Gujarat State Fertilizers & Chemicals Limited

September 29, 2020

Ratings

Facilities / Instruments	Amount (Rs. crore)	Ratings[1]	Rating Action
Long Term Bank Facilities	465.00	CARE AA+; Stable (Double A Plus; Outlook: Stable)	Reaffirmed
Short Term Bank Facilities	2,700.00	CARE A1+ (A One Plus)	Reaffirmed
Total Facilities	**3,165.00 (Rupees Three thousand one hundred sixty five crore only)**		
Commercial Paper (CP) Issue	1,000.00	CARE A1+ (A One Plus)	Reaffirmed
Total Instruments	**1,000.00 (Rupees One Thousand crore only)**		

Detail of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings of Gujarat State Fertilizers & Chemicals Ltd (GSFC) continue to derive strength from its established and integrated operations in fertilizers and industrial chemical products with a diversified product profile, dominant market position in most of its products with most of the plants operating at optimum capacity, strategic investment for backward integration to secure supply of key raw materials, its comfortable leverage and liquidity along with high degree of financial flexibility and rationalisation of its previously envisaged large size capex plans. The ratings also derive comfort from stable operations of its fertilizer division further supported by substantial reduction in prices of its key raw materials & natural gas along-with good monsoon. CARE also notes that GSFC has not availed any moratorium as a Covid relief measure, in line with Reserve Bank of India (RBI) guidelines, for servicing of its bank facilities which underlines its strong liquidity profile.

The long-term rating, however, continues to be constrained by decline in its profitability on the back of subdued performance of its industrial chemical products division along-with employee wage revision, risk associated with regulated nature of fertilizer industry, delay in release of subsidy from Government of India (GoI) mainly in the second half of the financial year which leads to elongation of operating cycle and in turn higher reliance on short term borrowings, volatility in prices and supply of key raw materials, fluctuations in forex rate and cyclicality associated with other industrial products.

CARE takes cognizance of the fact that the matter related to issuance of office memorandum (OM) by DoF for recovery of 'undue benefits' accrued with use of domestic gas for production of P&K fertilizers is pending before the authority for deliberations. Further, GSFC had provided financial guarantee towards borrowings of Tunisian Indian Fertilizers, S.A. (TIFERT) and lenders issued a call notice towards the guaranteed amount in April 2017. The guarantee has, however, expired on March 31, 2018. CARE has not factored in the event risk pertaining to the above issues, however, any adverse deliberations on these counts could affect the credit metrics of the company.

Rating Sensitivities

Positive Factors

- Significant diversification of GSFC's operations to other fertilizer products along with significant increase in its scale
- Improved profitability margin in both fertilizer & industrial products division leading to overall PBILDT margin of more than 12% on a sustained basis
- Effective management of its working capital requirements with timely receipt of subsidy from GoI resulting in contraction in its operating cycle to less than 90 days

Negative Factors

- Sustained pressure on its profitability margin, most likely arising from its industrial products division, resulting in PBILDT margin remaining less than 6%
- Moderation in its market position in fertilizer business
- Delay in receipt of subsidy dues leading to elongation in operating cycle beyond 220 days on a sustained basis which could have an adverse impact on its liquidity

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

- Major debt funded capex leading to deterioration in its overall gearing to more than 0.60 times on a sustained basis
- PBILDT/ Interest coverage ratio inching below 3 times
- Any adverse changes in the regulations governing fertilizer industry and/or unforeseen material liability arising w.r.to any long-pending disputed matters

Detailed description of the key rating drivers
Key Rating Strengths
Well-established and integrated operations along with diversified product profile
GSFC's product range includes fertilizer products (manufacturing) like Di-Ammonium Phosphate (DAP), Ammonium Sulphate (AS), Ammonium Phosphate Sulphate (APS), Urea and industrial chemical products like Caprolactam, Nylon-6 (N-6), Melamine, Nylon chips, MEK Oxime, etc. Also, during 5MFY21, it has restarted its hitherto closed Methanol operations. Furthermore, GSFC trades in DAP, Methanol, Melamine and other fertilizer as well as Industrial products.
GSFC's operations are marked by high level of vertical integration across both fertilizers and industrial products division. GSFC meets its ammonia requirements for manufacturing of fertilizers such as urea, AS and APS and few industrial products through captive production. Furthermore, captive production of caprolactam is used for manufacturing N-6. The integrated manufacturing facilities attempt better utilization of available resources.

