High Conviction Report

KEYNOTE

Deepak Fertilisers and Petrochemicals Ltd.

28th August 2024

Growth with mega expansion under-way

Deepak Fertilisers and Petrochemicals Corporation Limited (DFPCL) is a leading Indian conglomerate with diverse business segments. In Industrial Chemicals, DFPCL is the largest producer of Nitric Acid in India with a capacity of 1,123 KTPA, holding a ~60% market share in Concentrated Nitric Acid (CNA) and ~28% market share in Diluted Nitric Acid (DNA), and produces Isopropyl Alcohol (IPA) with a capacity of 70 KTPA, commanding a 30% market share. In Fertilizers, the Company manufactures high-efficiency fertilizers, including NPK complex and Bentonite Sulphur, with a total capacity of 1,185 KTPA and a leading market share. In Mining Chemicals, DFPCL leads in Technical Ammonium Nitrate (TAN) and provides comprehensive mining solutions, holding a 44% market share, with a capacity of 629 KTPA. Additionally, DFPCL has a non-core business in realty industry with the name Creaticity, a lifestyle center focusing on home interiors and design.

Capacity expansion in TAN segment

The Company is expanding its TAN capacity driven by strategic initiatives and favorable market conditions. The Company is boosting its TAN production capacity with a new 376 KTPA plant in Gopalpur, Odisha, operational by FY26. This will increase total capacity from ~629 KTPA to ~1,000 KTPA, meeting 60% of India's TAN demand. The lifting of the export ban and the strategic location of the Gopalpur plant, in Odisha, will enhance export opportunities.

Capacity expansion in Nitric Acid

DFPCL is expanding its nitric acid capacity from ~1,123 KTPA to ~ 1,573 KTPA. As India's largest producer of nitric acid, DFPCL is poised to meet rising demand across various sectors, benefiting from the shift of global specialty chemical intermediates from China to India. The expansion includes 150 KTPA of CNA and 300 KTPA of DNA of nitric acid and a focus on specialty products to command premium pricing.

Backward integration into ammonia

DFPCL has initiated a backward integration project by establishing a 500 KTPA ammonia plant to secure a steady supply of ammonia, essential for its products. This move reduces dependency on volatile global ammonia prices and logistical issues, previously costing $450-$480 per ton. Producing ammonia in-house at $260-$280 per ton enhances EBITDA margins by $160-$200 per ton, offering significant logistics and fiscal savings. Despite challenges like natural gas price fluctuations and initial stabilization costs, the project is expected to improve operational efficiency, cost savings, and supply chain management.

View & Valuation

We believe that with expansion and backward integration, the Company shall be able to boost is topline and profitability. Further, with better macro trends like demand supported by no dumping and booming GDP, coupled with better prospects for monsoon, the Company will be able to make the most of its capacity. Resultantly, we see improvement in gross margins from ~32% in FY24 to ~36% in FY27 and EBITDA margins to increase from ~15% to ~20% over the same period. Consequently, we initiate a coverage of DFPCL with a BUY rating. Subsequently, we ascribe an EV/EBITDA multiple of ~10 times, to arrive at a target share price of ~Rs. 2,132, suggesting an upside of ~98%.

BUY

CMP Rs. 1,079

TARGET Rs. 2,132 (+98%)

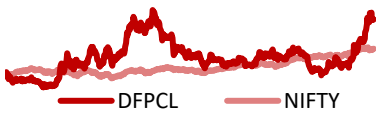
Company Data

Bloomberg Code	DFPC IN
MCAP (Rs. Mn)	1,35,954
O/S Shares (Mn)	126
52w High/Low	1,124/453
Face Value (in Rs.)	10
Liquidity (3M) (Rs. Mn)	1,778

Shareholding Pattern %

	Jun-24	Mar-24	Dec-23
Promoters	45.6	45.6	45.5
FIIs	9.9	8.9	9.3
DIIs	6.3	7.0	7.4
Non-Institutional	38.2	38.5	37.9

DFPCL vs Nifty



Aug, 21 Aug, 22 Aug, 23 Aug, 24

Source: Keynote Capitals Ltd.

Key Financial Data

(Rs Bn)	FY24	FY25E	FY26E
Revenue	87	100	119
EBITDA	13	18	22
Net Profit	4	7	10
Total Assets	118	141	152
ROCE (%)	8%	11%	12%
ROE (%)	8%	13%	15%

Source: Company, Keynote Capitals Ltd.

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About the Nitric Acid Industry

Imperative initial information on Nitric Acid

About the chemical

Nitric acid (HNO_3) is a strong chemical used in industries to make explosives, fertilisers, and clean metals.

Grades of the chemical

Nitric Acid (98-99%) + Water (1-2%) → Concentrated Nitric Acid (CNA)

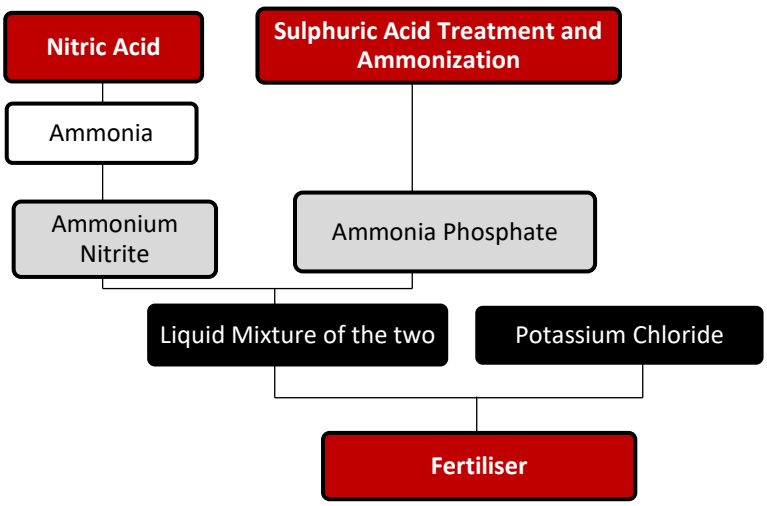
Nitric Acid (64-72%) + Water (28-36%) → Strong Nitric Acid (SNA)

Nitric Acid (60%) + Water (40%) → Diluted Nitric Acid (DNA)

Applications of the chemical

*The chemical has several applications, such as fertilisers, dye intermediates, explosives, adhesives, and purifying metals. According to ReAgent, a UK-based chemical manufacturer, ~80% of nitric acid is consumed in making fertilisers, w*hereas *only 20% is used for other applications such as nitrobenzene, adipic acid, and chloronitrobenzene, which are vital for the construction, automotive, and plastics sectors.*

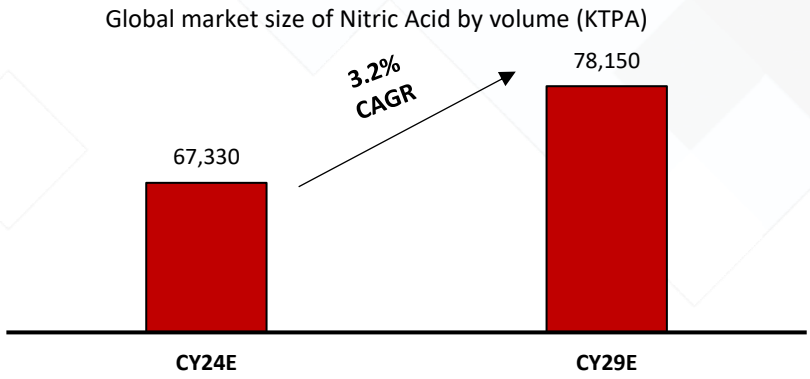
Illustration of an application



Source: Keynote Capitals Ltd.

The global industry of Nitric Acid

The estimated size of the Nitric Acid Market in 2024 is 67,330 KT and it is projected to reach 78,510 KT by 2029. The market is expected to grow at a CAGR of 3.2% during the forecast period (2024-2029).

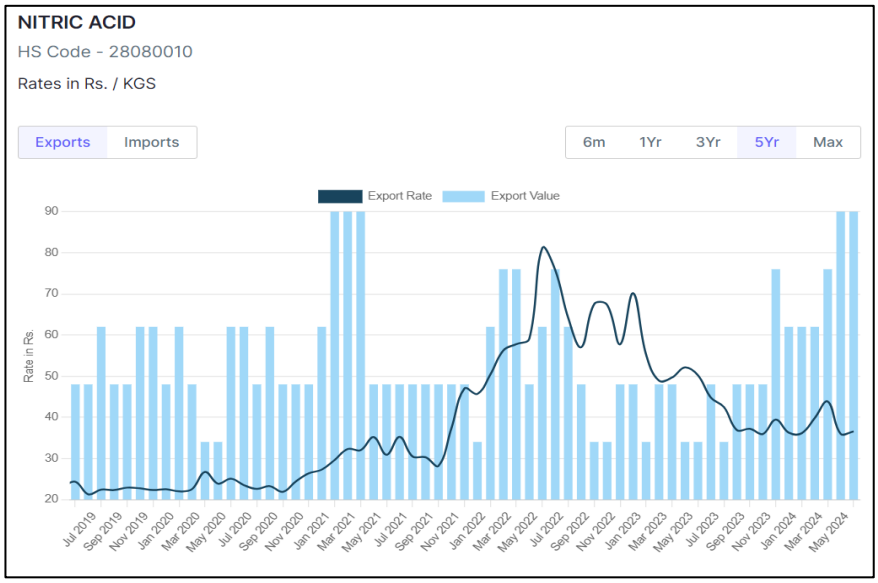


Source: Mordor Intelligence, Keynote Capitals Ltd.

Asia-Pacific is expected to be the dominant market in nitric acid production, owing to the largest production and consumption of fertilizers in Asia-Pacific countries, including China, India, and South Korea.

The world's largest producers of nitric acid include Yara International ASA (Norway), BASF SE (Germany), TKG Huchems (South Korea), Nutrien Ag Solutions (Canada), CF Industries Holdings (United States), and DFPCL (India).

Price of Nitric Acid



Source: Screener, Keynote Capitals Ltd.
Export prices from India can be considered in parity with global nitric prices.

The Indian Nitric Acid market

The Indian nitric acid industry is ~1,720 KT in FY23, is primarily driven by the fertilizer industry, which plays a crucial role in producing ammonium nitrate and supporting domestic agricultural activities through the manufacturing of nitrate-based fertilizers. This strong connection directly links the nitric acid market to the agricultural sector's demand for essential fertilizers.

Additionally, nitric acid is used to produce adipic acid, toluene di-isocyanate, nitrobenzene, and other chemicals. Adipic acid is vital for nylon production and is widely used in the automotive and textile industries. Toluene di-isocyanate and nitrobenzene are essential components in manufacturing polyurethane foams, which are extensively utilized in furniture, bedding, automotive seating, insulation, and various other industries.

Indian manufacturers of Nitric Acid

Company	Capacity (KT)	Description (grades)
DFPCL	1,123	DNA, WNA, CNA
Gujarat Narmada Valley Fertilisers & Chemicals Ltd. (GNFC)	514	WNA, CNA
Rashtriya Chemicals and Fertilizers Ltd (RCF)	70	DNA, SNA, CNA

WNA is Weak Nitric Acid
Source: Companies, Keynote Capitals Ltd.

Factors Influencing the Indian Nitric Acid Market

Demand-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Fertilizers	Rice Wheat Cotton	Rainfall
2.	Medical uses	Pharmaceutical	-
3.	Nylon	Automotive	Increasing disposable income
4.	Dyes & Pigments	Textile	Fast fashion, increasing disposable income

Source: Keynote Capitals Ltd.

Supply-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Ammonia	Natural gas	Global market dynamics
2.	Freight charges	Global supply chain stability/ disruptions	-
3.	China dumping/withdrawing	Surplus inventory/production cuts in China	-
4.	Global demand shift	Channel destocking/restocking	-

Source: Keynote Capitals Ltd.

Nitric acid prices to rise in coming months

The global ammonia and nitric acid market is currently facing significant changes due to several key factors. Strict environmental regulations and high compliance costs are leading to the closure of ammonia production facilities across Europe, reducing regional supply. At the same time, natural gas prices are rising because of higher domestic demand and LNG exports, which is driving up production costs for ammonia producers, especially in Europe.

As a result of these developments, global prices for both ammonia and nitric acid are expected to rise, benefiting producers in regions with lower raw material costs, such as India. However, industries that rely on these chemicals, such as fertilizer and explosives manufacturers, may need help with these increased costs.

IPA

Imperative initial information on IPA

About the chemical

Isopropyl Alcohol (IPA) is a colorless versatile chemical used across various industries. The highest demand comes from the Asia-Pacific region, driven by the pharmaceutical, cosmetics, personal care, and electronics industries.

Chemical process

Propylene and Sulfuric Acid (H_2SO_4) are raw materials

Grades of the chemical

IPA (99.0-99.8%) + Water (0.2-1.0%) → Technical Grade

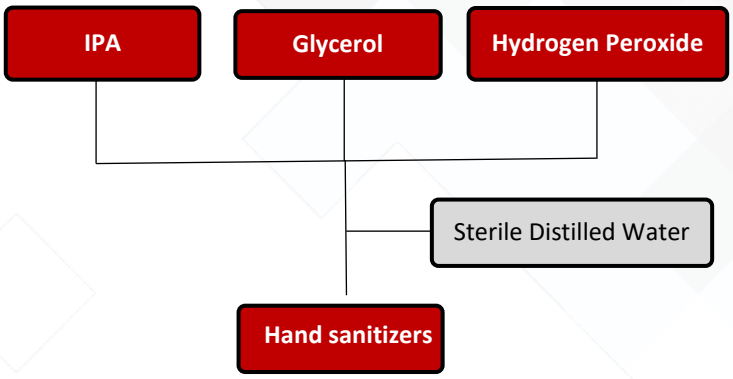
IPA (99.0-99.9%) + Water (0.1-1.0%) → Medical/Pharmaceutical Grade

IPA (99.9%) + Water (0.1%) → ACS (Spectrophotometric) Grade

Applications of the chemical

IPA is a versatile chemical with numerous applications across various industries. According to ChemAnalyst, ~42% of IPA is consumed by the pharmaceuticals industry, where it is used primarily for cleaning and disinfecting purposes. The second-biggest consumer of IPA is the cosmetics and personal care industry with ~24% share. The remaining share is split among several industries such as electronics and paint industry.

