Gujarat Alkalies and Chemicals Limited

September 20, 2023

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	723.98	CARE AA+; Stable	Reaffirmed
Short-term bank facilities	339.50 (Enhanced from 45.00)	CARE A1+	Reaffirmed
Commercial paper	100.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The ratings assigned to the bank facilities and instrument of Gujarat Alkalies and Chemicals Limited (GACL) continue to derive strength from its strong position in the domestic chlor-alkali industry along with its integrated operations and state-of-the-art technology. The ratings also derive strength from wide product portfolio, which finds application across diversified end-use industries, captive power generation to meet part of its energy requirement, along with its comfortable leverage, debt coverage indicators, and strong liquidity. The ratings also draw comfort from the completion of its major ongoing capital expenditure (capex) during FY23 and expected growth in the scale of operations from the same in the near to medium term.

The long-term rating, however, continues to be constrained due to its presence in an inherently cyclical chlor-alkali industry, as evident from the volatile electrochemical unit (ECU)[2] realisations leading to moderation in its operational performance during Q1FY24. Moreover, the ratings are constrained due to the competition from imports; the susceptibility of its profitability to adverse movement in the market prices of gas and power, which constitutes a significant part of its cost structure; and the risk related to adverse movement in foreign exchange rates.

Furthermore, the long-term rating is also tempered by the post-implementation saleability risks associated with its large-sized recently completed projects. The ratings are further constrained by subdued performance of its joint venture (JV) with National Aluminium Company Limited (NALCO), viz, GACL-NALCO Alkalies & Chemicals Pvt Ltd (GNAL; rated 'CARE BBB+; Stable/ CARE A2'), which is expected to require timely financial support from both of its promoters in the short to medium term.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Significant volume-driven growth in its scale of operations along with diversification of its operations to other chemical products thereby insulating itself from inherent cyclicality of the chlor-alkali industry and thus earning healthy PBILDT margin on a sustained basis; along with maintaining total debt/PBILDT below 0.25x on a sustained basis.
- Gaining significant market leadership position in the caustic soda industry while securing significant portion of its power requirement (its major cost component) through captive low-cost sources; along with greater share of value-added products in its sales mix to consistently earn high PBILDT margin with greater resilience, despite impact of inherent cyclicality in the chlor-alkali industry and competition from imports.
- Improvement in its return on capital employed (RoCE) to more than 25% on a sustained basis.

Negative factors

- Sustained pressure on its profitability marked by PBILDT margin remaining below 20% on a sustained basis owing to lower ECU realisations.
- Deterioration in consolidated total debt / PBILDT beyond 2.50x on a sustained basis.
- Heavy dumping of caustic soda products significantly impacting its ECU realisations.
- Significantly more-than-envisaged debt-funded capex/investments leading to its overall gearing deteriorating to more than 0.50x on a sustained basis.
- Any tightening of prevailing pollution control/ environmental norms and/or regulatory ban on production and sales of certain major products thereby significantly impacting its business and profitability.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

[2]Caustic soda, chlorine and hydrogen are co-products and hence ECU refers to weighted average realizations of the above co-products.

Analytical approach: Consolidated.

CARE Ratings Limited (CARE Ratings) has considered the 'Consolidated' analytical approach for the ratings of GACL as there are strong operational and financial linkages of GACL with its JV company, i.e., GACL-NALCO Alkalies and Chemicals Limited (GNAL), which has set up a caustic soda manufacturing facility at Dahej, wherein, GACL holds 60% equity stake.

Outlook: Stable

The 'Stable' outlook on the rating reflects that the entity shall continue to hold a dominant position in the domestic caustic soda industry with its integrated operations. Furthermore, CARE Ratings expects the entity to maintain its comfortable financial risk profile despite moderate cash accruals upon no large debt-funded capex plans in the near term.

