Aarti Surfactants Limited

June 28, 2024

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	150.00 (Reduced from 189.50)	CARE A-; Stable	Revised from CARE BBB+; Stable
Long-term instruments – Preference shares - Redeemable	18.50	CARE BBB+; Stable	Revised from CARE BBB; Stable

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

The upgrade in ratings of Aarti Surfactants Limited's (ASL's) long-term bank facilities and instrument reflects the consistent improvement in its profitability, aided by stabilisation of raw material prices and economies of scale. While ASL's revenue from operations declined marginally to ₹590 crore in FY24 due to pressure on realisations despite higher sales volume, its profitability improved by around 290 bps YoY to 10.7% on the back of improving gross margin and better absorption of fixed costs. ASL's net worth was bolstered by raising of additional equity through rights issue translating into deleveraging of the capital structure as indicated by overall gearing and total outside liabilities to tangible net worth (TOL/TNW) improving to 0.46x and 0.86x, respectively, as on March 31, 2024 from 0.89x and 1.31x, respectively, as on March 31, 2023. Going forward, CARE Ratings Limited (CARE Ratings) expects the company's revenue to grow by 10-15% p.a. over the next two years with profit before interest, lease rentals, depreciation and taxation (PBILDT) margin sustaining above 10% p.a. driven by focus on increasing export market share, new product development, and expected stability in raw material prices.

Ratings derive comfort from the company's established market position in the domestic surfactants industry, reputed client base with a history of repeat orders, and promoters' extensive experience. Ratings also factor in the company's healthy liquidity position and comfortable capital structure. These strengths are partially offset by the vulnerability of ASL's operating margin to volatility in raw material prices, sizeable capex plans for new product development and capacity expansion and intensive competition in the surfactants industry.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Sustained growth in scale of operations to above ₹800 crore while maintaining healthy working capital cycle translating into comfortable liquidity buffer.
- Improving EBITDA margin to above 12% driven by new product launches on a sustained basis.

Negative factors

- Lower-than-expected growth in sales volume with EBIDTA margin below 7% impacting cash accruals.
- Higher-than-anticipated debt-funded capex or investment in group entities impacting the capital structure and/or liquidity profile.
- Total debt to PBILDT deteriorating above 2.5x on a sustained basis.

Analytical approach: Standalone

For arriving at the ratings of ASL, CARE Ratings has considered its standalone financials. ASL has one subsidiary namely, Aarti HPC Limited, which remained non-operational as on March 31, 2024.

Outlook: Stable

The Stable outlook reflects CARE Ratings' expectation that ASL will generate healthy cash flows to fund debt repayment obligation over the medium term driven by steady volume growth and sustenance of healthy profitability margins.

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

Detailed description of key rating drivers:

Key strengths

Established market position with reputed client base

ASL is among the largest surfactants manufacturers in the country and enjoys a healthy market position in the domestic market with reputed clientele including multinationals and domestic customers in FMCG sector. It is a preferred supplier for Hindustan Unilever Limited, Procter & Gamble Home Products Pvt. Ltd., and Dabur India Limited. While ASL's customer concentration risk remains high as contribution from top three customers to total sale was around 68% in FY24, long relations with large customers, and barriers to entry as suppliers to large multinationals to largely mitigate the risk.

Healthy scale of operations; growth momentum expected to continue

The revenue from operations has grown at a healthy CAGR of ~16% in the last four years till FY24 to ~₹590 crore driven by steady volume growth. While the company's revenue marginally declined in FY24 owing to correction in realisations considering reduction in input costs, the same contributed to better profitability with EBITDA margin growing by ~290 bps YoY to 10.7% in FY24. The contribution of export sales has remained in the range of 25-30% over the last three years. Going forward, CARE Ratings expects the company's scale of operations to continue to grow through increase in wallet share from existing domestic clients, addition of new clients with a focus on export markets and new product development, translating into steady operating profitability over the medium term.

