Gujarat State Fertilizers & Chemicals Limited

September 28, 2021

Ratings

Facilities / Instruments	Amount (Rs. crore)	Ratings[1]	Rating Action
Long-term Bank Facilities	300.00	**CARE AA+; Stable (Double A Plus; Outlook: Stable)**	**Reaffirmed**
Short-term Bank Facilities	2,865.00	**CARE A1+ (A One Plus)**	**Reaffirmed**
Total Facilities	**3,165.00 (Rs. Three thousand one hundred sixty five crore only)**		
Commercial Paper (CP) issue	**1,000.00 (Rs. One thousand crore only)**	**CARE A1+ (A One Plus)**	**Reaffirmed**

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings of Gujarat State Fertilizers & Chemicals Limited (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 and strategic investment towards backward integration for securing supply of key raw materials.

The ratings also derive comfort from improved performance of its fertilizer division during FY21 (refers to the period April 1 to March 31) and Q1FY22 supported by favourable raw material and natural gas prices along-with good monsoon. Performance of its industrial products division also improved during the same period aiding its overall profitability. Also, the ratings draw strength from its comfortable leverage and strong liquidity arising from substantial realization of its subsidy dues in FY21.

The long-term rating, however, continues to be constrained by 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 the Department of Fertilizer (DoF) for recovery of ‘undue benefits’ accrued due to use of domestic gas for production of P&K fertilizers is pending before the authority for deliberations. Furthermore, 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 outcome on these counts could affect the credit metrics of the company.

Rating Sensitivities

Positive Factors *(factors that could lead to positive rating action/upgrade)*

- Significant diversification of GSFC’s operations to other fertilizer products along with significant increase in its scale
- Improved profitability margin in both fertilizer and 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 *(factors that could lead to negative rating action/downgrade)*

- Sustained pressure on its profitability margin resulting in PBILDT margin remaining less than 6%
- Moderation in its market position in fertilizer business
- Significant build up of subsidy receivables leading to elongation in operating cycle beyond 200 days on a sustained basis which could have an adverse impact on its liquidity
- Major debt-funded capex leading to deterioration in its overall gearing to more than 0.50 times on a sustained basis
- Any adverse changes in the regulations governing fertilizer industry and/or unforeseen material liability arising w.r.to any long-pending disputed matters

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

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, MEK Oxime etc. Also, during FY21, it had restarted its hitherto closed Methanol production. Furthermore, GSFC trades in DAP, Urea, Ammonia, Methanol, and other fertilizers 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 part of its ammonia and sulphuric acid requirement for manufacturing of fertilizers 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.

Improved performance of fertilizer division supported by favourable raw materials and natural gas prices on the back of good monsoon during FY21
The performance of GSFC's fertilizer division improved during FY21 marked by sales volume (excluding trading) of 19.45 Lakh Metric Tonne (LMT) during FY21 vis-à-vis 16.82 LMT during FY20 in line with overall increase in fertilizer sales in domestic market aided by good monsoon. Fertilizer division's income (excluding trading) increased from Rs.4,451 crore in FY20 to Rs.4,692 crore in FY21 whereas its PBIT margin from fertilizer segment improved from 5.21% during FY20 to 6.29% during FY21 aided by favourable raw material prices and lower trading activity. GSFC's trading income declined from Rs.1,891 crore in FY20 to Rs.1,247 crore in FY21 due to covid-19 related supply chain disruptions.
In Q1FY22, performance of fertilizer division remained stable, marked by TOI of Rs.1,246 crore (Rs.1,432 crore in Q1FY21) with PBIT margin of 6.74% (6.26% in Q1FY21), despite substantial increase in raw material prices, due to benefit of enhanced subsidy from May 2021.
Department of Fertilizers (GoI) hiked subsidy rates under Nutrient based Subsidy (NBS) scheme during May 2021 amidst rising raw material prices. However, raw material prices continued to increase even after May 2021 rendering revised subsidy rates inadequate. Consequently, profitability of fertilizer segment is expected to moderate from Q2FY22 onwards, in case of sustained high level of raw material prices and absence of any additional subsidy rate hikes.

