



Press Release

Kalpataruvu Spinning Mills Pvt Ltd

October 15, 2020

Ratings

| Instrument / Facility | Amount (Rs. Crore) | Ratings | Rating Action |
|---|-----------------------|---|---------------|
| Long Term Bank Facilities- Cash Credit | 30.00 | IVR BB + / Stable Outlook (IVR Double B Plus with Stable Outlook)) | Reaffirmed |
| Long Term Bank Facilities- Term Loan | 19.13 | IVR BB + / Stable Outlook (IVR Double B Plus with Stable Outlook)) | Reaffirmed |
| Total | 49.13 | | |

Details of Facilities are in Annexure 1

Detailed Rationale

The reaffirmation of the ratings assigned to the bank facilities of Kalpataruvu Spinning Mills Private Ltd (KSML) continues to derive comfort from its experienced promoters, proximity to cotton growing areas, established clientele and stable financial profile marked by its stable operating income with moderate margin. The ratings also note improvement in its capital structure and moderate debt service coverage indicator in FY20 (provisional). However, these 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 and working capital intensive nature of its operations.

Key Rating Sensitivities

Upward Rating Factor

- Significant growth in scale of business with improvement in profitability metrics thereby leading to overall improvement in cash accruals on a sustained basis
- Improvement in the capital structure and debt protection metrics
- Effective working capital management with improvement in operating cycle and liquidity

Downward Rating Factor

- Dip in operating income and/or profitability impacting the debt coverage indicators,



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- Withdrawal of subordinated unsecured loan amounting to Rs.9.25 crore and /or deterioration in the capital structure with overall gearing to below 1.5x and interest coverage to below 1.2x
- Elongation in the operating cycle impacting the liquidity

List of Key Rating Drivers with Detailed Description

Key Rating Strengths

Experienced promoters with demonstrated support

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 affairs of the company is looked after by Mr. Raghu Rami Reddy (Managing Director). Further, the promoters have supported the business by infusing funds in the form of subordinated unsecured loans (Rs.9.25 crores outstanding as on March 31, 2020) and have demonstrated positive commitments since inception.

Proximity of cotton growing areas

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

Established clientele

Long presence of the promoters in cotton trading segment has helped the company to develop longstanding relationship with various intermediaries in the value chain. Beside the domestic market, gradually it also expanded its operation in the overseas market, mainly China which is the largest importer of cotton yarn. KSML used to derive a substantial portion of its revenues from the export market (~64% of its net sales in FY19), most of which are repeat orders validating its quality and timely delivery. Established presence in the domestic market as well as in various geographies has helped the company to perform well even in FY 19-20 where export market was not good due to US - China trade war initially and then COVID 19. During FY19-20 export sales contributed around ~4% of its revenue.

Stable financial profile marked by moderate margin

There has been a moderation in the total operating income in FY20 (Prov.) mainly due to subdued demand trends in the key cotton importing countries (like china) and due to



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prevailing COVID situation worldwide in last few months of FY20. KSML has reported revenue of Rs.102.70 crore as per provisional FY20 numbers as against revenue of Rs.121.36 crore in FY19. Both sales quantity and sales realisation has declined in FY20. With decline in sales realisations coupled with decline in the capacity utilization, the EBIDTA margin of the company also declined from 9.11% in FY19 to 8.89% in FY20 (Prov.). Further, the PAT margin also declined from 2.03% in FY19 to 1.23% in FY20 (Prov.). The company earned a GCA of Rs.4.20 crore in FY20 as against a GCA of Rs.5.40 crore in FY19. However, despite the deterioration the financial performance of the company remained more or less stable.

Satisfactory capital structure with moderate debt service coverage indicator

The capital structure of KSML has improved with improvement in its overall gearing to 0.98x as on March 31, 2020 from 1.14x as at March 31, 2019, considering the unsecured loans from the promoters as quasi equity and excluding it from debt. Interest coverage remained moderate at 1.68x in FY20 (prov.). However, due to past 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 resulting in around unity DSCR as on March 31, 2020. However, the company has been regular in servicing of its repayment obligations by infusing unsecured loans as and when required. The interest coverage ratio though improved from 1.54x in FY19 to 1.68x in FY20 continued to remained moderate. Infomerics believes that the debt-funded capital expenditure undertaken by the company in the past and the high working capital intensity of its operations is expected to keep the credit metrics stretched in the near term.

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. 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



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

Working capital intensive nature of 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 piles up cotton to ensure uninterrupted production which generally resulted in high inventory holding as on the account closing date. However, the company has managed its receivables cycles well which get 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 mostly funded 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 ~93% during the past 12 months ended September, 2020.

Analytical Approach: Standalone

Applicable Criteria:

Rating Methodology for Manufacturing Companies
Financial Ratios & Interpretation (Non-financial Sector)

Liquidity: Stretched

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

About the Company

Incorporated in 2006, Kalpataru Spinning Mills Private 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).



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Financials (Standalone):

| For the year ended* / As On | (Rs. crore) | |
|-----------------------------|-------------|-------------|
| | 31-03-2019 | 31-03-2020 |
| | Audited | Provisional |
| Total Operating Income | 121.36 | 102.70 |
| EBITDA | 11.06 | 9.13 |
| PAT | 2.49 | 1.27 |
| Total Debt | 48.84 | 43.62 |
| Tangible Net worth | 42.94 | 44.29 |
| EBITDA Margin (%) | 9.11 | 8.89 |
| PAT Margin (%) | 2.03 | 1.23 |
| Overall Gearing Ratio (x) | 1.14 | 0.98 |

*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

Rating History for last three years with Infomerics:

| Sr. No. | Name of Instrument/Facilities | Current Rating (Year 2020-21) | | | Rating History for the past 3 years | | |
|---------|---|-------------------------------|--------------------------------|-------------------------------|--|---|---|
| | | Type | Amount outstanding (Rs. Crore) | Rating | Date(s) & Rating(s) assigned in 2019-20 | Date(s) & Rating(s) assigned in 2018-19 | Date(s) & Rating(s) assigned in 2017-18 |
| 1. | Long Term Fund Based Limits - Cash Credit | Long Term | 30.00 | IVR BB+/ Stable Outlook | IVR BB+/ Stable Outlook (August 12, 2019) | - | - |
| 2. | Long Term Fund Based Limits - Term Loan | Long Term | 19.13 | IVR BB+/ Stable Outlook | IVR BB+/ Stable Outlook (August 12, 2019) | - | - |



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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 |



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|--|---|---|------------|-------|-------------------------|
| Long Term Fund Based Limits –Term Loan | - | - | March 2025 | 19.13 | IVR BB+/ Stable Outlook |
|--|---|---|------------|-------|-------------------------|

