November 27, 2023

Sagar Manufacturers Private Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund Based Cash Credit	260.00	260.00	[ICRA]A-(Stable); reaffirmed
Long Term - Fund Based Term loan	468.55	442.29	[ICRA]A-(Stable); reaffirmed
Short Term – Non-Fund Based	16.00	16.00	[ICRA]A2+; reaffirmed
Long Term/Short Term – Unallocated	3.64	29.90	[ICRA]A-(Stable)/[ICRA]A2+; reaffirmed
Total	**748.19**	**748.19**	

**Instrument details are provided in Annexure-I*

Rationale

The ratings derive comfort from Sagar Manufacturers Private Limited's (SMPL) large spinning capacity of ~2 lakh spindles and its consistently healthy capacity utilisation level of around 90%, which provide benefits of economies of scale. ICRA also notes that SMPL's profit margins are supported by its access to fiscal incentives and a favourable cost structure. The ratings further derive comfort from SMPL's established position in the business-to-business (B2B) segment in both domestic and export markets, which coupled with good product quality and diverse product offerings under the yarn category, result in repeat orders. The ratings also favourably factor in the proximity of SMPL's plant to the cotton belt of Madhya Pradesh (MP), Maharashtra and Gujarat, which result in savings on transportation costs.

SMPL reported a heathy operating performance in FY2023, with the company posting an all-time high operating income (OI) of around Rs. 1,578.4 crore. While its operating profit margin (OPM) plummeted to 11.0% in FY2023 due to weakening gross contribution margin emanating from unfavourable price differential between cotton yarn and cotton, it improved marginally to 11.3% in H1 FY2024, indicating modest recovery of gross contribution margins. Notwithstanding the softening of cotton yarn realisations, the company is expected to witness only a marginal YoY decline in revenues on the back of higher volume offtake. Besides, increased production level, led by new capacity of 39,840 spindles (to manufacture polycotton yarn) which has been operational since September 2023, is expected to support the revenues, going forward.

These strengths are, however, partially offset by SMPL's moderate financial profile, characterised by elevated debt levels, resulting from regular large debt-funded capital expenditure (capex) towards expansion of spinning capacities. ICRA notes that the company has incurred sizeable capex of Rs. 220 crore in FY2023 and H1 FY2024 towards setting up unit-6, which has spinning and knitting capacities of 9,821 MTPA and 2,366 MTPA, respectively, which was funded via debt of Rs. 157 crore, equity contribution from promoters of Rs. 13.5 crore and the balance Rs. 49.2 crore from internal accruals. Additionally, the company is in the process of setting up a 300-bed multi-speciality hospital in Bhopal (MP) under its wholly-owned subsidiary, Sagar Services & Resources Private Limited (SSRPL) at a total cost of Rs. 153.3 crore, funded via debt of Rs. 98.5 crore and the balance via internal accruals. Of this, the company has incurred capex of Rs. 135 crore till September 30, 2023. The hospital is expected to commence operations in Q4 FY2024. Notwithstanding the increased debt levels, healthy revenues and profits generated from the spinning business are expected to adequately support the financial profile over the medium term. The ability of the company to complete the hospital project within the budgeted costs and time as well as ramp up operations in a timely manner thereafter would be the key rating factors.

The ratings are also tempered by the company's exposure to the pricing pressure due to non-integrated nature of operations and intensely competitive nature of the cotton spinning industry. ICRA also notes that cotton stocking during the harvest season exposes the company to fluctuations in cotton and cotton yarn prices during the non-harvest period, with fixed procurement cost and fluctuating yarn realisations. Nevertheless, the company's lower-than-industry-average cotton stocking mitigates the risk to some extent.

The Stable outlook on the [ICRA]A- rating reflects ICRA's opinion that SMPL will continue to exhibit healthy capacity utilisation level, which coupled with its favourable cost structure (stemming from its low manufacturing and employee expenses) would lead to healthy profitability in the medium term. Amid lack of large capex plans, this should adequately support the financial profile over the near term.

Key rating drivers and their description

Credit strengths

Large-scale spinning operations – SMPL has 2,30,784 spindles as of September 20, 2023, which translate into a spinning capacity of 51,951 MTPA and offers the company benefits of economies of scale and cost control. This includes 39,840 spindles installed under the Phase-6 expansion project, which was commissioned on September 20, 2023. The company manufactures combed compact yarn, organic yarn, better cotton initiative (BCI) yarn, slub yarn and conventional combed yarn across a wide range of counts. Since the commencement of operations of its phase-6, the company has started producing poly cotton as well. The ability to manufacture diversified products across various counts and varieties provides flexibility to switch among product offerings and retain some pricing power, given the otherwise commoditised nature of yarn. Besides, its considerable presence in the B2B segments reduces expenses related to intermediaries.

