

Infomerics Valuation And Rating Pvt. Ltd.

Press Release

Kalpataru Spinning Mills Ltd

August 12, 2019

Ratings

Instrument / Facility	Amount (Rs. crore)	Ratings	Rating Action
Long Term Bank Facilities- Cash Credit	30.00	IVR BB+/Stable (IVR Double B Plus with Stable Outlook)	Assigned
Long Term Bank Facilities-Term Loan	18.45	IVR BB+/Stable (IVR Double B Plus with Stable Outlook)	Assigned
Long Term Bank Facilities- Cash Credit- Proposed	1.55	IVR BB+/Stable (IVR Double B Plus with Stable Outlook)	Withdrawn
Total	50.00		

Details of Facilities are in Annexure 1

Detailed Rationale

The aforesaid ratings assigned to the bank facilities of Kalpataru Spinning Mills Ltd (KSML) derives comfort from its experienced promoters, proximity to cotton growing areas, established clientele and improvement in operating performance in FY19 (Provisional). However, the rating strengths are partially offset by susceptibility of its profit margins to fluctuations in cotton and cotton yarn prices, intense competition in the cotton yarn segment, working capital intensive nature of operations and financial profile marked by modest gearing and weak debt service coverage ratio (DSCR). Growth in scale of operations with improvement in profitability, improvement in gearing level and efficient working capital management are the key rating sensitivities.

List of Key Rating Drivers with Detailed Description

Key Rating Strengths

Experienced promoters

KSML' operations are managed by Mr. Raghu Rami Reddy, having an experience of more than three decades in the cotton industry including cotton trading. Long presence in the industry has helped the company in establishing comfortable relationship with its suppliers and customers. The day to day affairs of the company is looked after by Mr. Raghu Rami Reddy (Managing Director). Further, the promoters have supported the business by infusing

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funds in the form of subordinated unsecured loans (Rs.7.59 crores outstanding as on March 31, 2019) and have demonstrated positive commitments since inception.

Proximity to cotton growing areas

The unit is located near major cotton growing areas in Guntur District of Andhra Pradesh, resulting in easy availability of quality raw materials and savings in transportation costs.

Established clientele

Long presence of the promoters in the cotton industry has helped the company in developing longstanding relationship with various intermediaries in the value chain. Besides the domestic market, it also caters to the overseas market, mainly China, which is the largest importer of cotton yarn. KSML derives a substantial portion of its revenues from the export market (~65% of its net sales in FY19).

Improvement in operating performance in FY19 (Prov.)

Following a moderation in the total operating income in FY18 mainly due to subdued demand trends in the key importing countries (like china) and strengthening of Indian rupee against currencies of key competing nations (reducing competitiveness of Indian exporters), the company reported a revenue growth of ~14% in FY19 (Prov.). Both, sales quantity and sales realisation increased in FY19. The growth was mainly driven by smoothening of GST related headwinds along with higher spreads between Indian and international cotton, which kept Indian cotton yarn prices competitive (in the export market). With increased sales realisations, the EBIDTA margin of the company improved from 8.31% in FY18 to 10.57% in FY19 (Prov.). Further, the PAT margin also improved from 1.10% in FY18 to 1.97% in FY19 (Prov.).

Key Rating Weaknesses

Susceptibility to fluctuations in cotton and cotton yarn prices

The margins are highly susceptible to changes in the prices of cotton. The price of cotton is fixed by the government through the Minimum Support Price (MSP). However, the purchase price depends on the prevailing demand-supply situation which restricts bargaining power with suppliers as well. Any adverse movement of cotton prices further impacts profitability.

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Additionally, demand for yarn to a large extent is driven by international demand supply dynamics, resulting in volatile margins.

Intense competition in the cotton yarn segment

The cotton yarn segment in India is characterised by high fragmentation and intense competition resulting in limited pricing flexibility for KSML. Further, KSML' product offering is restricted to carded yarn only, in the otherwise commoditized industry, further restricting pricing flexibility.

Working capital intensive operations

KSML's operations are working capital intensive as a large part of its working capital remains blocked in inventories, mainly cotton bales (the primary raw material). With the harvesting season ending in March, the company stocks up on cotton to ensure uninterrupted production which results in high inventory holding as on the account closing date. However, the company has managed its receivables cycles well which gets reflected in the debtor days (being below 20 days) in the past three years. This along with the ability to avail credit from its suppliers (30-40 days), has kept the working capital cycle in the vicinity of 100 days as on the last three account closing dates. The company funds its working capital requirements through bank borrowings which resulted in high utilisation of its working capital limits. The average utilisation of bank borrowings of the company remained high at ~97% during the past 12 months ended May, 2019.

