February 04, 2020 Revised

Nandan Denim Limited: Ratings downgraded to [ICRA]BBB+(Stable)/[ICRA]A2

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based-Term Loan	390.35	390.35	Revised to [ICRA]BBB+(Stable) from [ICRA]A-(Negative)
Fund based- Working Capital Facilities	249.80	249.80	Revised to [ICRA]BBB+(Stable) from [ICRA]A-(Negative)
Fund based-Working Capital Facilities (Short term)	15.20	15.20	Revised to [ICRA]A2 from [ICRA]A2+
Non- Fund based facilities	80.00	80.00	Revised to [ICRA]A2 from [ICRA]A2+
Total	**735.35**	**735.35**	

*Instrument details are provided in Annexure-1

Rationale

The revision in ratings considers lower-than-expected growth in scale and the continued moderation in profit margin in H1FY2020, which are likely to moderate the expected cash flows from FY2020 onwards. Nandan Denim Limited (NDL) has witnessed moderation in average denim realisation, which further declined to Rs. 120.3 per metre in H1FY2020 from Rs. 122.5 per metre in FY2019 (Rs. 131 per metre in FY2018), despite the increase in average raw material prices. The decline can be attributed to the stiff competition and the prevalent over-capacity in the denim industry. Consequently, the operating margin declined to 8.4% in H1FY2020 from 11.0% in FY2019. Further, the ratings continue to be constrained by the inherent cyclicality associated with the textile sector and the prevalent over capacity in the domestic denim industry, which continues to pressurise the realisation. The ratings also factor in the vulnerability of profitability to fluctuations in the raw material prices (majorly cotton), the moderate return indicators as well as the working capital intensive nature of NDL's operations.

The industry headwinds are off-set to some extent by NDL's strong market position as leader in terms of denim capacity in the domestic denim industry, diversified product portfolio, established distribution network and extensive industry experience of its promoters. The ratings take comfort from NDL's higher backward integration within the denim value chain, gives it competitive advantage over its peers and allows the company to better manage its cost structure. ICRA also notes that the capex undertaken in the past is eligible for various government incentive schemes, which will support profitability going forward; however, the timely receipt of subsidy will remain crucial. The ratings also take comfort from NDL's strong net worth base of Rs. 497 crore and gearing of 1.0 times as on September 30, 2019, along with adequate liquidity position to meet the scheduled debt repayments.

The Stable outlook on [ICRA]BBB+ rating reflects ICRA's belief that over the medium term, denim demand and prospects for denim industry should improve, however, the turnaround would be a monitorable. ICRA also believes that Nandan Denim Limited (NDL) should be able to at least maintain the current performance in terms of debt coverage going forward despite the current weak business environment.

Key rating drivers and their description

Credit strengths

Established market position as one of the largest denim manufacturers; strong marketing network in domestic markets– The promoters of NDL, i.e, the members of the Chiripal family, have more than 40 years of experience in the textile industry. The company has an integrated manufacturing unit, which comprises production facilities from spinning to fabric finishing. Additionally, it has a captive power plant of 15 megawatts (MW). NDL is a part of the Chiripal Group, which has been present in the textile business since 1972 and has diversified operations in the textile value chain. In addition to denim fabric, the Group also has fabric processing operations and also manufactures partially-oriented yarn (POY), fully drawn yarn (FDY) and draw texturised yarn (DTY).

NDL has an established market position in the Indian denim industry and is one of the largest denim manufacturers in India, with an installed denim capacity of 110-million metres per annum (mmpa). NDL primarily caters to the medium quality denim segment, which has a larger market size than the premium denim segment, which is mostly targeted to the export markets. NDL has a well-established network of distributors in the domestic market and enjoys strong relationship with clients in several global markets, attributable to the Chiripal Group's long presence in the textile business. The company has tie-ups with about 40 distributors across the country, including some exclusive distributors.

Backward integrated operations to support operational risk profile; timely receipts of various eligible incentives under central and state textile policies remains crucial– In order to backward integrate, NDL took periodical capex to increase its cotton spinning capacity to 142 TPD from 40 TPD. At present, ~89% of yarn requirement is met from in-house spinning unit. This enables NDL to better manage its cost structure and profitability that its competitors. Further, various sections of NDL's capex are eligible for lucrative Central and State government's incentive schemes such as interest subsidy on loan availed, capital subsidy on plant and machinery (P&M), GST (earlier VAT) refund on eligible fixed investment in machinery P&M and exemptions in power tariff, meant for textile units.