Comfortable capital structure and debt coverage metrics

ASL's capital structure has improved in FY24 with the raising of additional equity of ~₹49 crore through a rights issue. Its overall gearing and TOL/TNW reduced to 0.46x and 0.86x, respectively, as on March 31, 2024, from 0.89x and 1.31x, respectively, as on March 31, 2023. The debt coverage metrics also remained comfortable with interest cover of 3.35x and total debt/PBILDT of 1.60x in FY24 against 2.11x and 3.20x, respectively, in FY23. With the expectations of steady performance going forward, ASL's financial risk profile is likely to remain healthy.

Strong background of promoters in chemical industry through Aarti Industries Limited

ASL continues to benefit from promoters' rich experience in the chemicals/pharma sector through the Aarti Group. The company was formed through the demerger of the home and personal care division of Aarti Industries Limited (AIL), with the shareholders of AIL being the shareholders of ASL at the time of demerger. ASL is managed under the guidance of Chandrakant Vallabhaji Gogri, who is the founder and the current Chairman Emeritus of AIL. ASL's Managing Director, Nikhil Parimal Desai, is the son of Parimal H Desai, Whole Time Director of AIL. Aarti Industries was incorporated in 1984 and is a leading Indian manufacturer of speciality chemicals and pharmaceuticals with a global footprint. AIL possesses a diverse portfolio of basic chemicals, agrochemicals, speciality chemicals, and intermediates, which are extensively used in manufacturing pharmaceuticals, agri-products, polymers, additives, pigments, and dyes. The promoter's shareholding has increased to 49.81% as on March 31, 2024 (FY22: 45%) due to the rights issue in January 2023.

Key weaknesses

Operating profitability susceptible to volatility in raw material prices

ASL has high dependency on Lauryl alcohol (LA), fatty acids (HCFA), and Alpha Olefin (AO) which forms major portion of the raw material costs. The raw material pricing is volatile in nature and is linked to palm oil prices. Any volatility in raw material prices can impact ASL's profitability, as witnessed in the past, as raw material cost accounts for ~76% of the revenue in FY24. Nevertheless, with raw material prices having stabilised in the recent quarters, ASL's operating profitability remained relatively stable at ~10% in the last six quarters till Q4 FY24.

Capex plans for new product and capacity development

ASL has planned a capex of ₹25-30 crore per annum over the next three years for new product line development and capacity expansion, at both Pithampur and Silvassa facility and R&D Unit in Mumbai, which will be funded entirely from internal accruals. The company's ability to timely execute the capex without significant cost overruns and its translation into increased revenue and profitability remains a key monitorable.

Intense competition from domestic and international players

The speciality chemicals industry is highly competitive. The primary competitors of ASL are multi-national companies such as BASF Corporation, Godrej Industries Limited, Clariant Limited, Croda International Plc, Evonik Industries, Solvay S.A., Stepan Company, and The Dow Chemical Company. In the domestic market, Galaxy Surfactant Limited is the largest pure play surfactant manufacturer. Flexibility to respond to changing business conditions, including research and creation capabilities, is an important element towards maintaining a competitive position in the surfactants industry. In addition to competition within the surfactants industry, ASL is also affected by competition faced by its customers, specifically manufacturers of FMCG products which also limits its pricing power.

Liquidity: Adequate

The liquidity is adequate with free cash and liquid investments of ₹6.2 crore and buffer from unutilised working capital facilities of more than ₹75 crore (with commensurate drawing power) as on March 31, 2024. ASL is projected to generate cash flow from operations of ₹35-40 crore per annum over the next 2-3 years. Also, the company has debt repayment obligations of ₹26 crore in FY25, ₹21 crore in FY26, and ₹28 crore in FY27. Additionally, the company plans to incur growth capex of ₹20-30 crore per annum over the next three years, funded entirely through internal accruals. The average working capital utilisation remained at around 48% for the 12-months ended April 30, 2024, for fund-based limits providing a healthy cushion to the liquidity. In Q4FY24, the company received the remaining 60% of the rights issue (₹29 crore), which was utilised to meet working capital requirements.

