

Reliance Chemotex Industries Limited

February 15, 2018

Summary of rated instruments

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	52.48	30.03	[ICRA]BB+(Stable); Downgraded from [ICRA]BBB-(Negative)
Cash Credit	33.00	33.00	[ICRA]BB+(Stable); Downgraded from [ICRA]BBB-(Negative)
Standby Limit	3.00	3.00	[ICRA]A4+; Downgraded from [ICRA]A3
Non-fund based limits	34.44	35.50	[ICRA]A4+; Downgraded from [ICRA]A3
Unallocated Limit	-	21.39	[ICRA]BB+(Stable)/[ICRA]A4+; Downgraded from [ICRA]BBB-(Negative)/ [ICRA]A3
Total	122.92	122.92	

Rating action

ICRA has downgraded the long-term rating to [ICRA]BB+ (pronounced ICRA double B plus) from [ICRA]BBB- (pronounced ICRA triple B plus minus) with a Negative outlook to the Rs. 30.03-crore¹ (previously Rs. 52.48 crore) term loan facility and Rs. 33.00-crore cash credit facility of Reliance Chemotex Industries Limited (RCIL or the company). ICRA has also downgraded the short-term rating to [ICRA]A4+ (pronounced ICRA A four plus) from [ICRA]A3 (pronounced ICRA A three) which was assigned to the Rs. 3.00-crore standby limit and Rs. 35.50-crore (previously Rs. 34.44 crore) non-fund based facility of RCIL². ICRA has also downgraded the [ICRA]BB+ and [ICRA]A4+ ratings to the Rs. 21.39-crore (previously nil) unallocated limits of RCIL. The outlook on the long-term rating is Stable.

Rationale

The ratings revision takes into account the weakening operating performance of the company during the current year, with a sharp decline of 21% in its operating profitability levels, owing to escalation in power costs, leading to ~200 bps dip in its operating margins and the subsequent adverse impact on its return and debt coverage indicators as reported in H1 FY2018. ICRA also takes note of RCIL's plan to go for a debt-funded capital expenditure in the near term, which is likely to further put stress on the debt metrics. Given its high repayment liabilities, there are concerns related to adequate debt service coverage with RCIL's net cash accruals (NCA) being pressurised by the dividends paid on cumulative redeemable preference shares, which are issued to related companies and are redeemable at par starting in FY2022. Amid a sluggish demand scenario and intense competition in the textile industry, the ability to control power cost, manage raw material price as well as forex fluctuation risks effectively will also be a key monitorable from the profitability perspective. The ratings also take note of the increasing working capital borrowings in the last few months due to pressures on the liquidity front emanating from working capital blockage arising from shifting to the GST regime.

¹100 lakh = 1 crore = 10 million

²For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

The ratings, however, continue to favourably factor in the established track record of the promoters, which has facilitated in established relationship with prominent domestic suppliers of key raw materials as well as international customers. The ratings also continue to factor in the diversified product portfolio, fairly high capacity utilisation levels culminating into moderate scale of operations. The ratings draw comfort from the steady contribution from exports, which fetch higher realisations, to RCIL's total revenues.

Going forward, generating commensurate returns from the capex and favourable funding terms in terms of moratorium period and interest subsidies will be a key in determining the project viability. Amid significant debt repayment obligations and dividend payouts over the next three years, the company's ability to generate sufficient cash accruals, as well as availability of adequate bank lines to support its liquidity profile will be critical from the credit perspective.

Outlook: Stable

ICRA believes RCIL will continue to benefit from the extensive experience of its promoters and the management. However, RCIL is likely to face continued pressures on its profitability, debt protection metrics owing to the repayment obligations on its existing and proposed loans. The outlook may be revised to Positive if substantial growth in revenue and improvement in profitability levels is witnessed, thereby supporting the cash accruals, which strengthens the financial risk profile. Commensurate returns from the proposed capex, which aids in improving the debt serving ability will also be a positive rating trigger. The outlook may be revised to Negative if cash accrual is lower than expected to meet the current and proposed loans debt repayments, or there is delay in stabilisation or lack of commensurate returns from the proposed capital expenditure plan. Any further dip in profitability levels or stretch in the working capital cycle which weakens the liquidity profile will also be credit negative for the company.

Key rating drivers

Credit strengths

Established track record of the promoters with extensive experience in the textile industry - The promoter and Chairman, Mr. S.L. Shroff, has an experience of more than 40 years in the textile industry. The Managing Director, Mr. Sanjiv Shroff, son of Mr. S.L. Shroff, at present manages the overall operations of the company and has been associated with the textile industry for over 30 years. Mr. Rahul Shroff and Mr. Ameya Shroff, sons of Mr. Sanjiv Shroff are also actively involved in the business and are a part of the management.

Healthy relations with prominent domestic suppliers and international customers fetches repeat orders - The experienced and professional setup has been instrumental in developing a reliable clientele in the international markets as well as forge established relationship with key domestic suppliers of fibre and yarn, having a significant domestic market holding. Apart from Belgium, which is a key export market, RCIL exports to several countries across the world. It has a diversified customer profile including a few reputed clients and continues to focus on the export markets, as the export realisation is higher than domestic realisations. At present, its proportion of domestic sales to export is 36:64.