Illustration of an application



Source: Keynote Capitals Ltd.

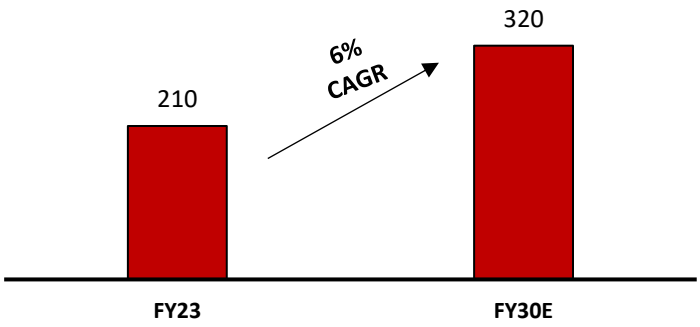
The global industry of IPA

In CY24E, the global IPA market volume was expected to reach 3,300 KTPA, with a market value of ~ $3.2 Bn. It is projected to grow at a CAGR of 3.3%, reaching 3,900 KTPA by 2029.

Indian IPA industry

In FY23, the Indian IPA market volume stood at ~210 KTPA and is projected to reach ~320 KTPA by FY30, growing at a CAGR of 6%. The demand for IPA in India is primarily driven by its extensive use in the pharmaceutical sector due to its excellent disinfecting properties, making it a key ingredient in the production of sanitizers and disinfectants.

Indian IPA market (KTPA)



Source: ChemAnalyst, India Isopropyl alcohol (IPA) market analysis, Keynote Capitals Ltd.

Out of the total requirement, the country's dependence on import stood at 132 KT in FY24, forming ~60% share for the year.

DFPCL is a market leader in IPA, with majority of the quantity is imported in the country.

Factors Influencing the Indian IPA Market

Demand-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Antiseptics, disinfectant	Hygiene awareness	
2.	Solvent for drug formulation	Pharmaceutical	Development of new drugs
3.	Aftershave lotions/Bath products	Awareness	Rise in disposable income
5.	Makeup products	Rise in beauty standards	Economic growth
6.	Solvent for coatings, quick-drying inks and oils		

Supply-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Propylene/Acetone	Crude oil	Global market dynamics
2.	China dumping/withdrawing	Surplus inventory in China/global demand	-

Source: Keynote Capitals Ltd.

Ammonium Nitrite

Imperative initial information on Ammonium Nitrate

About the chemical

Ammonium Nitrate (AN) is a widely used chemical compound with significant applications in agriculture, mining, and defense industries.

Chemical process

Nitric Acid + Ammonia → Ammonium Nitrite

Grades of the chemical

AN (96-99.8%) + Additives (0.2-4%) → Low-Density Ammonium Nitrate (LDAN)

AN (96-99.8%) + Additives (0.2-4%) → High-Density Ammonium Nitrate (HDAN)

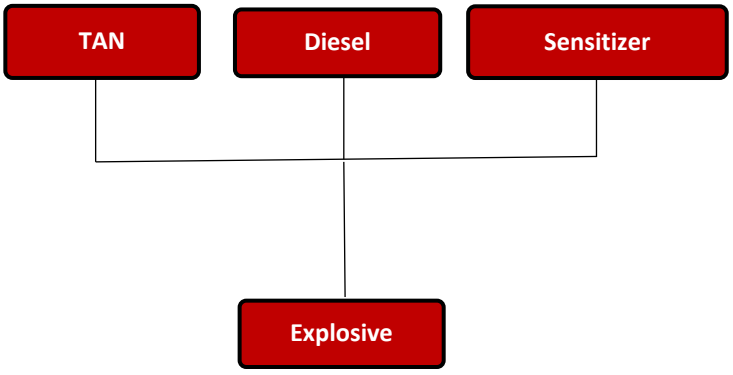
AN (85-92%) + Water (8-15%) → Ammonium Nitrate Solution (ANSOL)

Applications of the chemical

Fertiliser-Grade Ammonium Nitrite (FGAN) is used in agriculture to provide nitrogenous content. Technical-Grade Ammonium Nitrate (TAN) is used in making explosives for mining, and construction.

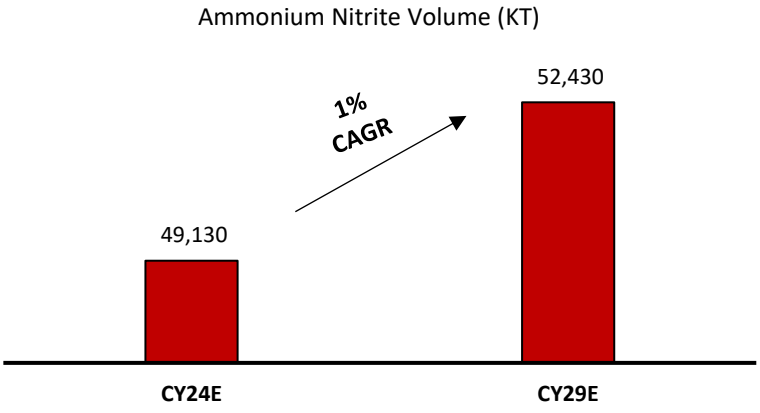
Electronic-Grade Ammonium Nitrate (EGAN) is a highly purified grade used in manufacturing circuits and microchips. Medical-Garde Ammonium Nitrate (MGAN) is used in healthcare to produce nitrous oxide which serves as an analgesic and anesthetic in surgery and dentistry. Of all the grades, FGAN is the most used grade of ammonium nitrate. The FGAN is the most widely used, primarily in agriculture as a high-nitrogen fertilizer. This grade is essential for enhancing plant growth and crop yields, making it a critical component in the agricultural sector. TAN is predominantly used in the manufacturing of civil explosives and for chemical purposes. It is a key raw material in the mining and construction industries, where it is utilized for its oxidizing properties to produce explosives. In India, coal mining accounts for ~63% of TAN consumption, non-coal mining for ~9% and infrastructure for ~28%. Another specialized form is the EGAN, which is exceptionally high-purity (99.9%) and is used to produce nitrous oxide for Very Large-Scale Integration (VLSI) and Ultra-Large-Scale Integration (ULSI) in the electronics industry. This grade is crucial for gas-phase chemical deposition processes in semiconductor fabrication, ensuring high purity and reliability in the production of electronic components such as chips, circuits, and transistors.

Illustration of an application



Source: Keynote Capitals Ltd.

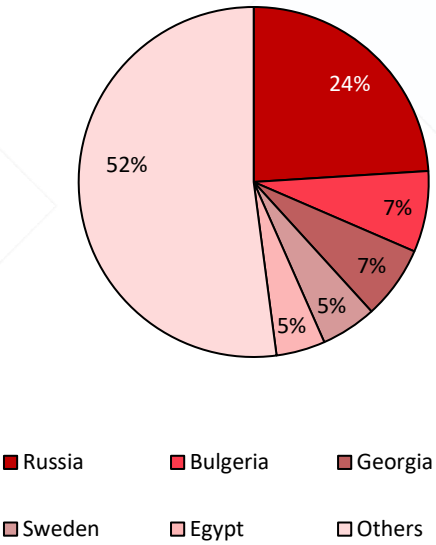
The global industry of Ammonium Nitrite



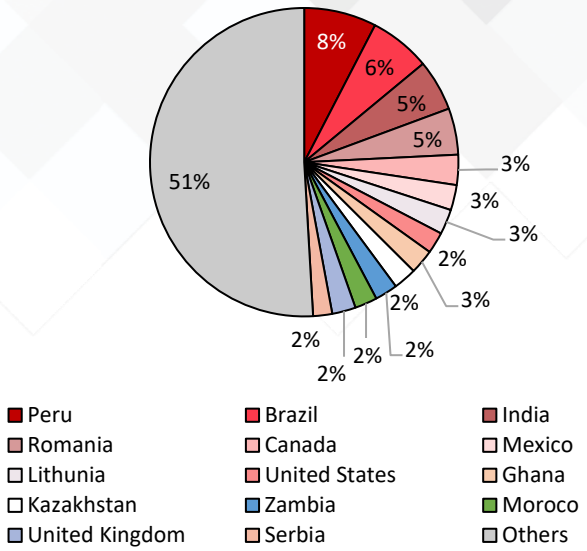
Source: Mordor Intelligence, Keynote Capitals Ltd.

The global trade of export-import of ammonium nitrite stood at $4.37 Bn.

Top Sellers of Ammonium Nitrate in CY22 (%)



Top Buyers of Ammonium Nitrate in CY22 (%)



Source: The Observatory of Economic Complexity

Indian Ammonium Nitrate Industry

In India, the current installed capacity for AN production is ~1,100 KTPA. This capacity is expected to increase significantly with an additional 1,000 KMPTA capacity under construction, which would raise the total capacity to ~2,100 KTPA per annum by FY26. According to the Indian Ammonium Nitrate Manufacturers Association (IANMA), capacity utilization has decreased from 86% in FY19 to 75% during April-December '23 due to uncontrolled imports.

India's dependence on imports for TAN stands between ~25-30%.

Factors Influencing the Indian TAN Market

Demand-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Explosives	Coal mining	Power consumption (from coal)
		Limestone mining	Real estate
		Cement production	Real estate
		Steel production	Real estate and infrastructure
2.	Nitrogenous fertilizers	-	-
3.	Rainfall	-	-

Source: Keynote Capital Ltd.

Supply-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Ammonia	Natural Gas	Global market dynamics
2.	Russia dumping	Sanctions on Russia	Global market dynamics
3.	Government regulations	Allowing/restricting export/import	Domestic demand scenario

Source: Keynote Capital Ltd.

Nitrogen Phosphate Potassium Fertiliser

Imperative initial information on NPK Fertiliers

About the fertiliser

NPK fertilizer is a crucial agricultural product that provides essential nutrients for plant growth and overall health. The term "NPK" stands for nitrogen (N), phosphorus (P), and potassium (K).

Production process

Ammonium Nitrate + Phosphoric Acid + Potassium Chloride → NPK Fertilizer

Grades of the fertilizer

There are many grades with different combinations of NPK, namely:

NPK Ratio: 14-28-14

NPK Ratio: 8-21-21

NPK Ratio: 9-24-24

Applications of the fertiliser

NPK is a fertiliser used in different ratios depending on the crop and geography.

Illustration of an application

NPK is the final end-use and has no further application.

The Indian fertilizer market

Fertilizers are essential for plant growth. They are classified into organic and inorganic (synthetic) fertilizers with Inorganic further divided into Single nutrient (Straight), Multi-nutrient (Complex), and Micro-nutrients.

1. Single-nutrient fertilizers, also known as straight fertilizers, provide only one essential nutrient to the plant, such as nitrogen (N), phosphorus (P), or potassium (K). Common examples include Urea and Ammonium Nitrate for nitrogen, and Single Superphosphates (SSP) and Muriate of Potash (MOP) for phosphorus and potassium, respectively.

2. Multi-nutrient fertilizers, also known as complex fertilizers, contain two or more nutrients. They can be binary, such as Di-Ammonium Phosphate (DAP) or NP fertilizers, or ternary, providing all three primary nutrients (NPK). NPK fertilizers are widely used for balanced fertilization and often follow a rating system that describes the content of nitrogen (N), phosphorus (P), and potassium (K) in the fertilizer. For example, 20-20-20 NPK fertilizers are commonly used, with 20% content of N, P, and K each.

3. Micro-nutrient fertilizers provide the essential micronutrients iron, manganese, boron, and zinc, which are crucial for various plant metabolic processes.

Below is a table showing all-India use of fertilisers, with Urea consistently being a leader. The following table shows consumption of fertilisers in India in KT:

Year	UREA	DAP	MOP*	NPKS	SSP
2018-19	31,900	10,100	3,000	9,000	4,500
2019-20	33,700	9,400	2,800	9,600	4,400
2020-21	34,200	9,300	2,500	11,500	4,700
2021-22	34,200	11,900	2,500	11,500	4,700
2022-23	35,700	10,500	1,600	10,100	5,000

Source: Department of Fertilizers

In India, fertilizers are crucial for increasing agricultural productivity. As of FY23, India is the world's second-largest consumer of fertilizers, after China, supporting over 190 Mn hectares of gross cropped area and benefiting 140 Mn farmlands. Despite limited reserves of raw materials for fertilizer production, India ranks as the third-largest global producer, meeting 70-75% of its nutrient demands through domestic production. In FY23, total fertilizer market valued at Rs. 942 Bn is projected to grow at a CAGR of 4.3%, reaching Rs. 1,380 Bn by FY32. The overall dependency on imports is ~30% (FY23), while the dependency for NPK is ~15% (FY24).

Factors influencing the Indian fertilizer market

Supply-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Ammonia	Natural gas	Global market dynamics
2.	Domestic inventory level	Dependence on imports	

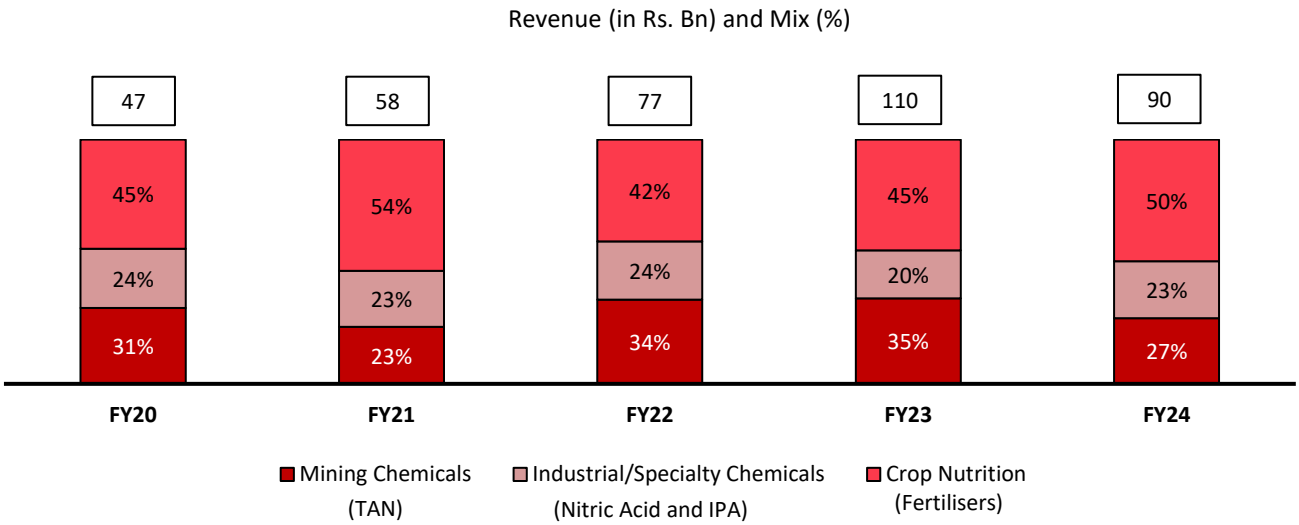
Source: Keynote Capitals Ltd.