Healthy financial risk profile– The financial risk profile remains healthy, marked by a strong net worth base of Rs. 497 crore and gearing of 1.0 times as on September 30, 2019, and an adequate liquidity position.

Credit challenges

Weakening in profitability and return indicators– The company's operating profit moderated to 8.4% in H1FY2020 from 11.0% in FY2019 which had moderated from 14.6% in FY2018, due to erosion in denim realisations and volumes. Consequently, the net profit margin also declined to 0.6% in H1FY2020 compared to 1.5% and 2.9% in FY2019 and FY2018 respectively. The return indicators of NDL weakened, with RoCE at 5.3% in FY2019, which is expected to further moderate to sub 5% in FY2020, due to decline in profitability.

Prevalent over-capacity in domestic denim industry pressurises realisations - The denim industry has witnessed significant cyclicality in the past, wherein there have been periods of excess capacity in the market as well as periods with tight demand-supply situations. Over the last four to five years, denim demand has increased steadily and several Indian denim players such as NDL have increased their capacity under the prevailing government incentive scheme. However, with several capacity additions in the recent past, denim supply has exceeded the demand growth, exposing NDL to an over-supply situation in the domestic market. The company's average realisation from denim fabric continued to decline, moderating to an average of Rs. 120.29 per metre in H1FY2020 compared to Rs. 122.57 per metre in FY2019 and Rs. 131 per metre in FY2018. Currently, NDL generates majority of its sales from the domestic market and thus its performance will remain exposed to the inherent cyclicality in the denim industry.

Vulnerability of profitability to adverse fluctuations in key raw material prices - The margins of the company are largely affected by the raw material price fluctuation which in turn affects the sales realisations. Any adverse movement in the price of key raw materials like cotton could have an adverse impact on the company's margins, as the company may not be able to pass on the price hike to its customers owing to high competition and overcapacity in the industry. ICRA, however, believes that NDL's large scale and integrated setup should help to cushion the impact of such adverse movements to some extent.

High working capital intensity - The working capital intensity for NDL remained high with NWC/OI at 31% as on FY2019 end. The inventory remains high as the company stocks cotton during year end with expectations of price increase during lean supply. Thus, on one hand, the company remains susceptible to unforeseen corrections to cotton prices, which can lead to inventory losses; on the other hand, a stable price may lead to higher carrying cost without any foreseen benefits.

Liquidity position: Adequate

NDL's liquidity position remains adequate, marked by sufficient cash accruals (though it has moderated due to moderation in profitability) against debt obligations, which is further supported by the absence of any major capex and the cushion in working capital limits.

Rating sensitivities

Positive triggers – Substantial increase in revenue and profitability, resulting in improved coverage metrics. Specific indicators that may lead to rating upgrade will be TD/OPBDITA of less than 2.0 times and ROCE of more than 10% on a sustained basis

Negative triggers – Negative pressure on NDL's ratings could arise if any substantial decline in revenue and profitability, due to a material decline in realisations or demand, impacts the key financial indicators. Further, any major stretch in working capital intensity or significant delays in receipt of subsidy, which impacts the liquidity, may also lead to a rating downgrade. Specific indicators that may lead to rating downgrade will be interest TD/OPBDITA more than 3 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Indian Textiles Industry –Fabric Making
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financials of NDL.

About the company

Incorporated in 1994 by the members of the Chiripal family, Nandan Denim Limited (NDL) (earlier known as Nandan Exim Limited) was initially involved in manufacturing, trading and export of textile products – primarily denim products. The company is a part of the Chiripal group, which is based in Ahmedabad (Gujarat), and has presence in various industries such as textiles, education, real estate, packaging and chemicals.

The company forayed into manufacturing operations in FY2004 with a project for weaving of denim fabric and the commercial production of 20 million metres per annum (MMPA) capacity of denim fabric was commenced in FY2006. With periodic expansions, the installed capacity of denim manufacturing now stands at 110 MMPA. Denim fabrics manufactured by NDL are either made of 100% cotton yarn or mixed with Lycra, Polyester, and so on in weft, depending on the market requirement. NDL underwent backward integration by installation of a cotton spinning unit of 40TPD capacity in FY2011, which was increased to 142 TPD in the current fiscal. Further, NDL diversified its portfolio by setting up 10 million meters per annum shirting capacity in March 2014. The company also operates a 15-MW power plant within its premises, which meets its entire power requirements. NDL has its manufacturing facilities at Sejpur-Gopalpur at Ahmedabad.

