Fairchem Organics Limited

September 16, 2020

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long Term Bank Facilities	80.91	**CARE A; Stable (Single A; Outlook: Stable)**	Assigned
Long Term / Short Term Bank Facilities	2.50	**CARE A; Stable/ CARE A1 (Single A; Outlook: Stable / A One**	Assigned
Total Facilities	**83.41 (Rupees Eighty three crore and forty one lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

Upon approval of the scheme of demerger of Fairchem Speciality Ltd. (FSL) through the National Company Law Tribunal (NCLT) approval route, its erstwhile businesses of oleo chemicals & nutraceuticals along-with largely its entire assets and liabilities has been hitherto transferred to Fairchem Organics Ltd. (FOL) with an appointed date of April 01, 2019.

The ratings assigned to the bank facilities of FOL draw strength from its resourceful and experienced promoters, long standing operational track record of the business of manufacturing of specialty chemicals which has diverse industry applications and its established relation with reputed customers. The ratings also take in to account its comfortable capital structure and debt coverage indicators, along with healthy return ratios and adequate liquidity.

The ratings are, however, constrained on account of FOL's moderate scale of operations along with susceptibility of its profitability margins to volatile raw material prices and foreign exchange rates. The ratings are further constrained due to its exposure to technology obsolescence risk, risk of import substitutability from low cost Chinese products and stringent pollution control norms.

CARE also takes note of the company availing the moratorium granted by its lenders as a Covid relief measure (as permitted by the Reserve Bank of India) for a period of three months from March 2020 to May 2020 for its term debt repayment obligations.

Rating Sensitivities

Positive Factors

- Growth in scale of operations marked by TOI of more than Rs.700 crore along with earning PBILDT margin of around 18% on a sustained basis
- Improvement in its capital structure with TOL/TNW and overall gearing remaining below 0.50 times on a sustained basis
- Greater diversification of its revenue stream leading to reduced dependence on few major customers

Negative Factors

- Decline in its scale of operations marked by TOI of less than Rs.250 crore on sustained basis
- Reduction in its PBILDT margin to less than 12% on a sustained basis
- Elongation in its operating cycle beyond 120 days affecting its liquidity
- Any large size debt funded capex leading to moderation in its overall gearing beyond unity

Detailed description of the key rating drivers

Key Rating Strengths

Experienced and resourceful management

Mr. Nahoosh Jariawala, Managing Director, is a commerce graduate 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. The promoters are well supported by a qualified second tier management.

FIH Mauritius Investment Limited, an investment arm of Fairfax India Holdings Corporations (Fairfax India), held 48.75% equity stake in FOL as on March 31, 2020. Headquartered in Toronto, Canada, Fairfax India was founded in 2014 by Mr V. Prem Watsa (CEO of Fairfax group). The investment portfolio of Fairfax India includes India Infoline Finance Limited, National Collateral Management Services Limited (CARE A; Stable/ CARE A1), Bangalore International Airport Limited amongst others.

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

Established track record of operations along with diversified revenue stream
FOL operates in the specialty chemicals segment where it manufactures niche products with diverse industry applications for the last two decades. FOL's product portfolio includes Mixed Tocopherol Concentrate, Dimer Acid and Linoleic Acid which have diversified industry applications. Diverse application of its products across various industry segments tends to bring greater stability to its revenue. Moreover, company also exports its products to USA. Export contribution to net sales has remained at around 10%-15% over the past three years.

Reputed clientele
FOL has long association with its customers in domestic as well as export markets. Moreover, majority of its clientele enjoy leading position in their respective industry segments and hence credit risk is envisaged to be minimal. Furthermore, FOL has a moderately diversified client base with top 10 customers contributing around 64% of total income during FY20.

Growth in scale of operations and improved profitability during FY20
FOL's scale of operations improved during FY20 marked by ~23% growth in its total operating income (TOI) to Rs.313.08 crore compared with TOI of Rs.254.21 crore clocked by this business under FSL in FY19. Further, FOL's PBILDT margin improved by around 200 bps to 18.44% during FY20 due to optimum utilization of its manufacturing capacity coupled with benefit of economies of scale. PAT margin also improved to 11.67% during FY20 in line with improvement in its PBILDT margin. It also had a healthy ROCE of around 27% during FY20.

Comfortable capital structure and debt coverage indicators
FOL's overall gearing stood at a comfortable 0.52 times as on March 31, 2020. Further, its debt coverage indicators during FY20 also remained comfortable marked by PBILDT interest coverage of 8.91 times and Total debt/GCA of 1.59 times.

Good business prospects with fortunes directly linked to end user industries which have steady demand
The products manufactured by FOL find application in high growth consumer goods industries like Nutraceuticals, Paints, Printing Ink, Adhesives, Soap manufacturing, etc. As per various industry reports, all these end-user industries are expected to grow steadily due to factors such as rising population and increasing spending on healthcare and nutrition products.

