Mangalore Chemicals
& Fertilizers Limited

MCFL/SE/2019

October 9, 2019

The Asst. Vice President,
National Stock Exchange of India Limited
Exchange Plaza, C-1, Block G,
Bandra Kurla Complex,
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Department of Corporate Services - CRD
Bombay Stock Exchange Limited,
Floor 25, Phiroze Jeejeebhoy Towers, Dalal Street
MUMBAI - 400 001
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Dear Sir

Sub: Intimation of Revision in Rating

Pursuant to the provisions of Regulation 30 and Sub Para 3 of Para A of Part A of Schedule III of the SEBI (Listing Obligations and Disclosure Requirements) Regulations, 2015, please note that, CARE has revised the rating of Long Term Bank Facilities to CARE BBB; Stable (read as Triple B; Outlook: Stable) from CARE BBB+;Stable (read as Triple B plus; Outlook: Stable) and of Long Term / Short Term Bank Facilities to CARE BBB; Stable / CARE A3 (read as Triple B; Outlook: Stable / A Three) from CARE BBB+;Stable / CARE A3+ (read as Tripe B plus; Outlook: Stable / A Three pluls).

The rationale given by CARE is included in the attached press release by CARE.

Kindly take the same on record.

Thanking you,

Yours faithfully,
for Mangalore Chemicals and Fertilizers Limited

Vijayamahantesh V. Khannur
Company Secretary

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Corporate Identity Number: L24123KA1966PLC002036

Mangalore Chemicals and Fertilizers Limited

October 09, 2019

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long term Bank Facilities	267.08 (reduced from Rs.283.21 crore)	**CARE BBB; Stable (Triple B; Outlook: Stable)**	**Revised from CARE BBB+; Stable (Triple B Plus; Outlook: Stable)**
Long term/ Short term Bank Facilities	2167.92 (enhanced from Rs. 2151.79 crore)	**CARE BBB; Stable/CARE A3 (Triple B; Outlook: Stable/A Three)**	**Revised from CARE BBB+; Stable/CARE A3+ (Triple B Plus; Outlook: Stable/A Three plus)**
Total	**2435.00 (Rupees Two Thousand Four Hundred Thirty Five crore only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Mangalore Chemicals & Fertilizers Ltd (MCFL) takes into account the moderation in its financial risk profile as reflected by its declining profitability margins owing to lower production in FY19 (refers to period from April 01 to March 31) along with higher raw material prices and deterioration in its debt service coverage indicators. The rating revision also factors in deterioration in the liquidity & financial profile of the promoters of the company (Zuari Agro Chemicals Ltd, ZACL). The ratings continue to be constrained by its leveraged capital structure, high dependence on timely fertilizer subsidy receivable from the government and highly regulated nature of the fertilizer industry.

The ratings, however, continues to factor in its established position in the Southern states of India with wide customer base, its long track record of operations in fertilizer industry and diversified product range. The rating also factors in expected improvement in profitability of the company (due to increase in govt notified energy consumption norms) with the conversion to gas based plant after commissioning of pipeline for supply of gas. The ratings also factors in company being part of Adventz group with diversified business & operational synergies with other companies of the group in the fertilizer business.

Going forward, the ability of the company to improve the conversion efficiency on a sustainable basis, on timely completion of gas pipeline and timely receipt of subsidy from the government will be critical for its credit risk profile. Further, the execution of the planned debt funded capex for energy savings project within the envisaged cost and time without adversely impacting its capital structure shall remain the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Established position and wide customer base

MCFL is one of the leading companies catering to the fertilizer 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 in the state. MCFL also maintains good market share in Kerala and a modest share in neighbouring states of Tamil Nadu, Andhra Pradesh, Telangana and Maharashtra. The fertilizers and plant nutrient products are marketed in these regions through a network of more than 2,500 dealers. 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:

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

MCFL 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. MCFL commenced production of Ammonia & Urea in 1976, set up Ammonium bi-carbonate plant in 1982, Di-ammonium phosphate and captive power plants in 1986, Sulphonated Naphthalene Formaldehyde plant in 2010 and Specialty Fertilizers plant in 2011.

