Gujarat Alkalies and Chemicals Limited

August 05, 2024

Facilities/ instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	598.42 (Reduced from 723.98)	CARE AA; Stable	Reaffirmed
Short-term bank facilities	339.50	CARE A1+	Reaffirmed
Commercial paper	100.00	CARE A1+	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Ratings assigned to 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 with captive power generation to meet part of its energy requirement and state-of-the-art technology. Ratings also derive strength from wide product portfolio, which finds application across diversified end-use industries, and its comfortable capital structure. CARE Ratings Limited (CARE Ratings) also factors proposed issue of compulsory convertible debentures (CCDs) by its joint venture (JV) entity, GACL-NALCO Alkalies & Chemicals Private Limited [GNAL; rated 'CARE BBB+; Stable/ CARE A2' and 'Provisional CARE AA (CE); Stable' for CCDs], which shall support its liquidity.

However, long-term rating is constrained due to GACL's presence in an inherently cyclical chlor-alkali industry with volatility in the electrochemical unit (ECU)[2], competition from imports, the susceptibility of its profitability to adverse movement in the market prices of gas and power constituting a significant part of its cost structure, and the risk related to adverse movement in foreign exchange rates. Ratings also factor in significant moderation in its profitability in FY24 (refers to April 1 to March 31) on the back of lower sales realisations led by oversupplied domestic market condition in the caustic soda industry and consequent weakening of its debt coverage indicators and liquidity. Further, sustained losses in GNAL pressurises GACL's consolidated financial profile. CARE Ratings expects gradual improvement in the profitability of GACL and GNAL from Q1FY25 onwards backed by improvement in the ECU realisations and increase in capacity utilisation.

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 the inherent cyclicality of chlor-alkali industry and thus earning healthy PBILDT margin on a sustained basis; along with improvement in total debt/ PBILDT below 1.50x on a sustained basis.
- Gaining significant market leadership position in the caustic soda industry while securing significant portion od 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

- Lower than envisaged improvement in profitability with PBIDLT margin remaining below 8-9% on standalone basis and below 10% on consolidated basis for H1FY25.
- Sustained pressure on its profitability marked by PBILDT margin remaining below 15% from FY26 owing to continued lower ECU realisations.
- Deterioration in consolidated total debt/ PBILDT beyond 3x on a sustained basis.
- Heavy dumping of caustic soda products significantly impacting its ECU realisations.
- 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.

Analytical approach: Consolidated.

CARE Ratings has considered 'Consolidated' analytical approach for ratings of GACL, as there are strong operational and financial linkages of GACL with its JV company, GNAL, which has set up a caustic soda manufacturing facility at Dahej, wherein, GACL holds 60% equity stake as placed at Annexure-6. GACL has applied equity method for the JV accounting for GNAL to arrive at consolidated financial results while CARE Ratings applied full consolidation of financials of GNAL to arrive at consolidated financial results.

[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

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. CARE Ratings expects the entity to improve its financial risk profile with expected improvement in industry scenario in near to medium-term with no large debt-funded capex plans in the near term.

Detailed description of key rating drivers:

Key strengths

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

GACL is the third-largest player of caustic soda in the country in terms of capacity, with an installed capacity (for caustic soda lye and caustic soda flakes combined) of around 2,230 metric tonne per day (MTPD) as on March 31, 2024, 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 in the last four decades. It has also commissioned caustic soda project in the JV with NALCO for 800 MTPD. On a consolidated basis, GACL with GNAL has the second-largest installed capacity in the country.

Over the years, GACL has also introduced new chlorine derivatives (downstream products) for higher captive utilisation of chlorine, an essential by-product generated during manufacturing 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

GACL's operations 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 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, and paint among others. This allows the company to cater to a diversified customer base, thus helping it counter the slowdown in any industry or a group of industries. However, due to subdued demand from the end-user industries and oversupply in global market, GACL suffered losses in FY24.

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

GACL's cost structure 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. 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 wind power generation capacity of 171.45 MW and captive 90-MW gas-based power plant. The average cost of power consumed by GACL stood at ₹8.32 per unit in FY24 (FY23: ₹8.42 per unit). Moreover, GNAL has already commissioned its 130-MW coal-based CPP, wherein the excess power to the tune of around 20 MW can be availed by GACL for its adjacent chloromethane plant as required.