Assumptions/Covenants: Not applicable

Environment, social, and governance (ESG) risks

Majority of ASL's raw materials are palm oil derivatives imported from southeast Asian countries such as Indonesia and any change in policy, including import restrictions or tariffs, can directly impact ASL's business. Moreover, the raw material availability is dependent on production of palm which is an agricultural product susceptible to vagaries of the climate. In process of making chemicals, ASL discharges effluents and takes steps to reduce air and water pollution including air filters and water treatment plants. Any tightening of pollution control norms could entail significant capex by the company thereby impacting its financial risk profile. Additionally, non-compliance with existing norms could lead to regulatory actions on the company which could impact its business. In terms of social factors, the company has around 334 permanent employees with an additional ~200 contract-based labour working at their facilities and maintaining harmonious relations with employees remains critical for its operations.

Applicable criteria

Definition of Default
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Manufacturing Companies
Financial Ratios – Non financial Sector

About the company and industry

Industry classification

Macro-economic Indicator	Sector	Industry	Basic Industry
Commodities	Chemicals	Chemicals & petrochemicals	Commodity chemicals

ASL was formed because of demerger of the home and personal care division of AIL. ASL is engaged in manufacturing ionic and non-ionic surfactants and specialty products serving the home and personal care (HPC) industry. Its product portfolio includes surfactants, mild surfactants, rheology modifiers, pearlising agents, UV filters, soap bases, and conditioning agents. ASL supplies surfactants, including concentrates for shampoo, hand wash, dish wash, and oral care. Apart from India, ASL also exports its products to USA, Europe, and Southeast Asian countries with exports accounting for 25% of the sales in FY24. ASL is a preferred supplier to Hindustan Unilever, Proctor & Gamble, Patanjali, and Dabur. Its manufacturing units are at Pithampur in Madhya Pradesh and Silvassa in Dadra Nagar Haveli.

Brief Financials (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)
Total operating income	600.18	589.86
PBILDT	46.63	63.01
PAT	12.71	22.27
Overall gearing (times)	0.89	0.46
Interest coverage (times)	3.15	4.49

A: Audited UA: Unaudited; Note: 'these are latest available financial results'

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years: Annexure-2

Covenants of rated instrument / facility: Annexure-3

Complexity level of various instruments rated: Annexure-4

Lender details: 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
Fund-based - LT-Cash credit	-	-	-	-	70.00	CARE A-; Stable
Fund-based - LT-Cash credit	-	-	-	-	30.00	CARE A-; Stable
Fund-based - LT-Term loan	-	-	-	-	50.00	CARE A-; Stable
Preference Shares-Redeemable	-	August 20, 2019	0.00	August 19, 2026	18.50	CARE BBB+; Stable

Annexure-2: Rating history for 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 2024-2025	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
1	Fund-based - LT-Term loan	LT	50.00	CARE A-; Stable	-	1)CARE BBB+; Stable (07-Aug-23)	1)CARE BBB+; Stable (24-Aug-22)	1)CARE BBB+; Stable (11-Aug-21)
2	Preference Shares-Redeemable	LT	18.50	CARE BBB+; Stable	-	1)CARE BBB; Stable (07-Aug-23)	1)CARE BBB; Stable (24-Aug-22) 2)CARE BBB; Stable	1)CARE BBB (RPS); Stable (11-Aug-21)

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2024-2025	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
							(15-Apr-22)	
3	Fund-based - LT-Cash credit	LT	70.00	CARE A-; Stable	-	1)CARE BBB+; Stable (07-Aug-23)	1)CARE BBB+; Stable (24-Aug-22)	1)CARE BBB+; Stable (11-Aug-21)
4	Fund-based - LT-Cash credit	LT	30.00	CARE A-; Stable	-	1)CARE BBB+; Stable (07-Aug-23)	1)CARE BBB+; Stable (24-Aug-22)	1)CARE BBB+; Stable (11-Aug-21)

LT: Long term; ST: Short term; LT/ST: Long term/Short term

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

Annexure-4: Complexity level of various instruments rated

Sr. No.	Name of the Instrument	Complexity Level
1	Fund-based - LT- Cash credit	Simple
2	Fund-based - LT- Term loan	Simple
3	Preference Shares - Redeemable	Highly Complex

Annexure-5: Lender details

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

Note on complexity levels of 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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