Detailed description of the key rating drivers:

Key strengths

Dominant position in the domestic caustic soda industry which is likely to be maintained

GACL is the second-largest player of caustic soda in the country, with an installed capacity (for caustic soda lye and caustic soda flakes combined) of around 2,230 metric tonne per day (MTPD) as on April 30, 2023, at its plants in Vadodara and Dahej, in Gujarat. GACL has gradually built a strong position in the industry through the continuous expansion of production capacities to cater to the growing demand for its products over the past four decades. It has already commissioned its caustic soda project in the JV with NALCO for 800 MTPD and have also successfully completed its caustic soda expansion of 525 MTPD at its Dahej plant, which shall further consolidate its position in the chlor-alkali industry in India.

Over the years, GACL has also introduced new chlorine derivatives (downstream products) for higher captive utilisation of chlorine, an essential by-product generated during the manufacturing of caustic soda. The company has more than 36 products in its basket, which has enabled it to leverage upon its large production capacity and protect its profitability from the effects of the volatility in chlorine prices, to some extent.

Integrated operations and diversified customer base

The operations of GACL are well-integrated, with the by-product of one process used as a raw material for another, thus enabling the company to optimally utilise its large production capacity. It also protects GACL's profitability, to an extent, from the effects of the inherent cyclicality in the demand for its major products, as the adverse demand scenario for one set of products is countered by the favourable movement in other products. GACL's products find application in various processes across a diverse range of industries, including textile, pulp and paper, alumina, soaps and detergents, rayon, fertilisers, petroleum, fertilisers, pharmaceuticals, agrochemicals, water treatment, ink, paint, etc. This allows the company to cater to a diversified customer base, and thus, helps it counter the slowdown in any industry or a group of industries.

Competitive cost structure owing to state-of-the-art technology and captive power generation to meet part of its energy requirements

The cost structure of GACL has remained competitive because of its membrane cell technology used for the electrolysis of salt, which consumes one-third less power as compared to the traditional mercury cell technology and is also less polluting. The captive power plant (CPP) for meeting part of its energy requirements and the investment in windmills and solar power plants to offset the higher cost of power purchased from the market, aids its cost structure. The total installed capacity of the solar power plant stood at 35 MW at the Charanka Solar Park – Patan, 640 kW floating solar power plant on the reservoir of the captive power plant, and 220 kW solar rooftop installations at its Dahej complex. This is apart from a wind power generation capacity of 171.45 MW, captive 90 MW gas-based power plant, and 40-50 MW participation in a 145-MW group captive gas-based power plant operated by Gujarat Industries Power Company Limited (GIPCL; rated 'CARE AA-; Stable/CARE A1+'). The average cost of power consumed by GACL stood at ₹8.42 per unit in FY23. Furthermore, GNAL has already commissioned its 130-MW coal-based CPP, wherein the excess power generated shall be availed by GACL as required.

Continued growth in revenue during FY23; albeit moderation during Q1FY24

The total operating income (TOI) of the company continued to increase during FY23 reflected by 20% growth on a y-o-y basis largely owing to the improved caustic realisations coupled with healthy demand in the industry. However, the PBILDT margin dipped from 26.38% in FY22 to 24.56% in FY23 primarily due to moderation in caustic realisations in Q4FY23 and increase in power and fuel costs during the year. The profit after tax (PAT) margin also declined to 9.10% in FY23 from 14.91% in FY22 primarily due to losses reported in its JV, GNAL, as well as higher finance cost due to high interest rates during the year. During Q1FY24, the TOI of the company decreased by around 19% on a y-o-y basis despite operating at an optimum capacity utilisation mainly due to continued decline in the caustic realisations during the quarter. The PBILDT margin also dipped to around 5% during Q1FY24 as compared with 32% during Q1FY23 led by bottoming out of ECU realisations. Furthermore, the company also reported net losses during Q1FY24 primarily due to continued losses reported in GNAL on account of adverse market scenario coupled with high interest costs. However, going forward, with expected improvement in the ECU realisations and completion of its major capex during FY23, CARE Ratings expects the company to reap the benefits of the same which should result in continued increase in its scale of operations.