Demand-side factors			
Sr. no.	**First-order**	**Second-order**	**Third-order**
1.	Rainfall		
2.	Government subsidy	Usage of urea	
3.	Increase in food production *(and high-value fruits/vegetables)*	Increase in population and income level	Economic growth
3.	Other government policies		

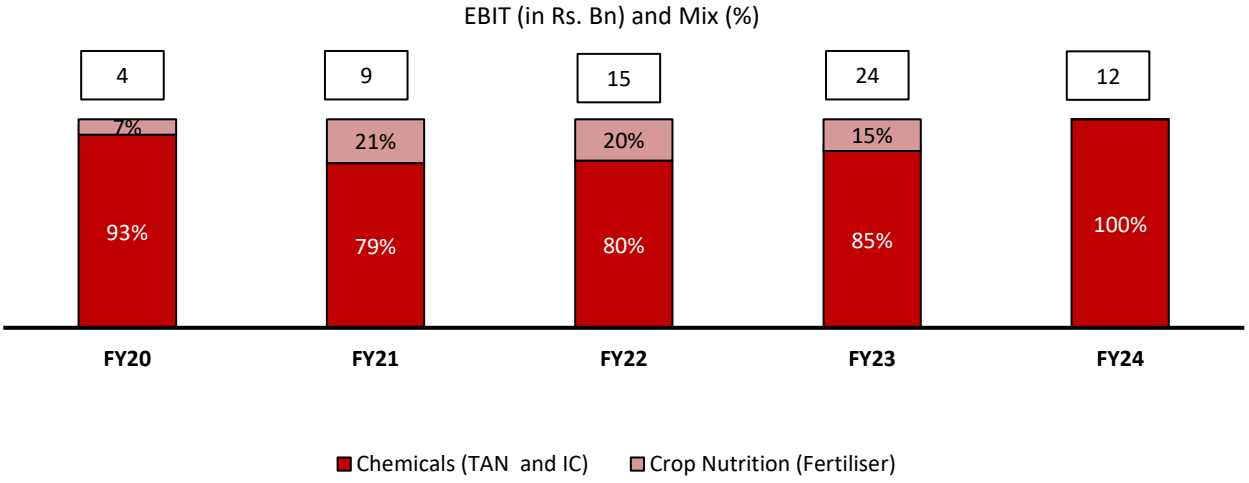
Source: Keynote Capital Ltd.

Business Overview

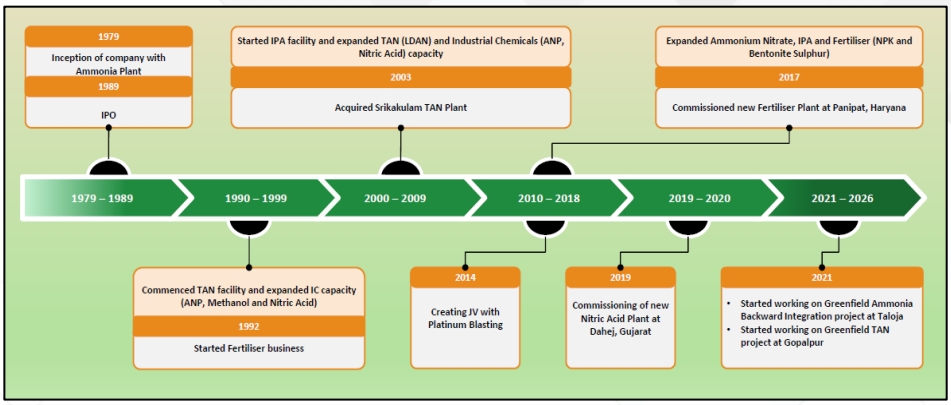
Deepak Fertilisers and Petrochemicals Corporation Limited (DFPCL) was incorporated in 1979 and began commercial production of ammonia in 1983 at its Taloja unit in Maharashtra. Over the years, DFPCL has expanded its portfolio to include a variety of chemicals and fertilizers, such as Dilute Nitric Acid, Concentrated Nitric Acid, Ammonium Nitrate, and Ammonium Nitro Phosphate (ANP) fertilizer, with production starting in 1992. The Company has also diversified into Methanol, Liquid Carbon Dioxide, Isopropyl Alcohol, and Sulphur Bentonite Fertilizer. DFPCL is a leading manufacturer in India, producing high-quality chemicals that meet both domestic and international standards. Its products cater to sectors such as pharmaceuticals, agrochemicals, refining of precious metals, defense, and textiles. The Company is the largest producer of Nitric Acid in Southeast Asia and a market leader in IPA in India. In recent years, DFPCL has continued to innovate and expand, including the commissioning of a 500 KT ammonia plant in FY24 and planning to commission the upcoming capacity of 376 KTPA of TAN and 450 KTPA of Nitric Acid by FY26.



Source: Company, Keynote Capitals Ltd.



Source: Company, Keynote Capitals Ltd.



Source: Company, Keynote Capitals Ltd.

Nitric Acid

The Company is the foremost manufacturer of nitric acid in India, producing three grades: concentrated, diluted, and strong nitric acid. These products are utilized in various industries, including nitro-aromatics, pharmaceuticals, dyes, the steel rolling industry, defence, and explosives.

The evolving portfolio:

Nitric Acid – bulk (various grades) → Industry-specific grades (solar/steel Grade) → Application based industry-specific grades

Source: Company, Keynote Capitals Ltd.

The acids segment is undergoing a shift from a focus on commodity products to a specialty-oriented approach. In the FY23, it successfully introduced Solar Grade Nitric Acid (SGNA), a premium speciality product that garnered positive feedback from solar cell manufacturers, resulting in a significant number of repeat orders. To cater to the increasing demand, the Company is strategically planning to augment the production capacity of SGNA at its Taloja facility in the immediate term.

Additionally, the business aims to cater to other traditional and high-growth industries with innovative speciality products, such as steel-grade nitric acid. In FY23, multi-stage commercial trials for steel-grade nitric acid and pharma-grade Pure DIPE (Di-isopropyl Ether) were completed successfully, with commercial launches planned for FY24.

The strategic shift from commodity to speciality products is yielding positive results in the nitric acid segment. The Company's brownfield facility at Dahej is expected to provide further opportunities for cost-effective capacity enhancements.

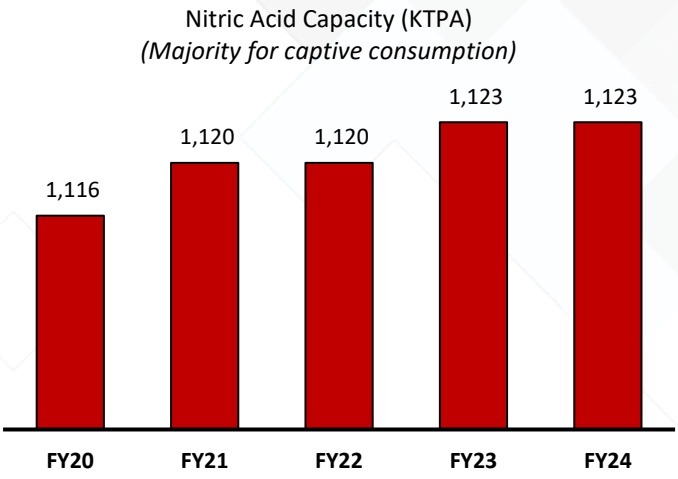
Manufacturing footprint

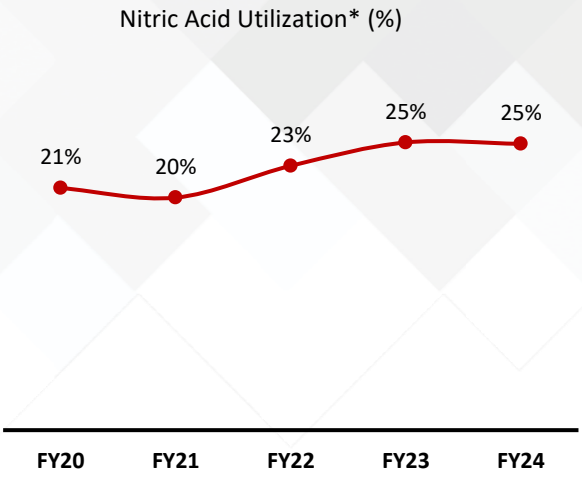
Two of the Company's proprietary products, TAN and ANP fertilizer, account for a significant portion of the nitric acid produced, resulting in considerable captive consumption.

The Company’s capacity for nitric acid has been consistently split between DNA and CNA with ~80% and 20%, respectively.

DFPCL is one of the largest producers and importers of industrial chemicals in India, with Nitric Acid and Solvents being its key flagship products.

Manufacturing footprint



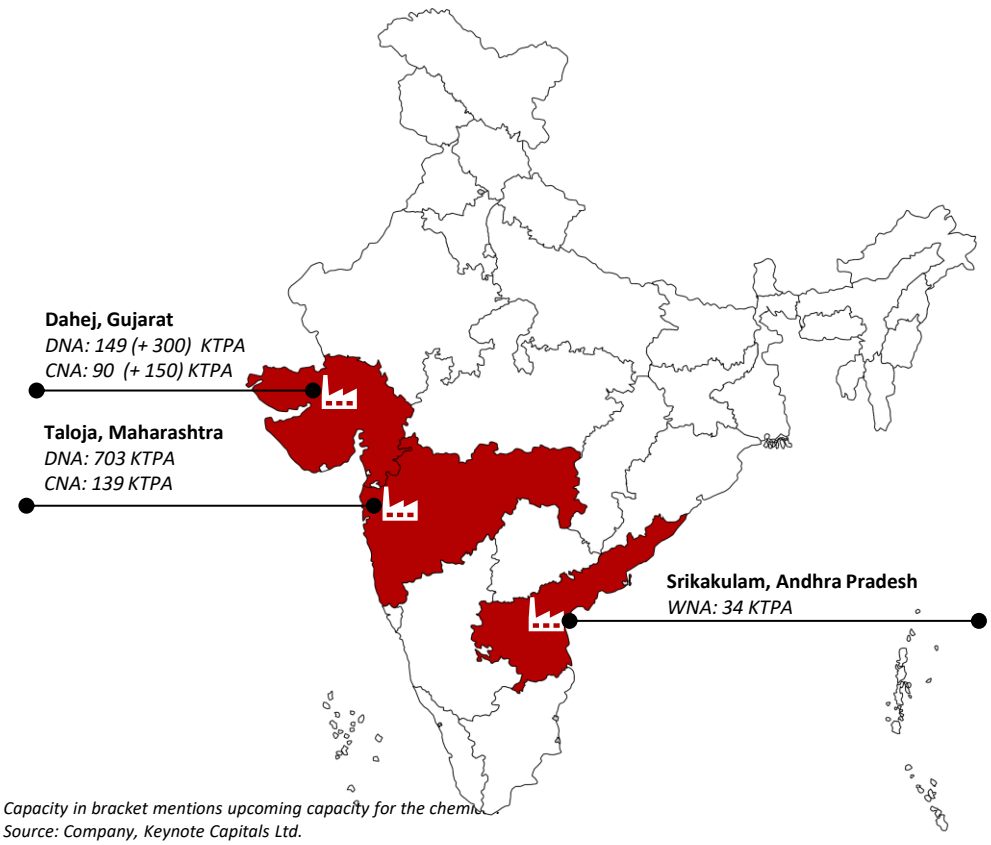


Source: Company, Keynote Capitals Ltd.
** The volume under consideration for Utilization refers to the merchandise business, while the capacity denotes the total installed.*

The Company plans to add ~300 KT of DNA and ~150 KT of CNA by FY26. The project's estimated cost is ~Rs. 20 Bn, which banks have sanctioned for lending purposes.

On a consolidated basis, the Company has guided to reach a peak debt level of ~Rs. 55-60 Bn from the present ~Rs. 42 Bn.

This expansion is part of DFPCL's strategic growth plan to address the increasing demand from downstream sectors such as nitroaromatics, pharmaceuticals, and speciality chemicals. The demand-supply gap for WNA for DFPCL is expected to rise from ~140 KTPA in FY24 to ~330 KTPA by FY30, while the gap for CNA is projected to increase from 85 KTPA in FY24 to ~ 300 KTPA by FY30. Owing to the demand-surplus environment, DFCPL has tied ~65% of its incremental CNA capacity in a 20-year contract.



Capacity in bracket mentions upcoming capacity for the chemi
Source: Company, Keynote Capitals Ltd.

Distribution

~75% of the capacity is present in Gujarat. This location is advantageous due to the proximity to several downstream industries that utilize nitric acid, including nitroaromatics, pharmaceuticals, dyes, steel rolling, defense, and explosives sectors; there, the Company is are looking to invest close to ~Rs. 20 Bn.

Customers

Customer demands have also led DFPCL to import nitric acid to ensure a consistent supply for its clients. Specifically, the Company has predominantly imported WNA rather than CNA due to the logistical challenges and higher costs associated with importing CNA.

CNA is highly corrosive and requires specialized containers and equipment for safe transport. This increases the complexity and cost of logistics, including the need for corrosion-resistant materials and adherence to stringent safety regulations during shipping and storage.
Capitals Ltd.

To meet customer commitments and adapt to market scenarios, DFPCL also imports DNA and converts it to CNA, ensuring that it can fulfil its contractual obligations and maintain production efficiency.

