July 30, 2021

Oriental Carbon & Chemicals Limited: Ratings reaffirmed for bank lines; Fixed Deposit rating reaffirmed and withdrawn

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fixed Deposit Programme	5.00	0.00	MAA (Stable) reaffirmed and withdrawn
Term Loans	178.00	161.68	[ICRA]AA- (Stable) reaffirmed
Long term/Short term Fund-based limits	75.00	85.00	[ICRA]AA- (Stable)/[ICRA]A1+ reaffirmed
Long term/Short term Interchangeable#	75.00	85.00	[ICRA]AA- (Stable)/[ICRA]A1+ reaffirmed
Non-Fund Based Limits	29.00	29.00	[ICRA]A1+ reaffirmed
Total	**287.0**	**275.68**	

**Instrument details are provided in Annexure-1*

Rationale

For arriving at the rating, ICRA has considered the consolidated financials of the Oriental Carbon & Chemicals Limited (OCCL), including its subsidiary Duncan Engineering Limited (DEL, rated [ICRA]A- (Stable)/[ICRA]A2+). The ratings factor in the long and established track record of OCCL in the business of producing Insoluble sulphur, dominant position in the domestic market and favourable position as a second supplier to all major tyre manufacturer in global markets. The ratings also consider healthy financial risk profile characterised by large un-encumbered cash balances, healthy cash generation form operations and low debt repayments in the near to medium term. The ratings also factor in the stable outlook for the tyre industry, which is the key consumer of Insoluble sulphur, in the medium to long term with demand expected to grow at a healthy pace post the impact of Covid-19 pandemic in FY2021. OCCL has a market share of around 60% in the domestic insoluble sulphur market and ~10% globally. While it has dominant position in the domestic market, it has been able to position itself as the preferred / second preferred supplier to most of the global tyre makers.

OCCL's credit profile has witnessed a significant improvement with healthy cash accruals in the last couple of years, which has resulted in its net debt level remaining low at Rs. 10.9 crore at the end of FY2021 on a consolidated basis. The capitalisation and coverage indicators have been healthy with net gearing (Net debt/Tangible Networth) and net leverage (Net Debt/OPBDITA) remaining low at the end of FY2021. ICRA also takes note of OCCL's ongoing capacity expansion in the IS capacity by 11,000 MTPA and sulphuric acid capacity by 42,000 MTPA, with a total outlay of Rs. 216 crore at its Dharuhera facility of which the first phase of IS capacity expansion by 5500 MTPA along with Sulphuric acid capacity at an outlay of Rs 156 crore is underway. The commissioning for the project has been pushed to October 2021 from July 2021 as envisaged earlier for phase-1 due to slowdown in work driven by Covid-19 led restrictions on movement of goods and labour. Additionally, given the evolving industry dynamics the company would take a call on the execution of the second phase post commissioning of the phase-1. While the project commissioning has been delayed, no cost over runs are envisaged.

The ratings, however, are constrained by risks associated with the revenues being derived primarily from a single product i.e. Insoluble sulphur which is mostly supplied to the automotive sector; threat of competition from Chinese players partly mitigated by high entry barriers and challenge of maintaining high quality of products and high standards of health and safety at plants; vulnerability to foreign exchange rate movements; exposure to raw material price risk given sulphur prices have been volatile in past few years; high working capital intensity and the project execution risks related to the ongoing capex

partly mitigated by the track record of the company in executing such projects within the budgeted timelines and capital outlay.

The Stable outlook on the long term rating reflects ICRA's opinion that OCCL will continue to benefit from its established track record of operations, favourable market position in the domestic and overseas markets, healthy financial risk profile and stable outlook for the tyre demand in the medium to long term.

Key rating drivers and their description

Credit strengths

Well experienced management and long track record of OCCL in the business of producing IS: OCCL has a long and established track record in the chemicals industry. It started operations as Dharuhera Chemicals Limited in 1978 and was later merged with Oriental Carbon Limited in 1984 to form Oriental Carbon and Chemicals Limited. It started production of insoluble sulphur in 1994 with a capacity of 3000 MTPA and has since then ramped up its capacity to 34,000 MTPA currently. The company is expanding its IS capacity by another 11,000 MTPA in two phases with the first phase expected to be commissioned by October 2021. The second phase of expansion will be undertaken post commissioning of the phase-1 and after factoring in the demand outlook for IS by October 2021.

Dominant market position in the domestic industry; favourable market position as a 'Second Supplier' to major tyre companies across the world: OCCL is the sole manufacturer of IS in the domestic market**.** OCCL continues to retain its leadership position in the domestic market with nearly 55%-60% of the market share and around 10% market share in the global market.