Stable operations of fertilizer division further supported by substantial reduction in prices of raw materials & natural gas on the back of good monsoon
Operations of GSFC's fertilizer division remained stable during FY20 marked by TOI of Rs.6,238 crore (PY: Rs.6,314 crore) whereby its PBIT margin improved from 4.59% during FY19 to 5.21% during FY20. Profitability of fertilizer division improved in FY20 mainly due to softening of input prices along-with lower trading activity. On the back of good monsoon & substantial reduction in raw material & natural gas prices in Q1FY21, performance of fertilizer division stood comfortable in-spite of Covid-19 marked by TOI of Rs.1,432 crore with PBIT margin of 6.26% during Q1FY21.

Comfortable leverage & debt coverage indicators
GSFC had a comfortable leverage with an overall gearing of 0.23 times which however marginally moderated from 0.15 times as on March 31, 2019 mainly on account of higher working capital borrowings at year-end coupled with reduction in its net-worth due to losses under comprehensive income w.r.to diminution in market value of its investments and additional provision pertaining to wage revision. With major portion of its total debt in the form of working capital borrowings, its debt coverage indicators also stood comfortable marked by Interest coverage ratio of 3.60 times during FY20.

Strategic investments in backward integration mainly to secure steady supplies of raw material and power
To secure steady supply of Phosphoric Acid (PA) (the availability of which remains volatile) so as to increase the capacity utilization of its complex fertilizer portfolio at its Sikka plant, GSFC had bought 15% stake in Tunisian Indian Fertilizers S.A. (TIFERT; Joint Venture in Tunisia). Through this investment, GSFC is entitled to receive 1,80,000 MT of PA per annum at market price. During FY20, GSFC received 75,000 MT of PA from TIFERT compared to 76,000 MT in FY19.
Further, to add Potassium (K) in its fertilizer portfolio and to capture the larger market share in NPK fertilizers, GSFC has also invested in a Canada based company Karnalyte Resources Inc. (Karnalyte; engaged in the business of exploration and development of high quality agricultural and industrial potash and magnesium products). GSFC has signed off-take agreement with Karnalyte for 20 years for purchase of approximately 350,000 tonne of potash per year from phase-I of the project. Currently, phase-I of the project has been stalled and its revival is under consideration.
GSFC also benefits from its wind farm with a capacity of 152.80 MW, captive gas based power plant of 45 MW and waste heat recovery steam generator of 15 MW. GSFC also has investments in Gujarat Industries Power Co Ltd (GIPCL; rated CARE AA-; Stable/ CARE A1+), where, by virtue of being a promoter, GSFC has availability of 38 MW of power out of GIPCL's gas based power plant of 145 MW.

Rationalization of its previously envisaged large size capex plans
Earlier, GSFC had proposed capex for phosphoric acid and sulphuric acid plant at Sikka. Also, GSFC had envisaged to develop a jetty at Sikka in JV with Gujarat Maritime Board (GMB). However, company has decided to not move ahead with these plans looking at the additional operational cost and complexity of the operations and rather it has initiated discussion with Essar port for unloading of imported rock phosphate for its PA project at Sikka considering it as a cheaper option. Also, GSFC had signed a License Agreement with Mitsui Chemicals Incorporation (MCI) for establishing a Methyl Metha Acrylate (MMA) plant of 60,000 MTPA. However, considering uncertainty for sourcing of major raw material C4 Raffinate and recent downtrend in the chemical market and global demand / supply outlook, GSFC is not moving ahead with this project. As articulated by management, company has not incurred any cost for both these projects. Both these projects were earlier envisaged to be funded at a debt-equity ratio of 2.33:1.

GSFC has now proposed to undertake capex for Ammonium Sulphate and Sulphuric Acid plant with manufacturing capacity of 400 MTPD to be completed over next 18 months which is proposed to be entirely funded through internal accruals. Also, in order to reduce energy consumption, company is planning to revamp existing Urea plant which is proposed to be partially funded through term debt and expected to be completed in next 30 months.
Accordingly, GSFC has deferred its two large size capex plans of around Rs.3,600 crore and now its capex plan for next three years stood at around Rs.615 crore.

