Gujarat Alkalies and Chemicals Limited

October 03, 2019

Ratings

Facilities	Amount (Rs. crore)	Ratings[1]	Rating Action
Long term Bank Facilities	378.53 (reduced from Rs.433.55 crore)	**CARE AA+; Stable (Double A Plus; Outlook: Stable)**	**Reaffirmed**
Short term Bank Facilities	45.00	**CARE A1+ (A One Plus)**	**Reaffirmed**
Total	**423.53 (Rupees Four Hundred Twenty Three Crore and Fifty Three Lakh only)**		
Commercial Paper Issue	100.00 (Rupees One Hundred Crore only)	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of facilities/instruments in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings for the bank facilities and instrument of Gujarat Alkalies and Chemicals Ltd (GACL) continue to draw strength from its strong parentage, well-established position as the market leader in domestic chlor-alkali industry along with its integrated operations, wide product portfolio which finds application across diversified end-use industries, state-of-the-art technology, captive power generation to meet part of its energy requirements along with its comfortable liquidity and strong debt coverage indicators. The ratings also factor improvement in its scale of operations and profitability during FY19 (refers to period from April 1 to March 31) due to increased sales realization for caustic soda products primarily driven by global supply-demand dynamics.

The ratings also take cognizance of the fact that GACL has infused its entire equity requirement for its joint venture (JV) with National Aluminium Company Ltd (NALCO) for manufacturing caustic soda. Apart from project implementation risk, GACL would also have to manage the saleability risk associated with the new capacity including the disposal of chlorine after factoring the off-take arrangement with NALCO.

The long term rating, however, continues to be constrained by susceptibility of its profitability to adverse movement in market price of gas and power cost which constitute a significant part of its cost structure, risk related to adverse movement in foreign exchange rates, large-sized capex plans and its presence in a cyclical industry which also faces competition from imports; albeit the same is currently being mitigated due to presence of anti-dumping duty.

GACL's ability to increase its scale of operations and maintain stability of its high profitability by securing significant portion of its power requirement through captive low cost sources (i.e., renewable energy) so as to shield against market driven fluctuations of gas/energy prices and through greater share of value-added products in its sales-mix so as to improve captive consumption of chlorine; thereby resulting in greater resilience of its profitability even in the scenario of any future withdrawal of anti-dumping duty by Government of India on import of caustic soda shall be the key rating sensitivities. Further, significant adverse impact of more than envisaged large-size debt funded capex/investments on its capital structure shall also be a key rating monitorable.

Detailed description of the key rating drivers

Key Rating Strengths

Market leader in domestic caustic soda industry

GACL is the largest independent producer of caustic soda in the country with an installed capacity of 412,500 metric tonne per annum (MTPA) as on March 31, 2019 at its plants at Vadodara and Dahej in Gujarat. GACL has gradually built its leadership position through continuous expansion of production capacities to cater to the growing demand for its products over the last four decades.

Over the years, it has also introduced new chlorine derivatives (downstream products) for captive utilization of chlorine, an essential by-product generated during manufacturing of caustic soda. This has equipped the company to leverage upon its large production capacity and protect its profitability from the effects of volatility in chlorine prices to some extent.

Integrated operations and diversified customer base

The operations of GACL are well-integrated with by-product of one process being used as raw material for another process, enabling the company to optimally utilize its large production capacity. It also protects GACL's profitability to an extent from the effects of inherent cyclicality in the demand for its major products, as adverse demand scenario for one

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

set of products is countered by favorable movement in other products. GACL's products find application across diverse range of industries.

State-of-the-art technology and captive power generation to meet part of its energy requirements
The cost structure of GACL has remained competitive on account of its membrane cell technology used for electrolysis of salt which consumes one-third less power as compared to the traditional mercury cell technology and is also less polluting, captive power plant for meeting some of its energy requirements and investment in wind-mills & solar power plants to offset higher cost of power purchased from the market. Further, it commissioned new 20 Megawatts (MW) solar power plant at Charanka, Gujarat by September 2019 in a phased manner. Thus the total installed capacity of solar power plant stood at 35 MW on even date apart from wind 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 Ltd *(GIPCL; rated CARE AA-; Stable/ CARE A1+).*

Healthy financial risk profile
GACL's financial risk profile continued to remain healthy. Its TOI increased by ~28% during FY19 to Rs.3223 crore with improvement in PBILDT margin to 36.58% during FY19 compared to 33.62% during FY18 primarily on account of increased sales realization for caustic soda products despite increase in cost of majority of its raw materials. Further, it had comfortable debt protection indicators marked Total Debt/GCA of 0.28 years and PBILDT Interest coverage of 56.30x as on March 31, 2019.