In FY24, due to China dumping, the demand for companies like DFCPL declined, followed by discounted realizations. This impacted revenue and profitability of the Company. However, the Company managed to record a flat volume growth over the previous year.

As a testament to this commitment, DFPCL signed a long-term Nitric Acid supply agreement with Aarti Industries Ltd (AIL), valued at over Rs. 80 Bn (an average of Rs. 4 Bn per year). This binding term sheet, effective from April 1, 2023, spans 20 years and includes specific volume commitments with supply-or-pay and take-or-pay obligations by both parties, ensuring financial security and protecting commercial interests.

Additionally, this agreement reinforces DFPCL's dedication to support its customers and sustaining growth in the speciality chemical sector, positioning the Company for long-term success and stability in a competitive market.

Future Outlook

The prices of Nitric Acid in China had skyrocketed to ~Rs. 25,000 per KT, which was double the long-term average of ~Rs. 12,000 per KT. With China imposing quassi ban on the chemical to improve the domestic prices and availability, the prices have receded to ~Rs. 20,000 per KT recently. Because the prices are yet to approach its long-term average, the supply from China cannot be expected in the near term, whereby providing a favourable outlook for the Indian players.

IPA

DFPCL is the sole manufacturer of Isopropyl Alcohol (IPA) in India. This status is due to the fact that DFPCL is the only Company in India that produces IPA domestically. The Company has an installed capacity of 70 KTPA and uses a direct hydration process to manufacture high-purity IPA, which meets international standards for various applications, including pharmaceuticals and speciality chemicals.

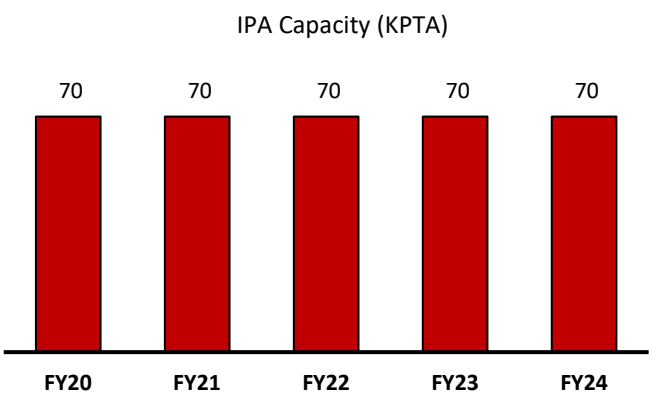
Source: Company, Keynote Capitals Ltd.

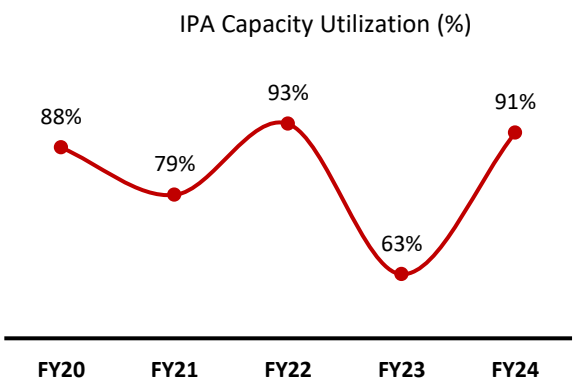
DFPCL has undertaken several strategic initiatives to enhance its product offerings and market position. The Company has increased its focus on producing pharma-grade IPA, demonstrating its commitment to health and safety standards. This product meets stringent international pharmacopoeia standards, making it suitable for critical pharmaceutical applications. Starting with IPA and the other 3 non-IPA solvents (methanol, acetone and MDC), the brand plans to put more pharma-grade solvents under its umbrella in future.

In FY21, DFPCL launched Cororid, an IPA-based brand for hand sanitisers, disinfectants, and wipes. In FY24, DFPCL launched the PUROSOLV brand, consolidating all its pharmacopeia-certified solvents under one umbrella. This brand focuses on high-quality, benzene-free solvents, including IPA, methanol, acetone, and Methylene Dichloride (MDC), with advanced features like QR codes for authenticity and on-demand online authentication checks.

The Company has a strong position in supplying pharmacopeia-certified grade IPA, primarily used in the pharmaceutical industry. Additionally, the Company has consistently sought CDSO approvals to ensure that its chemicals, including IPA, meet stringent quality standards. Low pricing of phenol affects the feasibility of selling IPA at higher prices. This trend is expected to continue over the short term, possibly extending to a couple of years, leading to sustained demand for IPA.

Manufacturing Footprint





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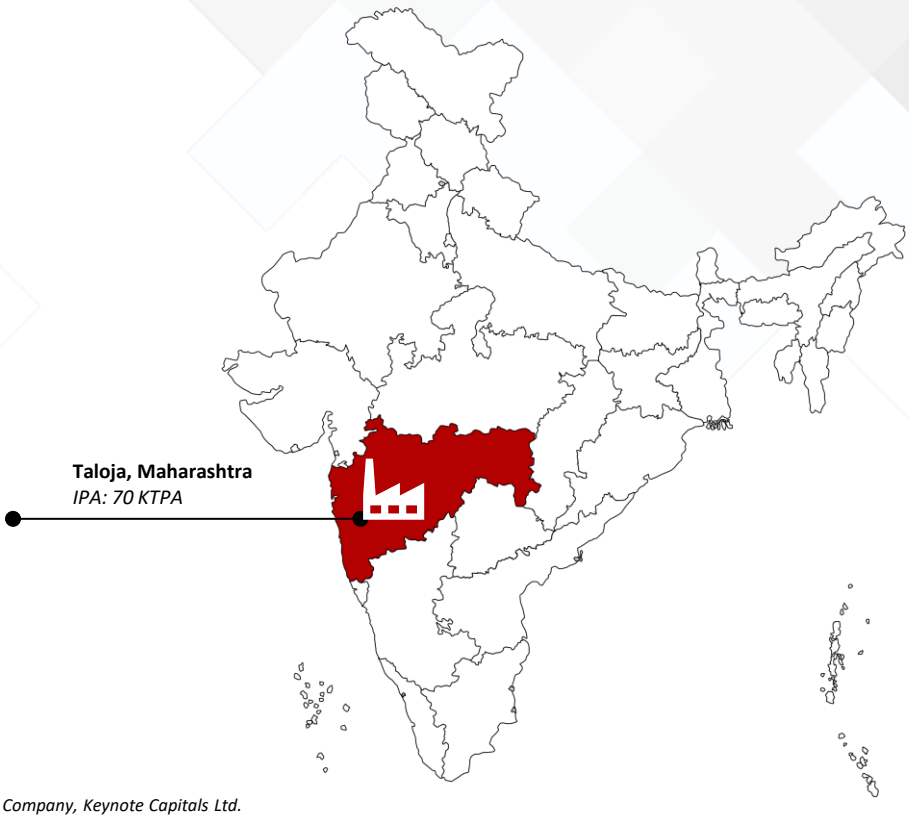


Source: Company, Keynote Capitals Ltd.

Anticipated heightened demand is foreseen across various sectors including the chemical, electronic, solar, automotive, flavor and fragrance, and cosmetics industries. Isopropyl alcohol (IPA) is poised to function as a speciality product within these industries, introducing new avenues of sustained demand.

Distribution

DFPCL's IPA has gained considerable traction in various international markets, including the USA, EU, Africa, the Middle East, and the Far East. Complying with pharmacopoeia standards, our solvents also adhere to other regulatory benchmarks such as OHSAS, FDA, CFDA, HALAL, and KOSHER, securing recognition across the diverse markets of the USA, EU, Africa, Middle East, and Far East.

Customers

To uphold its market leadership and meet the increasing domestic demand, DFPCL also imports and distributes IPA from global suppliers. IPA plays a crucial role in the pharmaceutical sector, serving as a solvent in the production of bulk drugs, intermediates, and formulations. Moreover, it finds application in printing inks, coatings, and the synthesis of derivatives like IPA.

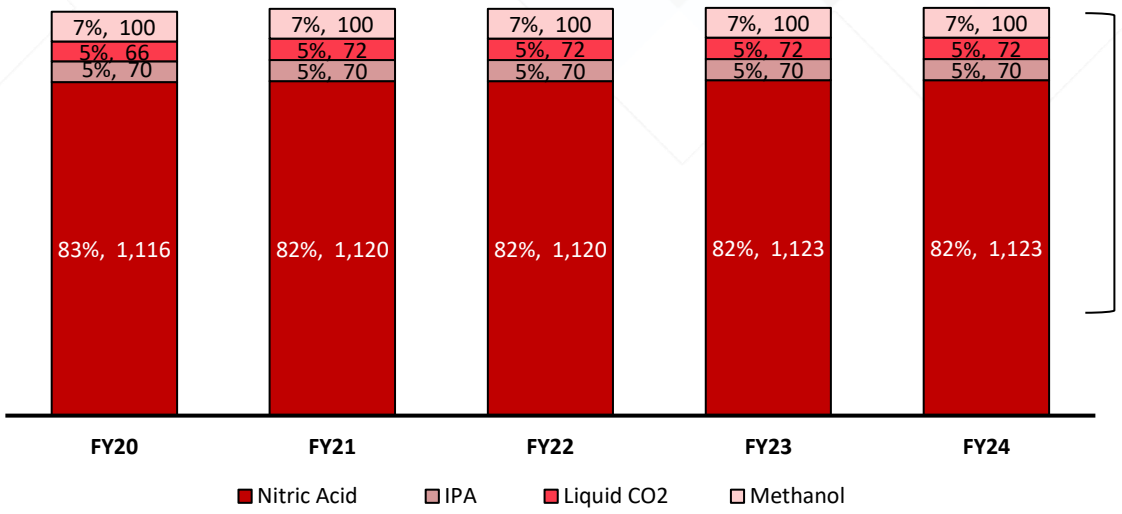
Outlook

The domestic demand for IPA remains strong, driven by its use in various industries, including pharmaceuticals, dyes, and paints. The demand for IPA is expected to maintain healthy growth, supported by the growing end-user industries

Industrial Chemicals (IC)

DFPCL holds leadership positions in the manufacturing of Industrial Chemicals such as Nitric Acid (DNA, CNA, WNA, Solar grade, Steel grade), Iso Propyl Alcohol (IPA - pharma grade, food grade, cosmetic grade, standard grade, etc.), Ammonia, Liquid Carbon Dioxide.

IC Capacity Mix (in % and KTPA)

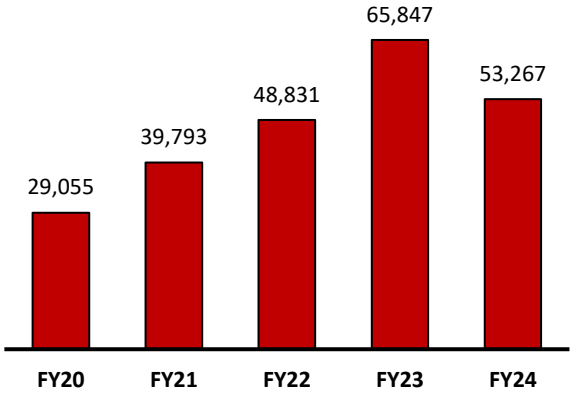


Most of the IC capacity serves as a form of backward integration for internal use.

Source: Company, Keynote Capitals Ltd.

Revenue from IC (Rs. Bn)

Realization per KT (in Rs.)



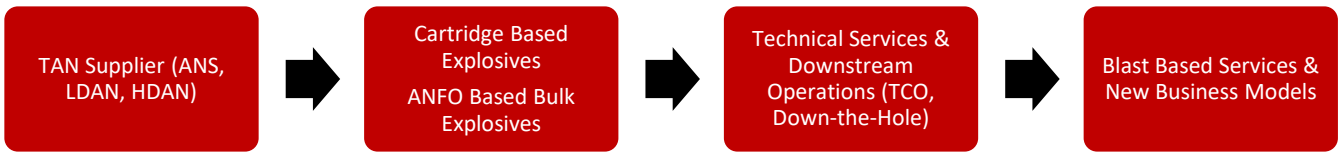
Source: Company, Keynote Capitals Ltd.

Mining Chemicals

Smartchem Technologies Limited (STL), a wholly-owned subsidiary of DFPCL, is one of the world's largest TAN manufacturers, producing High-Density Ammonium Nitrate (HDAN), Low-Density Ammonium Nitrate (LDAN) and Ammonium Nitrate Melt (AN Melt). The Company is the only producer of explosives-grade TAN solids in India & also manufactures Medical-Grade Ammonium Nitrate, which is widely used in the production of medical-grade nitrous oxide for use as an anesthetic/analgesic.

DFPCL's transition in the TAN segment represents a strategic evolution from being a traditional supplier of TAN products to becoming a comprehensive provider of blasting solutions and services. Initially, DFPCL focused on producing various grades of TAN, including Ammonium Nitrate Solution (ANS), LDAN, and HDAN. These products were primarily used in the mining, infrastructure, and construction industries for the production of explosives. Over time, DFPCL expanded its offerings to include cartridge-based explosives and Ammonium Nitrate Fuel Oil (ANFO) bulk explosives, addressing the specific needs of its customers more effectively. This shift allowed the Company to provide more tailored and efficient solutions, enhancing its value proposition in the market. The Company has built on its unique position in the LDAN segment with customer transformation initiatives to drive the market from conventional explosives to ANFO. The introduction of cost-effective and high-performance ANFO explosives as a substitute for conventional emulsion explosives is expected to further support our TAN business.

The transition further includes the implementation of advanced technical services and downstream operations aimed at optimizing blasting efficiency and cost-effectiveness. DFPCL has introduced initiatives such as Total Cost of Ownership (TCO) projects and down-the-hole services, which focus on improving mine and quarry productivity through optimized drilling and blasting techniques. By deploying Bulk Mixing and Delivery (BMD) trucks and planning to integrate advanced technologies like drones and AI-based blast modeling, DFPCL is enhancing its operational capabilities and compliance with regulatory norms. This customer-centric approach has enabled DFPCL to build stronger partnerships with its clients, positioning itself not just as a supplier but as a strategic partner in optimizing their operations. This comprehensive service-oriented model has reinforced DFPCL's competitive position in both the Indian and global markets, driving growth and ensuring long-term sustainability.