Liquidity: Strong
Liquidity of GSFC is strong marked by healthy cash accruals against negligible term debt repayment obligations of Rs.56 crore in FY21 and quoted equity investments to the tune of Rs.2,223 crore as on June 30, 2020. With a gearing of 0.23 times as of March 31, 2020, the issuer has sufficient gearing headroom, to raise additional debt for its capex. Its unutilized bank lines to the tune of ~55% are more than adequate to meet its incremental working capital needs over the next one year. GSFC has not opted for loan moratorium on any of its debt obligation as allowed by RBI under Covid-19 relief package on the back of its strong liquidity. GSFC has sanctioned fund based working capital limit of Rs.465 crore with consortium of lenders and it has Rs.1200 crore of working capital limit with a set of lenders outside the consortium. However, it has been largely utilising CP limit of Rs.1000 crore at competitive rate of interest and keeps its working capital limit available to the extent of its outstanding CP issuances so as to meet CP redemption obligation at any time. Further, it has sanctioned non-fund based working capital limit of Rs.1500 crore which is utilised for import of its raw material requirements.

Key Rating Weaknesses
Regulated nature of fertilizer industry and delays in release of subsidy from GoI
The allocated fertilizer subsidy budget has been trimmed by GOI by 12.1% to Rs.71,309 crore for FY21 as against Rs.81,124 crore for FY20 which could be insufficient for the fertiliser industry leading to subsidy backlog, thereby impacting liquidity position of the industry, factoring the back-log of unpaid subsidy (estimated at Rs.45,000 crore for FY20 year-end). Lower than required budgetary allocation leads to exhaustion of available funds for fertilizer subsidy by October-November of the financial year as GoI has already paid 44% of budgeted subsidy till July 2020.
Further, two new urea capacities under the New Urea Investment Policy-2012 (NIP-2012) are also expected to start production, leading to an increase in the urea subsidy requirement. However, there is simultaneous reduction in prices of major raw materials & natural gas which could lead to lower subsidy requirement.
The shortfall in subsidy budget usually affects the cash flow position of companies in second half of the financial year and thus companies have to resort to higher short term borrowings to fund extended subsidy receivables. However, the government is planning to implement second phase of DBT and is planning to explore the option of directly transferring the subsidy to farmer's account which could be beneficial for the fertilizer companies. However, it would have substantial burden on the Govt. finances and accordingly, roll out of Second Phase of DBT might take some time.
Urea carries the highest subsidy component whereas subsidy in other P&K fertilizers is based on the nutrient content which is on the lower side compared to Urea. In case of GSFC, since urea sales constitute ~13% of its TOI, it has lower reliance on subsidy. Subsidy receivable of GSFC stood at Rs.1791 crore as on March 31, 2020 compared with Rs.1658 crore as on March 31, 2019.

Moderation in performance in Industrial products division impacting its overall profitability
Performance of GSFC's industrial products division moderated significantly during FY20 marked by TOI of Rs.1560 crore (PY: Rs.2176 crore) with losses at PBIT level of Rs.69 crore (PY: PBIT of Rs.382 crore). This was mainly due to decline in caprolactum-benzene spread from its high of USD 1200 /MT during FY19 to USD 750/MT during FY20. Decline in spread was mainly due to lower realization of caprolactum on the back of dumping by China due to China-US trade war. Further, performance of industrial products division continued to remain subdued even in Q1FY21 on the back of continued lower spread & Covid-19 induced lockdowns affecting the demand for industrial products from downstream industries. Accordingly, during Q1FY21, GSFC reported TOI of Rs.205 crore from industrial products division with PBIT level losses of Rs.23 crore.
Apart from subdued performance of industrial products division, GSFC booked additional employee cost of Rs.200 crore in FY20 w.r.to employee wage revision (wage revision once in four years) leading to moderation in its overall PBILDT margin from 9.77% during FY19 to 5.24% during FY20.

Event risk arising from order issued by DoF to recover 'undue benefits' earned by P&K fertilizer producers using cost effective domestic gas as feedstock; and any potential obligation under financial guarantee provided to TIFERT
DoF issued an OM on January 6, 2014 to GSFC and Rasthriya Chemicals & Fertilizers Ltd. for recovery of 'undue benefits' on account of usage of cost effective administered price mechanism (APM) gas to manufacture P&K fertilizers from the date of OM considering differential price of fertilizers based on imported ammonia and the APM gas.
GSFC has taken up the matter with the DoF and challenged the OM before the Hon. High Court of Gujarat which has granted a stay order on the said OM. However, any significant recovery by DoF from mopping up of 'undue benefits' by

GoI for the ammonia produced using domestic gas could affect the company's credit metrics and will be crucial from credit perspective.
Also, GSFC had provided a sponsor guarantee for USD 41.1 million (proportionate to the shareholding of 15%) towards the borrowings of TIFERT. In March 2017, TIFERT had requested re-scheduling of instalment due to its lenders. However, while the same was under discussion, an acceleration notice was served on TIFERT by its lenders on March 28, 2017. The loan instalment was immediately paid by TIFERT along with interest on March 31, 2017. However, on April 4, 2017 the lenders followed up with a call notice on TIFERT's shareholders towards the guaranteed amount. TIFERT has paid the subsequent instalments due as per schedule and the guarantee provided by GSFC got expired on March 31, 2018.
As articulated by the company, TIFERT would be in a position to meet the debt obligations in future and it is unlikely that such an event of payment under guarantee amount will arise on GSFC.