Stable outlook for the caustic soda industry
The outlook for the domestic chlor-alkali industry is likely to remain stable in the near-term, mainly on account of expectation of steady demand from its key end-use industries like textile, pulp and paper, aluminum, pharmaceuticals and agrochemicals. As per Centre for Monitoring Indian Economy (CMIE), the demand for caustic soda is expected to increase by around 5% in FY20. Profitability of the industry had increased significantly during FY18 and FY19 largely driven by better sales realization of caustic soda products due to supply cuts from China and Europe on account of stricter environmental norms which had led to closure of some plants in the said countries. However, the prices have started to normalize and moderate in current year i.e., FY20. Further, in current year the cheaper imports have risen which has led to relatively low capacity utilisation for domestic manufacturers. Significant imports are from countries having surplus capacities like China, Turkey, US, Russia, etc. In order to help domestic manufacturers, Alkalies Manufacturers Association of India (AMAI) has sought a level playing field from the government by way of increase in customs duties on caustic soda and soda ash imports, a GST structure for electricity taxes and the imposition of export duty on salt. Further, extension of anti-dumping duty on caustic soda from certain countries is also likely to help in limiting the imports thereby benefitting the domestic players.

Liquidity: Strong
Liquidity of GACL is marked by strong accruals against negligible debt repayment obligations and presence of liquid investments to the tune of Rs.795 crore as on March 31, 2019. With an overall gearing of 0.06 times as of March 31, 2019, it has sufficient gearing headroom, to raise additional debt for its capex. Its entirely unutilized bank lines are more than adequate to meet its incremental working capital needs over the next one year. The operating cycle also remained stable at 46 days during FY19 and current ratio remained healthy at 3.12x as on March 31, 2019.

Key Rating Weaknesses

Susceptibility of its profitability to adverse movement in market price of gas and power cost along with competition from imports
GACL's profitability is susceptible to adverse movement in market price of gas and power cost since electrolysis is an energy intensive process and power cost constitutes a significant part of its cost structure. The power cost comprised around 28% of GACL's total operating income in FY19 (29% in FY18). The Indian chlor-alkali industry faces competition from cheap imports of lower power cost countries; however, the same is being mitigated by presence of anti-dumping duty on imports of caustic soda.

Risk of adverse movement in foreign exchange rates; however, export volumes help to provide natural hedge
GACL is exposed to risk of adverse movement in foreign exchange rates on account of its long-term borrowings denominated in USD, raised for part-funding of its capex plans. Further, as a matter of policy, GACL does not hedge its foreign currency exposure. During FY19, GACL imported raw materials and capital goods worth Rs.274.46 crore and had repayment liabilities of Rs.56.49 crore against which it made exports of Rs.340.85 crore, thus providing a natural hedge to its foreign currency exposure. Although, the interest cost on the forex borrowings is lower than that on comparable domestic rupee loans; the recent depreciation of rupee may have an adverse impact on the profitability of GACL.

Large-size own capex plan and in JV along with associated salability risk

GACL has plans to incur capex of around 2,591 crore over the next four year period ending FY23 which is expected to be funded by debt of Rs.1,612 crore and the balance through internal accruals. Further, GACL has entered into 60:40 joint venture with NALCO; GACL-NALCO Alkalies & Chemicals Pvt Ltd (GNAL; rated CARE A; Stable) for setting up a chlor-alkali plant for producing 292,000 MTPA of caustic soda at Dahej, in the vicinity of GACL's existing plant. The joint venture would also establish a coal-based power plant (130 MW) to meet the power requirements on a captive basis. The cost of the JV project is expected to be around Rs.2,000 crore, to be funded through debt and equity in the ratio of 2.33:1, translating into an exposure of Rs.360 crore of equity investment by GACL, which GACL has already infused by July 2019 with strong cash accruals and low debt repayment liabilities. The project achieved financial closure in February 2019 and as indicated by the management currently the physical progress of the project is on track and as on June 15, 2019 caustic soda plant has achieved 30% physical progress while captive power plant has achieved 60% physical progress. Further, both the sponsors have extended undertaking to fund any project cost overrun in their shareholding ratio as well as to fund an additional Rs.179 crore (over & above the project cost of Rs.2,000 crore) to be paid towards release of retention money of the contractors which are mostly payable within six months of COD. Out of the total caustic soda to be produced from the JV plant, 54,750 MTPA would be provided to NALCO's alumina refinery and the remaining would be sold in the open market; the marketing rights of which would vest with GACL. The unit would also contain manufacturing facilities for other downstream products, for utilization of chlorine, an essential by-product generated for manufacturing of caustic soda. Thus, GACL will be exposed to marketing risk as well as risk of chlorine disposal for GNAL.