The company recorded a net profit of Rs. 22.1 crore on an operating income (OI) of Rs. 1467.9 crore in FY2019 as against a net profit of Rs. 46.4 crore on an OI of Rs. 1597.7 crore in FY2018. Further, the company recorded a net profit of Rs. 5.4 crore on an OI of Rs. 857.6 crore in H1FY2020 (Provisional financials).

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	1,597.7	1,467.9
PAT (Rs. crore)	46.4	22.1
OPBDIT/OI (%)	14.6%	11.0%
RoCE (%)	10.7%	5.3%
Total Outside Liabilities/Tangible Net Worth (times)	2.0	1.6
Total Debt/OPBDIT (times)	2.7	3.7
Interest Coverage (times)	4.0	6.0
DSCR	1.9	1.6

Status of non-cooperation with previous CRA:

CRISIL's rationale dated October 24, 2019.

Despite repeated attempts to engage with the management, CRISIL failed to receive any information on either the financial performance or strategic intent of NDL, which restricts CRISIL's ability to take a forward-looking view on the entity's credit quality. CRISIL believes information available on NDL is consistent with 'Scenario 4' outlined in the 'Framework for Assessing Consistency of Information'. Based on the last available information, the ratings on bank facilities of NDL revised to be 'CRISIL BB+/Stable/CRISIL A4+ Issuer not cooperating'.

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)					Rating History for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Rating		FY2019		FY2018		FY2017
					04 February 2020	04 June 2019	11 March 2019	23 August 2018	23 Nov 2017	16 Nov 2017	27 Dec 2016
1	Fund based-Term Loan	Long Term	390.35	339.55^	**[ICRA]BBB+ (Stable)**	**[ICRA]A- (Negative)**	**[ICRA]A (Negative)**	**[ICRA]A (Negative)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A- (Stable)**
2	Fund based- Working Capital Facilities	Long Term	249.80		**[ICRA] BBB+ (Stable)**	**[ICRA]A- (Negative)**	**[ICRA]A (Negative)**	**[ICRA]A (Negative)**	**[ICRA]A (Stable)**	**[ICRA]A (Stable)**	**[ICRA]A- (Stable)**
3	Fund based-Working Capital Facilities	Short Term	15.20		**[ICRA]A2**	**[ICRA]A2+**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A2+**
4	Non- Fund based facilities	Short Term	80.00		**[ICRA]A2**	**[ICRA]A2+**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A1**	**[ICRA]A2+**

Amount in Rs. Crore,^ Sep 30,2019

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website click here

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan- 1	Feb-2015	NA	Dec-2025	24.78	[ICRA]BBB+(Stable)
NA	Term Loan- 2	Jul-2011	NA	Mar-2020	22.47	[ICRA]BBB+(Stable)
NA	Term Loan- 3	Sep-2011	NA	Sep-2021	22.80	[ICRA]BBB+(Stable)
NA	Term Loan- 4	Oct-2011	NA	Mar-2026	42.03	[ICRA]BBB+(Stable)
NA	Term Loan- 5	Jul-2012	NA	Sep-2023	37.58	[ICRA]BBB+(Stable)
NA	Term Loan- 6	Mar-2015	NA	Dec-2025	64.47	[ICRA]BBB+(Stable)
NA	Term Loan- 7	Jul-2014	NA	Dec-2025	34.37	[ICRA]BBB+(Stable)
NA	Term Loan- 8	Jul-2014	NA	Sep-2025	19.60	[ICRA]BBB+(Stable)
NA	Term Loan- 9	Feb-2015	NA	Dec-2025	60.75	[ICRA]BBB+(Stable)
NA	Term Loan- 10	Dec-2014	NA	Dec-2025	40.50	[ICRA]BBB+(Stable)
NA	Term Loan- 11	Jun-2017	NA	Jun-2027	21.00	[ICRA]BBB+(Stable)
NA	Fund based- Working Capital Facilities				249.80	[ICRA]BBB+(Stable)
NA	Fund based-Working Capital Facilities – Short Term				15.20	[ICRA]A2
NA	Non- Fund based facilities				80.00	[ICRA]A2

Source: Nandan Denim Limited

Corrigendum

Document dated February 04, 2020 has been corrected with revisions as detailed below: • Rating history for past three years on page number 5 • Rating action dated 23 Nov, 2017 has been added

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About ICRA Limited

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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