

India Ratings Upgrades Sudarshan Chemical Industries to 'IND A+'; Outlook Stable

23

By [Neermoy Shah](#)

DEC 2016

India Ratings and Research (Ind-Ra) has upgraded Sudarshan Chemical Industries Limited's (SCIL) Long-Term Issuer Rating to 'IND A+' from 'IND A'. The Outlook is Stable. A full list of rating actions is at the end of this commentary.

KEY RATING DRIVERS

Consolidated View: Ind-Ra continues to take a consolidated view of SCIL and its subsidiaries, namely Prescient Color Limited (100% subsidiary), RIECO Industries Limited (100% subsidiary), Sudarshan Europe B.V. (100% subsidiary) and Sudarshan North America Inc. (step-down subsidiary), for the rating purpose. All the companies are in the same line of business except RIECO Industries which runs an engineering business. Prescient Color manufactures colours and additive master batches, while Sudarshan Europe and Sudarshan North America are the marketing and trading arms of SCIL. SCIL has provided corporate guarantees to the debt of two of its subsidiaries.

Improvement in Profitability and Credit Metrics: The upgrade reflects the improvement in SCIL's EBITDA margins to 11.9% in FY16 (1HFY17 standalone EBITDA margins of 15.7%) from 10.7% in FY15, resulting in an improvement in its net financial leverage (adjusted debt/EBITDA) to 2.4x from 3.2x and EBITDA interest coverage to 4.9x from 3.4x. The improvement in margins was driven by a reduction in the price of the company's key raw material on account of sourcing efficiencies, a decline in input prices, and better realisation from the higher-margin high-performance pigments and effect pigments. Ind-Ra expects SCIL to maintain its EBITDA margins and overall credit profile with a focus on higher-margin pigments and on the developed market of Europe and North America and closure of highly polluting pigment manufacturing units in China.

Long Track Record and Market Leadership: The ratings continue to reflect SCIL's over 60-year-long operating track record and leadership position in the Indian pigment industry with a market share of around 35% and presence across the Azo, phthalocyanine and sub-segments of higher-margin high-performance pigments (source: SCIL). There is no other domestic competitor having a presence across all the segments, according to SCIL. The company's management also has 30-year-long operating experience.

Well-developed Global Distribution Network: The company has a global distribution network with six sales offices, 19 stock points and 80 channel partners. It has been operating in the pigment business for more than 60 years and has developed strong relationships with its customers and suppliers. To cater to the developed market of Europe and North America, management has set up marketing subsidiaries in both the geographies, which is likely to support revenue growth over the next four to five years. It has also registered a wholly owned Chinese subsidiary to distribute pigments in local markets and improve the sourcing efficiency.

Healthy Liquidity: SCIL has healthy liquidity with average bank limit utilisation of 73% for the trailing 12 months ended September 2016. Ind-Ra believes that its cash from operations will be adequate over FY17 and FY18 to repay its debt obligations. The cash from operations has been positive through the three years ended FY16.

Large Capex in Pipeline: The company's expansion in Roha has been granted Mega Project status under the Package Scheme of Incentives, 2013, by the government of Maharashtra in October 2015. Under the scheme, it has to invest a minimum of INR7.5 billion in eligible fixed assets at the site within a period of five years from the date of application. The board has already approved capex of INR1,620 million, which will be spent over FY17 and FY18. Ind-Ra believes that the company will take incremental debt for this expansion and the credit metrics initially will come under pressure; however, better EBITDA margins from the value-added pigments will result in an improvement in the metrics, making them comfortable for the ratings.

Volatility in Input Costs: Volatility in input costs could lead to fluctuations in the company's margins. The prices of the basic chemicals required to manufacture pigments are fairly volatile as they depend on the international prices of key inputs with varying lags to pass on price hikes. Hence, the margins are volatile.

RATING SENSITIVITIES

Positive: A sustained improvement in the EBITDA margins with a higher proportion of revenue from value-added pigments resulting in an improvement in the overall credit profile with the net leverage reducing below 1.5x on a sustained basis could result in a positive rating action.