Favourable growth prospects in the domestic tyre industry driven by radialisation of tyres and capacity expansion being undertaken by tyre manufacturers in India: Insoluble sulphur is used as an input for manufacturing of tyres and with rising radialisation the consumption of insoluble sulphur is expected to rise. The outlook for tyre demand remains stable in near to medium term driven by rising preference of personal mobility and growing OEM demand. With healthy growth rate for the tyre segment going forward, the demand outlook for IS is expected to remain healthy as well.

Track record of healthy plant performance and significant ramp up of newly installed capacity: OCCL's plant performance has been healthy over past few years with healthy capacity utilisation levels. Capacity utilisation post capacity additions have also been healthy. While the capacity utilisation had moderated in FY2020 and FY2021 due to auto sector slowdown and Covid-19 pandemic thereafter, the capacity utilisation had witnessed sharp uptick in H2 FY2021 driven by healthy demand from the tyre industry.

Healthy financial risk profile characterised by robust cash generation, large cash balances resulting in healthy credit metrics: OCCL's capitalisation and coverage indicators have improved significantly over last few years despite undertaking significant capex given the healthy cash generation and low reliance on debt. The net debt levels stood at Rs. 10.9 crore at the end of FY2021 leading to low net financial leverage (Net Debt/OPBDITA) 0.1x at the end of FY2021. The interest coverage ratio also remains robust at 18.1x in FY2021 vis-à-vis 11.7 in FY2020. ICRA expects further improvement in the credit metrics of the company given healthy cash generation and limited capex planned going forward.

Stable performance of subsidiary Duncan engineering Limited: Duncan Engineering (DEL rated [ICRA]A- (Stable)/ [ICRA]A2+, earlier known as Schrader Duncan), incorporated in 1962, was promoted as a joint venture between Schrader Bridgeport International (SB Intl, a wholly owned subsidiary of Tomkins Plc), and the Duncan group (managed by the Goenka family, which is promoter group of OCCL). DEL is into manufacturing of automotive tyre valves and pneumatic products such as air cylinders, valves, and accessories. OCCL holds 50.01% stake in DEL making it a subsidiary of OCCL. DEL's operating income moderated to Rs. 41.5 crore in FY2021 as against Rs. 43.4 crore in FY2020 as the sales were impacted by shutdown in Q1 FY2021 due to the Covid-19 lockdown. The operating profit was lower at Rs. 4.5 crore in FY2021 as against Rs. 5.8 crore in FY2020 as Covid related slowdown and the rise in steel prices impacted margins. The net profit however was higher mainly due to a deferred tax benefit

at Rs. 8.0 crore in FY2021 as against Rs. 3.3 crore in FY2020. The entity had long term debt of around Rs. 0.2 crore by the end of FY2021 and around Rs. 6.0 crore of unencumbered cash.

Credit challenges

Majority of revenue being derived from a single product i.e. insoluble sulphur with demand primarily from the automotive sector: Nearly 93% of OCCL's revenue is derived from the sale of insoluble sulphur which results in high reliance of the company on a single product. Additionally, the majority of demand for insoluble sulphur is derived from the automotive tyres, resulting in significant reliance on a single sector for demand.

Vulnerable to residual project execution risk with the upcoming capacity expansion partly mitigated by the track record of executing similar projects: OCCL is undertaking a Rs. 216 crore capacity expansion project for increasing it's IS capacity by 11,000 MTPA and sulphuric acid capacity by 42,000 MTPA with phase-1 of 5500 MTPa SI capacity and 42,000 MTPA of sulphuric acid capacity slated to commissioned in October 2021. The second phase will be executed after the company takes stock of the demand situation post completion of the first phase. The project is being funded with a debt equity ratio of 2:1. The project being large, exposes the company to project execution risks and also capacity ramp up risk post completion of the project.

Threat of competition from Chinese players; partly mitigated by high entry barriers and inconsistent quality of products and lower Environment, Health and Safety (EHS) standards: Chinese IS manufacturers are usually able to offer their product at a lower cost and are a threat to players like OCCL. However, large tyre manufacturers do not procure from Chinese players mainly due to the apprehension of inconsistent quality levels and lower EHS standards.

Vulnerable to forex rate movements; booking forward contracts mitigates the risk to an extent: OCCL derives significant share of revenues from export sales thus exposing the company to foreign exchange fluctuations. However, the risk is partially mitigated as the company has a policy to hedge nearly 75% of its net exposure for the forward 6 months using forward contracts.

Vulnerable to the volatility in raw material prices though largely mitigated by periodic price revision clauses in the contracts: Sulphur and coating oil are the major raw materials for manufacturing insoluble sulphur. Sulphur prices have been volatile over the years which exposes the company to raw material price risk. The risks are however largely mitigated given the periodic price revisions that happen with the end users albeit there can be a lag in passing on the raw material price impact.

Liquidity position: Strong

OCCL's liquidity is strong backed by large un-encumbered cash balances, availability of un-utilised fund-based limits vis-à-vis the capex requirement and term debt repayments in the near to medium term. The company as on FY2021 had net debt of Rs. 10.9 crore. Going forward the cash generation is expected to remain stable in FY2022 and grow meaningfully in FY2023 with the commissioning of the new capacity, which should keep the liquidity position strong for OCCL.

