July 11, 2019

Dhanuka Agritech Limited: Ratings placed under watch with negative implications

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based - Working Capital Facilities	30.0	30.0	[ICRA]AA- @; rating placed under watch with negative implications
Non-fund based – LC/BG	33.35	33.35	[ICRA]A1+ @; rating placed under watch with negative implications
Total	**63.35**	**63.35**	

**Instrument details are provided in Annexure-1*

Rationale

Update: Dhanuka Agritech Limited (DAL)'s related company, Dhanuka Laboratories Limited[1] (DLL), is involved in manufacturing and marketing of active pharmaceutical ingredients (APIs) and advanced intermediates in the field of cephalosporin antibiotics. The National Company Law Tribunal (NCLT) recently approved DLL's resolution plan for the acquisition of Orchid Pharma Limited (OPL), under the Insolvency and Bankruptcy Code (IBC). As per the resolution plan approved, the creditors of OPL are expected to get ~Rs. 1,116 crore, which includes a consideration of Rs. 570 crore (funded through a mix of debt and equity) to be provided by DLL. As per the discussion with DAL's management, its promoters are likely to pledge a part of their shareholding[2] in DAL to raise debt (in an SPV) to support part funding of the OPL acquisition by DLL. Pledging of sizeable shareholding of DAL's promoters would impact the company's financial flexibility. Thus, the ratings have been placed under watch with negative implications. As more clarity on the aforesaid development is expected over the next few weeks, ICRA will continue to monitor the same and take the appropriate rating action.

ICRA also notes that the company recorded revenues of Rs. 1,005.8 crore in FY2019. Its operating margin declined to 14.5% from 17.3% in FY2018. Nevertheless, the debt coverage metrics remained comfortable with interest coverage of 164.0 times and nil debt/OPBITDA for FY2019.

The rating action factors in the position of DAL among the leading players of the agrochemical industry, supported by its established operational track record and the experience of its promoters in the industry. ICRA notes DAL's sizeable manufacturing capacities across multiple locations in the country and its diverse product portfolio comprising speciality as well as generic formulations (across all agro-chemical categories). DAL benefits from its healthy brand presence across regions and product categories, supported by an entrenched distribution network. Leveraging on these strengths, the company has developed strong relations with reputed international technicals manufacturers. This has also enabled it to regularly come up with new formulations. Steady revenue growth has led to healthy internal accrual generation, which has been deployed for funding its working capital requirements, resulting in minimal reliance on external debt. This has translated into strong debt coverage indicators and comfortable liquidity, as marked by low utilisation of the bank limits and cash/liquid investments (~Rs. 32 crore as on March 31, 2019).

---

1 Rated [ICRA]BBB-@/[ICRA]A3@

2 Promoters presently hold 75% stake in DAL

However, the business has been under pressures over the last few quarters. A sub-par monsoon and lower pest infestation in some crops have affected the demand for agro-chemicals. Thus, the revenue growth over FY2018 and FY2019 stood at 9.0% and 4.5% against a CAGR of 11% in the four preceding years. The profitability was impacted by intense competition as well as increase in raw material prices. Imports, which meet up to 30% of DAL's requirements, became expensive, partly due to the closure of plants in China, and due to the rupee depreciation. Further, DAL's tie-ups for speciality chemicals over the last few years have not yielded the anticipated revenues, impacting margins. The ratings remain constrained by high working capital intensity of the business, and any disruption from discontinuation of tie-ups with international technical manufacturers.

ICRA has also noted the inventory/equipment loss due to a fire accident at DAL's Keshwana (Rajasthan) facility during FY2019. The company has filed an insurance claim of ~Rs. 65 crore, which is expected to cover the loss of assets, while the business loss was minimal. Delay in the recovery of the claim receivable can impact the financials of the company. Moreover, in FY2019, DAL has extended funding support to its associate company, Dhanuka Laboratories Limited[3], with the board approved limit being Rs. 25 crore (4% of DAL's net worth). While it is not anticipated, any increase in the fund flows would be a rating sensitivity.

Outlook: Not applicable

Key rating drivers

Credit strengths

Established track record of the company and extensive experience of the promoters - DAL has an established operational track record and its promoters have extensive experience of around three decades in the agro-chemical industry.

Wide distribution network and well-established brand – Over the years, the company has developed a well-entrenched distribution network comprising around 7,500 dealers that further service around 80,000 retailers across the country. DAL's brand is well established in the market and is further supported by its regular marketing initiatives.

Established associations with reputed international technical manufacturers – The company has established associations with reputed international technical manufacturers (such as Nissan Chemicals, FMC Corporation and Chemtura Corporation), which provide access to speciality molecules. Almost two-thirds of the company's revenues are driven by the sale of speciality formulations, which also support profit margins.