Comfortable capital structure and strong debt coverage indicators, albeit expected to moderate on consolidation of JV

GACL's capital structure remained comfortable, with an overall gearing of 0.10x as on March 31, 2023. Furthermore, its debt coverage indicators stood strong, marked total debt/ PBILDT improved at 0.54x during as on March 31, 2023 (1.49x as on March 31, 2022) owing to healthy operating profitability during the year coupled with minimal increase in debt. However, owing to dip in its operating profitability during Q1FY24, its PBILDT interest coverage moderated to 4x during the quarter as against 56x in FY23. Furthermore, its debt coverage indicators are expected to moderate over the medium term considering the consolidation of the JV, i.e., GNAL, which stabilised its operations during FY23. However, the debt coverage indicators are expected to be supported by gradual repayment of debt as well as healthy cash accruals on the back of commissioning of its large-size projects in FY23.

Liquidity: Strong

The liquidity of GACL is marked by strong accruals and the presence of liquid investments to the tune of ₹362 crore as on June 30, 2023 (₹527 crore as on March 31, 2023). With an overall gearing of 0.10x as on March 31, 2023, it has sufficient gearing headroom to avail additional debt for its capex. Although over the past few years, the company has largely funded its capex through its healthy internal cash accruals. Furthermore, GACL has recently commissioned most of its ongoing capex and has no major debt-funded capex plans in the near term. The company's entirely unutilised bank lines are more than adequate to meet its incremental working capital needs over the next one year. Furthermore, the operating cycle remained comfortable at 24 days during FY23 (FY22: 26 days), and the current ratio remained healthy at 1.67x as on March 31, 2023 (1.48x as on March 31, 2022).

Key weaknesses

Presence in an inherently cyclical caustic soda industry which is currently going through downturn

The caustic soda industry is inherently cyclical. The industry witnessed a cyclical downturn after H1FY20, which was further exacerbated during FY21 owing to the COVID-19 pandemic-related contraction in demand from major end-use industries. ECU realisations dropped to a decadal low level of around ₹23,000 per metric tonne (MT) in FY21. However, from March 2021 onwards, the sector saw a revival with an improvement in demand from end-user industries and better availability of raw materials, leading to a rebound in the ECU realisations to around ₹55,000 per MT. Thereafter, the caustic prices reduced drastically by end of Q1FY24 owing to oversupply in the global market coupled with subdued demand in downstream chlorine industries, which led to moderation in ECU realisations to around 32,000/MT during June 2023, impacting the profitability of the caustic soda players including GACL in the near term. CARE Ratings expects moderation in profitability of the industry players during Q2FY24 as well on account of low ECU realisations currently prevailing in the market.

Susceptibility of its profitability to adverse movement in the prices of gas and power and the threat of cheaper import

GACL's profitability is susceptible to adverse movements in the market prices of gas and power since electrolysis is an energy-intensive process and power cost constitutes a significant part of its cost structure. Power cost constituted around 33-34% of GACL's TOI during FY23 and Q1FY24 (FY22: 29%). Besides, the Indian chlor-alkali industry faces competition from cheap imports from lower power-cost countries. Of India's total imports, more than 90% are contributed by Japan, China, Korea, Qatar, and Iran, with over 50% imports from Japan alone, mainly due to the tax treaty and lower logistics cost to cater to the requirement of aluminium manufacturers on the eastern coast of India. Domestic manufacturers have sought a level-playing field from the government by way of an increase in customs duty on caustic soda imports, a GST structure for electricity taxes, and the imposition of export duty on salt, to effectively compete against imports.

