Mangalore Chemicals and Fertilizers Ltd

May 18, 2017

Ratings

Facilities	**Amount (Rs. crore)**	**Rating[1]**	**Rating Action**
Fund-based - LT-Term Loan	165.23	CARE BBB; Stable [Triple B; Outlook: Stable]	Revised from CARE BBB-; Stable [Triple B Minus; Outlook: Stable]
Fund-based-LT/ ST-Cash Credit	1784.77	CARE BBB; Stable / CARE A3 [Triple B; Outlook: Stable/ A Three]	Revised from CARE BBB-; Stable/ CARE A3 [Triple B Minus; Outlook: Stable/ A Three]
Total Facilities	**1,950 (Rupees One thousand Nine hundred Fifty crore only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the long-term rating assigned to the bank facilities of Mangalore Chemicals & Fertilizers Ltd (MCF), takes into account the decline in the prices of key raw materials (ammonia and phosphoric acid) which has led to expansion in margins of NPK fertilizers, lower prevailing prices of naphtha compared to R-LNG and substantial subsidy release for the company by the Department of Fertilisers (DoF) which is likely to improve the working capital position of MCF. The ratings continue to factor in its strong parentage, being part of the Adventz group which has business interests in diverse sectors and financial & operational synergies with other companies of the Adventz group in the fertilizer business. The ratings also favorably considers MCF's established position in the Southern states of India, diversified product range and wide customer base. These ratings strengths are, however, partially off-set by the moderate financial risk profile with losses during FY16 (refers to the period April 1 to March 31), high dependence on fertilizer subsidy receivable from government and highly regulated fertilizer industry.

Going forward, the ability of the company to improve capacity utilization on a sustainable basis through energy efficient operations, timely receipt of subsidy from the government and improvement in the capital structure will remain the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Part of resourceful and diversified group: MCF is a part of the Adventz group which has interests in agri-inputs, engineering, infrastructure, real estate, consumer durables and services sectors. The flagship company of the group, Zuari Ago Chemicals Ltd (ZACL) also acts as a holding company for the group companies engaged in manufacturing of fertilizers while the non-fertilizers business are under another subsidiary Zuari Global ltd (ZGL). As part of this group, MCF benefits from centralized procurement of key raw materials and traded goods, a wider distribution network, and better cost efficiencies. Moreover, it is also supported by the healthy financial flexibility of the Adventz group.

Decline in the prices of key raw materials: Lower raw material prices (phosphoric acid & ammonia) leads to lower cost of production of NPK complexes. Consequently, lower raw material cost provides scope for the private players to undertake cuts in the retail prices as advised by GoI. Normal monsoons and lower retail prices might also lead to a pick-up in demand for NPK fertilizers with the narrowing of the price differential between urea and non-urea fertilizers. This should be a positive for the soil nutrient balance as well, which has suffered due to the excessive use of cheaper urea compared to other nutrients.

Lower prevailing prices of naphtha compared to R-LNG: In current declining crude oil price scenario, naphtha prices have declined at a faster pace being linked to last fortnight/month crude price, whereas LNG price are linked with 3-month average crude oil price. Lower dependence on government subsidies due to lower prices of raw material and finished products, will be a positive driver for the fertiliser sector in FY18. The MCF plant which is running successfully on naphtha / furnace oil as feedstock/fuel, can seamlessly continue to operate with natural gas without interruption, whenever natural gas would be made available. Slow progress in laying of gas pipeline from Kochi to Mangalore by GAIL (India)

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

Limited (which was commissioned in September 2013) has prevented MCF from receiving gas for Ammonia/urea production. Furthermore, in the current scenario, with lower prevailing prices of naphtha compared to R-LNG & subsidy mechanism of GoI being based on lower of Naphtha or R-LNG prices shall help in improving the financial profile of MCF.

Subsidy release for the company: The working capital position of the company had weakened in the past due to delay in subsidy payments by the Department of Fertilisers (DoF), resulting in significant build-up of short-term debt. However, the DoF in FY17 has released Rs.1465 crore of the outstanding subsidy to the company (with outstanding subsidy amount of Rs.679 crore as on March 31, 2017). In the current year FY18, Rs.316 crore is further released by DoF. Timely subsidy release is positive for the company & shall help in reducing the short-term debt in the short to medium-term.

Established position and wide customer base: MCF is also one of the leading companies catering to the markets in Southern India. About 60% of the company's products are sold in the state of Karnataka, which meets about 20% of the needs of the farmers. MCF has a wide customer base and the top 10 customers account for less than 10% of the total operating income.

Long track record of operations in fertilizer industry: MCF was incorporated in July 1966, as a private limited company under the name Malabar Chemicals & Fertilizers Pvt. Ltd and was converted into a public company in 1967 and subsequently in 1971, the name of the company was changed to the present one. The company went public in 1972. Subsequently, MCF diversified to other complex fertilizers over the years.

Key Rating Weaknesses

Subdued financial risk profile: The operating income and operating profits of the company have remained volatile over the past few years. While, the company incurred a loss in FY16 (refers to the period from April 1 to March 31), there was an improvement in profitability during 9MFY17 (refers to the period from April 1 to December 31). The overall gearing deteriorated in FY16 primarily on account of loss in that year due to one-time provisioning for investment in one of UB group companies.

Focus on energy efficient units: The government through the new urea policy focuses on reducing energy consumption and maximizing output. The subsidy payment for the company is based on lower of the cost of Naphtha or Reliquefied Natural Gas (RLNG). This entails constant timely capex to meet the envisaged energy savings in line with the norms with a view to reduce overall cost to maximize profitability.

