

October 04, 2022

Dhanuka Agritech Limited: Ratings reaffirmed at [ICRA]AA(Stable)/[ICRA]A1+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based-Working capital facility	30.00	30.00	[ICRA]AA (Stable) reaffirmed
Non fund based-LC/BG	33.35	33.35	[ICRA]A1+ reaffirmed
Total	63.35	63.35	

*Instrument details are provided in Annexure-1

Rationale

The ratings factor in the healthy credit profile of the company and expectations of the trend continuing, going forward, though the operating margins are likely to moderate in the current fiscal owing to elevated raw material prices. The ratings also factor in the planned backward integration into manufacturing technicals which is expected to provide raw material security as well as expand the contribution levels. ICRA expects the cash generation from operations along with ~Rs. 222.67 crore of cash at hand at the end of FY2022 to remain adequate to meet the capex requirements as well as cash outflow to investors in the form of dividends/buybacks, leading to no reliance on external debt. The performance of the company in FY2022 was marked by healthy revenue growth with the increase in realisation and volume growth. The operating margins continued to be healthy, leading to strong cash generation and net cash position. The performance is expected to moderate marginally in FY2023 given the increase in the raw material prices which has impacted the operating margins. Nevertheless, the cash flows are expected to remain robust to keep the credit profile healthy, going forward.

Additionally, the ratings factor in DAL's established market position, supported by its diverse product portfolio (across all agrochemical categories), strong brand presence, wide distribution network and geographical presence in the domestic market. Its long-standing relations with reputed international technical manufacturers, which enable it to regularly introduce specialty formulations, also support the ratings. DAL's liquidity position remains comfortable on the back of healthy internal accrual generation, robust free cash balances/liquid investments, undrawn bank lines and no debt repayment liability.

However, the ratings are constrained by the moderately high working capital intensity of the business, intense competition in the industry that limits the pricing flexibility of industry participants, including DAL, and the susceptibility of operations to any adverse regulatory development related to manufacturing/sales of agrochemicals or any discontinuation of tie-ups with international technical manufacturers. Moreover, DAL's revenues and profitability remain vulnerable to agroclimatic conditions, volatility in raw material prices and foreign exchange rates, given that part of the raw material requirement is met through imports. ICRA notes that the management had in the past demonstrated support towards the inorganic growth plans of DLL, although currently no support has been extended to the entity. Any materially large support to the Group's ventures would remain a key monitorable.

The Stable outlook on the rating reflects ICRA's expectation that DAL's credit profile will remain comfortable, going forward, driven by healthy cash generation coupled and large cash balances at hand which should allow the company to comfortably meet the capex requirement and remain free from long-term debt.

Key rating drivers and their description

Credit strengths

Leading player in industry - DAL has an established operational track record and its promoters have extensive experience of around three decades in the agrochemical industry. The company is one of the few scaled-up players in the industry with a healthy scale of operations and well entrenched distribution network spanning across the country. The company undertakes several initiatives for educating and supporting farmers, which has enabled the company to develop a strong brand recall among the end users.

Well-diversified product portfolio and geographical presence mitigate risk of poor performance of any region or crop - DAL has a well-diversified portfolio of products across the product segment i.e. insecticides, herbicides etc. as well as across crops. The company also has a well-entrenched distribution network spanning across the country. As a result, DAL's performance is largely protected against the poor performance of a particular crop or region.

Long-standing relations with reputed MNC technical manufacturers allow entry into speciality products which offer better margins than generic products - DAL has associations with reputed international technical manufacturers (such as Nissan Chemicals, FMC Corporation, and Hokko Chemicals), which provide access to speciality molecules. Almost 40–50% of the company's revenues are driven by the sales of speciality formulations, which also support the profit margins. Going forward too, the increased revenue contribution from speciality formulations is expected to aid the company's profit margins as the company has a healthy pipeline of product launches.

Comfortable financial profile - DAL's financial risk profile remains comfortable, characterised by healthy cash generation, low debt levels and a robust liquidity position. The company's capitalisation and coverage metrics have remained robust with gearing levels of 0.01 times in FY2021. The interest coverage moderated marginally to 77.2 times in FY2022 vis-à-vis 94.6 times in FY2021 albeit still remaining robust. The liquidity profile of the company remains strong with nearly Rs. 222.67 crore of cash and equivalents at the end of FY2022.

Expected benefits of backward integration post operationalisation of technical manufacturing plant from FY2024 - DAL is setting up a technical manufacturing plant at Dahej, Gujarat, with a total capital outlay of Rs. 300 crore over the next two years. The plant will provide raw material security and the benefit of backward integration in the form of lower raw material costs. Thus, ICRA expects DAL to start deriving benefit from the backward integration from FY2024 when the first phase of the plant is expected to be commissioned. However, given the large scale of the project, the company will remain exposed to project execution risks.