Financial profile marked by modest gearing and weak DSCR

The financial profile is marked by moderate gearing of 1.48x as at March 31, 2019, considering the unsecured loans from the promoters as neither equity nor debt. Interest coverage remained moderate at 1.77x in FY19 (prov.). However, due to the debt funded capex done by the company for enhancing capacity (in 2011) and setting up of wind mill (in 2016), repayment obligations have been higher than the cash accruals resulting in below unity DSCR as on the last three account closing dates. However, the company has been regular in servicing its repayment obligations by infusing unsecured loans as and when required. The interest coverage ratio and the Total debt to GCA though improved from 1.59x and 15.64x in FY18 to 1.77x and 9.38x in FY19, continued to remain moderate. The debt-funded capital expenditure undertaken by the company in the past and the high working capital intensity of

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operations is expected to keep the capital structure and credit metrics stretched in the near term.

Analytical Approach: Standalone.

Applicable Criteria:

Rating Methodology for Manufacturing Companies

Financial Ratios & Interpretation (Non-financial Sector)

Liquidity

Liquidity is marked by tightly matched accruals to repayment obligations and its highly utilized bank limits.

About the Company

Incorporated in 2006, Kalpataruvu Spinning Mills Limited (KSML) is promoted by Mr. Raghu Rami Reddy. The company is engaged in the manufacturing of cotton yarn in the count range of 20' to 40' (Carded Yarn). The manufacturing facility of the company is located in Edlapadu in Guntur district of Andhra Pradesh with an installed capacity of 30,048 spindles. Besides, KSML also has a wind mill for captive power consumption (catering to about 20-25% of the power requirement).

Financials (Standalone):

For the year ended* / As On	(Rs. crore)	
	31-03-2018	31-03-2019
	Audited	Provisional
Total Operating Income	106.57	121.36
EBITDA	8.85	12.83
PAT	1.18	2.40
Total Debt (Excl. Subordinated Loans)	63.94	49.82
Tangible Net worth	31.28	33.69
EBITDA Margin (%)	8.31	10.57
PAT Margin (%)	1.10	1.97
Overall Gearing Ratio (x) (Excl. Subordinated Loans)	2.04	1.48

*Classification as per Infomerics' standards.

Status of non-cooperation with previous CRA:

Ind-Ra has moved the rating of KSML into the Issuer Non-Cooperating category as the company did not co-operate in the rating procedure despite repeated follow ups as per the Press Release dated November 27, 2018.

Any other information: Nil

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Rating History for last three years:

Sr. No.	Name of Instrument/Facilities	Current Rating (Year 2019-20)			Rating History for the past 3 years		
		Type	Amount outstanding (Rs. Crore)	Rating	Date(s) & Rating(s) assigned in 2018-19	Date(s) & Rating(s) assigned in 2017-18	Date(s) & Rating(s) assigned in 2016-17
1.	Long Term Fund Based Limits - Cash Credit	Long Term	30.00	IVR BB+/ Stable Outlook	-	-	-
2.	Long Term Fund Based Limits - Term Loan	Long Term	18.45	IVR BB+/ Stable Outlook	-	-	-

Note on complexity levels of the rated instrument: Infomerics has classified instruments rated by it on the basis of complexity and a note thereon is available at www.infomerics.com.

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About Infomerics:

Infomerics commenced rating & grading operations in April 2015 after having spent over 25 years in various segments of financial services. Infomerics is registered with the Securities and Exchange Board of India (SEBI) and accredited by Reserve Bank of India. It is gradually gaining prominence in domestic rating and/or grading space. Infomerics is striving for positioning itself as the most trusted & credible rating agency in the country and is gradually widening its product portfolio. Company's long experience in varied spectrum of financial services is helping it to fine tune its product offerings to best suit the market.

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Annexure 1: Details of Facilities

Name of Facility	Date of Issuance	Coupon Rate/ IRR	Maturity Date	Size of Facility (Rs. Crore)	Rating Assigned/ Outlook
Long Term Fund Based Limits–Cash Credit	-	-	-	30.00	IVR BB+/ Stable Outlook
Long Term Fund Based Limits –Term Loan	-	-	March 2023	18.45	IVR BB+/ Stable Outlook