March 06, 2023

Nandan Denim Limited: Ratings reaffirmed; Outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based- Cash Credit	240.00	240.00	[ICRA]BBB (Negative); reaffirmed; outlook revised to Negative from Stable
Fund -based- Term Loan	251.56	251.56	[ICRA]BBB (Negative); reaffirmed; outlook revised to Negative from Stable
Non-fund-based facilities- Letter of Credit/Bank Guarantee	60.00	60.00	[ICRA]A3+; reaffirmed
Total	**551.56**	**551.56**	

**Instrument details are provided in Annexure-1*

Rationale

The revision of the outlook on the long-term rating of Nandan Denim Limited (NDL) factors in the significantly weaker-than-expected performance in 9M FY2023 and the continuing weakness in the current quarter as well, both of which have weakened NDL's liquidity and debt coverage. The company's operating income declined 55% on a YoY basis in Q3 FY2023 to Rs.262.2 crore with an operating profit (OPBITDA) of -Rs.0.03 crore. A sharp decline in revenues and net losses in Q3 FY2023 as well as 9M FY2023 can be attributed to slowdown in demand and high raw material prices.

The ratings continue to draw strength from NDL's strong market position as one of the leading denim capacities in the domestic market, its diversified product profile and the extensive industry experience of its promoters. The ratings also take comfort from the company's proximity to the cotton-growing belt and its backward integrated operations, which support its cost structure. ICRA also notes NDL's eligibility for various Government incentives on the capex in the past, which supports its profitability, though timely receipt of the same is important.

The ratings remain constrained by the decline in NDL's profitability in 9M FY2023, inherent cyclicality associated with the denim sector and the working capital-intensive nature of the company's operations.

Key rating drivers and their description

Credit strengths

Established market position as one of the country's leading denim manufacturers – NDL is a part of the Ahmedabad-based Chiripal Group, which has been in the textile business since 1972 and enjoys diversified operations in the textile value chain with manufacturing partially-oriented yarn (POY), fully drawn yarn (FDY) and draw texturised yarn (DTY), along with fabric processing. NDL has an integrated manufacturing unit, comprising production facilities from spinning to fabric finishing. The company has an established market position and is one of the largest denim manufacturers in India, with a capacity of 110 million meters per annum (MMPA). NDL primarily caters to the low-medium quality denim segment, which has a larger market size than the premium denim segment. NDL has an established network of distributors in the domestic market and enjoys strong relationship with its clients, which can be attributed to the Chiripal Group's long presence in the textile business.

Proximity to cotton-growing belt and backward-integrated operations support operational risk profile – NDL's manufacturing facilities at Sejpur-Gopalpur in Ahmedabad are in proximity to the cotton-growing belt in Gujarat. Further, the backward-integrated operations enable the company to meet a significant share of its yarn requirement from the in-house capacities. While its presence in the spinning segment exposes the company's profitability to volatility in cotton prices, it facilitates cost savings on transportation. While surge in yarn prices has been steeper than the increase in cotton prices, captive yarn capacity reduced the impact on the company's profitability.

Eligibility for Government schemes supports overall returns; timely receipt of the same remains crucial – Various sections of capex undertaken by NDL are eligible for incentives under different Central and state Government schemes such as interest subsidy on term loan, capital subsidy on plant and machinery, Goods & Service Tax (GST) refund and power subsidy. These incentives support the company's overall returns, however, timely receipt of the same remains crucial.

Credit challenges

Sharp decline in performance amid increased raw material prices; profitability remains vulnerable to adverse fluctuations in key raw material prices – The profit margins of the company are mainly affected by the raw material price fluctuations, as the ability to fully pass on cost increases gets constrained due to cyclical demand conditions and intense competition in the sector. The operating margins of NDL declined to 7.9% in FY2022 and further to 3.1% in 9M FY2023 (including operating losses in Q3 FY2023) from 9.2% in FY2021. Further, NDL reported net losses and PAT/OI stood at -0.1% in 9M FY2023 against 3.1% in FY2022. Amid cost side pressure this year, NDL's profitability is expected to be sharply lower than the previous estimates, resulting in weaker-than-expected debt coverage metrics.

High working capital intensity – The working capital intensity for NDL has remained high with NWC/OI at 19% in H1 FY2023- and 24% in FY2022 primarily because of elongated receivables and high inventory holding. The inventory remains high as the company stocks cotton during the year-end with expectations of price increase during the lean season. Thus, on one hand, the company's profitability remains susceptible to unforeseen corrections in cotton prices, which can lead to inventory losses, on the other hand, a stable price may lead to higher carrying cost without any foreseen benefit.

Exposed to cyclicality in the denim industry – The denim industry is exposed to inherent cyclicality, with periods of excess market capacity and tight demand-supply situations. An oversupply situation exerts pressure on the company's profitability by affecting the volumes and the pricing power, in line with the industry trends.

Liquidity position: Stretched

NDL's liquidity profile is stretched as the company incurred operating losses in Q3 FY2023. ICRA expects Q4 FY2023 would remain weak for the company. NDL has availability of free cash and cash equivalents of ~Rs.26.8 crore as on December 31, 2022 and a cushion of Rs. ~Rs.85 crore (equivalent to ~35% of the sanctioned limits) in the company's fund-based working capital limits as of end-December 2022. The company had made prepayment of ~Rs. 42 crore in 9M FY2023 and has debt repayment obligations of ~Rs. 11.3 crore for Q4 FY2023. Overall, ICRA expects NDL to be able to meet its near-term commitments through internal as well as external sources.