Risk of adverse movement in foreign exchange rates

GACL is exposed to the risk of adverse movement in foreign exchange rates because of its long-term borrowings denominated in US Dollar, raised for part-funding of its capex plans. Furthermore, as a matter of policy, GACL does not hedge its foreign currency exposure. During FY23, GACL imported raw materials of around ₹466 crore and had term debt repayment liabilities of ₹44 crore, against which it made exports of around ₹752 crore, thus providing a natural hedge to its foreign currency exposure to a large extent. Furthermore, to mitigate its forex risk, GACL has opened an Exchange Earners' Foreign Currency Account (EEFC) US Dollar account, as per the Reserve Bank of India (RBI) guidelines, to deposit the export earnings in the said account and to utilise the same for making US Dollar repayments towards servicing its foreign currency debt and import pay-outs. This mitigates the exchange rate risk to a large extent.

Saleability risk associated with large-sized recently completed projects
During FY23, GACL commissioned major ongoing capex of expanding the caustic soda capacity by 525 TPD and chloromethane plant after facing delays in completion on account of COVID-19 pandemic. Both these plants were operating at 70% of installed capacity as on April 30, 2023. As a part of the expansion plan, GACL also commissioned a new 700-TPD caustic evaporation unit. Furthermore, the company commissioned a hydrazine hydrate plant in September 2022 and phosphoric plant in April 2023. No major capex is expected in the near term except the ongoing chlorotoluene project of ₹350 crore which shall be funded by internal accruals and expected to be completed by October 2024. CARE Ratings notes that the company has completed its debt-funded capex during FY23 and has no major debt-funded capex plans in the near term. However, the company is still exposed to the stabilisation risks associated with its recently completed projects.

Weak performance of GNAL requiring financial support from its sponsors, viz., GACL and NALCO
GACL's project under the 60:40 JV with NALCO, viz, GNAL, for setting up a manufacturing unit for producing an 800 MTPD of caustic soda plant along with a 130-MW captive power plant at Dahej, in the vicinity of GACL's existing plant, had commissioned operations on March 30, 2022, along with its one unit of coal-based captive power plant (CPP) of 65 MW and the second unit of CPP (65 MW) commissioned operations in April 2023. From the caustic soda produced from the plant, at least 450 MTPD has been agreed to be sold to NALCO (Odisha plant) at market rates and the remaining will be sold in the open market; the marketing rights of which will vest with GACL. The unit also contains manufacturing facilities for other downstream products and for the utilisation of chlorine, an essential byproduct generated for manufacturing caustic soda. The balance quantities of all the products manufactured by the JV will be sold by GACL as the sole commission selling agent of the JV. Thus, GACL will be exposed to the marketing risks as well as the risk of chlorine disposal for GNAL. GNAL's project completion was with significant delay and then due to challenges in chlorine disposal, its plant could not ramp-up production in FY23 leading to significant cash losses in FY23. Furthermore, during Q1FY24, GNAL continued to report cash losses on back of lower ECU realisations despite increase in its production levels. On the back of lower ECU realisations prevailing in the market, CARE Ratings expects GNAL to continue to incur cash losses in FY24, necessitating timely financial support from both of its promoters.

Environment, social, and governance (ESG) risks

Risk factors	Compliance and action by the company
Environmental	The treated wastewater after conforming to Gujarat Pollution Control Board (GPCB) norms is discharged to channel of Vadodara Enviro Channel Limited (VECL) which is finally discharged into Bay of Khambhat. Furthermore, GACL's air emission is maintained within GPCB norms. The wastes are disposed of at the Treatment, Storage and Disposal facility (TSDF) or Common Hazardous Waste Incineration Facility (CHWIF) depending on whether the same is hazardous or otherwise. GACL ensures energy audit at regular intervals and have installed 35-MW solar power plant and 171.45 MW of wind power plants.
Social	GACL follows all the required protocols for their employee safety and well-being. For instance: providing personal protective equipment and trainings to workers on safety and health aspects of handling chemicals.
Governance	50% of the GACL's board comprises independent directors. GACL has a dedicated investor grievance redressal mechanism with healthy disclosures. GACL assures separate meetings for independent and non-independent directors along with regular internal risk management committees to address the risks and measures to mitigate them.