Healthy ramp-up in scale of operations – Over the years, SMPL has continuously expanded its spinning capacity and has been able to ramp up the operations quickly, as reflected in healthy capacity utilisation level of close to 90% consistently. SMPL reported an all-time high revenue of Rs. 1,578 crore in FY2023 despite declining yarn realisations. The revenue was largely supported by increased volume sales to various export markets namely, Egypt, Vietnam, South Korea, among others apart from western markets. Notwithstanding softening of cotton yarn realisations, the company is expected to witness only a marginal YoY drop in revenues on the back of higher volume offtake. Besides, increased production level, led by new capacity of 39,840 spindles (to manufacture polycotton yarn) which has been operational since September 2023, is expected to support the revenues, going forward.

Established market position – SMPL has established position in several export markets like Bangladesh, Mauritius, Portugal, and Egypt. Exports accounted for 59% of SMPL's yarn sales in H1 FY2024. Its domestic clients include many large and reputed textile companies and there is no involvement of intermediaries. The company also has long relationships with its customers, which reflect SMPL's good product quality and result in repeat orders.

Proximity to cotton belt – SMPL's manufacturing facility is in Raisen district of Madhya Pradesh. It is located 30 km away from Bhopal and is well connected by NH-12. It is situated close to the cotton belt of Madhya Pradesh, Maharashtra, and Gujarat. The proximity to the cotton belt reduces its transportation costs and supports the operating profitability.

Credit challenges

Leveraged capital structure; moderation in financial profile in FY2024 – Given the large debt-funded capex towards capacity expansion in the past and working capital intensive nature of operations, SMPL's reliance on external borrowings has remained high, resulting in a leveraged capital structure with a gearing of 1.3 times as on March 31, 2023. Besides, the company is setting up a 300-bed multi-speciality hospital in Bhopal under its wholly-owned subsidiary, SSRPL. The total capex of around Rs. 153.3 crore would be funded by term loans of Rs. 98.5 crore and the balance through internal accruals. The hospital is expected to commence operations before the planned timeline of April 2024. Additionally, the company has undertaken Phase-6 expansion project in H1 FY2024 in addition to 39,840 spindles and 14 knitting machines at a total cost of Rs. 215 crore, which has been funded via debt of Rs. 157 crore, equity contribution from promoters of Rs. 10 crore and the balance Rs. 49.2 crore from internal accruals. Besides pressure on profitability in FY2024 due to weakening gross contribution margin emanating from unfavourable price differential between cotton yarn and cotton, SMPL's debt coverage indicators are expected to moderate in FY2024. Nonetheless, these are expected to recover from FY2025 on the back of improving operating leverage of all the spinning units, improvement in contribution margins and ramp-up of operations of the hospital. This remains a key rating monitorable.

Pricing pressure owing to non-integrated operations and fragmented industry structure – The spinning industry is highly fragmented with a significant share of unorganised players. While SMPL manufactures a wide variety of yarns with different count range, its presence predominantly in the yarn segment limits its ability to pass on the increase in raw material costs.

Exposure to volatility in cotton/yarn prices – The requirement of stocking cotton during the harvest season results in working-capital intensive operations and exposes SMPL's profit margins to fluctuation in cotton prices. SMPL's OPM plummeted to 11.0% in FY2023 due to weakening gross contribution margin, though it improved marginally to 11.3% in H1 FY2024, indicating modest recovery of gross contribution margins coupled with cost-saving measures undertaken by the company.

Liquidity position: Adequate

SMPL's liquidity position is **adequate** supported by healthy cash flow from operations. Notwithstanding the decline in gross contribution levels in the current fiscal, SMPL's retained cash flows are expected to remain adequate in the range of Rs. 140-150 crore in FY2024, supported by increased yarn production and additional export benefits. Besides, the liquidity position is supported by long residual tenure of loans of 10 years. SMPL's average utilisation of the sanctioned Rs. 260 crore working capital limits stood at 57% during August 2022 to July 2023. The company's sanctioned working capital limits have increased to Rs. 260 crore in December 2023 to meet the incremental working capital requirements. The company incurred capex of ~Rs. 135 crore towards the hospital project and ~Rs. 219.7 crore towards Phase-6 expansion project in FY2023 and H1 FY2024. The remaining capex towards the hospital project of about Rs. 18 crore would be incurred in Q3 FY2024, funded by internal accruals. These projects have been funded by debt of ~Rs. 258 crore and equity contribution of Rs. 10 crore from the promoters and the balance via internal accruals. The cash generation from the business is likely to remain sufficient against debt repayments of Rs. 63.2 crore in FY2024 and Rs. 57.0 crore in FY2025. The company has no major capex plans in FY2025, other than the maintenance capex.