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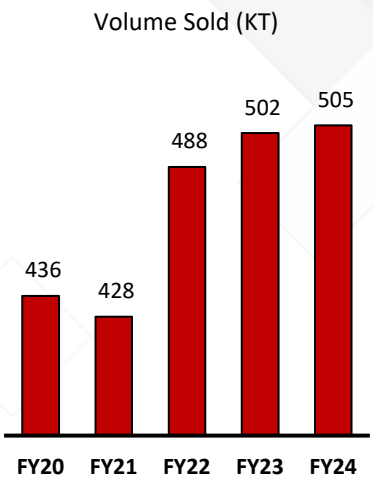
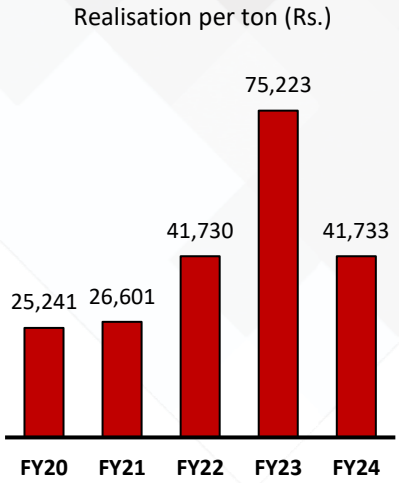
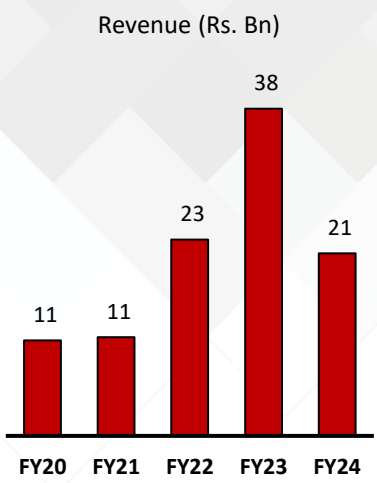






Source: Company, Keynote Capitals Ltd.

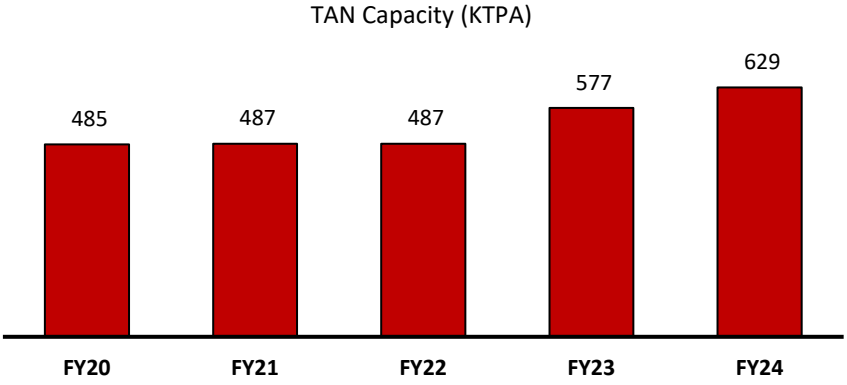
Total Cost of Ownership (TCO) in mining refers to the comprehensive cost of extracting minerals or rocks, encompassing all expenses from initial drilling to final crushing. DFPCL's Mining Solutions business model aims to optimize TCO by improving five key value streams: Drilling, Blasting, Excavation, Transport, and Crushing. Unlike traditional explosives manufacturers who charge for inputs alone, DFPCL guarantees specific outcomes and shares in the resulting benefits with clients. This approach ensures enhanced efficiency and cost-effectiveness in mining and infrastructure projects, setting DFPCL apart in the industry.

Manufacturing Footprint

The Company holds a significant market share of ~44% in the domestic TAN market. The Company aims to become the third-largest TAN manufacturer worldwide within the next five years by increasing its TAN capacity from 629 KTPA.

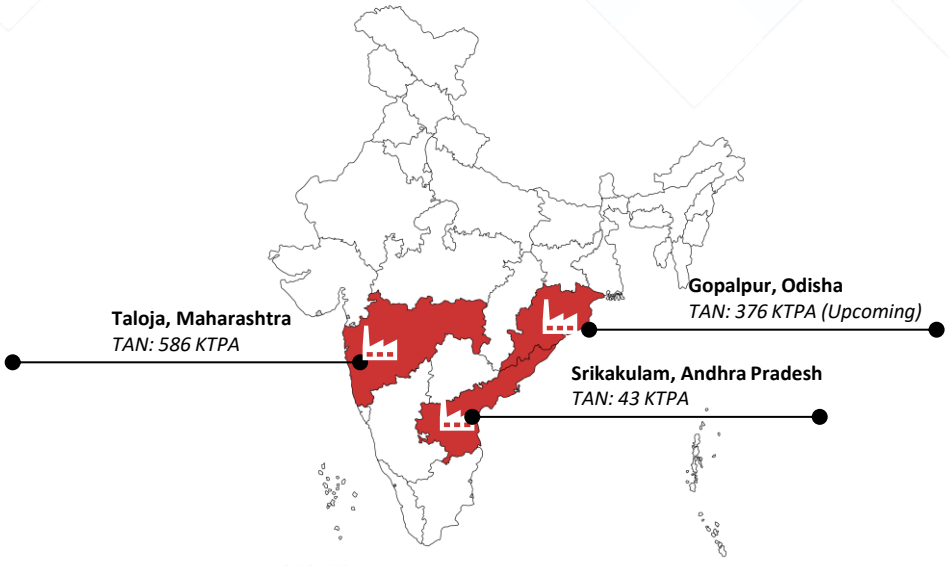
Further, DFPCL is working on a significant Greenfield project in Gopalpur, Odisha, which will enhance its TAN production capacity by 376 KTPA at a project cost of Rs. 22 Bn. This project is expected to increase DFPCL's overall installed capacity to ~1,000 KTPA, meeting about 60% of India's demand for ammonium nitrate, from the current ~44%. This capacity is expected to commission in FY26. The strategic location near major mining hubs and the proximity to Gopalpur port in Odisha will facilitate both domestic distribution and export opportunities.

On a consolidated basis, the Company has guided to reach a peak debt level of ~Rs. 55-60 Bn from the present ~Rs. 42 Bn.



Source: Company, Keynote Capitals Ltd.

A critical aspect of this project is the agreement with Gopalpur port for the import of ammonia, a key raw material for TAN production. This partnership ensures a reliable and efficient supply chain for ammonia, which is essential for the continuous operation of the Gopalpur TAN plant. The proximity of the plant to Gopalpur port not only facilitates the import of ammonia but also positions the Company advantageously for exporting TAN products to international markets, including the Middle East, Africa, and Southeast Asia. The ammonia required for the Gopalpur plant will be imported through the Gopalpur port, while the new ammonia plant at Taloja, Maharashtra, will primarily serve the western facilities of DFPCL.



Source: Company, Keynote Capitals Ltd.

Distribution

The Company predominantly serves the Indian market and also exports to key markets such as the Middle East, Africa, and Southeast Asian countries. DFPCL benefits from the advantageous location of its TAN plants, situated near major mining hubs in East and Central India.

Despite challenges such as the influx of cheaply Fertilizer Grade Ammonium Nitrate (FGAN) from Russia and export bans in FY24, DFPCL showed resilience, with the TAN business achieving its second-highest sales volume of 505 KT in the Company's history, by maintaining flat growth over FY23. However, with improved AN inventory in India, the export ban, resulting from short supplies, was lifted in March 2024. Subsequently, the Company has commenced exporting TAN following the lifting of the export ban in March 2024, starting with an initial quota of 20,000 tons for the year.

In addition to this, the Company is actively collaborating with leading mining educational institutions and research organizations to develop innovative solutions and best practices. The introduction of high-performance ANFO explosives and down-the-hole (DTH) delivery systems are part of this transformative journey. These technologies not only enhance the efficiency of blasting operations but also address environmental concerns by utilizing waste oil from mines, thereby reducing diesel consumption and maximizing rock production.

Customers

The Company's core markets encompass private coal, limestone, and the quarrying/construction industries, primarily utilizing the conventional bulk TAN approach. However, beginning in FY23, the Company has embraced the TCO business model, forging close partnerships with end consumers such as mining companies and infrastructure projects. Together, they work to analyze and optimize operating costs, leveraging technology and specialized explosive products to enhance efficiency and productivity in mining and infrastructure operations. This collaborative approach is designed to create a mutually beneficial scenario, fostering success for all parties involved.

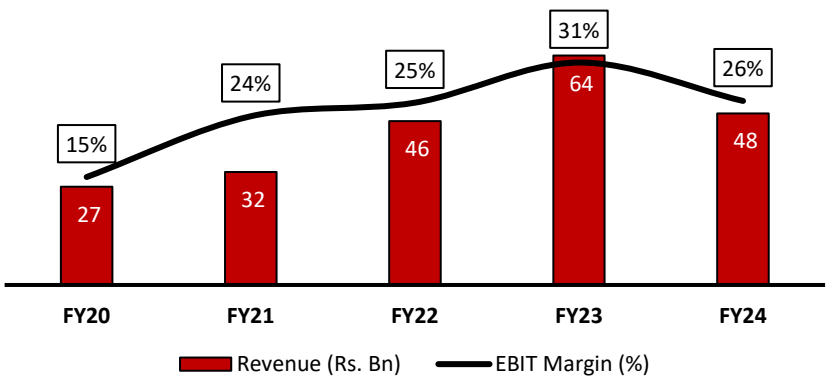
Outlook

The Gopalpur facility is on track to commence production by FY26, representing a significant boost to DFPCL's total TAN capacity, which is poised to reach ~1,000 KTPA. Besides, DFPCL is dedicated to offering comprehensive solutions to its customers through the TCO approach. This involves streamlining the entire value chain of mining operations, encompassing drilling, blasting, excavation, hauling, and crushing. Further, DFPCL has announced a demerger of its TAN business from Smartchem Technologies Limited to Deepak Mining Services Private Limited. This strategic restructuring aims to cultivate specialized leadership and unleash the full potential of the TAN business by facilitating industry-specific strategic and financial investments.

Profitability of the Chemicals Segement – IC and TAN

The contribution of TAN (27% in FY24) in revenue is higher than IC (23% in FY24). The average EBITDA per ton for TAN is ~Rs. 16-18 KPT and that for IC is ~ Rs. 14-16 KPT, implying a similar level of profitability in both the chemical businesses. During FY24, the margins depleted due to Russia dumping FGAN in India, enormously impacting realizations and profitability for the TAN business.

Chemicals Segment Revenue (in Rs. Bn) and EBIT Margin (in %)



Source: Company, Keynote Capitals Ltd.

Fertiliser

DFPCL is one of the leading manufacturers of NPK and speciality fertilisers in India. The Company's Crop Nutrition Business is housed under its 100% subsidiary, Smartchem Technologies Limited (STL). The Company under its flagship brand 'Mahadhan' offers a wide range of NP (Nitro Phosphate), NPK (Nitrogen Phosphorous Potassium) variants, Water Soluble Fertilisers and Bentonite Sulphur to Indian farmers. DFPCL offers a basket of 48 products which include value-added fertilisers, speciality fertilisers, water-soluble fertilisers, micronutrients and secondary nutrients, catering to every farmer's crop nutrient requirement. The Crop Nutrition business has a strong presence in the horticultural belt of India in the states of Maharashtra, Karnataka and Gujarat. In the last few years, DFPCL has been further expanding its geographical reach to the south and north states of India over last few years.

DFPCL has transitioned from commodity fertilizers to differentiated, value-added products. This strategic shift includes

Plain grade fertilisers → High efficiency differerntiated grade fertiliser "Smartek" → Crop Nutrient Solution – "Croptek" Crop specific fertiliser → Crop and stage-specific fertiliser – "Solutek"

Smartek: Enhanced Efficiency NPK fertilizers that improve nutrient bioavailability, root growth, plant height, and yield.

Croptek: Crop-specific nutrient solutions with major, secondary, and micronutrients tailored for crops like onion, cotton, sugarcane, and maize. These products use Nutrient Unlock Technology (NUT) to enhance nutrient uptake and efficiency.

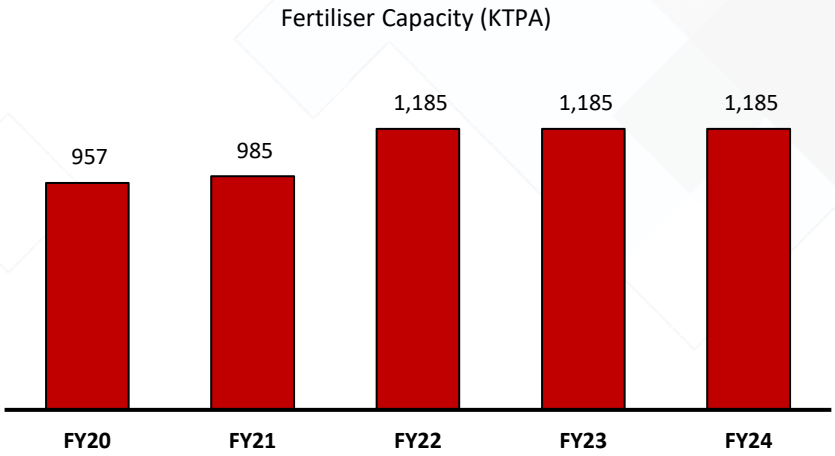
Solutek: Fertiliser for crop-specific and stage-specific requirements (uniformity and colour of fruits) launched for tomatoes, grapes, and pomegranates. It also helps the farmers to reduce number of products to be applied over farmer practice.

Source: Company, Keynote Capitals Ltd.

