations. Hence, the continuous adherence to the prevailing pollution control norms would remain crucial from the credit perspective.

##### ***Product obsolescence and substitution risks***

Companies like FOL which operate in the niche specialty chemical segment carry risk in terms of challenges emanating from the development of alternative technologies and introduction of newer products and hence is exposed to the risk of product obsolescence and substitution. However, FOL has expanded its R&D capabilities which facilitate launching of new derivatives of its existing products to its product portfolio.

**Analytical approach:** Standalone

#### **Applicable Criteria:**

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Criteria for Short Term Instruments](#)

[Financial Ratios – Non-financial Sector](#)

[Rating Methodology-Manufacturing Companies](#)

[Liquidity Analysis of Non-financial sector](#)

#### **About the Company:**

Fairchem Organics Limited (CIN - U24200MH2019PLC323176) is established in 2019, wherein Fairchem Speciality Limited (FSL) has transferred Oleo chemicals & Nutraceuticals businesses (entire business of FSL) as per scheme of demerger. FOL is engaged in the manufacturing of specialty chemicals like Dimer Acid, Linoleic Acid, Mixed Tocopherol Concentrate and Sterols Concentrate which find application in various industries like nutraceuticals, paints, printing ink, detergents, adhesives, etc. FOL's manufacturing facility is located at Chekala village near Sanand, Gujarat with an installed capacity of 72,000 MTPA as on May 31, 2021.

FSL (formerly known as Adi Finechem Limited) was promoted by Mr. Rajan Harivallabhdas in May 1985. During FY10, Mr. Harivallabhdas sold his stake to three new promoters namely Mr. Utkarsh Shah, Mr. Bimal Parikh and Mr. Hemant Shah. Moreover, during FY16, Fairfax India through its wholly owned subsidiary FIH Mauritius Investment Limited (FMIL) acquired controlling equity stake in FSL. Post demerger, FMIL increased its equity stake to 66.65% as on June 30, 2021 from 48.75% stake as on March 31, 2021.

Brief Financials (Rs. Crore)	FY20 (A)	FY21 (A)
Total Operating Income	312.74	396.80
PBILDT	54.62	68.90
PAT	34.70	42.48
Overall gearing (times)	0.53	0.34
Interest coverage (times)	8.30	10.33

A: Audited

As per Q1Y22 (UA), the company has reported TOI of Rs.139.53 crore (Q1FY21 – Rs.35.09 crore) and PAT of Rs.22.31 crore (Q1FY21 – Rs.1.19 crore).

**Status of non-cooperation with previous CRAs:** None

**Any other information:** None

**Rating History for last three years:** Please refer Annexure-2

**Detailed explanation of covenants of the rated instrument / facilities:** Annexure-3

**Complexity level of various instruments rated for this Company:** Annexure 4

#### 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-Term Loan	-	-	February, 2026	16.15	CARE A+; Stable
Fund-based - LT-Cash Credit	-	-	-	58.49	CARE A+; Stable
Non-fund-based - LT/ ST-BG/LC	-	-	-	2.50	CARE A+; Stable / 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 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Fund-based - LT-Term Loan	LT	16.15	CARE A+; Stable	-	1)CARE A; Stable (08-Mar-21) 2)CARE A; Stable (16-Sep-20)	-	-
2.	Fund-based - LT-Cash Credit	LT	58.49	CARE A+; Stable	-	1)CARE A; Stable (08-Mar-21) 2)CARE A; Stable (16-Sep-20)	-	-
3.	Non-fund-based - LT/ ST-BG/LC	LT/ ST	2.50	CARE A+; Stable / CARE A1+	-	1)CARE A; Stable / CARE A1 (08-Mar-21) 2)CARE A; Stable / CARE A1 (16-Sep-20)	-	-

#### Annexure 3: Detailed explanation of covenants of the rated instrument / facilities

Bank Facilities	Explanation
Financial covenant	Minimum tangible net worth of Rs.80 crore

#### Annexure 4: 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 - LT-Cash Credit	Simple
3.	Non-fund-based - LT/ 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](http://www.careratings.com). Investors/market intermediaries/regulators or others are welcome to write to [care@careratings.com](mailto:care@careratings.com) for any clarifications

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### About CARE Ratings:

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