Analytical Approach: Consolidated

CARE has considered 'Consolidated' analytical approach for rating of GACL on account of strong operational & financial linkages of GACL with its JV company i.e. GACL-NALCO Alkalies and Chemicals Limited (GNAL) which is setting-up a caustic soda manufacturing facility at Dahej wherein GACL holds 60% equity stake.

Applicable Criteria

Criteria on assigning Outlook to Credit Ratings
Criteria for Short Term Instruments
CARE's Policy on Default Recognition
CARE's Methodology for Factoring Linkages in Ratings
CARE's methodology for manufacturing companies
Financial ratios – Non-Financial Sector

About the Company

GACL (CIN: L24110GJ1973PLC002247) was promoted in 1973 by the Government of Gujarat (GoG) through its industrial investment arm, Gujarat Industrial Investment Corporation Ltd (GIIC). As on March 31, 2019, GoG as the promoter, through its various undertakings, held 46.28% equity in the company, the largest being through Gujarat State Investments Ltd (GSIL) with 20.87% holding. GACL is among top three players 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, pharmaceutical, water treatment and agricultural chemicals. GACL's manufacturing facilities had a combined installed capacity for production of 412,500 metric tonne (MT) of caustic soda per annum as on March 31, 2019.

Moreover, in December 2015, GACL entered into a 60:40 joint-venture with National Aluminium Company Ltd. (NALCO); GACL-NALCO Alkalies & Chemicals Pvt Ltd (GNAL; rated CARE A; Stable) to set up 800 metric tonne per day (MTPD) caustic soda plant along with a 130 megawatt (MW) coal based captive power plant at Dahej in the vicinity of GACL's existing plant and the SCOD of the project is expected by April 2021.

(Rs.Crore)

Brief Financials (Consolidated)	FY18 (A)	FY19 (A)
Total operating income	2,511	3,223
PBILDT	844	1,179
PAT	534	690
Overall gearing (times)	0.08	0.06
Interest coverage (times)	56.67	56.30

A: Audited

As per Q1FY20 (Prov.) results, GACL has reported a TOI of Rs.765 crore with a PAT of Rs.159 crore vis-à-vis TOI of Rs.762 crore with PAT of Rs.183 crore during Q1FY19 (Prov.).

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History (Last three years): Please refer **Annexure-2**

Annexure-1: Details of Facilities/Instruments

Name of the Instrument/Bank Facilities	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Term Loan-Long Term	-	-	September 2024	248.53	CARE AA+; Stable
Fund-based - LT-Cash Credit	-	-	-	130.00	CARE AA+; Stable
Non-fund-based - ST-BG/LC	-	-	-	45.00	CARE A1+
Commercial Paper-CP/STD	-	-	7-364 days	100.00	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 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.	Term Loan-Long Term	LT	248.53	CARE AA+; Stable	-	1)CARE AA+; Stable (08-Oct-18)	1)CARE AA+; Stable (05-Oct-17)	1)CARE AA+ (20-Oct-16)
2.	Commercial Paper-CP/STD	ST	100.00	CARE A1+	-	1)CARE A1+ (08-Oct-18)	1)CARE A1+ (05-Oct-17)	1)CARE A1+ (20-Oct-16)
3.	Fund-based - LT-Cash Credit	LT	130.00	CARE AA+; Stable	-	1)CARE AA+; Stable (08-Oct-18)	1)CARE AA+; Stable (05-Oct-17)	1)CARE AA+ (20-Oct-16)
4.	Non-fund-based - ST-BG/LC	ST	45.00	CARE A1+	-	1)CARE A1+ (08-Oct-18)	1)CARE A1+ (05-Oct-17)	1)CARE A1+ (20-Oct-16)

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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