

Deep Industries Limited

June 07, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings ¹	Rating Action
Long term Bank Facilities	150.62	CARE A- (Single A Minus) (Credit Watch with developing implications)	Revision in Credit Watch from 'Credit Watch with negative implications' to 'Credit Watch with developing implications'
Short term Bank Facilities	2.17	CARE A2+ (A Two Plus) (Credit Watch with developing implications)	Revision in Credit Watch from 'Credit Watch with negative implications' to 'Credit Watch with developing implications'
Long term / Short term Bank Facilities	90.00	CARE A-/CARE A2+ (Single A Minus / A Two Plus) (Credit Watch with developing implications)	Revision in Credit Watch from 'Credit Watch with negative implications' to 'Credit Watch with developing implications'
Total Facilities	242.79 (Rupees Two Hundred Forty Two Crore and Seventy Nine lakh only)		

Details of facilities in Annexure -1

Detailed Rationale & Key Rating Drivers

The 'credit watch' on the ratings assigned to the bank facilities of Deep Industries Ltd. (DIL) have been revised from 'Credit Watch with negative implications' to 'Credit Watch with developing implications' on account of receipt of significant orders (new and renewal), during the period February 2019-April 2019, from its major client Oil and Natural Gas Corporation Ltd. (ONGC; rated CARE AAA; Stable / CARE A1+) which has mitigated the hitherto uncertainty associated with receipt of future orders from ONGC in light of dispute between the two parties due to termination of two Gas Dehydration Units (GDU) contracts in June 2018. However, the ratings assigned to the bank facilities of DIL are placed under 'Credit Watch with developing implications' on account of the impending possible impact of the proposed demerger of the company's various oil & gas services business segment into a separate company subject to receipt of necessary approvals.

As such, CARE will continue to closely monitor the developments with respect to the above-mentioned demerger and will take a view on the ratings of the company once the exact implication of this event on the credit risk profile of the company becomes clear.

The ratings continue to derive strength from DIL's established position in the domestic gas compression services business along-with its increasing operations in rigs and related services business, its healthy profitability and comfortable leverage and debt coverage indicators. The ratings also derive comfort from geographical diversification in the company's revenue profile with recent commencement of operations in its Middle-East based subsidiary; along-with prepayment of the entire outstanding term debt related to its terminated GDU contracts resulting in significant reduction in debt repayment obligations of the company in the medium term.

The ratings, however, continue to remain constrained by DIL's moderate scale of operations with intense competition in the rigs service business which is also susceptible to volatile day rates due to its linkages with crude oil prices, inherent risk associated with its E&P (exploration & production) business and inherent risk associated with renewal of contracts arising from client concentration risk; albeit it has track record of renewal of various contracts. The ratings are further constrained by its long pending receivables from ONGC pertaining to its terminated GDU contracts.

DIL's ability to increase its scale of operations through growth in its order book and efficient deployment of its resources along with ramp up of operations of its overseas venture, achieve substantial diversification in its client-base, sustain its healthy profit margin amidst high competition along with maintaining its comfortable capital structure and debt coverage indicators while efficiently managing any future investment requirement in its subsidiaries shall be the key rating sensitivities.

Furthermore, outcome of the proposed demerger and of the legal proceedings against the terminated GDU contracts shall be key monitorables.

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

Detailed description of the key rating drivers***Receipt of fresh large orders from ONGC***

During the period February 2019-April 2019 DIL has received significant fresh orders (new and renewal) from its major client ONGC. The total contract value of the said orders received in the above-mentioned period amounts to ~Rs.228 crore (around 50% of its outstanding order book of ~Rs.549 crore as on April 15, 2019). Though majority of the said orders are for its rigs segment, receipt of these significant orders from ONGC (in the light of pending clarity on DIL's rejoinder challenging the termination order of ONGC for DIL's 2 GDU contracts) mitigates the hitherto uncertainty associated with receipt of future orders from ONGC in other business segments. It has also been able to renew a gas compression contract from ONGC in February 2019.

Apart from emergence of clarity due to receipt of the above new orders from ONGC which has improved the revenue visibility of DIL, the company management has submitted a written communication to CARE that they do not foresee payment of any penalty to ONGC with respect to the termination of DIL's 2 GDU contracts in June 2018. In light of the above developments, CARE has removed the ratings of the bank facilities of DIL from 'credit watch with negative implications'.