Improved performance of industrial products division aiding its overall profitability
The performance of GSFC's industrial products division improved marked by TOI of Rs.1,771 crore (PY: Rs.1,560 crore) and its segment PBIT of Rs.126 crore (PY: losses at PBIT level of Rs.69 crore) during FY21. Commencement of methanol production and improvement in sales volume of other industrial products contributed to the improved performance during FY21.
Performance of industrial products division improved further during Q1FY22 marked by TOI of Rs.605 crore (Rs.205 crore in Q1FY21) and PBIT of Rs.96 crore (losses at PBIT level of Rs.23 crore) aided by improved caprolactum-benzene spread and melamine prices. Consequently, GSFC's overall profitability marked by PBILDT margin improved from 5.13% in FY20 to 8.60% in FY21 and further improved to 11.90% in Q1FY22.

Comfortable leverage and debt coverage indicators
GSFC had almost nil leverage as on March 31, 2021 and June 30, 2021 vis-à-vis leverage marked by overall gearing of 0.23 times as on March 31, 2020. Improved capital structure was primarily on account of repayment of external debt from healthy cash flow from operation of Rs.2,459 crore due to receipt of subsidy backlog along with improved profitability during FY21. Its debt coverage indicators also improved marked by interest coverage of 15.45 times during FY21 vis-à-vis 3.52 times during FY20.

Strategic investments towards 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) in order 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 FY21 and 4MFY22, GSFC received 52,388 MT and 30,878 MT of PA from TIFERT respectively.
Furthermore, 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.

Modular capex under progress, albeit large size capex plans under deliberation

GSFC has proposed to undertake few modular size projects which includes ammonium sulphate plant (400 MTPD), sulphuric acid plant (600 MTPD), N-6 compounding lines (48 MTPD), solar power project (15 MW) along with revamping of its urea plant at Vadodara to meet NUP 2015 energy consumption norms. Overall, its capex plan for next three years amounts to around Rs.700 crore which is expected to be funded entirely from its internal accruals and surplus liquidity.

However, GSFC has few major capex plans under deliberation stage which includes phosphoric acid (1000 MTPD) and sulphuric acid (3000 MTPD) plant at Sikka and a melamine plant (around 120 MTPD). Also, GSFC had signed a license agreement with Mitsui Chemicals Incorporation for establishing a methyl metha acrylate plant of around 180 MTPD. Size of these projects are expected to be substantially high.

GSFC has significant headroom for undertaking some debt-funded capex with a very comfortable overall gearing. However, undertaking of any of these major capex plan with high reliance on debt would be a key credit monitorable.

Liquidity: Strong

Liquidity of GSFC is strong marked by healthy expected cash accruals against no term debt repayment obligations and low average utilization of its fund-based limit at around 42% in last 12 months ended June 2021. It had cash and fixed deposit (largely parked with Gujarat State Financial Services Limited) of around Rs.1,101 crore as on March 31, 2021. It also had substantial quoted equity investments to the tune of Rs.3,773 crore as on March 31, 2021. With minimal leverage as of June 30, 2021, GSFC has sufficient gearing headroom, to raise additional debt for its capex. Its unutilized bank lines are more than adequate to meet its incremental working capital needs over the next one year. GSFC has sanctioned fund-based working capital limit of Rs.300 crore with consortium of lenders and it has Rs.1,265 crore of working capital limit with a set of lenders outside the consortium. However, it has been largely utilising CP limit of Rs.1,000 crore at competitive rate of interest and keep its working capital limit available to the extent of its outstanding CP issuances so as to meet CP redemption obligation at any time. Furthermore, GSFC has not issued CPs since December 2020 onwards amidst substantial surplus liquidity. Further, it has sanctioned non-fund based working capital limit of Rs.1,600 crore which is utilised for import of its raw material requirements.

Key Rating Weaknesses

Regulated nature of fertilizer industry and inherent delays associated with release of subsidy from GoI

Fertilizer manufacturer's profitability is influenced by the regulations governing various types of fertilizers wherein government controls the fertilizer prices and provides subsidy. Quantum of subsidy receivables and delays associated with receipt of the same, inherently impacts the liquidity of fertilizer industry; albeit it differs with the type of fertilizer. With release of additional subsidy of Rs.65,000 crore in FY21 over and above allocated subsidy of Rs.71,309 crore in FY21 budget estimate, subsidy receivables have declined significantly leading to significant decline in debt level of fertilizer companies.