Rating sensitivities

Positive factors – ICRA could upgrade SMPL's ratings if there is a substantial growth in its scale of operations and profits, aided by a successful ramp-up of capacities, leading to an improvement in credit metrics and liquidity position such that SMPL's consolidated net debt-to-operating profit remains below 2.0 times on a sustained basis.

Negative factors – Pressure on the ratings may emerge if any sharp decline in revenues and profits or any large debt-funded capex adversely impacts its credit metrics or liquidity position. Specifically, SMPL's consolidated debt service coverage ratio (DSCR) remaining below 1.6 times on a sustained basis, would be a negative factor.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Indian Textiles Industry – Spinning
Parent/Group support	Not applicable

Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of SMPL along with its wholly-owned subsidiary, SSRPL, which is setting up a greenfield hospital in Bhopal. As on March 31, 2023, the company had one subsidiary, enlisted in Annexure-2.

About the company

SMPL is promoted by the Agrawal family of Bhopal and was incorporated in 2010. SMPL is a part of the Sagar Group and is involved in cotton yarn spinning in the counts of 20-40s. Its manufacturing facility is located in Raisen, MP and has an installed capacity of 1,90,944 spindles as on March 31, 2023. Following the commencement of operations of the phase-6 unit in September 2023, the installed capacity has increased to ~2,30,000 spindles. The company commenced its operations in 2013 with a capacity of 33,120 spindles (7,000 MT). The company undertook phased capacity expansion, which led to an increase in the spinning capacity to 33,330 MT per annum when run in three shifts at 100% utilisation. It produces 100% cotton yarn under the brand name, SAGAR YARN. Besides the spinning capacity, the company has 30 knitting looms.

It has one subsidiary, SSRPL. While the company has no operations at present, it has recently set up a greenfield multi-specialty hospital in Bhopal. The commercial operations are expected to commence in Q4 FY2024.
The Sagar Group caters to infrastructure, education and textiles verticals. The Group launched its first real-estate project in 1983. In 2001, the Group forayed into the field of education with its flagship education venture, Sagar Public School, in Bhopal. At present, the Group is operating five schools, three engineering institutes, one B-school, one pharmacy institute, several real-estate projects and a spinning mill in Bhopal.

Key financial indicators (audited)

	FY2022	FY2023	H1 FY2024 (Prov)
Operating income	1,219.9	1,578.4	672.6
PAT	95.2	62.0	21.9
OPBDIT/OI	17.2%	11.0%	11.3%
PAT/OI	7.8%	3.9%	3.2%
Total outside liabilities/Tangible net worth (times)	1.9	1.4	
Total debt/OPBDIT (times)	2.5	2.9	
Interest coverage (times)	8.2	7.2	

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years							
		Type	Amount rated (Rs. crore)	Amount outstanding as of Aug 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022		Date & rating in FY2021			
					Nov 27, 2023	Oct 06, 2022	Jun 22, 2022	Jan 10, 2022	Jun 18, 2021	Mar 11, 2021	Feb 12, 2021	Jan 13, 2021	Dec 31, 2020
1	Cash Credit	Long term	260.00	--	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	
2	Term Loans	Long term	442.29	442.29	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	
3	Credit exposure Limit	short term	16.00	--	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	
4	Unallocated Limit	Long term and short term	29.90	--	[ICRA]A-(Stable)/ [ICRA]A2+	[ICRA]A-(Stable)/ [ICRA]A2+	-	-	-	-	-	-	
5	Unallocated Limit	Long-term	-	--	-	-	-	-	-	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	
6	Issuer Ratings	Long-term	-	--	-	-	-	-	-	[ICRA]A-(Stable); Withdrawn	[ICRA]A-(Stable); Put on notice for Withdrawn	[ICRA]A-(Stable)	[ICRA]A-(Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long Term - Fund Based Cash Credit	Simple
Long Term - Fund Based Term loan	Simple
Short Term – Non-Fund Based	Very Simple
Long Term/Short Term Unallocated	Not Applicable

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 analysing 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 are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Cash Credit**	-	-	-	260.00	[ICRA]A-(Stable)
NA	**Term Loans**	FY2015	8.5-9.0%	FY2033	442.29	[ICRA]A-(Stable)
NA	**Credit exposure Limit**	-	-	-	16.00	[ICRA]A2+
NA	**Unallocated Limit**				29.90	[ICRA]A-(Stable)/[ICRA]A2+

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Sagar Manufacturing Private Limited	Rated Entity	Full Consolidation
Sagar Services & Resources Private Limited	100.00%	Full Consolidation

Source: Company

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