Comfortable capital structure despite consolidation of JV

GACL's capital structure remained comfortable, with consolidated overall gearing of 0.38x as on March 31, 2024 and is expected to remain comfortable below 0.30x in medium term. GNAL is in the process to restore its earlier capital structure by way of raising CCDs of ₹500 crore which is to be placed by end-August 2024. The CCDs are expected to have a tenor of 60 months with bullet repayment. The CCDs are to be guaranteed or backstopped in form of put option by GACL and NALCO in their shareholding ratio. The proceeds from CCDs shall be utilised largely for repayment/prepayment of partial ECB to the tune of ₹390 crore and balance for working capital requirements. With the said placement of CCDs, GNAL's overall gearing is expected to improve significantly.

Liquidity: Strong
GACL's liquidity is marked by presence of cash and liquid investments to the tune of ₹155 crore as on March 31, 2024 (₹527 crore as on March 31, 2023). With consolidated overall gearing of 0.38x as on March 31, 2024, it has sufficient gearing headroom to avail any additional debt, if required. Although in the last few years, GACL has largely funded its capex through its healthy internal cash accruals. GACL has capex plans of around ₹350 crore for its chlorotoluene plant out of which, around ₹50 crore has been incurred in FY24 and balance is expected to be incurred by December 2024. GACL's entirely unutilised bank lines are more than adequate to meet its incremental working capital needs and the company may resort to short-term loans from Gujarat State Financial Services to the tune of around ₹100-125 crore. Furthermore, the operating cycle remained comfortable at around 24 days in FY24.

Key weaknesses

Significant deterioration in profitability and debt coverage indicators in FY24 albeit expectation of gradual improvement from Q1FY25 onwards
GACL's total operating income (TOI) declined in FY24 as ECU realisations which had peaked to around ₹55,000/MT in FY23, moderated significantly to around ₹32,000/MT in FY24. This was mainly due to weak caustic soda industry scenario which is currently in an oversupplied situation on the back of large capacity additions in the recent past. Subdued demand from the end-user industries further exacerbated the industry scenario. However, GACL achieved healthy capacity utilisation levels of over 80% in FY24. The consolidated PBILDT margin dipped from 21.00% in FY23 to 3.62% in FY24 due to substantial moderation in ECU realisations. Further, GACL had commissioned large size capex in FY22 and FY23, which did not yield desired returns while adding overhead costs leading to net losses in FY24. This led to moderation in its consolidated debt coverage indicators in FY24 marked by total debt/ PBILDT and PBILDT interest coverage to 14.92x (FY23: 2.43x) and 0.86x (FY23: 9.72x) respectively.
As informed by the management, the ECU realisations have improved from around ₹32,000/ MT in Q4FY24 to over ₹34,500/ MT in Q1FY25. The ECU realisations are expected to gradually improve in the near to medium term backed by expected growth in demand from the end-user industries, thereby leading to increase in capacity utilisation. CARE Ratings expects improvement in the operating profitability of GACL and GNAL from Q1FY25 supported by improvement witnesses in ECU realisations and increase in capacity utilisation. CARE Ratings expects GACL to achieve PBILDT margin of around 10-11% in FY25 on a standalone basis and around 12% on a consolidated basis.
GACL's debt coverage indicators are expected to moderate over the medium term considering the sub-optimal profitability. However, the debt coverage indicators are expected to be supported by improvement in profitability of GACL and GNAL from Q1FY25 onwards and gradual repayment of consolidated debt along with prepayment of debt by GNAL in Q2FY25 from proceeds of proposed CCDs of ₹500 crore.