Highly regulated fertilizer industry: GoI subsidizes the sale of fertilizers and exercises control over distribution to a large extent. While, the complex fertilizers have been decontrolled with prices being governed by the market dynamics, Urea has been kept out of the Nutrient based subsidy scheme and the MRP is decided by the government. This makes the fertilizer companies and their profitability vulnerable to timely receipt of subsidy.

Analytical approach: Standalone

Applicable Criteria

CARE's Criteria on assigning Outlook to Credit Ratings
CARE's Policy on Default Recognition
CARE's Methodology for fertilizer companies
Financial ratios – Non-Financial Sector

About the Company

MCF is one of the largest manufacturers of chemical fertilizers in the state of Karnataka with an aggregate installed capacity of 6.81 lakh metric tons per annum (MTPA). The company has a wide range of products that include Urea (capacity: 3.79 lakh MTPA), Di-Ammonium Phosphate (along with other P&K fertilizers – with capacity of 2.55 lakh MTPA) and Muriate of Potash, Granulated Fertilizers, Micronutrients, Soil Conditioners and Specialty Fertilizers. The company sells its product under the brand "Mangala".
As per the audited results for FY16 (refers to the period April 1 to March 31), MCF had a total operating income of Rs.3,002.54 crore with a net loss of Rs.240.12 crore as compared with the total operating income of Rs.2,577.79 crore with a PAT of Rs.37.54 crore in FY15. As per the unaudited results for 9MFY17, MCF reported a total operating income of Rs.1,956.69 crore and PAT of Rs.14.73 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

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.*

Analyst Contact:
Name: Mr Gaurav Dixit
Tel: 011-45333235
Mobile: 9717070079
Email: gaurav.dixit@careratings.com

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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	-	-	March 31, 2023	165.23	CARE BBB; Stable
Fund-based - LT/ ST-Cash Credit	-	-	-	1784.77	CARE BBB; Stable / CARE A3

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 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015
1.	Fund-based - LT-Term Loan	LT	165.23	CARE BBB; Stable	-	1)CARE BBB- (25-Apr-16)	-	-
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	1784.77	CARE BBB; Stable / CARE A3	-	1)CARE BBB- / CARE A3 (25-Apr-16)	-	-

CONTACT

Head Office Mumbai

Mr. Mehul Pandya
Cell: +91-98242 56265
E-mail: mehul.pandya@careratings.com

Mr. Saikat Roy
Cell: + 91 98209 98779
E-mail: saikat.roy@careratings.com

CREDIT ANALYSIS & RESEARCH LIMITED
Corporate Office: 4th Floor, Godrej Coliseum, Somaiya Hospital Road, Off Eastern Express Highway, Sion (East), Mumbai - 400 022
Tel: +91-22-6754 3456 | Fax: +91-22-6754 3457 | E-mail: care@careratings.com

AHMEDABAD
Mr. Deepak Prajapati
32, Titanium, Prahaladnagar Corporate Road,
Satellite, Ahmedabad - 380 015
Cell: +91-9099028864
Tel: +91-79-4026 5656
E-mail: deepak.prajapati@careratings.com

BENGALURU
Mr. Deepak Prajapati
Unit No. 1101-1102, 11th Floor, Prestige Meridian II,
No. 30, M.G. Road, Bangalore - 560 001.
Cell: +91-9099028864
Tel: +91-80-4115 0445, 4165 4529
E-mail: deepak.prajapati@careratings.com

CHANDIGARH
Mr. Sajan Goyal
SCF No. 54-55,
First Floor, Phase 11,
Sector 65, Mohali - 160062
Chandigarh
Cell: +91 99888 05650
Tel: +91-172-5171 100 / 09
Email: sajan.goyal@careratings.com

CHENNAI
Mr. V Pradeep Kumar
Unit No. O-509/C, Spencer Plaza, 5th Floor,
No. 769, Anna Salai, Chennai - 600 002.
Cell: +91 98407 54521
Tel: +91-44-2849 7812 / 0811
Email: pradeep.kumar@careratings.com

COIMBATORE
Mr. V Pradeep Kumar
T-3, 3rd Floor, Manchester Square
Puliakulam Road, Coimbatore - 641 037.
Tel: +91-422-4332399 / 4502399
Email: pradeep.kumar@careratings.com

HYDERABAD
Mr. Ramesh Bob
401, Ashoka Scintilla, 3-6-502, Himayat Nagar,
Hyderabad - 500 029.
Cell : + 91 90520 00521
Tel: +91-40-4010 2030
E-mail: ramesh.bob@careratings.com

JAIPUR
Mr. Nikhil Soni
304, Pashupati Akshat Heights, Plot No. D-91,
Madho Singh Road, Near Collectorate Circle,
Bani Park, Jaipur - 302 016.
Cell: +91 – 95490 33222
Tel: +91-141-402 0213 / 14
E-mail: nikhil.soni@careratings.com

KOLKATA
Ms. Priti Agarwal
3rd Floor, Prasad Chambers, (Shagun Mall Bldg.)
10A, Shakespeare Sarani, Kolkata - 700 071.
Cell: +91-98319 67110
Tel: +91-33- 4018 1600
E-mail: priti.agarwal@careratings.com

NEW DELHI
Ms. Swati Agrawal
13th Floor, E-1 Block, Videocon Tower,
Jhandewalan Extension, New Delhi - 110 055.
Cell: +91-98117 45677
Tel: +91-11-4533 3200
E-mail: swati.agrawal@careratings.com

PUNE
Mr.Pratim Banerjee
9th Floor, Pride Kumar Senate,
Plot No. 970, Bhamburda, Senapati Bapat Road,
Shivaji Nagar, Pune - 411 015.
Cell: +91-98361 07331
Tel: +91-20- 4000 9000
E-mail: pratim.banerjee@careratings.com

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