Negative: Deterioration in the EBITDA margins and/or any debt-led capex over and above the agency's expectation leading to the net leverage exceeding 2.5x on a sustained basis could lead to negative rating action.

COMPANY PROFILE

SCIL is a public limited company. It manufactures a wide range of organic and inorganic pigments as well as intermediates and pesticides with close to 90% revenue coming from pigments.

SCIL's ratings:

- Long-Term Issuer Rating: upgraded to 'IND A+'; Outlook Stable from 'IND A'; Outlook Positive
- INR1,893.6 million term loans (increased from INR1,366.5 million): upgraded to 'IND A+'; Outlook Stable from 'IND A'; Outlook Positive
- INR1,860 million fund based working capital limits (reduced from INR2,237.5 million): upgraded to 'IND A+'; Outlook Stable from 'IND A'; Outlook Positive
- INR378 million* fund based working capital limits: assigned 'IND A1'
- INR1,013 million non-fund based working capital limits (increased from INR1,012.5 million): affirmed at 'IND A1'
- INR534 million term deposit (reduced from INR900 million): affirmed at 'IND tA+'; Outlook Stable
- Proposed INR750 million long-term loans: 'Provisional IND A' withdrawn as company did not proceed with the instrument as envisaged.

* Earlier part of INR2,237.5 million fund-based working capital limits.

SOLICITATION DISCLOSURES

Additional information is available at www.indiaratings.co.in. The ratings above were solicited by, or on behalf of, the issuer, and therefore, India Ratings has been compensated for the provision of the ratings.

Ratings are not a recommendation or suggestion, directly or indirectly, to you or any other person, to buy, sell, make or hold any investment, loan or security or to undertake any investment strategy with respect to any investment, loan or security or any issuer.

DISCLAIMER

ALL CREDIT RATINGS ASSIGNED BY INDIA RATINGS ARE SUBJECT TO CERTAIN LIMITATIONS AND DISCLAIMERS. PLEASE READ THESE LIMITATIONS AND DISCLAIMERS BY FOLLOWING THIS LINK: [HTTPS://WWW.INDIARATINGS.CO.IN/RATING-DEFINITIONS](https://www.indiaratings.co.in/rating-definitions). IN ADDITION, RATING DEFINITIONS AND THE TERMS OF USE OF SUCH RATINGS ARE AVAILABLE ON THE AGENCY'S PUBLIC WEBSITE WWW.INDIARATINGS.CO.IN. PUBLISHED RATINGS, CRITERIA, AND METHODOLOGIES ARE AVAILABLE FROM THIS SITE AT ALL TIMES. INDIA RATINGS' CODE OF CONDUCT, CONFIDENTIALITY, CONFLICTS OF INTEREST, AFFILIATE FIREWALL, COMPLIANCE, AND OTHER RELEVANT POLICIES AND PROCEDURES ARE ALSO AVAILABLE FROM THE CODE OF CONDUCT SECTION OF THIS SITE.

Rating Outstanding

(As on 23/Dec/2016)

Long Term Issuer Rating	IND A+ / Stable	
External Commercial Borrowing	WD	INR 0 m
Fund Based Working Capital Limit	IND A+ / Stable	INR 1860 m
Non-Fund Based Working Capital Limit	IND A1	INR 1013 m
Non-Fund Based Working Capital Limit	IND A1	INR 378 m
Term Deposit	IND 1A+ / Stable	INR 534 m
Term loan	IND A+ / Stable	INR 1893.6 m
Term loan	WD	INR 750 m

Applicable Criteria

[Corporate Rating Methodology](#)

Analyst Names

[Primary Analyst](#)

Neermoy Shah

Senior Analyst

India Ratings and Research Pvt Ltd Wockhardt Towers, 4th floor, West Wing Plot C-2, G Block.

Bandra Kurla Complex Bandra (East), Mumbai 400051

+91 22 40001721

[Secondary Analyst](#)

Amey Joshi

Associate Director

+91 22 40001794

Committee Chairperson

Sudarshan Shreenivas

Director

+91 22 40001783

Media Relation

Mihir Mukherjee

Manager Corporate Communications and Investor Relations

+91 22 40356121