Well-diversified product portfolio and geographical presence – The company's product portfolio includes up to 90 formulations and its sales are spread across all regions of the country. This cushions it from the slowdown in offtake for any particular crop or region to a large extent.

Strong financial profile – The company's financial strength is characterised by steady revenue growth, stable profitability, healthy internal accrual generation, low reliance on debt and robust debt-protection metrics.

Comfortable liquidity position – DAL enjoys a comfortable liquidity position as marked by the marginal utilisation of working-capital limits, healthy cash accrual generation and positive cash flows.

[3] *Rated [ICRA]BBB-(Stable)/[ICRA]A3*

Credit challenges

Intensely competitive industry – The intensely competitive and fragmented nature of the agro-chemical industry exerts pricing pressure and necessitates constant marketing and branding expenditure.

Exposure to agro-climatic conditions – Vulnerability of sales and profitability to agro-climatic conditions, development of pest-resistant genetically modified (GM) seeds and regulatory risks inherent in the business. This is also demonstrated by revenue growth moderation and some contraction of margins in FY2019 on the back of a sub-par monsoon as well as relatively lower pest infestation in certain crops.

Exposure to raw material price and foreign exchange volatility – Lack of backward integration into technical manufacturing and dependence on imports for around 25-30% of its raw material requirement exposes DAL's profit margins to volatility in raw material prices as well as foreign exchange rates. This is also demonstrated by the contraction in operating margins in FY2019. Moreover, since the tie-ups for technicals is a key for DAL's business position, it remains exposed to the risk of discontinuation of such tie-ups or increase in competition from other formulators, or in case the primary supplier develops its own formulation.

High working-capital intensity – Given the diverse product portfolio and wide distribution network across the country, the company needs to maintain high raw material and finished goods inventory. This results in continuously high working-capital intensity for the company.

Funding support to extended to associate company - During FY2019, DAL has extended funding support to its associate company, DLL, with the board approved limit being Rs. 25 crore. While it is not anticipated, but any increase in the fund flows would be a rating sensitivity.

Liquidity position

The company's liquidity position remains comfortable on the back of strong internal accrual generation, cash balances/liquid investments (~Rs. 32 crore as on March 31, 2019), no major capex plans, undrawn bank lines and no debt repayment liability. This has resulted in low reliance on external debt, as highlighted by low utilisation of the working capital limits availed from the bank.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Methodology for Agrochemical Industry
Parent/Group Support	NA
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Dhanuka Agritech Limited. As on March 31, 2019, the company had one subsidiary (enlisted in Annexure-2).

About the company

DAL is part of the Delhi-based Dhanuka Group. It is involved in the formulation and marketing of agro-chemicals like insecticides, pesticides, herbicides, etc. The company's manufacturing facilities are in Sanand (Gujarat), Udhampur (Jammu and Kashmir) and Keshwana (Rajasthan).

In FY2019, the company reported a net profit of Rs. 112.6 crore on an OI of Rs. 1005.8 crore compared with a net profit of Rs. 126.2 crore on an OI of Rs. 962.6 crore in the previous year.

Key financial indicators (Consolidated)

	FY2018	FY2019
Operating Income (Rs. crore)	962.6	1005.8
PAT (Rs. crore)	126.2	112.6
OPBDITA/OI (%)	17.3%	14.5%
RoCE (%)	29.0%	24.0%
Total Debt/TNW (times)	0.0	0.0
Total Debt/OPBDITA (times)	0.0	0.0
Interest coverage (times)	190.2	164.0

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

		Current Rating (FY2020)					Chronology of Rating History for the past 3 years		
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating July 2019	Date & Rating May 2019	Date & Rating in FY2018 Mar 2018	Date & Rating in FY2017 Feb 2017	Date & Rating in FY2016 Feb 2016
1	Fund based-Working Capital Facilities	Long Term	30.0	-	[ICRA]AA-@	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)
2	Non-fund based – LC/BG	Short Term	33.35	-	[ICRA]A1+@	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+

@ - rating placed under watch with negative implications

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument Details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund based- Working Capital Facilities	-	-	-	30.0	[ICRA]AA- @
NA	Non-fund based – LC/BG	-	-	-	33.35	[ICRA]A1+ @

& - rating placed under watch with negative implications *Source: Dhanuka Agritech Limited*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Dhanuka Agri-Solutions Private Limited	100%	Full Consolidation

ANALYST CONTACTS

Sabyasachi Majumdar
+91 124 4545 304
sabyasachi@icraindia.com

Harsh Jagnani
+91 124 4545 394
harshj@icraindia.com

Deepak Jotwani
+91-124-4545870
deepak.jotwani@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 2556 0194/ 6606 9999