Rating sensitivities

Positive factors – OCCL's rating may be revised upwards with significant increase in the scale of operations with commensurate returns.

Negative factors – The rating may be downgraded if there is significant contraction in the scale of operations of the company for a sustained period resulting in weak cash accruals. Any large debt funded organic/in-organic growth initiatives leading to weakening of the credit profile will put downward pressure on the ratings

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in Chemical Industry
Parent/Group Support	Not applicable
Consolidation / Standalone	The ratings are based on the consolidated financials of the company

About the company

Oriental Carbon & Chemicals (OCCL) was incorporated in 1978 as Dharuhera Chemicals Limited (DCL) and in 1983 DCL was merged with Oriental Carbon Limited (OCL), a group company engaged in the production of Carbon Black, to form OCCL. In 1994, OCCL had set-up a manufacturing facility for the production of Insoluble Sulphur, which is now the flagship product of the company as the company sold carbon black unit to Continental Carbon Company in 2000. OCCL currently has three production units: two at Dharuhera Industrial Unit in Haryana and one at Mundra SEZ in Gujarat. The company is currently engaged in the production of Insoluble Sulphur, Sulphuric Acid and Oleum. The production capacity of OCCL stands at 34,000 metric tonnes per annum (MTPA) for Insoluble Sulphur (IS), 46,200 MTPA for Sulphuric Acid & Oleum. The company is in the midst of a capex program of expansion of IS capacity by 11,000 MTPA at Dharuhera, with 5500 MTPA to be commissioned by October 2022 along with expansion of sulphuric acid capacity by 42,000 MTPA. The schedule for the commissioning of the second phase of capacity expansion of 5,500 MTPA is yet to be decided.

Key financial indicators (audited)

OCCL Consolidated	FY2020	FY2021
Operating Income (Rs. crore)	387.8	374.6
PAT (Rs. crore)	74.8	83.0
OPBDIT/OI (%)	28.9%	31.6%
PAT/OI (%)	19.3%	22.1%
Total Outside Liabilities/Tangible Net Worth (times)	0.5	0.5
Total Debt/OPBDIT (times)	1.3	1.5
Interest Coverage (times)	11.7	18.1

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 (FY2022)				Chronology of Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of June 30, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021		Date & Rating in FY2020		Date & Rating in FY2019
					3 Aug 2021	24 Nov 2020	20 Jul 2020	01-Aug-2019	24-Jul-2019	18 Jul 2018
1	Term Loans	Long Term	161.68	135.43	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Positive)
2	Fund Based Limits	Long Term/Short Term	85.00	-	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+
3	Non-fund based limits	Short Term	29.00	-	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+
4	Fixed deposits	Medium term	0.00	-	MAA (Stable) reaffirmed and withdrawn	MAA (Stable)	MAA (Stable)	MAA (Stable)	MAA (Stable)	MAA-(Positive)
5	Long term/Short Term -Interchangeable#	Long term/Short Term	85.00	-	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]AA- (Stable) /[ICRA]A1+	[ICRA]A+ (Positive)/ [ICRA]A1+

Complexity level of the rated instruments

Instrument	Complexity Indicator
Term Loans-Long term	Simple
Fund Based Limits-Long Term/Short Term	Simple
Non-fund based limits-Short Term	Simple
Fixed deposits-Medium Term	Simple
Long term/Short Term-Interchangeable	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 analyzing 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, is available on ICRA's 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
-	Fixed Deposits	-	-	-	-	MAA (Stable) reaffirmed and withdrawn
-	Term Loan-1	FY2018	NA	FY2023	21.00	[ICRA]AA- (Stable)
-	Term Loan-2	FY2018	NA	FY2023	11.00	[ICRA]AA- (Stable)
-	Term Loan-3	FY2018	NA	FY2023	4.00	[ICRA]AA- (Stable)
-	Term Loan-4	FY2019	NA	FY2025	12.17	[ICRA]AA- (Stable)
	Term Loan-5	FY2019	NA	FY2025	6.31	[ICRA]AA- (Stable)
	Term Loan-6	FY2019	NA	FY2026	7.20	[ICRA]AA- (Stable)
-	Term Loan-Proposed	-	-	-	100.00	[ICRA]AA- (Stable)
-	Long Term/Short Term Fund based	-	-	-	85.00	[ICRA]AA- (Stable)/ [ICRA]A1+
-	Non-fund based	-	-	-	29.00	[ICRA]A1+
-	Long Term/Short Term-Interchangeable#	-	-	-	85.00	[ICRA]AA- (Stable)/ [ICRA]A1+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	HMEL's ownership	Consolidation Approach
Duncan Engineering Limited	50.05%	Full consolidation

Source: *OCCL*

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