Weak operational and financial performance of GNAL
GACL's project under the 60:40 JV with NALCO, 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 in the open market, the marketing rights of which are vested 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. Balance quantities of products manufactured by the JV are sold by GACL as the sole commission selling agent of the JV. Thus, GACL is exposed to the marketing risks as well as the chlorine disposal risk for GNAL.
GNAL's project completion was with significant delay and due to challenges in chlorine disposal, its plant could not ramp-up production in FY23 leading to significant losses in FY23. Furthermore, in FY24, GNAL continued to report net loss of ₹174 crore in FY24 owing to subdued caustic soda prices and negative chlorine realisations despite operating at around 65% capacity (increased from 49% in Q1FY24 to 82% in Q4FY24). This led to significant erosion of its net worth base leading to worsening of its leverage though proposed CCDs of ₹500 crore are expected to improve GNAL's capital structure and liquidity.
GNAL is ramping-up its scale of operations and is further expected to achieve 85-90% capacity utilisation in near to medium term. With improvement in ECU realisations from Q1FY25 and increase in capacity utilisation, operating profitability is expected to improve from FY25 onwards.

Susceptibility of its profitability to adverse movement in gas and power prices and 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 since past two years (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, 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. As a matter of policy, GACL does not hedge its foreign currency exposure. In FY24, GACL imported raw materials of around ₹358 crore and had term debt repayment liabilities of ₹137 crore, against which it made exports of around ₹753 crore, thus providing a natural hedge to its foreign currency exposure to a large extent. Moreover, 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.

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. GACL's air emission is maintained within GPCB norms. The waste is 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 has installed 35-MW solar power plant and 171.45 MW of wind power plants.
Social	GACL follows required protocols for its 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 and regular internal risk management committees to address the risks and measures to mitigate them.

Applicable criteria

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

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, 2024, GoG as the promoter, through its undertakings, held 46.28% equity in the company, the largest being through Gujarat State Investments Limited (GSIL) with 20.87% holding. GACL is the third-largest player in terms of the installed capacity 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 applications across a diversified group of industries, including textile, pulp and paper, aluminium, detergents, soaps, rayon, plastics, pharmaceuticals, water treatment, and agricultural chemicals.

Brief Financials – Consolidated (₹ crore)	March 31, 2023 (A)	March 31, 2024 (A)	March 31, 2023 (UA) ^	March 31, 2024 (UA) ^
Total operating income	4,503	3,785	4,664	4,379
PBILDT	1,106	115	979	159
PAT	410	(237)	299	(307)
Overall gearing (times)	0.10	0.09	0.38	0.38
Interest coverage (times)	56.83	2.57	9.72	0.86

A: Audited; UA: Unaudited; Note: these are latest available financial results
^ basis the full consolidation of GNAL; Financials classified as per CARE Ratings' standards

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 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
Commercial paper-CP/STD *	NA	NA	NA	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	468.42	CARE AA; Stable

*No commercial paper was outstanding as on July 15, 2024; NA = Not applicable

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	Term loan-Long term	LT	468.42	CARE AA; Stable	-	1)CARE AA; Stable (13-Feb-24) 2)CARE AA+; Stable (20-Sep-23) 3)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)
2	Commercial paper-CP/STD	ST	100.00	CARE A1+	-	1)CARE A1+ (13-Feb-24) 2)CARE A1+ (20-Sep-23) 3)CARE A1+ (26-Jun-23)	1)CARE A1+ (27-Jun-22)	1)CARE A1+ (06-Jul-21)
3	Fund-based - LT-Cash credit	LT	130.00	CARE AA; Stable	-	1)CARE AA; Stable (13-Feb-24) 2)CARE AA+; Stable (20-Sep-23) 3)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)
4	Non-fund-based - ST-BG/LC	ST	339.50	CARE A1+	-	1)CARE A1+ (13-Feb-24) 2)CARE A1+ (20-Sep-23) 3)CARE A1+ (26-Jun-23)	1)CARE A1+ (27-Jun-22)	1)CARE A1+ (06-Jul-21) 2)CARE A1+ (07-May-21)

LT: Long term; ST: Short term

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

Annexure-4: Complexity level of 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 lender-wise details of bank facilities please click here

Annexure-6: List of entities consolidated

Sr No	Name of the entity	Extent of consolidation	Rationale for consolidation

1	GACL-NALCO Alkalies & Chemicals Pvt Ltd	Full	JV; operational and financial linkages

Note: Till FY24, GACL had applied equity method for the JV accounting for GNAL to arrive at consolidated financial results as GNAL was not material subsidiary. However, CARE Ratings has considered the full consolidation of financials of GNAL to arrive at consolidated financial results of GACL.

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 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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