Furthermore, amidst substantial increase in raw material prices from February 2021 onwards, GoI made additional fertilizer subsidy allocation of Rs.14,755 crore in May 2021 for FY22 over and above normal budget of Rs.79,530 crore for FY22. However, sustained rise in raw material prices could result in faster exhaustion of budget for the fertiliser subsidy which may led to subsidy backlogs in case raw material prices remains at such an elevated level. With substantial increase in DAP and APS subsidy, which contributes around 24% and around 10% to TOI of GSFC respectively, its subsidy receivables could again increase by end-FY22.

The shortfall in subsidy budget usually affects the cash flow 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 government finances and accordingly, roll out of second phase of DBT could take some time.

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 the 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 an event of payment under guarantee amount will arise on GSFC.

Analytical Approach: Consolidated
CARE Ratings has adopted 'Consolidated' analytical approach for GSFC as there are strong operational and 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 4**.

Applicable Criteria
Criteria on assigning Outlook and Credit Watch to Credit Ratings
CARE's Policy of Default Recognition
Rating Methodology – Manufacturing Companies
Rating Methodology – Fertilizer Companies
Rating Methodology – Consolidation
Financial Ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Criteria for Short Term Instruments

About the Company
Incorporated in 1962, GSFC is a public sector undertaking 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 appointed by GoG.
GSFC operates in two segments (1) fertilizers and (2) industrial products, with integrated manufacturing facilities enabling it to benefit from synergies by manufacturing a host of fertilizers and industrial products. Fertilizers contribute around 70-80% to the total income, whereas industrial products contribute the balance 20%-30%. GSFC manufactures fertilizers like di-ammonium phosphate (DAP), ammonium sulphate (AS), ammonium phosphate sulphate (APS), urea and industrial products like caprolactam, nylon 6, melamine, methanol, MEK oxime, polymers etc.

Brief Financials- Consolidated (Rs. crore)	FY20 (A)	FY21 (A)
Total operating income	7,877	7,724
PBILDT	404	664
PAT	110	450
Overall gearing (times)	0.23	0.00
Interest coverage (times)	3.52	15.45

A: Audited

As per Q1FY22 published consolidated results, GSFC reported TOI of Rs.1,873 crore (Q1FY21: Rs.1,648 crore) with a PAT of Rs.136 crore (Q1FY21: Rs.30 crore).

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Complexity level of various instruments rated for this company: Please refer **Annexure-3**

Bank lender details: Please refer **Annexure-5**

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-Cash Credit	-	-	-	300.00	CARE AA+; Stable
Non-fund-based - ST-BG/LC	-	-	-	1600.00	CARE A1+
Fund-based - ST-Others	-	-	-	1265.00	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 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1.	Fund-based - LT-Cash Credit	LT	300.00	CARE AA+; Stable	-	1)CARE AA+; Stable (29-Sep-20)	1)CARE AA+; Stable (04-Oct-19)	1)CARE AA+; Stable (19-Sep-18)
2.	Non-fund-based - ST-BG/LC	ST	1600.00	CARE A1+	-	1)CARE A1+ (29-Sep-20)	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18)
3.	Commercial Paper-Commercial Paper (Standalone)	ST	1000.00	CARE A1+	-	1)CARE A1+ (29-Sep-20)	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18) 2)CARE A1+ (15-May-18)
4.	Fund-based - ST-Others	ST	1265.00	CARE A1+	-	1)CARE A1+ (29-Sep-20)	1)CARE A1+ (04-Oct-19)	1)CARE A1+ (19-Sep-18)

Annexure 3: 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

Annexure 4: List of companies getting consolidated (As on March 31, 2021)

Name of Entity	% holding
GSFC Agrotech Ltd	100.00%
Gujarat Arogya Seva Pvt Ltd	50.94%
Gujarat Port & Logistics Company Ltd	60.00%
Vadodara Jalsanchay Pvt Ltd	60.00%
Vadodara Enviro Channel Ltd	28.57%
Gujarat Green Revolution Company Ltd	46.87%
Karnalyte Resources Inc	38.73%

Annexure 5: Bank Lender Details: Click here to view Bank Lender Details

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
Mr. Mradul Mishra
Contact No.: +91-22-6837 4424
Email ID: mradul.mishra@careratings.com

Analyst Contact 1
Mr. Hardik Shah
Contact No.: +91-79-4026 5620
Email ID: hardik.shah@careratings.com

Analyst Contact 2
Name: Ranjan Sharma
Contact no. +91-79-4026 5617
Email ID: ranjan.sharma@careratings.com

Business Development Contact
Mr. 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