Proposed demerger of DIL's oil & gas services business segment into a separate entity, which is still pending

In May 2018, DIL's Board of Directors had proposed the demerger of its oil and gas service business and E&P business segments in to two different companies so that the management can have a focussed approach in the two different business segments as they entail different skill sets and have varied growth opportunities/strategies. While the company had initially planned to complete this demerger by end-March 2019, the process has encountered some delay and the management now envisages completing the same by end-September 2019 subject to receipt of requisite approvals from various stakeholders. The company management has further articulated through a written submission that all the assets pertaining to oil & gas service business of DIL will be transferred to the resulting company. All the running contracts along with all the debts, liabilities, duties and obligations relating to the oil and gas service business, specific loans and borrowings raised and any other such borrowing will be transferred to the resulting company. The residual assets and liabilities pertaining to its E&P business segment would remain vested in DIL. Also, since the entire debt as on June 5, 2019 pertains to the oil and gas services business only and the same will be transferred to the resulting company, the residual DIL will then become a debt-free company. However, on account of the impending possible impact of this demerger on the credit profile of DIL, CARE has placed the rating on its bank facilities on 'credit watch with developing implications'. CARE will closely monitor the developments in this regard and shall take a view on the ratings once the exact implications of this event on its credit profile become clear post completion of the demerger process.

Key Rating Strengths

Established position in gas compression services with increasing operations in rigs and related service business: DIL has been serving the oil and gas industry since past two decades and has varied service offerings including gas compression, work-over rigs and drilling rigs and gas dehydration units in its portfolio. It has a leading position in providing third party gas compressing services with a dominant domestic market share, and is increasing its presence in the rigs and related service business. This apart, it has also ventured into the oil and gas exploration and production (E&P) business; which is albeit at nascent stage of development. DIL has also ventured overseas for providing oil & gas services through its subsidiary in the Middle-East which is envisaged to result in greater geographical diversification of its revenue. During FY19 (Prov.), it earned Rs.58.39 crore revenue from its overseas operations. Significant increase in its overseas operations through establishment of a longer track record will be a key monitorable.

Healthy profitability along with comfortable leverage and debt coverage indicators: DIL's profitability, though declined during FY19 (Prov.) as compared to FY18 (A), remained healthy with a PBILDT margin of 52.43% and PAT margin of 22.80% in FY19 (Prov.) (as compared to PBILDT margin of 54.97% and PAT margin of 24.77% during FY18).

DIL's capital structure too remained comfortable marked by improvement in its overall gearing to 0.16x as on March 31, 2019 (Prov.) from 0.51x as on March 31, 2018 (A) on account of prepayment of significant amount of its debt pertaining to its terminated GDU contracts by utilizing its available liquidity as well as on account of healthy accretion of profits to reserves. The debt coverage indicators also remained comfortable during FY19 as indicated by Total Debt/GCA of 0.80 years during FY19 (Prov.) as compared to 1.88 years during FY18 (A). Its interest coverage was also healthy at 11.78 times during FY19.

Revised hydrocarbon licensing and exploration policy likely to expedite E&P activities: DIL's growth prospects are linked to the growth in the oil and gas E&P industry and extent of outsourcing by the E&P players. The revised licensing policy formulated by the government, viz. 'Hydrocarbon Exploration and Licensing Policy (HELP)' and 'Discovered Small Field' (DSF) policy, is likely to increase the pace of E&P activities and thus likely to bring additional business opportunities for oil and gas field service providers like DIL.

Liquidity: As on March 31, 2019 (Prov.) DIL has unencumbered cash and cash equivalents amounting Rs.26.97 crore. The working capital limit utilization of DIL has reduced as on balance sheet date from Rs.13.58 crore as on March 31, 2018 (A) to Rs.3.40 crore as on March 31, 2019 (Prov.). The current ratio of DIL as on March 31, 2019 was 2.07 times (1.83 times as on March 31, 2018). However, there is an increase in the amount of receivables which has increased from ~Rs.85 crore as on March 31, 2018 (A) to ~Rs.117 crore as on March 31, 2019 (Prov.) primarily due to increase in receivables pertaining to GDU segment from ONGC which has been pending on account of the ongoing dispute between the two parties arising from the termination of the two GDU contracts (the outstanding receivables pertaining to the GDU segment stood at ~Rs.61 crore as on March 31, 2019 and the same is outstanding since more than six months as on even date).

Key Rating Weaknesses

Moderate scale of operations with high competition in rigs business segment: The total operating income (TOI) of DIL declined from ~Rs.307 crore during FY18 (A) to ~Rs.262 crore during FY19 (Prov.) primarily due to decline in revenue on account of termination of its 2 GDU segment contracts by ONGC. Also, DIL's orders are availed through tendering; hence it remains exposed to competition in the industry, particularly in the niche segment of rigs and its related business; albeit it holds a leadership position in the gas compression business. The company also remains exposed to the risk of renewal of contracts on their expiry which is, however, inherent in the oil and gas industry as it is linked to the capex and growth plans of the major oil & gas E&P companies. Furthermore, the company also remains exposed to risks associated with volatility in day rates of rigs, which largely move in tandem with crude oil prices and hence are volatile in nature.