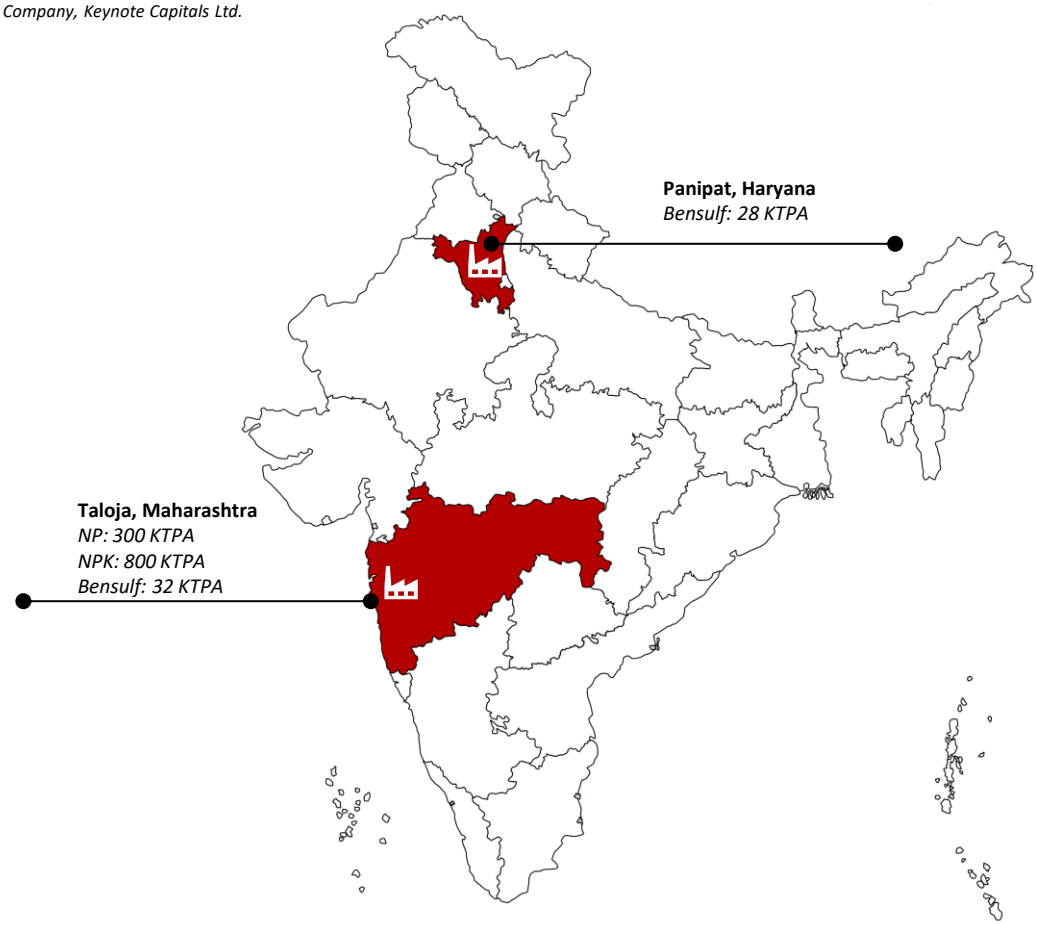
Over the past few years, DFPCL launched many products in these categories - Smartek 14.28.00, Superfast Bensulf, Grape Crop Specific Package (3 Grades), Tomato Crop Specific Package (2 Grades), Croptek Onion, Croptek Sugarcane, Croptek Cotton, Croptek Soyabean, Smartek Paddy, Smartek Pulses, Solutek for grapes, and tomato crops Croptek Cotton (Kharif season), Croptek Maize (Kharif season), Croptek Groundnut, Solutek Pomegranate grades, Solutek Grapes and Tomato grades.

Manufacturing Footprint

DFPCL's manufacturing infrastructure for fertilisers is robust and strategically located to cater to key agricultural regions in India.



Source: Company, Keynote Capitals Ltd.



Source: Company, Keynote Capitals Ltd.

Distribution

The fertilizer segment shifted their Route to Market (RTM) strategy from selling to farmers via distributors to directly selling them from FY20. Additionally, they also transformed from commodity to specialty fertilisers during the year. This involved organizational restructuring, improved manufacturing processes, R&D, revamped distribution channels, and farmer-focused marketing. The subsidiary operates in 12 states with 150 sales and marketing personnel and a network of 3,800+ distributors and 20,000+ retailers. They also started promoting crop-specific fertilizers through events like crop seminars and product demonstrations in the field.

The Company ran targeted campaigns for specific crops in Maharashtra, Karnataka, and Gujarat to increase market share. Paddy was the focus in Tamil Nadu, Andhra Pradesh, and Telangana. The Company is evaluating the benefits of Marginal Cost-Benefit Ratio (MCBR) trials for future value-based pricing.

In 2021, the Company partnered with Samunnati to provide crop-based advisory services and affordable loans to farmers through Farmer Producer Organizations (FPOs). This aimed to support FPO farmers in improving their crop yields and earnings across four states. As per the MoU, FPOs will have access to advisory services, agricultural inputs through DFPCL, and finance options through Samunnati. By FY23, the fertilizer business transitioned from commodity NPK to the Smartek product, which enhances nutrient use efficiency and is currently moving towards Croptek, a more crop-specific grain. These efforts at the farmer level were recognized by the Asian Development Bank, which has introduced a unique Blue Loan program, providing not only debt funding but also certain grants for farmer-level initiatives, marking the first of its kind in the country.

Customers

A strong retreating monsoon and higher water levels led to a demand recovery in the second half of the year. Even as the overall market remained subdued, the Company remained focused on demand generation. It embarked on crop-specific market development campaigns including promotional activities, crop seminars, farmer meetings and product demonstrations across farmer fields. The Company focused on various sales and distribution efficiency improvement areas, including sales team automation and the development of alternative vendors for key raw materials.

A team of highly qualified and experienced agriculture scientists work on developing different technologies through in-house and third-party collaborations to deliver value products. CNB's "Go To Market" strategy is based on the 'seeing is believing' approach, wherein the pull team engages with farmers in the potential market through various on the ground activities to conduct product or portfolio demos. Farmers are then acquainted with product value proposition on multiple crops across geographies.

Outlook

The Company has partnered with Haifa Group, a global leader in specialty fertilizers, to promote high-performance fertilisers in India. Furthermore, the forecast of a good monsoon by the India Meteorological Department (IMD) is likely to support growth in the crop nutrition business.

Profitability of the Fertiliser segment

The fertilizer segment's profitability and realizations have been influenced by various factors over the years. In FY19, severe drought conditions in Maharashtra led to high inventory levels and a decline in NPK sales volumes, although the introduction of differentiated products like Smartek helped mitigate some losses. By FY20, improved market conditions, favorable monsoons, and strategic cost optimization initiatives led to a significant turnaround, with margins improving from negative (-2%) to positive (2%).

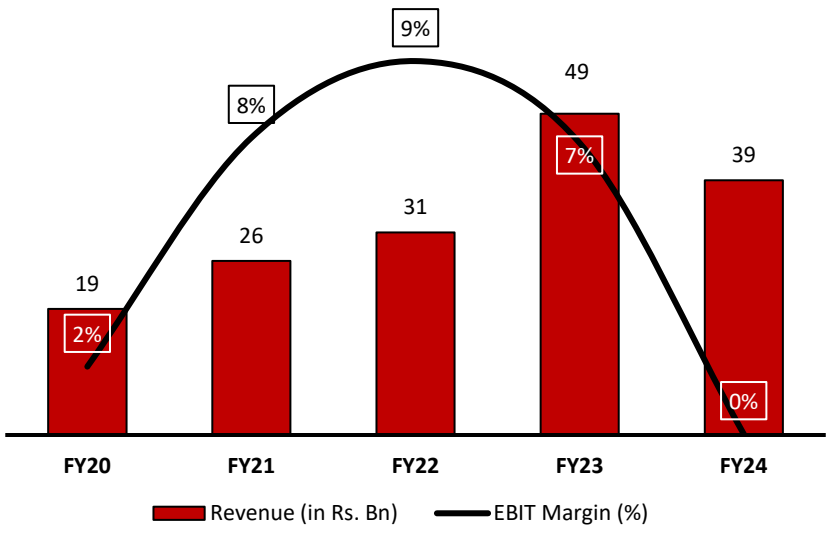
The following year, FY21 presented challenges due to rising raw material prices, but government subsidies helped stabilize margins, and the Company's strategic shift to differentiated products resulted in substantial volume growth. This year the NPK volume transitioned to differentiated products, recording a growth of ~198% on a YoY basis. This also showed in margin, with an improvement of ~6%.

However, in FY22, geopolitical tensions, particularly the Russia-Ukraine conflict, caused raw material shortages and price hikes, impacting production volumes, though government subsidy enhancements provided some relief.

FY23 was marked by erratic weather patterns affecting crop yields, but specialty products like Croptek and Smartek experienced growth. A reduction in government subsidies led to financial impacts, affecting margins.

Entering FY24, the backward-looking subsidy policy posed challenges, with subsidies based on past prices affecting profitability when global prices fluctuated.

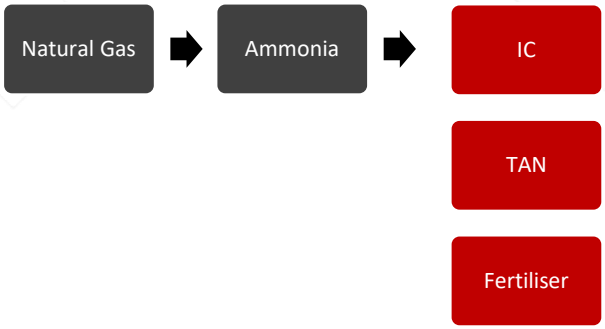
Fertiliser Segment Revenue (in Rs. Bn) and EBIT Margin (%)



Source: Company, Keynote Capitals Ltd.

Backward Integration

The Company had an existing ammonia production capacity of 128 KTPA. Historically, ammonia was purchased at an average price of $370 to $390 per ton (FOB Middle East), with a landed cost of ~ $450 to $480 per ton including logistics. To mitigate the high costs and supply chain risks associated with external procurement, the Company embarked on a backward integration project to produce ammonia in-house.



Source: Company, Keynote Capitals Ltd.

The new ammonia plant, commissioned in FY24, has a production capacity of 500 KT. The total capital expenditure for this project is Rs. 44 Bn.

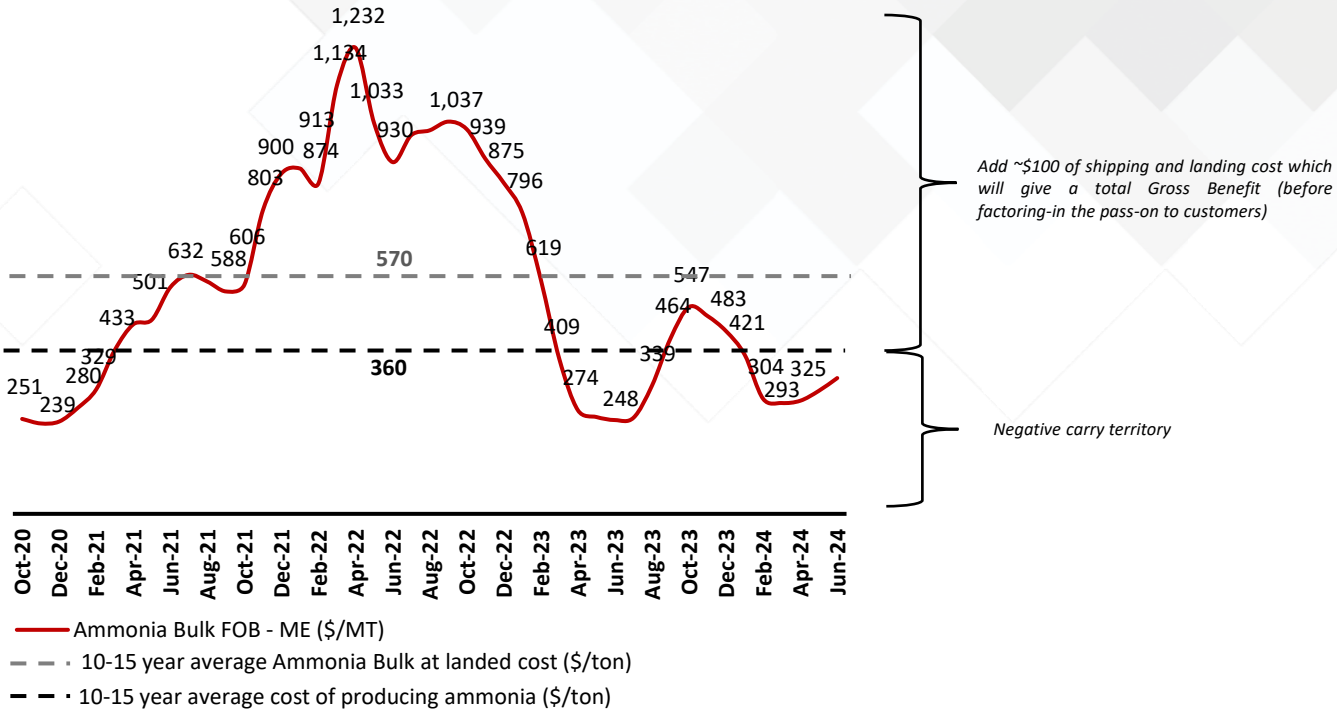
Toyo India served as the Engineering, Procurement, and Construction (EPC) partner for the project, while Icons took on the role of Project Management Consultant (PMC). The plant's Performance Guarantee Test was successfully completed in January 2024, following its commissioning. Since that time, the facility has been operating at its full design capacity without any issues.

Backward integration offers several economic and financial benefits. Firstly, it significantly reduces raw material costs, with in-house production expected to lower the cost of ammonia to $260 to $280 per ton. Additionally, logistics savings are anticipated to be $70 to $80 per ton due to the plant's proximity to downstream facilities. The exothermic nature of ammonia production generates additional heat, which can be utilized in downstream processes, resulting in further savings of $10 to $15 per ton. These cost reductions are expected to improve EBITDA margins to $160 to $200 per ton. The project also mitigates supply chain risks by reducing dependency on external suppliers and import logistics. This stability is crucial given the volatility in global ammonia prices and supply chain disruptions. The state government of Maharashtra has granted the project ultra-mega project status, providing fiscal benefits such as state GST reimbursements of 9%, which will cover 100% of the capex over time.

The majority of the ammonia produced (~70%+) will be used internally for the Company's downstream products, ensuring no offtake risk. Any surplus ammonia can be sold in the domestic market, as India is a significant importer of ammonia.

The vertical integration strengthens the Company's control over its supply chain, ensuring a steady supply of ammonia for its downstream products, including fertilizers, industrial chemicals, and mining chemicals.