Moderate Operational Performance

The company has Re- Assessed Capacity of 379500 MT for production of Urea and company had produced additional 30,000 MT of Urea in FY18 after getting approvals from the Department of Fertilizers (DoF) i.e. company had produced 409500 MT of Urea in FY18. Further, company had projected to produce full Reassessed Capacity [RAC] of 3,79,500 MT during 2018-19 after getting the approval of DoF. As per the management, however, the approval for 2018-19 from DoF was sought, but the conditions proposed by DoF were not favorable and hence the Company decided to produce the RAC after adjusting the excess production of 30,000 MT produced in FY18 against the RAC of the FY19 and it had produced 3,49,500 MT only [after adjusting for 30,000 MT].

However, the capacity utilization of N & P Fertilizers (Non Urea Fertilizers) has increased during FY19. Company had produced 296829 MT of N&P Fertilizers in FY19 as against 265552 MT in FY18.

Part of diversified group; however moderation in liquidity and financial profile of the holding company

MCFL is a part of the Adventz group which has interests in agri-inputs, engineering, infrastructure, real estate, consumer durables and services sectors. MCFL was earlier a UB group company, however, in May 2015, Zuari group acquired an additional 36.56% stake in MCFL over and above its earlier 16.47% stake to become the majority stakeholder in the company with 53.03% stake. As part of the Adventz group, MCFL is being benefitting from centralized procurement of key raw materials at group level leading to the benefit of economies of scale, a strong marketing and distribution network, resulting in better cost efficiencies, besides the savings in fixed overheads as a result of integrated operations with the other group companies which are in similar line of business. 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).

However, ZACL's liquidity position deteriorated considerably in FY19 on account of business losses and delays in subsidy receivables from GoI. ZACL reported negative PAT of Rs. 240.19 crore in FY19 as against positive PAT of Rs. 17.02 crore in FY18 on account of subdued agroindustry resulting in inability of the company to pass on the increase in raw material price to farmers. As a result of cash flow mismatches, ZACL was not able to timely service its debt repayment obligations. Further, as on August 31, 2019, 49394819 shares of MCFL are pledged by ZACL, which is equivalent to 78.60% of shareholding of ZACL and 41.68% of total shareholding of MCFL. ZACL is however in process of raising funds by issuing Compulsorily Convertible Debentures (CCDs) to improve its liquidity position.

Conversion to Gas Based Plant

As mandated by Department of Fertilizers, GOI, the Company has successfully completed gas conversion project of urea operations in June 2014 at a cost of around Rs.305 crore. The plant can therefore work on dual feed of natural gas and naphtha. The Company has signed a gas supply agreement with Indian Oil Corporation Limited and a Gas Transmission Agreement with GAIL (India) Limited in February 2011. Though Petronet LNG terminal of Kochi has been commissioned in September 2013, unsatisfactory progress in laying of gas pipeline from Kochi to Mangalore has deprived MCFL and other 2 Naptha-based units in south India from receiving gas for urea production. In February 2017, GAIL has awarded two contracts for building Kochi-Koottanad-Mangalore pipeline and the gas is expected to reach the plant by December 2019.

However, till the commissioning of pipeline for supply of gas, company would continue to receive subsidy based on the criteria for naphtha based units i.e. at current Govt. notified consumption norms of 6.902GCal/ Mt and with the conversion of plant to Gas based plant, the subsidy will be received at 7.356 GCal/ MT (for the next 5 years from the date of Gas supply). The energy norm will be revised at 6.50 Gcal/MT after a period of five years after receipt of natural gas.