Client concentration risk: Majority of DIL's present orders (including the integrated project management order for rigs and related oil & gas services business) are awarded by ONGC or ONGC-led consortium. This exposes the company to risks associated with concentration of clientele. However, DIL has tried to diversify its clientele through procurement of orders from reputed E&P players such as Cairn India; also it has ventured in to overseas operations by serving customers in the Middle-Eastern countries through its subsidiary.

Analytical Approach: Standalone

Applicable Criteria

[Criteria for placing ratings on Credit Watch](#)

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

[Criteria for Short Term Instruments](#)

[CARE's methodology for manufacturing companies](#)

[Financial ratios - Non- Financial Sector](#)

About the Company

Promoted by Mr Paras Savla and Mr Rupesh Savla in 1991, Ahmedabad based DIL is engaged in providing services such as gas compression, air compression, rigs (both work-over and drilling) and gas dehydration in the oil and gas industry. It is an established and a leading domestic gas compression service provider. DIL has also ventured in to E&P business of oil, gas, coal bed methane (CBM) and marginal oil fields.

Brief Financials (Rs. crore)	FY17 (A)	FY18 (A)	FY19 (Prov.)
Total operating income	286.17	306.93	261.56
PBILDT	164.57	168.72	137.13
PAT	75.19	76.02	59.64
Overall gearing (times)	0.71	0.51	0.16
Interest coverage (times)	7.39	14.58	11.78

A: Audited, Prov.: Provisional (published results on the stock exchange)

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Annexure-1: Details of 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	-	-	Sep 2021	115.62	CARE A- (Under Credit watch with Developing Implications)
Fund-based - LT-Cash Credit	-	-	-	35.00	CARE A- (Under Credit watch with Developing Implications)
Non-fund-based - LT/ ST-Bank Guarantees	-	-	-	90.00	CARE A- / CARE A2+ (Under Credit watch with Developing Implications)
Non-fund-based - ST-Credit Exposure Limit	-	-	-	2.17	CARE A2+ (Under Credit watch with Developing Implications)

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Term Loan	LT	115.62	CARE A- (Under Credit watch with Developing Implications)	-	1)CARE A- (Under Credit watch with Negative Implications) (21-Sep-18) 2)CARE A (Under Credit watch with Negative Implications) (04-Jun-18)	1)CARE A; Negative (05-Jan-18) 2)CARE A; Stable (07-Jul-17)	1)CARE A; Stable (11-Jan-17)
2.	Fund-based - LT-Cash Credit	LT	35.00	CARE A- (Under Credit watch with Developing Implications)	-	1)CARE A- (Under Credit watch with Negative Implications) (21-Sep-18) 2)CARE A (Under Credit watch with Negative Implications) (04-Jun-18)	1)CARE A; Negative (05-Jan-18) 2)CARE A; Stable (07-Jul-17)	1)CARE A; Stable (11-Jan-17)
3.	Non-fund-based - LT/ ST-Bank Guarantees	LT/ST	90.00	CARE A- / CARE A2+ (Under Credit watch with Developing Implications)	-	1)CARE A- / CARE A2+ (Under Credit watch with Negative Implications) (21-Sep-18) 2)CARE A / CARE A1 (Under Credit watch with Negative Implications) (04-Jun-18)	1)CARE A; Negative / CARE A1 (05-Jan-18) 2)CARE A; Stable / CARE A1 (07-Jul-17)	1)CARE A; Stable / CARE A1 (11-Jan-17)
4.	Non-fund-based - ST-Credit Exposure Limit	ST	2.17	CARE A2+ (Under Credit watch with Developing Implications)	-	1)CARE A2+ (Under Credit watch with Negative Implications) (21-Sep-18) 2)CARE A1 (Under Credit watch with Negative Implications) (04-Jun-18)	1)CARE A1 (05-Jan-18) 2)CARE A1 (07-Jul-17)	1)CARE A1 (11-Jan-17)

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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About CARE Ratings:

CARE Ratings commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI). CARE Ratings is proud of its rightful place in the Indian capital market built around investor confidence. CARE Ratings provides the entire spectrum of credit rating that helps the corporates to raise capital for their various requirements and assists the investors to form an informed investment decision based on the credit risk and their own risk-return expectations. Our rating and grading service offerings leverage our domain and analytical expertise backed by the methodologies congruent with the international best practices.

Disclaimer

CARE's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CARE has based its ratings/outlooks on information obtained from sources believed by it to be accurate and reliable. CARE does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CARE have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

In case of partnership/proprietary concerns, the rating /outlook assigned by CARE is based on the capital deployed by the partners/proprietor and the financial strength of the firm at present. The rating/outlook may undergo change in case of withdrawal of capital or the unsecured loans brought in by the partners/proprietor in addition to the financial performance and other relevant factors.

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