Cost of production vs purchase of ammonia (in USD)



FOB pricing means that the cost includes delivery to the ship but not the shipping cost itself
Source: Company, Keynote Capitals Ltd.

Long-term average cost of importing ammonia		Long-term average cost of producing ammonia	
Cost item	**USD/ton**	**Cost item**	**USD/ton**
Average FOB Middle East for ammonia	420-430	Gas cost ($8.5-10/MMBTU)	280-330 *(33 BTU of gas required per ton of ammonia)*
Freight, customs, etc	80-100	-	-
Other costs	65-70	Other costs	25-30
Estimated average cost	565-570	Estimated average cost	305-360
Long-term average spread		**$210-260 per ton (or ~Rs. 17,000-22,000 per ton)**	

Source: Company, Keynote Capitals Ltd.

The biggest reason to integrate backwards with ammonia was to migrate and mitigate from a high-volatility commodity – ammonia, to a low-volatility-commodity – natural gas. The volatility in ammonia is infused by demand growing at a higher rate (~2% p.a.) compared to supply (~1% p.a.). Amidst such an environment, integrating backwards shall provide risk mitigation to DFPCL. However, increase in natural gas prices can increase the cost of production, thereby reducing the spread. In the period between June-Oct'23, when the pirces hovered around long term average, the Company's spread was ~$75-100. Besides, a slowdown in end-consumer market like TAN, can also lead to passing on of greater benefit, eroding the benefits gained from producing ammonia internally. Therefore, the two critical factors – international prices of ammonia, natural gas prices and TAN prices shall collectively determine the net benefit of cost savings from ammonia plant. As of June'24, the prices of ammonia have been depressed, but from the perspective of merchandise capacity, the Company sold on premium over the import parity prices. However, the sales from ammonia is anticipated to not contribute meaningfully to the Company's profitability.

To minimize the risks associated with price volatility, DFPCL has entered into a significant long-term agreement with Norway's Equinor for the supply of Liquefied Natural Gas (LNG). This agreement will secure an annual supply of ~0.65 Mn tonnes of LNG for 15 years, starting from 2026. This contract is one of the largest signed by Equinor with a private sector Company in India, marking a strategic milestone for DFPCL.

The long-term LNG contract with Equinor is expected to bring several economic benefits to DFPCL. By securing a steady supply of LNG, DFPCL can stabilize its raw material costs, which is crucial to producing ammonia. Historically, the cost of purchasing ammonia has been volatile and higher due to market fluctuations and logistics costs. The agreement allows DFPCL to produce ammonia at a lower cost compared to buying it externally, significantly improving EBITDA margins. Additionally, the long-term nature of the contract ensures a reliable supply of LNG, reducing the risks associated with supply chain disruptions and price volatility.

Until the contract with Equinor, DFPCL has signed medium-term contracts with reliable suppliers like Gas Authority of India Limited (GAIL), Indraprastha Gas Limited (IGL), and Gujarat State Petroleum Corporation (GSPC) .

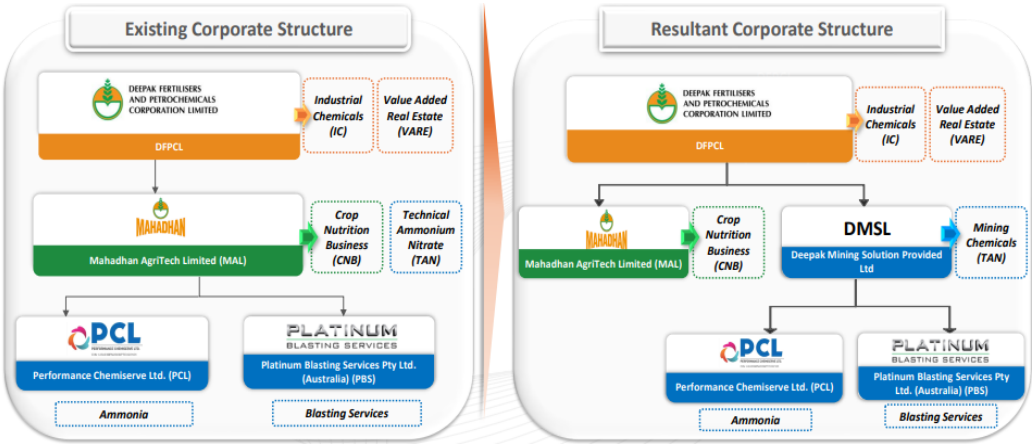
Regarding the pricing mechanism, the agreement is based on a formula-based pricing model rather than spot market prices. The pricing of the LNG under the Equinor agreement will be based on a combination of benchmarks, including Brent, Henry Hub, and Japan Korea Marker (JKM) prices which might include oil prices (such as Brent crude) or other natural gas indices.

In 2014, the Ministry of Petroleum and Natural Gas (MoPNG) issued a directive to halt the supply of APM (Administered Pricing Mechanism), Non-APM, PMT (Panna-Mukta-Tapti), and KG D-6 gas to DFPCL. This decision aimed to redirect the gas to urea manufacturers, thereby significantly reducing the government's subsidy burden. As a result, GAIL and Reliance Industries Limited (RIL) stopped supplying gas to DFPCL starting May 15, 2014.

Demerger

On December 15, 2022, the Board of Directors of Smartchem Technologies Limited (STL), a wholly-owned subsidiary of DFPCL, authorized a Corporate Restructuring Plan. This plan involves the separation of the TAN business from STL to Deepak Mining Services Private Limited (DMSPL), another wholly-owned subsidiary of DFPCL.

NCLT approved the demerger on July 6, 2024. Following the demerger, DFPCL will remain a listed holding Company of its two unlisted subsidiaries – STL and DMSPL. The demerger is intended to enhance leadership focus, elevate customer experience, and facilitate targeted strategic and financial investments in specific sectors.



Source: Company, Keynote Capitals Ltd.

Management Analysis of DFPCL

The Management team of DFPCL comprises of industry veterans who bring immense expertise and relevant experience of working with large entities.

Name	Designation	Previous Experience	Experience with DFPCL (Yrs.)
S.C. Mehta	Chairman and Managing Director	-	30+
Deepak Rastogi	President and CFO	Tata AutoComp Systems Ltd	2+
Naresh Deshmukh	COO	-	35+
Tarun Sinha	President, TAN	President at BlueScope, Multiple roles at Orica, Country Manager at CCM Chemicals	4+

Source: Company, Keynote Capitals Ltd.

Promoter Holding and Management Compensation

Particulars	FY20	FY21	FY22	FY23	FY24
% Promoter Holding (~)	52%	56%	48%	45%	46%
MD's salary (Rs Mn)	39	132	55	70	333
As a % of PAT (~)	4.38%	3.25%	0.80%	0.57%	7.0%

Source: Company, Keynote Capitals Ltd.

Top Shareholders with more than 3% stake (%)

Stakeholders	FY20	FY21	FY22	FY23	FY24
Small Cap World, Inc			3.76	4.94	-
International Finance Corporation				3.86	3.86

Source: Company, Keynote Capitals Ltd.

Peer Analysis

For peer comparision, we have taken Rashtriya Chemicals and Fertilisers Ltd. (RCFL) and Gujarat Narmada Valley Fertilisers & Chemicals Ltd. (GNFC) and Coromandel International Ltd.

TAN & IC			
	DFPCL	**RCFL**	**GNFC**
Metrics			
Products	TAN/NA/IPA	AN Melt/NA	AN Melt/NA
Revenue for FY24 (in Rs. Bn)	39	13	-
Contribution in revenue (%)	55%	10%	60%
EBIT Margin (%)	26%	13%	9%
Capacity (KT)	629/1,123/70	190	170/514
Upcoming capacity	376/450/0	155/0	-
Backward integrated capacity (in KTPA)	629 (Ammonia)	115 + 50 (Upcoming)	0/200
Volume (in KT)	505/278/63	176	NA
Valuation (EV/EBITDA)	11	21	8

Fertiliser			
	DFPCL	**RCFL**	**Coromandel**
Metrics			
Products	NP/NPK/Bensulf	Urea/Complex Fertilisers/etc	NPK/DAP/SSP/etc
Revenue for FY24 (in Rs. Bn)	39	11	197
Contribution in revenue (%)	44%	65%	90%
EBIT Margin in FY24 (%)	0%	0.6%	11%
Capacity (MTPA)	1,160	572	4,600
Upcoming capacity	-	438	-
Backward integrated	629 (Ammonia)	-	602 (Sulphuric acid)
Volume (KT)	598	638	5,390
Valuation (EV/EBITDA)	11	21	21

Source: Company, RCFL, GNFC, Coromandel, Keynote Capitals Ltd.

Opportunities

Changes in TAN – the expansion and transition

Capacity expansion: The Company is significantly expanding its TAN's production capacity to meet the increasing demand from the mining and infrastructure sectors. A new TAN manufacturing plant in Gopalpur, Odisha, with a capacity of 376 KT, is set to become operational by FY26. This project, with an investment of Rs. 22 Bn, will boost the Company's total capacity from 629 KTPA to 1,000 KTPA, enabling it to cater to about 60% of India's TAN demand.

The Company is expanding its TAN capacity to meet the anticipated growth in demand from its customers, particularly in the mining and infrastructure sectors. The demand for TAN is expected to grow significantly, driven by increased activities in coal mining, limestone extraction, and infrastructure projects. Specifically, the demand for coal mining is projected to grow by 10-12% annually, which directly correlates with the need for TAN, as it is a critical component in explosives used for mining operations.

Geographic expansion: Further, the lifting of the export ban on TAN by the Government of India opens up significant opportunities for international market penetration, with a permission to export upto 20 KTPA. The Company has a strong presence in key export markets such as the Middle East, Africa, and Southeast Asia. The strategic location of the new Gopalpur plant near the Gopalpur port will also facilitate easy access to overseas markets, enhancing the Company's global reach. This export potential is expected to drive revenue growth and strengthen the Company's position as a leading global player in the TAN segment.

Transition into solution-driven model: The TAN segment is transitioning from a commodity-focused business to a solutions-oriented approach. The Company is focusing on delivering cost-effective and productive blasting solutions through customized products and services. This includes the deployment of advanced technologies such as drones, AI-based blast modeling, and Bulk Mixing and Delivery BMD trucks. These initiatives aim to improve mine productivity and reduce the total cost of ownership for customers by optimizing drilling, blasting, excavation, transport, and crushing processes.

The Company's focus on technological advancements, strategic collaborations, and market expansion positions it well to capitalize on the growing demand from the mining and infrastructure sectors. The TAN business unit is executing several TCO projects aimed at improving productivity across infrastructure, non-coal mining, and coal mining segments. These initiatives are expected to drive long-term growth and establish the Company as a leading provider of mining solutions.

The new solutions-driven business model has better margins compared to the conventional product-driven business. The business model operates through a structured process involving baselining, pilot blasts, analysis, and proposal stages. Initially, the Company conducts a baseline assessment of the customer's current operational costs, including raw materials and other relevant factors.

This is followed by pilot blasts using the Company's designs, software, and technologies to test various approaches. The analysis phase identifies which of the five value streams—Drilling, Blasting, Excavation, Transport, and Crushing—can be impacted the most. Based on this analysis, the Company creates a comprehensive proposal outlining how it can improve the cost of extraction and overall efficiency. This approach is supported by highly skilled personnel who understand the specific needs of clients.

Advanced tools and software, including drones and AI-based blast modeling, are integrated into the solutions and billed based on their usage and impact on productivity. A unique aspect of this model is outcome-based contracts, where a portion of the revenue is tied to achieving specific performance metrics like cost savings and productivity improvements. This ensures that the Company shares in the financial benefits realized by the customer through the TCO model.

Capacity expansion of nitric acid

As the largest producer of nitric acid in India and a leading manufacturer of IPA, DFPCL's expansion efforts are poised to enhance its market position, operational efficiency, and profitability.

The expansion of nitric acid capacity is particularly timely given the rising demand in various sectors such as fertilizers, pharmaceuticals, nitro aromatics, dyes, steel rolling, and defense. The shift of global specialty chemical intermediates value chains from China to India further boosts the demand and prices of nitric acid in India, positioning DFPCL to capitalize on this trend. The Company's strategic location in the heart of the Nitroaromatics market in Gujarat, coupled with its ability to supply from multiple facilities, ensures a robust supply chain and competitive advantage. The development of new grades of nitric acid, including solar and steel grades, aligns with market needs and opens up new revenue streams. The Company's commitment to innovation and customer-specific formulations enhances its value proposition and market differentiation.

Backward integration into ammonia

DFPCL has embarked on a significant backward integration project with the establishment of its ammonia plant. This strategic move is aimed at ensuring a consistent supply of ammonia, a critical raw material for the Company's various product lines, including industrial chemicals, fertilizers, and mining chemicals. The ammonia plant, with additional capacity of 500 KTPA, is expected to bring several benefits to DFPCL, enhancing its operational efficiency and financial stability.

Previously, DFPCL relied heavily on external suppliers for ammonia, which exposed the Company to the volatility of global ammonia prices and logistical challenges. The cost of purchasing ammonia from the Middle East, including transportation and other associated costs, ranged between $450 to $480 per MT, with historical prices fluctuating from $370 to $390 (FOB Middle East), plus an additional $80 to $90 for landing at the plant. This dependency not only impacted the Company's margins but also posed risks related to supply chain disruptions and price volatility.

The backward integration of the ammonia plant is expected to mitigate these risks by providing a stable, in-house supply of ammonia. This move will reduce the Company's reliance on imports and third-party suppliers, thereby ensuring greater control over the supply chain and reducing the impact of price volatility. The cost of producing ammonia in-house is estimated to be significantly lower, with production costs ~$260-280 per ton, considering gas costs and conversion expenses. This translates to an EBITDA margin of ~$160-200 per MT, which is a substantial improvement over the margins when purchasing ammonia externally.

By producing ammonia internally, DFPCL can achieve greater margin stability as it will be less affected by the fluctuations in global ammonia prices. This stability is crucial for long-term financial planning and profitability.

The transition from commodity to specialty products is a key strategic initiative.