Moderate Liquidity Position

The liquidity position of the company remains moderate characterized by its high operating cycle. Operating Cycle of the company increased from 147 days for FY18 to 161 days for FY19 due to increased average inventory days of the company. Inventory of the company increased from Rs. 396.91 crore as on March 31, 2018 to Rs. 538.73 crore as on March 31, 2019

majorly on account of increase in commodity prices. Further, average receivables days of the company remains high and stood at 163 days for FY19 (164 days for FY18) on account of high receivables outstanding from GoI. Subsidy receivables from GoI increased from Rs. 817.72 crore as on March 31, 2018 (29.93% of Total operating Income of the company in FY18)to Rs. 1115.43 crore of subsidy as on March 31, 2019 (35.97% of total operating income of the company) due to delayed subsidy payment from GoI and increased fertilizers prices resulted in higher accumulation of subsidy. This has resulted in increased dependence of the company for working capital borrowings in FY19. Further, the company is having debt repayment obligations of Rs. 49.55 crore in FY20.
The company is having free cash and bank balance of around Rs. 41.65 crore as on March 31, 2019 as against Rs. 112.64 crore as on March 31, 2108. Current Ratio of the company stood at 1.05x as on March 31, 2109 (1.02x as on March 31, 2018).

Key Rating Weaknesses
Deterioration in financial risk profile
The operating income of the company although increased by 13.48% y-o-y in FY19, but has largely remained volatile over the past few years, owing to erratic monsoon patterns over the past few years, especially in South India. The increase in income in FY19 is majorly on account of increase in realizations with increased raw material prices as total production and sales volumes of the fertilizers had gone down in FY19. Lower Production (by 60,000 MTs) and sales of Urea (by 47046 MTs) during FY19 against FY18, higher commodity prices and furnance oil prices (naptha), rupee depreciation and not so favourable season in the marketing areas of Karnataka, Tamil Nadu, Andhra Pradesh and Telangana resulted in decline in PBILDT Margins in FY19 despite of increase in saving in energy consumption in FY19. The company also faced challenges in recovering the escalation in the cost of the products due to timing difference between import/manufacture and ultimate sale of finished goods. PBILDT Margin of the company declined from 7.57% in FY18 to 6.53% in FY19. Interest Cost of the company also increased from Rs. 91.41 crore in FY18 to Rs. 111.02 crore in FY19 due to delay caused by introduction of disbursement of subsidy under DBT and accumulation of subsidy due to higher commodity prices. As a result, PAT of the company declined from Rs. 61.13 crore in FY18 to Rs. 32.88 crore in FY19.

Leveraged capital structure
The overall gearing of the company continued to remain high at 3.47x as on March 31, 2019 as against 2.87x as on March 31, 2018. Total Debt of the company has increased from Rs. 1366.65 crore as on March 31, 2018 to Rs. 1713.02 crore as on March 31, 2019 owing to higher working capital requirements of the company due to delay in trade receivables and high commodity prices leading to high reliance on working capital borrowings. The total debt includes the loan received by the company as a Special Banking Arrangement (SBA) which is bridge funding for the delay is receipt of subsidy. The repayment of such loan shall be made directly by the government to the lenders and the amount so paid by the government shall be adjusted from the subsidy receivable (due from government).The balance outstanding as on March 31, 2109 is Rs. 175.41 crore (Rs. 96.88 crore as on March 31, 2018, Rs.273.69 crore as on March 31, 2017). The loan carries an interest rate of 8.20% p.a. (including 7.72% paid directly by the GoI to the bank). Total Debt of the company as on June 30, 2019 stood at Rs. 1689.83 crore.
The company also plans to undertake capital expenditure for energy savings projects in the next couple of years in order to comply with energy efficiency norms which will be applicable to the company going ahead.

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 from GoI.

Exposure towards fluctuations in raw material prices
MCFL imports naphtha and furnace oil for the manufacturing of urea; phosphoric acid and ammonia for manufacture of complex fertilizers, and also imports Di-Ammonium Phosphate [DAP] and Muriate of Potash [MOP] besides other variants of complex fertilizers for trading. The raw materials and the traded goods derive their prices from the global crude price while international prices of DAP and MOP etc., are based on the demand and supply, therefore the turnover and profitability of the company fluctuates based on the global crude & commodity prices and forex movement.

Vulnerability of sales to agro-climatic conditions
Financial health of fetilizers manufacturers largely depends on the sowing season, vagaries of rainfall, status of subsidy outgo and the existing channel inventory level.