Environmental and Social Risks

NDL's exposure to environmental risks are mainly related to exposure to climate impact of post-consumer waste. While these risks have not resulted in material implication so far, policy actions towards waste management and the environmental impact such as to recycle the textile as well as packaging waste being generated, could have cost implications for the companies. The company is focusing on using sustainable practices (including use of eco-friendly fabrics and chemicals) from the beginning to the end of the product life cycle.

NDL's exposure to social risks are mainly related to exposure to the risks of disruptions due to inability to properly manage the human capital in terms of their safety and the overall well-being. Besides, human rights issues and inability to ensure diversity, while providing equal opportunity could pose social risks for the company. Further, any significant increase in wage rates may affect the cost structure of apparel manufacturers, impacting the margins. Shortage of skilled workers could also affect operations/growth plan and remain a key concern.

Rating sensitivities

Positive factors – Any near-term upgrade in ratings is unlikely. The outlook can be revised to Stable if there is a continued growth in NDL's revenues and profitability, improving its coverage metrics. Strengthening of the liquidity profile while sustaining a comfortable capital structure may also have a positive impact.

Negative factors – ICRA could downgrade the ratings if there is pressure on the operating profitability, or any stretch in working capital cycle or any sizeable debt-funded capex, which adversely impacts the credit metrics and the company's liquidity position. A specific trigger for ratings downgrade includes an interest cover of less than 3 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology - Textiles Industry (Spinning) Rating Methodology - 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 August 1994 as a private limited company by Mr. Vedprakash Chiripal and Mr. Brijmohan Chiripal, Nandan Denim Limited (NDL, earlier known as Nandan Exim Limited) started with trading and exports of textile products and was converted into a public limited company in January 2004. In FY2004, the company forayed into manufacturing operations with weaving of denim fabric with a capacity of 20 million meters per annum (MMPA) and increased the capacity to 110 MMPA over the years. NDL installed a cotton spinning unit having a capacity of 40 TPD in FY2011 and increased the capacity to 142 TPD over the years (reduced to 104 TPD due to a fire incident in August 2020) in order to backward integrate. Further, to mitigate the product concentration risk, NDL installed a 10-MMPA shirting capacity in FY2014. The company has two manufacturing facilities located at Sejpur-Gopalpur in Ahmedabad (Gujarat). The company also operates a 15-MW solar power plant within its premises, which meets its entire power requirements.

Key financial indicators

	FY2021	FY2022	9M FY2023
Operating Income (Rs. crore)	1,110.5	2,188.4	1,569.6
PAT (Rs. crore)	-18.7	67.8	-2.2
OPBDIT/OI (%)	9.2%	7.9%	3.9%
PAT/OI (%)	-1.7%	3.1%	-0.1%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	1.7	NA
Total Debt/OPBDIT (times)	5.4	3.2	6.8
Interest Coverage (times)	2.4	4.1	1.7

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; NA: Not Available
Source: NDL

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for past three years

	Instrument	Type	Current Rating (FY2023)							Chronology of Rating History for the past 3 years					
			Amount Rated (Rs. crore)	Amount Outstanding as of December 31, 2022 (Rs. crore)	Date & Rating in FY2023				Date & Rating in FY2022	Date & Rating in FY2021		Date & Rating in FY2020		
					Mar 6, 2023	Nov 23, 2022	Oct 10, 2022	Aug 3, 2022	Jan 24, 2022	Mar 22, 2021	Dec 04, 2020 Aug 17, 2020	Feb 13, 2020	Feb 04, 2020	Jun 4, 2019
1	**Term Loan**	Long-term	251.56	234.51	[ICRA]BBB (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Positive)	[ICRA]BBB (Positive)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB+ @	[ICRA]BBB+ (Stable)	[ICRA]A- (Negative)
2	**Cash Credit**	Long-term	240.0	--	[ICRA]BBB (Negative)	[ICRA]BBB (Stable)	[ICRA]BBB (Stable)	[ICRA]BBB (Positive)	[ICRA]BBB (Positive)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB+ @	[ICRA]BBB+ (Stable)	[ICRA]A- (Negative)
3	**EPC/FBD**	Short term	--	--	--	--	--	--	--	--	[ICRA]A3	[ICRA]A2@	[ICRA]A2	[ICRA]A2+
4	**Letter of Credit / Bank Guarantee**	Short term	60.0	--	[ICRA] A3+	[ICRA] A3+	[ICRA] A3+	[ICRA] A3+	[ICRA] A3+	[ICRA]A3	[ICRA]A3	[ICRA]A2@	[ICRA]A2	[ICRA]A2+
5	**Unallocated Limits**	Long-term/ Short term	--	--	--	--	[ICRA]BBB (Stable)/ A3+	[ICRA]BBB (Positive)/ A3+	[ICRA]BBB (Positive)/ A3+	[ICRA]BBB- (Stable)/A3	--	--	--	--

@ rating placed on Watch with Negative Implications

Complexity level of the rated instrument

Instrument	Complexity Indicator
Fund-based- Cash Credit	Simple
Fund-based- Term Loan	Simple
Non-fund Based - Letter of Credit/Bank Guarantee	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (RS Crore)	Current Rating and Outlook
NA	Fund based - Cash Credit	NA	NA	NA	240.00	[ICRA]BBB (Negative)
NA	Fund based - Term Loan	FY2015	NA	FY2027	251.56	[ICRA]BBB (Negative)
NA	Non-fund Based - Letter of Credit/Bank Guarantee	NA	NA	NA	60.00	[ICRA]A3+

Source: NDL

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis – Not Applicable

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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.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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