

January 31, 2020

Nilons Enterprises Private Limited: Ratings reaffirmed; outlook on long-term rating revised to Negative from Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-Term, Fund-based – Term Loan	27.00	27.00	[ICRA]BBB-; Reaffirmed and outlook revised to Negative from Stable
Long-Term, Fund-based – Cash Credit	68.70	68.70	[ICRA]BBB-; Reaffirmed and outlook revised to Negative from Stable
Short-Term, Non-Fund Based	0.30	0.30	[ICRA]A3; Reaffirmed
Long-Term / Short Term – Unallocated	4.00	4.00	[ICRA]BBB-/[ICRA]A3; Reaffirmed and outlook revised to Negative from Stable
Total	100.00	100.00	

*Instrument details are provided in Annexure-1

Rationale

The revision in outlook on the long-term rating takes into consideration the decline in operating profit margin and net losses incurred by Nilons Enterprises Private Limited (NEPL or the company) in FY2019, on account of aggressive sale strategy undertaken by the company during FY2019, which included aggressive pricing as well as sales incentives for its stockists. The operating profit margin due to such developments coupled with much lower than anticipated sales, declined from 7.7% in FY2018 to 2.1% in FY2019 which also included a one-time provision created by the company for payment of sales incentives to its stockists. High depreciation and interest expenses further resulted in a net loss of Rs. 12.2 crore in FY2019. ICRA, however notes that the operating profit margin of the company has rebounded to 9.9% (provisional financials) in H1FY2020 because of roll back of extra incentives and also due to rise in realisations. Nonetheless, sustainability of profit margins for the full year FY2020 and going forward, remains critical from the credit perspective.

The ratings reaffirmation continues to draw comfort from the long operating history of the Nilon's group and experience of its management in the food industry. Further, NEPL enjoys healthy brand recognition and market position especially in the Hindi speaking regions of India and exhibits pan-India geographic presence with strong distribution network of around 4,000 distributors. The ratings further take into account NEPL's diversified product profile with continued focus on introducing new variants within current product portfolio to strengthen its revenue base.

The ratings, however, continue to remain constrained by high working capital intensity exhibited by NEPL, in line with the nature of business it is engaged in. Seasonal raw material procurement generally results in high inventory carrying costs for the company. Furthermore, NEPL's profitability remains vulnerable to fluctuations in raw material procurement prices as well as intense competition from numerous organised as well as unorganised players in the industry, which limits its pricing flexibility.

ICRA also notes that BanyanTree Growth Capital II (BanyanTree) and Lesma Ltd (Lesma) have invested in NEPL by way of compulsory convertible debentures (CCDs). As per the shareholders agreement with BanyanTree, the strategic buyout was expected to be carried out by September 30, 2019; however, the same has not happened. As discussed with the management, the timeline for strategic sale is malleable and neither the company nor the promoters are liable to provide an exit to the investors, in case the said strategic buyout does not take place within the stipulated timeline. The timeline and terms of exit by the third-party investors will be closely monitored by ICRA going forward and will remain a key rating monitorable.

Key rating drivers and their description

Credit strengths

Long operating history of the Nilon's Group and experience of the management in the food industry – Nilon's Group (which comprised NEPL along with group companies Sanghavi Foods Private Limited and Sanskar Recipes Private Limited, now merged with NEPL) has a long-standing operating track record. The experience of NEPL's management spans over decades, which has helped NEPL establish its brand over the years.

Healthy brand recognition and market position; pan-India geographic presence with strong distribution network – NEPL enjoys healthy brand recognition and market position in a vast part of India, especially in the Hindi-speaking regions of the country. The company has a strong distribution network comprising over 4,000 distributors, which ensures effective market penetration and brand recognition.

Diversified product profile with focus on introducing new variants within current product portfolio to strengthen revenue base – NEPL demonstrates diversified product profile that includes pickles, candied fruits, chutneys, jams and ketchups and spices, amongst others. Such diversified product profile ensures minimal susceptibility of company's operations to product-specific risks. The company focuses on introducing new variants within its current product portfolio in order to strengthen its revenue base. In the current year, company has launched new products such as dry fruits, ready to cook foods, breakfast cereals and soups.

Credit challenges

Net losses incurred in FY2019; weak coverage indicators – NEPL incurred net loss of Rs 12.2 crore in FY2019 primarily on aggressive sales target and strategies adopted for FY2019, which resulted in higher overheads (employee cost and one-time provision created for payment of sales incentives) and also adverse raw material costs along with lower realization levels. However, ICRA notes that the company has shown signs of recovery and has reported a net profit of Rs. 6.0 crore for H1FY2020 (on provisional basis) on account of improvement in realisations as well as roll back of aggressive incentive plans adopted last year. Nonetheless, sustainability of the profit margins in the near to medium term remains critical from credit perspective.