Project Risk associated with Energy Improvement Project
The company is planning to undertake an Energy Improvement Project (EIP) to further reduce the energy consumption for the manufacturing of Urea. The project is expected to be commissioned in FY21, after receipt of gas to their plant which is expected in December 2019. EIP will further reduce the consumption of feedstock in the production of ammonia by adopting new technology which requires replacement/addition of some of the equipment in ammonia plant. The EIP is expected to reduce the energy consumption from the current level of actual consumption (actual consumption norms of 6.289 Gcal/MT during FY19 and 6.385 GCal/MT in FY18) on naphtha to 5.50 Gcal/MT when it operates on natural gas [NG]. Since investment for natural gas project was completed in June 2014 the pre set energy norm of 7.356 Gcal/ MT will be made available to MCFL when it starts operating on natural gas. Also, according to the management not only the energy consumption will be lowered but also the normal maintenance expense will be reduced by operating the plant on natural gas. The company is expected to incur around Rs. 390 crore towards EIP with an estimated debt funding of Rs.280 Crore and the remaining from the internal cash generations.
The ability of the company to successfully execute the energy saving project within the envisaged cost and time without adversely impacting its capital structure will continue to be a key rating sensitivity.

Analytical approach: Standalone

Applicable Criteria
Criteria on assigning Outlook and Credit Watch to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short-term Instruments
CARE's Methodology for manufacturing companies
CARE's methodology for financial ratios (Non-Financial Sector)
CARE's methodology for Factoring Linkages in Ratings

About the Company
MCFL is one of the largest manufacturers of chemical fertilizers in the state of Karnataka and around 60% of the company's products are sold in the state of Karnataka, which meets about 20% of the needs of the farmers of the state. MCFL also maintains good market share in Kerala and a modest share in neighbouring states of Tamil Nadu, Andhra Pradesh, Telangana and Maharashtra. Further the company is also engaged in traded of complex fertilizers. MCFL has an aggregate installed capacity of 6.74 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 2.56 lakh MTPA) and Muriate of Potash, Granulated Fertilizers, Micronutrients, Soil Conditioners and Specialty Fertilizers. The company sells its product under the brand "Mangala".
MCFL is a part of Adventz group with majority shareholding held by the group company Zuari Agro Chemicals limited (ZACL, 53.03% holding as on June 30, 2019) (earlier stake (53.03%)held by Zuari Fertilizers & Chemicals Ltd., which was, merged with Zuari Agro Chemicals limited w.e.f. Nov 13, 2017). It was earlier a UB group company, however, in May 2015, Zuari group acquired an additional 36.56% stake in MCFL over and above its earlier 16.47% stake to become the majority stakeholder in the company with 53.03% stake.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	2732.32	3100.67
PBILDT	206.76	202.34
PAT	61.13	32.88
Overall gearing (times)	2.87	3.47
Interest coverage (times)	2.30	1.82

A: Audited

Status of non-cooperation with previous CRA: Not Applicable
Any other information: Not Applicable
Rating History for 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-Term Loan	-	-	-	267.08	CARE BBB; Stable
Fund-based - LT/ ST-Cash Credit	-	-	-	2167.92	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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Term Loan	LT	267.08	CARE BBB; Stable	-	1)CARE BBB+; Stable (22-Mar-19) 2)CARE BBB+; Stable (03-Oct-18) 3)CARE BBB; Stable (06-Apr-18)	1)CARE BBB; Stable (18-May-17)	1)CARE BBB- (25-Apr-16)
2.	Fund-based - LT/ ST-Cash Credit	LT/ST	2167.92	CARE BBB; Stable / CARE A3	-	1)CARE BBB+; Stable / CARE A3+ (22-Mar-19) 2)CARE BBB+; Stable / CARE A3+ (03-Oct-18) 3)CARE BBB; Stable / CARE A3 (06-Apr-18)	1)CARE BBB; Stable / CARE A3 (18-May-17)	1)CARE BBB- / CARE A3 (25-Apr-16)

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.*

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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.

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