Challenges

The fertiliser segment's reliance on subsidy

Subsidies play a crucial role in the economics of DFPCL's fertilizer segment by making fertilizers affordable for farmers, stabilizing market prices, and supporting the Company's revenue. However, the dependency on government subsidies also introduces vulnerabilities, especially when there are delays or reductions in subsidy rates.

DFPCL has experienced several instances where subsidies have impacted its operations and financial performance. Below are detailed instances when DFPCL struggled due to subsidies:

1. Subsidy Rate Reduction Impact (FY24):

In FY24, DFPCL faced a significant impact due to the reduction in subsidy rates. The Company had to take a hit of ~ Rs. 2.67 Bn due to the reduction in subsidy rates, which affected its financial performance. This reduction was primarily due to changes in government policies regarding subsidy disbursement and rates. Adjusting this one-time effect, the operating margin for the year would have been ~18%, compared to the registered ~15%.

2. Inventory and Subsidy Rate Mismatch (FY24):

The government's policy on fertilizer subsidies is based on historical pricing, specifically using the prices from the previous six months to determine the new subsidy rates. Subsidies are provided biannually and are based on the actual quantities purchased by farmers, tracked through a Point of Sale (POS) system. This approach affects inventory management for dealers and the industry. When global raw material prices decrease, the industry benefits from unsold inventory held by dealers, as the cost of these inventories is lower than the new subsidy rates. Conversely, when global prices increase, the industry incurs losses on this inventory because the cost of raw materials rises, but the subsidy is based on older, lower prices. During FY24, the Company experienced a financial impact of ~Rs. 1.06 Bn due to the subsidy policy and fluctuation in global raw material prices. Reversing this loss of subsidy due to the timing mismatch, would have increased the by another 100 bps.

3. Impact of Erratic Monsoon and Subsidy Micromanagement (FY23):

The crop nutrition business of DFPCL was adversely affected by erratic monsoon patterns and a drought-like situation in some operating states. Additionally, the government's micromanagement of product prices and subsidies, focusing on short-term orientation, further strained the Company's operations. These factors collectively led to lower utilization levels and impacted the overall performance of the fertilizer segment.

4. High raw material costs and delayed subsidy adjustments (FY22):

In FY22, DFPCL struggled with the steep increase in raw material prices, such as ammonia and phosphoric acid, which significantly raised the production costs of fertilizers. The war situation in Russia and Ukraine further exacerbated the raw material shortages and price hikes. The Company awaited appropriate subsidy enhancements from the Government of India (GOI) to balance these increased costs, indicating a delay in subsidy adjustments that impacted their margins and production volumes.

Commodity businesses are under the influence of myriad factors, and being a market leader doesn't help a lot

DFPCL is a prominent player in the industrial chemicals, mining chemicals, and fertilizers sectors. Despite its market leadership in several segments, DFPCL's business model is heavily influenced by external factors, making it vulnerable to market dynamics, regulatory changes, and geopolitical issues. This argument critically examines the challenges faced by DFPCL in its commodity business, highlighting that being a market leader does not necessarily insulate the Company from these myriad factors.

1. Vulnerability to Market Dynamics

Price Volatility: DFPCL's profitability is significantly affected by the volatility in the prices of raw materials and finished goods. For instance, the prices of ammonia and other inputs have fluctuated sharply, impacting the cost structure and margins of the Company's products.

Impact of Dumping: The Company faces intense competition from international players, particularly from China, which has been dumping cheaper products like nitric acid and isopropyl alcohol (IPA) into the Indian market. This has led to significant price undercutting, eroding DFPCL's market share and squeezing its profit margins. Despite being a market leader, DFPCL has struggled to maintain its competitiveness against these low-cost imports.

However, moving form a high-volatility commodity – ammonia, to a low-volatility – natural gas, is expected to mitigate the volatility to a considerable extent.

2. Regulatory and Geopolitical Challenges

Dependency on Government Policies: DFPCL's business is heavily influenced by government policies and regulations. For example, the imposition or lifting of anti-dumping duties can have a significant impact on the Company's competitive position. Any changes in subsidy policies or regulatory frameworks can lead to financial uncertainty and operational disruptions.

Geopolitical Risks: The Company's reliance on imported raw materials exposes it to geopolitical risks. For instance, tensions in the Middle East or trade wars can disrupt supply chains and lead to raw material shortages or price hikes. Such geopolitical factors are beyond the Company's control but can have a profound impact on its operations and profitability.

Demand slowdown may lead to negative operating and financial leverage

The Company was experiencing supply-deficit environment for TAN as the Taloja plant was operating at full capacity and still not able to meet its demand. Resultantly, the Company laid out a plan for a greenfield expansion of 376 KTPA at Gopalpur in Odisha. This project has anticipated cost of ~Rs. 200 Bn. Besides, Nitric Acid capacity is also expanding at Dahej plant in Gujarat by 450 KTPA, incurring a similar cost. Both the projects shall be funded by a mix of equity and debt, taking the gross debt level from ~Rs. 42 Bn in FY24 to ~Rs. 55-60 Bn in the near term.

While the incremental supply is anticipated to be consumed due to reasons like demand-surplus environment and import cuts by Russia (for TAN) and China (for Nitric Acid), the additional capacity is expected to be profitably utilised. However, a slow down in economy or investments by infrastructure companies shall reduce demand for the Company's chemicals, resulting in negative operating leverage. It can also magnify the impact at bottom line due to increase in interest cost. Subsequently, the payback period for the projects shall also be prolonged.

Financial Statement Analysis DFPCL

Income Statement

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
Net Sales	**1,13,007**	**86,761**	**1,00,383**	**1,18,893**	**1,49,725**
Growth %	47%	-23%	16%	18%	26%
Raw Material Expenses	76,692	58,981	65,751	77,280	96,573
Employee Expenses	5,944	5,265	5,521	6,539	8,235
Other Expenses	8,716	9,647	11,042	12,781	15,347
EBITDA	**21,654**	**12,867**	**18,069**	**22,292**	**29,571**
Growth %	60%	-41%	40%	23%	33%
Margin%	19%	15%	18%	19%	20%
Depreciation	2,392	3,337	4,958	5,888	6,353
EBIT	**19,262**	**9,530**	**13,111**	**16,404**	**23,217**
Growth %	71%	-51%	38%	25%	42%
Margin%	17%	11%	13%	14%	16%
Interest Paid	1,947	4,038	4,409	4,782	4,483
Other Income & exceptional	840	1,228	500	500	500
PBT	**18,155**	**6,720**	**9,202**	**12,122**	**19,234**
Tax	5,946	2,147	1,610	2,121	3,366
PAT	**12,209**	**4,572**	**7,591**	**10,000**	**15,868**
Others (Minorities, Associates)	-108	-147	-150	-150	-150
Net Profit	**12,101**	**4,425**	**7,441**	**9,850**	**15,718**
Growth %	74%	-63%	68%	32%	60%
Shares (Mn)	126.2	126.0	126.0	126.0	126.0
EPS	**95.86**	**35.12**	**59.06**	**78.18**	**124.75**

Balance Sheet

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
Cash, Cash equivalents & Bank	4,987	3,609	13,890	11,199	28,025
Current Investments	5,971	2,583	2,583	2,583	2,583
Debtors	16,905	14,758	15,058	17,834	22,459
Inventory	12,589	11,924	13,797	16,341	20,578
Short Term Loans & Advances	2,084	11	11	11	11
Other Current Assets	1,304	8,694	8,694	8,694	8,694
Total Current Assets	43,841	41,578	54,031	56,661	82,349
Net Block & CWIP	62,048	63,445	73,487	82,598	76,245
Long Term Investments	25	25	25	25	25
Other Non-current Assets	8,299	13,255	13,055	12,855	12,655
Total Assets	**1,14,212**	**1,18,303**	**1,40,597**	**1,52,138**	**1,71,273**
Creditors	17,774	12,849	14,054	16,645	20,962
Provision	1,169	601	601	601	601
Short Term Borrowings	1,151	9,826	10,000	10,000	10,000
Other Current Liabilities	8,081	7,268	7,268	7,268	7,268
Total Current Liabilities	28,174	30,544	31,923	34,514	38,831
Long Term Debt	32,310	30,626	45,000	45,000	45,000
Deferred Tax Liabilities	8	472	472	472	472
Other Long Term Liabilities	1,787	2,201	2,201	2,201	2,201
Total Non Current Liabilities	34,105	33,298	47,672	47,672	47,672
Paid-up Capital	1,262	1,262	1,262	1,262	1,262
Reserves & Surplus	49,408	52,820	59,211	68,012	82,680
Shareholders' Equity	50,670	54,082	60,474	69,274	83,942
Non Controlling Interest	1,263	378	528	678	828
Total Equity & Liabilities	**1,14,212**	**1,18,303**	**1,40,597**	**1,52,138**	**1,71,273**

Source: Company, Keynote Capitals Ltd. Estimates,

Cash Flow

Y/E Mar, Rs. Mn	FY23	FY24	FY25E	FY26E	FY27E
Pre-tax profit	18,155	6,720	9,202	12,122	19,234
Adjustments	3,842	6,350	9,017	10,321	10,486
Change in Working Capital	-11,705	-2,618	-967	-2,729	-4,546
Total Tax Paid	-5,361	-3,134	-1,610	-2,121	-3,366
Cash flow from operating Activities	**4,931**	**7,318**	**15,642**	**17,592**	**21,809**
Net Capital Expenditure	-12,086	-8,261	-15,000	-15,000	0
Change in investments	2,150	4,266	0	0	0
Other investing activities	148	243	700	700	700
Cash flow from investing activities	**-9,788**	**-3,752**	**-14,300**	**-14,300**	**700**
Equity raised / (repaid)	0	0	0	0	0
Debt raised / (repaid)	11,227	2,437	14,548	0	0
Dividend (incl. tax)	-1,142	-1,351	-1,200	-1,200	-1,200
Other financing activities	-4,047	-5,184	-4,409	-4,782	-4,483
Cash flow from financing activities	**6,039**	**-4,099**	**8,939**	**-5,982**	**-5,683**
Net Change in cash	1,182	-533	10,281	-2,690	16,826

Valuation Ratios

	FY23	FY24	FY25E	FY26E	FY27E
Per Share Data					
EPS	96	35	59	78	125
Growth %	70%	-63%	68%	32%	60%
Book Value Per Share	411	432	484	555	673
Return Ratios					
Return on Assets (%)	12%	4%	6%	7%	10%
Return on Equity (%)	27%	8%	13%	15%	20%
Return on Capital Employed (%)	19%	8%	11%	12%	15%
Turnover Ratios					
Asset Turnover (x)	1.1	0.7	0.8	0.8	0.9
Sales / Gross Block (x)	3.0	1.6	1.3	1.3	1.5
Working Capital / Sales (%)	10%	15%	17%	19%	22%
Receivable Days	37	67	54	50	49
Inventory Days	55	76	71	71	70
Payable Days	52	64	49	47	46
Working Capital Days	41	78	77	75	73
Liquidity Ratios					
Current Ratio (x)	1.6	1.4	1.7	1.6	2.1
Interest Coverage Ratio (x)	10.3	2.7	3.1	3.5	5.3
Total Debt to Equity	0.6	0.7	0.9	0.8	0.6
Net Debt to Equity	0.5	0.7	0.7	0.6	0.3
Valuation					
PE (x)	5.9	14.4	16.1	12.1	7.6
Earnings Yield (%)	17%	7%	6%	8%	13%
Price to Sales (x)	0.6	0.8	1.2	1.0	0.8
Price to Book (x)	1.4	1.2	2.0	1.7	1.4
EV/EBITDA (x)	4.6	7.8	8.7	7.0	5.3
EV/Sales (x)	0.9	1.2	1.6	1.3	1.0

DFPCL's Valuation

Valuation	
Expected (in Rs. Mn , otherwise stated)	**FY27E**
Revenue	1,49,725
EBITDA	29,571
EV/EBITDA	10
EV	2,95,707
Net Debt	26,974
Market Capitalization	2,68,732
Target Price	2,132
Current Market Price	1,079
% Upside/(Downside)	~98%

Source: Company, Keynote Capitals Ltd. estimates

We believe that with expansion and backward integration, the Company shall be able to boost is topline and profitability. Further, with better macro trends like demand supported by no dumping and booming GDP, coupled with better prospects for monsoon, the Company will be able to make th most of its capacity. Consequently, we initiate a coverage of DFPCL with a BUY rating. We anticipate revenue to grow by ~16% in FY25, driven by better pricing and a recovery in the fertilizer segment. In FY26, we anticipate a growth of ~18% as part of normal business course, followed by a ~26% growth due to commissioning of new capacities. However, we expect the ammonia plant to gradually benefit with increase in its prices in the International market. Resultantly, we see improvement in gross margins from ~32% in FY24 to ~36% in FY27 and EBITDA margins to increase from ~15% to ~20% over the same period. Subsequently, we ascribe an EV/EBITDA multiple of ~10 times, to arrive at a target share price of ~Rs. 2,132, suggesting an upside of ~98%.

Our Recent Reports


Indigo Paints Ltd. | Initiating Coverage Report
KEYNOTE
Indigo Paints Limited
4th July 2024
A challenger in the Indian paint industry
BUY
CMP Rs. 1,381
TARGET Rs. 1,594 (+15.4%)

Indigo Paints Ltd.


Structural Steel Pipes Industry | Industry Report
KEYNOTE
Structural Steel Pipes Industry
26th June 2024
Multiple levers for strong growth
POSITIVE

Structural Steel Pipes Industry


IFB Industries Ltd | Initiating Coverage Re
KEYNOTE
IFB Industries Limited
12th June 2024
Strong combination of growth and margin expansion
BUY
CMP Rs. 1,547
TARGET Rs. 2,268 (+46.6%)

IFB Industries Ltd.

Rating Methodology

Rating	Criteria
BUY	Expected positive return of > 10% over 1-year horizon
NEUTRAL	Expected positive return of > 0% to < 10% over 1-year horizon
REDUCE	Expected return of < 0% to -10% over 1-year horizon
SELL	Expected to fall by >10% over 1-year horizon
NOT RATED (NR)/UNDER REVIEW (UR)/COVERAGE SUSPENDED (CS)	Not covered by Keynote Capitals Ltd/Rating & Fair value under Review/Keynote Capitals Ltd has suspended coverage

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