Applicable criteria

CARE'S policy on default recognition
Rating methodology - Consolidation
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Criteria on assigning 'Rating Outlook' and 'Credit Watch' to credit ratings
Rating methodology - Short Term Instruments
Rating methodology - Manufacturing Companies

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Commodities	Chemicals	Chemicals & Petrochemicals	Commodity Chemicals

GACL was promoted in 1973 by the Government of Gujarat (GoG) through its industrial investment arm, Gujarat Industrial Investment Corporation Limited (GIIC). As on June 30, 2023, GoG as the promoter, through its various undertakings, held 46.28% equity in the company, the largest being through Gujarat State Investments Limited (GSIL) with 20.87% holding. GACL is the second-largest player in the domestic caustic chlorine industry with integrated operations. It produces a wide range of products, including caustic soda, liquid and gaseous chlorine, hydrogen peroxide, phosphoric acid and aluminium chloride, which find application across a diversified group of industries, including textile, pulp and paper, aluminium, detergents, soaps, rayon, plastics, pharmaceuticals, water treatment, and agricultural chemicals.

Brief Financials (₹ crore)	FY22 (A)	FY23 (A)	Q1FY24 (Prov.)
Total operating income	3,755	4,503	913
PBILDT	990	1,106	43
PAT / (Net loss)	560	410	(57)
Overall gearing (times)	0.10	0.10	NA
PBILDT Interest coverage (times)	161.15	56.83	3.91

A: Audited, Prov.: Provisional; NA: Not available; Financials are reclassified as per CARE Ratings' standards.
Note: 'the above results are latest financial results available'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3

Complexity level of various instruments rated: Please refer Annexure-4

Lender details: Please refer Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Commercial paper-CP/STD	-	-	-	7-364 days	100.00	CARE A1+
Fund-based - LT-Cash credit	-	-	-	-	130.00	CARE AA+; Stable
Non-fund-based - ST-BG/LC	-	-	-	-	339.50	CARE A1+
Term loan-Long term	-	-	-	March 2028	593.98	CARE AA+; Stable

*No commercial paper was outstanding as on September 01, 2023

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021
1	Term loan-Long term	LT	593.98	CARE AA+; Stable	1)CARE AA+; Stable (26-Jun-23)	1)CARE AA+; Stable (27-Jun-22)	1)CARE AA+; Stable (06-Jul-21) 2)CARE AA+; Stable (07-May-21)	1)CARE AA+; Stable (06-Oct-20)
2	Commercial paper-CP/STD	ST	100.00	CARE A1+	1)CARE A1+ (26-Jun-23)	1)CARE A1+ (27-Jun-22)	1)CARE A1+ (06-Jul-21)	1)CARE A1+ (06-Oct-20)
3	Fund-based - LT-Cash credit	LT	130.00	CARE AA+; Stable	1)CARE AA+; Stable (26-Jun-23)	1)CARE AA+; Stable (27-Jun-22)	1)CARE AA+; Stable (06-Jul-21) 2)CARE AA+; Stable (07-May-21)	1)CARE AA+; Stable (06-Oct-20)
4	Non-fund-based - ST-BG/LC	ST	339.50	CARE A1+	1)CARE A1+ (26-Jun-23)	1)CARE A1+ (27-Jun-22)	1)CARE A1+ (06-Jul-21) 2)CARE A1+ (07-May-21)	1)CARE A1+ (06-Oct-20)

*Long term/Short term.

Annexure-3: Detailed explanation of covenants of the rated instruments/facilities: Not applicable

Annexure-4: Complexity level of the various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Commercial paper-CP/STD	Simple
2	Fund-based - LT-Cash credit	Simple
3	Non-fund-based - ST-BG/LC	Simple
4	Term loan-Long term	Simple

Annexure-5: Lender details

To view the lender wise details of bank facilities please [click here]

Note on the complexity levels of the rated instruments: CARE Ratings has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:
Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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