Liquidity: Adequate
The liquidity of FOL is adequate on account of its strong cash accruals against moderate debt repayment obligations. With an overall gearing of 0.52 times as on March 31, 2020, FOL has sufficient gearing headroom to raise additional debt for its capex. Its average monthly utilization of fund based working capital limit for the trailing twelve months ended June 2020 stood at ~75% reflecting its unutilized bank lines are sufficient to meet its incremental working capital needs over the next one year. However, due to uncertainty arising from the Covid-19 pandemic induced lockdown, FSL had availed moratorium on repayment of its term loans for three months i.e. March-20 to May-20.

Key Rating Weaknesses
Moderation in scale of operations & profitability during Q1FY21 due to adverse impact of Covid-19 pandemic
The business operations of FOL were severely impacted during Q1FY21 on account of nationwide lockdown to contain the spread of Covid-19 pandemic. The manufacturing plant was closed from March 25, 2020 to May 21, 2020. In addition, as FOL operates in B2B segment, wherein its prime products are used in paint, printing ink, soap, epoxy hardeners, etc., which are not entirely classified into essential goods, hence its demand was also impacted. Due to above stated reasons and ~50 days loss of operations, its TOI declined during Q1FY21 by 61% and 51% compared to Q-o-Q and Y-o-Y respectively, its PBILDT margin almost halved on Y-o-Y basis and it reported net loss of Rs.0.19 crore on account of lower absorption of its fixed costs.

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 historically remained volatile. FOL's exports comprise around 10% of its gross sales over past two years; while 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. However, acid oil prices have witnessed relatively lower volatility over the past five years.

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 stiff competition from low cost products from China, especially Dimer acid. However, FOL has been able to gain significant market share in Dimer acid in India with its apt marketing strategy.

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.

Risk of compliance with stricter 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 has been complying with the required pollution control norms and is also expected to commission multi-effect evaporator shortly which would reduce its liquid waste. Continuous adherence to the prevailing pollution control norms would remain crucial from the credit perspective.

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
Liquidity Analysis of Non-financial sector
Rating Methodology-Manufacturing Companies
Financial ratios – Non-Financial Sector

About the Company

Promoted by Mr Rajan Harivallabhdas in May 1985, FSL was formerly known as Adi Finechem Limited. FSL was jointly managed by Mr Harivallabhdas and his cousin, Mr Nahoosh Jariwala. 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 acquired controlling equity stake in FSL from existing promoters. As on March 31, 2020, Fairfax India holds 48.75% equity stake in the company.

Recently, the Honourable National Company Law Tribunal (NCLT) has approved a scheme of demerger of FSL with an appointed date of April 01, 2019 and record date of August 24, 2020. As part of this scheme, the erstwhile Oleo chemicals & Nutraceuticals businesses of FSL has been hitherto transferred to FOL along-with transfer of largely the entire assets & liabilities of FSL to FOL.

FOL is engaged in the manufacturing of specialty chemicals like Mixed Tocopherol Concentrate, Sterols Concentrate, Dimer Acid and Linoleic Acid which find application in various industries like nutraceuticals, paints, printing ink, detergents, adhesives, etc. Its manufacturing facility is located at Chekala village near Sanand, Gujarat with an installed capacity (measured in terms of throughput of raw material) of 60,000 MTPA.

(Rs. Crore)

Brief Financials of FOL (i.e. erstwhile business under FSL)	FY19 (A)	FY20 (A)
Total operating income	254.21	313.08
PBILDT	40.81	57.73
PAT	21.52	36.55
Overall Gearing (times)	0.55	0.52
Interest coverage (times)	7.12	8.91

A: Audited

As per provisional results for Q1FY21, the company reported total operating income of Rs.35.23 crore (Q1FY20: Rs.71.32 crore) and incurred net loss of Rs.0.19 crore (Q1FY20: PAT of Rs.5.13 crore).

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 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	-	-	Feb 07, 2025	22.42	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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	22.42	CARE A; Stable	-	-	-	-
2.	Fund-based - LT-Cash Credit	LT	58.49	CARE A; Stable	-	-	-	-
3.	Non-fund-based - LT/ ST-BG/LC	LT/ST	2.50	CARE A; Stable / CARE A1	-	-	-	-

Annexure 3: 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.	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. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

Contact us

Media Contact
Name: Mradul Mishra
Contact no. : +91-22-6837 4424
Email ID – mradul.mishra@careratings.com

Analyst Contact
Name: Hardik Shah
Contact Number: +91-79-4026 5620
Email ID- hardik.shah@careratings.com

Business Development Contact
Name: Deepak Prajapati
Contact no. +91-79-4026 5656
Email ID - deepak.prajapati@careratings.com

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.

****For detailed Rationale Report and subscription information, please contact us at www.careratings.com**