

March 16, 2023

Gokak Textiles Limited: Rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. Crore)	Current Rated Amount (Rs. crore)	Rating Action
Short Term – Unallocated Limits	50.00	50.00	[ICRA]A4; Reaffirmed
Total	50.00	50.00	

*Instrument details are provided in Annexure-I

Rationale

ICRA has taken a consolidated view of Gokak Textiles Limited (GTL), which includes its subsidiary, while assigning the credit rating, given the common management and significant operational and financial linkages among them.

The reaffirmation of GTL's rating favourably factors in the company's strong parentage — Shapoorji Pallonji and Company Private Limited (SPCPL), rated [ICRA]A-(Stable)/[ICRA]A2+. The parent provides regular financial support in the form of interest-bearing unsecured loans/inter-corporate deposits (ICDs) (Rs 202.5 crore as on March 31, 2022) to meet the company's funding requirements. ICRA notes that the company has repaid all its external borrowings in FY2020 and has no external debt in the books as on date. Consequently, GTL will remain dependent on SPCPL to meet its cash flow mismatches and other funding requirements.

ICRA notes that, the company has proposed for a composite scheme of arrangement, wherein, there would be reduction of share capital and re-organisation of GTL's reserves and the merger of Suryoday One Energy Private Limited (another Shapoorji Pallonji Group entity) with GTL. This scheme of arrangement is pending for the NCLT approval at present and is expected to be completed in FY2024 post receipt of final approval from the NCLT.

The rating is, however, constrained by weak operational and financial performances for the last few years, characterised by stretched liquidity, negative net worth and inadequate coverage metrics owing to a moderate level of revenues and continuous losses at the operating level. The rating also considers the highly fragmented and competitive industry structure, which restricts pricing flexibility and exposes the company's earnings to volatility in cotton prices.

Key rating drivers and their description

Credit strengths

Strong parentage with demonstrated track record of regular support – SPCPL, rated [ICRA]A- (Stable)/[ICRA]A2+, is the holding company of GTL with 73.56% stake. GTL has received funding support from SPCPL over the years, by way of preference shares (Rs. 175 crore) and interest-bearing unsecured loans/ICDs for servicing of debt obligations. As on March 31, 2022, GTL had outstanding unsecured loans/ICDs of Rs. 202.5 crore from SPCPL on its balance sheet.

Credit challenges

Weak financial profile – GTL continued to report operating losses because of a moderate level of operating income in FY2022 and relatively higher overheads. In 9M FY2023, the performance has moderated further due to various macro factors. In 9M FY2023, they have reported an operating income of Rs. 62.5 crore with net loss of Rs. 25.9 crore. This has resulted in weak

coverage metrics and thereby a weak financial profile. The composite scheme of arrangement, which is pending with the NCLT, post completion of the same, operating profitability is expected to improve over the medium term.

Earnings exposed to fluctuations in cotton prices amid challenging demand scenario and intense competition – GTL's earnings are exposed to the volatility in cotton prices. The vulnerability is further compounded by the company's limited pricing flexibility due to intense competition and lower-than-expected demand during the recent quarters.

Environment and Social Risks

Social risks: Being in a labour-intensive segment, the entities operating in the textile sector are exposed to the risk of disruptions due to inability to properly manage human capital in terms of their safety and overall well-being. Entities also remain exposed to any major shift in consumer preferences or developments affecting discretionary consumer spending in the key markets.

Environmental risks: The industry is exposed to environmental risks, primarily through water, land use, and the impact of the climate on production as well as 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.

Liquidity position: Poor

The liquidity profile of GTL remains poor, evident from negative cash flow from operations in FY2022 and modest free cash balances of Rs. 1.3 crore as on September 30, 2022. Though there are no external debt servicing requirements, the company remains dependent on ICDs/unsecured loans (Rs. 202.5 crore as on March 31, 2022) from the promoter to meet the cash flow mismatches, particularly in the absence of any fund-based working capital limits.

Rating sensitivities

Positive factors – ICRA could upgrade the company's rating, if it is able to scale-up the operations with higher capacity utilisation becoming profitable at operating levels, on a sustained basis.

Negative factors – Downgrade pressure on GTL could arise, in case of any substantial decline in revenues and profitability or stretch in working capital cycle, leading to lower-than-expected cash accruals. Any weakening in funding support or business linkages with parent adversely affecting the credit profile may trigger a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Textile Industry - Spinning
Parent/Group support	Parent/Group Company: SPCPL The rating assigned to GTL factors in the high likelihood of its parent, SPCPL, extending financial support to it because of close business linkages between them
Consolidation/Standalone	For arriving at the rating, ICRA has considered the consolidated financials of GTL

About the company

GTL was incorporated in 2007, subsequent to a scheme of demerger of the textile arm of Forbes Gokak Limited (FGL) into a separate company. GTL has two units—a spinning mill at Gokak Falls (Karnataka) and a garment-manufacturing unit in Belgaum district of Karnataka. The spinning mill has a capacity of 69,792 spindles and other value-added yarns apart from small volumes of readymade items such as cotton canvas and terry towels. The Belgaum unit specialises in readymade knitted garments including combed polo and T-shirts for the export markets. In FY2012, the company hived off its power-generation business under a subsidiary named Gokak Power & Energy Limited (GPEL). While GTL holds a 51% stake in GPEL, the remaining 49% is held by Shapoorji Pallonji Infrastructure Capital Company Private Limited. The power generated by GPEL is primarily used by GTL for its spinning unit.