Analytical approach: Consolidated
CARE has adopted 'Consolidated' analytical approach for GSFC as there are strong operational & financial linkages among GSFC and its subsidiaries. Also, GSFC has actively started retail operations through its wholly owned subsidiary viz. GSFC Agrotech Ltd. through its retail stores. List of companies getting consolidated has been placed at **Annexure 3**.

Applicable Criteria
Criteria on assigning 'outlook' to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology: Consolidation and Factoring Linkages in Ratings
Rating Methodology-Manufacturing Companies
Rating Methodology - Fertilizer Companies
Financial ratios – Non-Financial Sector

About the Company
Incorporated in 1962, GSFC is a public sector company promoted by the Government of Gujarat (GoG). GoG, through its undertaking Gujarat State Investment Ltd (GSIL), owns 37.84% of the paid-up capital of the company. The Chairman and Managing Director of the company are being appointed by GoG.
GSFC operates in two segments (1) fertilizers and (2) industrial products, with integrated manufacturing facilities enabling it to benefit from synergies; it manufactures a host of fertilizers and industrial products. While fertilizers contributed about 80% to the total income of FY20, industrial products contributed the balance 20%. GSFC manufactures fertilizers like di-ammonium phosphate (DAP), ammonium sulphate (AS), ammonium phosphate sulphate (APS), urea and industrial products like caprolactam, melamine, MEK oxime, polymers and nylon 6 (N-6).

Brief Financials- Consolidated (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	8,576	7,877
PBILDT	838	413
PAT	493	110
Overall gearing (times)	0.15	0.23
Interest coverage (times)	13.73	3.60

A: Audited
As per Q1FY21 (published) results, GSFC reported TOI of Rs.1,648 crore (Q1FY20: 1,731 crore) with a PAT of Rs.30 crore (Q1FY20: Rs.42 crore).

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 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-Cash Credit	-	-	-	465.00	CARE AA+; Stable
Non-fund-based - ST-BG/LC	-	-	-	1500.00	CARE A1+
Fund-based - ST-Others	-	-	-	1200.00	CARE A1+
Commercial Paper-Commercial Paper (Standalone)	-	-	7-364 days	1000.00	CARE A1+

Annexure-2: Rating History (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-Cash Credit	LT	465.00	CARE AA+; Stable	-	1)CARE AA+; Stable (04-Oct-19)	1)CARE AA+; Stable (19-Sep-18)	1)CARE AA+; Stable (29-Aug-17)
2.	Non-fund-based - ST-BG/LC	ST	1500.00	CARE A1+	-	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18)	1)CARE A1+ (29-Aug-17)
3.	Commercial Paper-Commercial Paper (Standalone)	ST	1000.00	CARE A1+	-	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18) 2)CARE A1+ (15-May-18)	1)CARE A1+ (29-Aug-17)
4.	Fund-based - ST-Others	ST	1200.00	CARE A1+	-	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18)	1)CARE A1+ (29-Aug-17)

Annexure-3: List of entities getting consolidated in GSFC

Name of entity	Extent of consolidation	% holding as on March 31, 2020
GSFC Agrotech Ltd.	Full consolidation	100.00%
Gujarat Arogya Seva Pvt. Ltd.	Full consolidation	50.94%
Vadodara Enviro Channel Ltd.	Equity method	28.57%
Gujarat Green Revolution Company Ltd.	Equity method	46.87%
Karnalyte Resources Inc	Equity method	38.73%

Annexure – 4: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Commercial Paper-Commercial Paper (Standalone)	Simple
2.	Fund-based - LT-Cash Credit	Simple
3.	Fund-based - ST-Others	Simple
4.	Non-fund-based - 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
Mradul Mishra
Contact no. – +91-22-6837 4424
Email ID – mradul.mishra@careratings.com

Analyst Contact 1
Name: Hardik Shah
Contact Number: +91-79-4026 5620 / +91-9898802101
Email ID- hardik.shah@careratings.com

Analyst Contact 2
Name: Ranjan Sharma
Contact Number: +91-79-4026 5617 / +91-9824021823
Email ID- ranjan.sharma@careratings.com

Relationship Contact
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**