Credit challenges

High competitive intensity limits pricing flexibility - The intensely competitive and fragmented agro-chemical industry exerts pricing pressure and necessitates constant marketing and branding expenditure. Nevertheless, DAL benefits to an extent because of its strong brand presence.

Operations are vulnerable to varying agro climatic conditions and regulatory risks - The company's sales and profitability remain susceptible to the agro-climatic conditions, development of pest-resistant genetically modified (GM) seeds and the regulatory risks inherent in the business. This is also demonstrated by the moderation in revenue growth and contraction in margins in the previous years due to sub-par monsoons. The Government of India (GoI) had recently issued a draft order for banning the use of 27 pesticides after consultation with the Central Insecticides Board and Registration Committee (CIBRC/Registration Committee). While the order is being reassessed following the representations by industry participants, the imposition of the ban can adversely impact industry participants, including DAL.

Exposure to raw material price and foreign exchange volatility – Lack of backward integration into technical manufacturing and dependence on imports for around 20–30% of its raw material requirement expose DAL's profit margins to the volatility in raw material prices and foreign exchange rates. Moreover, given that the tie-ups for technicals is critical 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 the primary supplier developing its own formulation.

Moderately high working capital intensity - Given the seasonality inherent in demand, a diverse product portfolio, dependence on imports for raw materials and a wide distribution network across the country, the company needs to maintain high raw material and finished goods inventory. This has continued to result in high working capital intensity.

Environmental and Social Risks

DAL, being present in the chemical industry, is exposed to the risk of tightening regulations on environment and safety. However, DAL has been compliant with the environmental regulations. Nonetheless, it remains exposed to the ban on the use of hazardous chemicals, given their impact on human health. But the company is likely to introduce new products and phase out the hazardous ones to mitigate this risk.

Liquidity position: Strong

The company's liquidity position is strong on the back of healthy internal accrual generation, sizeable free cash balances/liquid investments (~Rs. 222.67 crore as of end of March 2022) and no debt repayment liability. Going forward, despite undertaking sizeable capex, the liquidity position is expected to remain strong, driven by healthy cash generation.

Rating sensitivities

Positive factors – The ratings could be upgraded if DAL demonstrates significant growth in revenue accompanied with healthy cash generation with limited reliance on debt.

Negative factors – The rating could be revised if there is a considerable decline in revenue and pressure on profit margins. Moreover, elongation in the working capital cycle, a sizeable debt-funded capex or funding support to related companies may put pressure on the liquidity position and lead to a downward revision of the ratings.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Agrochemical Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of DAL; as on March 31, 2022, 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 at Sanand (Gujarat), Udampur (Jammu and Kashmir) and Keshwana (Rajasthan).

Key financial indicators (audited)

DAL Consolidated	FY2021	FY2022
Operating income (Rs. crore)	1387.4	1477.7
PAT (Rs. crore)	210.5	208.8
OPBDIT/OI (%)	19.4%	17.9%
PAT/OI (%)	15.1%	14.1%
Total outside liabilities/Tangible net worth (times)	0.42	0.37
Total debt/OPBDIT (times)	0.03	0.00
Interest coverage (times)	94.63	77.20

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of rating history for the past 3 years			
		Type	Amount rated (Rs. crore)	Amount outstanding (Rs. crore)	Date & rating in	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020	
					October 04, 2022			September 6, 2021	September 21, 2020
1	Working Capital Facilities	Long-term	30.00	-	[ICRA]AA (Stable)	[ICRA]AA (Stable)	[ICRA]AA- (Positive)	[ICRA]AA- @	[ICRA]AA- (Stable)
2	Non-fund Based-LC/BG	Short term	33.35	-	[ICRA] A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+ @	[ICRA]A1+

@ - Under watch with negative implications

Instrument	Complexity Indicator
Long-term Fund-based – Working Capital facilities	Simple
Short Term-Non-fund Based	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: [Click Here](#)

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (RS Crore)	Current Rating and Outlook
-	Fund Based- Working Capital facilities	-	-	-	30.00	[ICRA]AA (Stable)
-	Non-fund Based- LC/BG	-	-	-	33.35	[ICRA]A1+

Source: Company

Annexure-2: List of entities considered for consolidated analysis- Not applicable

Company Name	Ownership	Consolidation Approach
Dhanuka Agritech Limited	100.00% (rated entity)	Full Consolidation
Dhanuka Agri Solutions Private Limited	100.00%	Full Consolidation

Source: DAL's annual report FY2022

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