Key financial indicators (audited)

Gokak Textiles Limited (Consolidated)	FY2021	FY2022
Operating income (Rs. in Crore)	110.8	125.8
PAT (Rs. in Crore)	-38.0	-31.5
OPBDIT/OI	-10.93%	-6.24%
PAT/OI	-34.31%	-25.02%
Total outside liabilities/Tangible net worth (times)	-1.5	-1.4
Total debt/OPBDIT (times)	-31.3	-51.5
Interest coverage (times)	-0.6	-0.4

Source: Company; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation;

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2023)		Chronology of rating history for the past 3 years			
		Amount rated	Amount outstanding as of Mar 31, 2022	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
		(Rs. crore)	(Rs. crore)	March 16, 2023	December 31, 2021	September 25, 2020	-
1 Unallocated	Short Term	50.0	--	[ICRA]A4	[ICRA]A4	[ICRA]A4	-
2 Fund based bank facilities	Long Term	-	--	-	-	[ICRA]B+ (Stable); Withdrawn	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Unallocated	NA

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	Unallocated	NA	NA	NA	50.00	[ICRA]A4

Source: Gokak

Annexure II: List of entities considered for consolidated analysis

Company Name	Gokak Ownership	Consolidation Approach
Gokak Textiles Limited	100.00% (Rated Entity)	Full Consolidation
Gokak Power & Energy Limited	51.00%	Equity Method

Source: GTL Annual report FY2022

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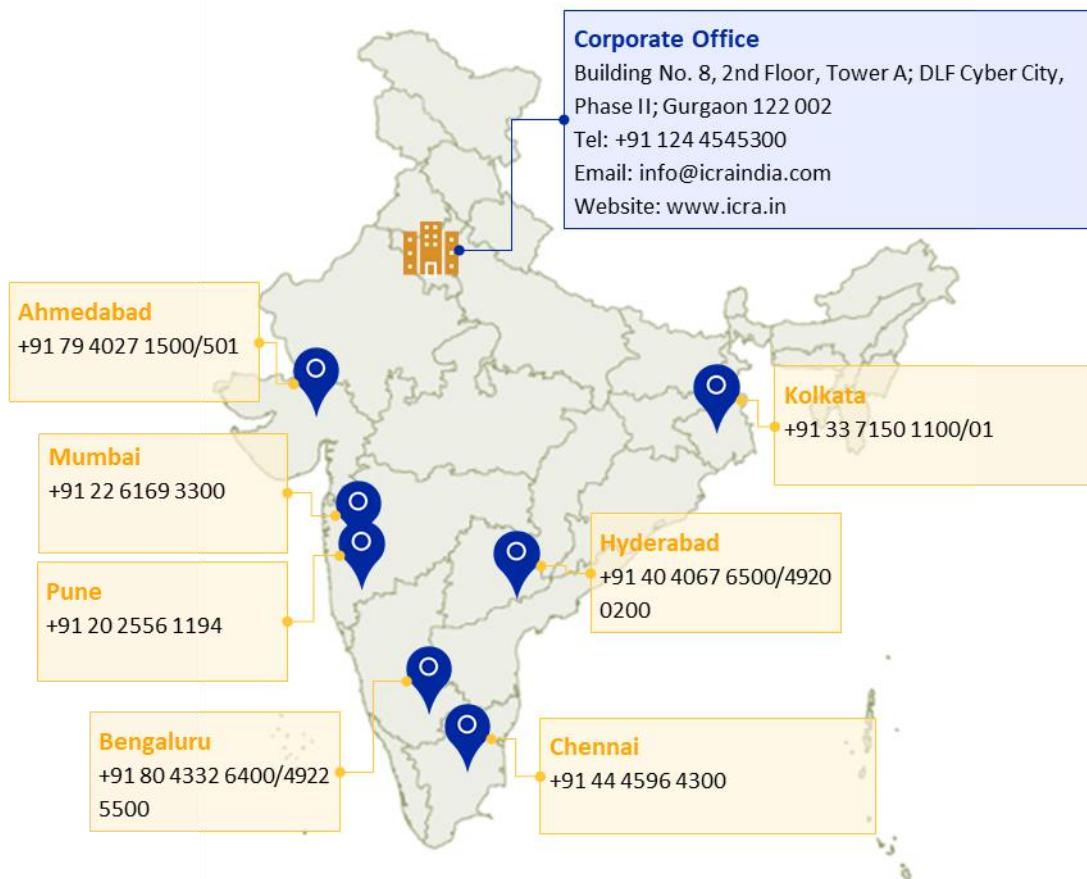
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