High working capital intensity inherent in the nature of business – NEPL exhibits high working capital intensity as inherent in the industry it operates in. The company recorded working capital intensity of 21% in FY2019. NEPL undertakes seasonal procurement of raw material, which results in high inventory levels at year end, thus leading to higher working capital requirements for the company.

Profitability remains vulnerable to raw material procurement prices – Given the commoditized nature of key raw material procured by NEPL, its profitability remains vulnerable to any fluctuations in raw material procurement prices. The company has limited scope for passing the raw material price fluctuations to its customers, which could deteriorate its margins in an eventuality of steep increase in raw material procurement costs.

Intense competition from both organised and well as unorganised players in the food industry – NEPL operates in the food industry which is characterized by the presence of several organised as well as unorganised players. It has to compete with numerous players in the domestic market, which limits its ability to command premium over its products. NEPL plans to focus more on high-margin products, which could strengthen its profitability and thus giving some comfort against the risks pertaining to intense competition from peers.

Liquidity Position: Stretched

The liquidity position of the company is stretched with net losses incurred in FY2019 and high working capital intensity of operations. The company had external term-loans of Rs. 24.75 crore as on March 31, 2019 with scheduled repayments of Rs. 6.2 crore, Rs. 5.8 crore and Rs. 5.8 crore in FY2020, FY2021 and FY2022 respectively. It also plans to incur a capex of ~Rs. 8.0 crore in FY2020 for capacity addition and modernization. It had free cash and cash equivalents of Rs. 4.33 crore as on September 30, 2019 and the average utilisation of fund-based limits has remained high at 90% during the past 15 months as on September 2019. Recovery of margins in HFY2020 however, provides cushion to liquidity and continuation of the same remains critical for the improvement of the liquidity profile.

Rating sensitivities

Positive triggers: A rating upgrade is unlikely in the near term. The outlook on the long-term rating could be revised to Stable if there is a) significant ramp up of operations and improvement in profitability on a sustained basis b) if the DSCR is above 2.0 times on a sustained basis.

Negative triggers: Ratings may be downgraded if there is any further deterioration in margins; and if the DSCR is below 1.5 times.

Analytical approach:

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not Applicable
Consolidation / Standalone	The ratings are based on the standalone financial statements of the rated entity.

About the company:

Promoted by the Jalgaon (Maharashtra) based Sanghavi family, NEPL is engaged in the manufacturing and marketing of wide range of food products such as pickles, papads, tooty-fruity, sauces, vermicelli, macaroni, tomato ketchup and jams, spices, instant mixes, and cooking pastes. The company markets all its products under the brand name of “Nilon’s”. It has five manufacturing units located at Jalgaon (four units) in Maharashtra and Dalgaon (single unit) in Assam. Its group companies, Sanghavi Foods Private Limited ([ICRA]BBB-(Stable)/[ICRA]A3 withdrawn) and Sanskar Recipes Private Limited were merged with NEPL in FY2018.

Key financial indicators

	FY2018 (Audited)	FY2019 (Audited)	H1FY2020 (Provisional)
Operating Income (Rs. crore)	283.8	294.7	162.0
PAT (Rs. crore)	3.4	-12.2	6.0
OPBDIT/OI (%)	7.7%	2.1%	9.9%
RoCE (%)	8.5%	-0.8%	11.2%
Total Debt/TNW (times)	0.5	0.6	0.6
Total Debt/OPBDIT (times)	2.9	12.9	2.3
Interest coverage (times)	2.1	0.6	3.5

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Chronology of Rating History for the Past 3 Years							
		Current Rating (FY2020)							
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2019			Date & Rating in FY2018	Date & Rating in FY2017
					31-Jan-20	10-Dec-18	6-Jul-18		
1	Term Loan	27.00	24.75	[ICRA]BBB-(Negative)	[ICRA]BBB-(Stable)	[ICRA]BBB-(Stable)	-	[ICRA]BBB-(Stable)	
2	Cash Credit	68.70	-	[ICRA]BBB-(Negative)	[ICRA]BBB-(Stable)	[ICRA]BBB-(Stable)	-	[ICRA]BBB-(Stable)	
3	Non-Fund Based – LER	0.30	-	[ICRA]A3	[ICRA]A3	[ICRA]A3	-	[ICRA]A3	
4	Unallocated amount	4.00	-	[ICRA]BBB-(Negative)/[ICRA]A3	[ICRA]BBB-(Stable) / [ICRA]A3	[ICRA]BBB-(Stable) / [ICRA]A3	-	-	

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 www.icra.in

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	March 2018	NA	March 2024	27.00	[ICRA]BBB- (Negative)
NA	Cash Credit	NA	NA	NA	68.70	[ICRA]BBB- (Negative)
NA	Non-Fund Based – LER	NA	NA	NA	0.30	[ICRA]A3
NA	Unallocated amount	NA	NA	NA	4.00	[ICRA]BBB- (Negative) / [ICRA]A3

Source: Nilons Enterprises Private Limited

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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