Fairly high capacity utilisation levels and moderate scale of operations - RCIL manufactures synthetic and blended yarn including 100% polyester, 100% viscose, 100% acrylic, 100% bamboo viscose as well as polyester/viscose, polyester/acrylic, polyester/viscose/acrylic blended yarns. These yarns (which can be produced with raw-white, or dyed fibres) are intended for knitting, weaving, upholstery, carpet, medical or other industrial end-uses. The company's products count range is from Ne 6s to Ne 50s in single, double and multi-ply yarns. With revenues of Rs. 290 crore in FY2017, RCIL's scale of operations is moderate. Its manufacturing facility is at Udaipur, Rajasthan with a current installed capacity of 53,280 spindles, which operates at a fairly high capacity utilisation. However, because of the enduring effects of demonetisation and the uncertainty pertaining to GST and its policy changes, the production volume slowed down to an extent in H1 FY2018.

Credit challenges

Persistent pressure on operating profitability since FY2016, rise in power cost in H1 FY2018 - The operating profit margin stood at ~9.5% levels over the period from FY2013 to FY2015 and declined to ~7.5% levels from FY2016 onwards due to pressures on raw materials price and power cost. The operating profit margin was lower at 7.65% in H1 FY2018 as compared to 9.55% H1 FY2017 primarily on account of higher power costs. RCIL had entered into a long-term power purchase agreement (PPA), whereby it would get power at a subsidised rate. Due to the disruptions in the supply of power at the agreed rates, the company now has to purchase power from open exchange, which in turn led to significant increase (~32% increase in H1 FY2018 over H1 FY2017) in power and fuel costs for the company, which has impinged the profitability.

Profitability vulnerable to changes in raw material prices on account of low bargaining power with suppliers and foreign-exchange fluctuations - The key raw materials for the company include polyester staple fibre (PSF), viscose staple fibre (VSF) and acrylic fibre. The raw material procurement is mainly made from the domestic market. For the variety of raw materials used by RCIL, the prices are primarily controlled by these large suppliers offering it with limited bargaining power and pricing flexibility.

Being a net exporter there is exposure to forex movements (Euro and USD). However, the company primarily hedges its receivables through forward contracts. Such effective forex hedging mechanism reduces the susceptibility of margins to unfavourable forex movement risks to a large extent.

Proposed debt-funded capex likely to increase debt levels and keep debt metrics stretched - RCIL has debt repayment obligations on its existing term loans for the next five years. ICRA also notes that it has a near term debt-funded capex plan of ~Rs. 40 crore, proposed to be funded through a debt of ~Rs. 34 crore to upgrade and expand its production capacity, which is likely to increase the debt levels and keep the debt metrics stretched in the medium term. Favourable funding terms in terms of a moratorium period and interest subsidies will be the key in determining the project viability. Generating commensurate returns from the capex is the key for its credit profile going forward, given the elevated debt levels and its consequent repayments.

Debt service coverage remain below 1 times in H1 FY2018; lower profitability affects return indicators and other debt metrics - Due to lower profitability reported in H1 FY2018, the return indicator (ROCE) declined and stood modest at ~10% while the total debt to operating profitability ratio (TD/OPBDITA) weakened to 4.4 times in H1 FY2018 as compared to 3.7 times in H1 FY2017. Besides lower profitability, the strain on the company's net cash accruals position also arise from the dividends paid on cumulative redeemable preference shares (amounting to Rs. 2.31 crore) and interest paid on unsecured loans from related companies. The preference shares issued to related companies, in which key management personnel have control or significant influence, are redeemable at par on the expiry of 20 years from the respective dates of allotment (starting in FY2022 stretching up to FY2025). However, the company is planning to convert the preference shares into equity which is likely to happen in FY2020 and will improve the capital structure and coverage indicators through reduced dividend payout. Any development on the implementation of this plan will be closely monitored. Nonetheless, in view of the current net cash accruals position and the impending debt repayments, the debt service coverage indicator (DSCR) continues to remain below 1 times in H1 FY2018. As per the H1 FY2018 financials, RCIL's gearing, however, moderated to 1.48 times (2.43 times in FY2017) attributable to the increased net worth base (post adjustment in retained earnings in INDAS reporting³).

³ Adjustment in retained earnings under INDAS of Rs. 24.21 crore (net) primarily on account of revaluation of Free Hold and lease hold land

Intense competition in the textile industry - RCIL faces competitive pressures from international as well as domestic yarn manufacturers. In the domestic market there is stiff competition and fragmentation, limiting the pricing power of textile companies and affecting their margins. Nevertheless, by the virtue of its presence in textile industry, RCIL is entitled to Government incentives in the form of interest subsidies, duty drawback scheme and duty-credit facilities, which provide sizeable support to its profitability.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

[Corporate Credit Rating Methodology](#)

[Rating Methodology for Entities in the Textiles - Spinning-Manmade and others](#)

About the company:

Incorporated in 1977, RCIL is a manufacturer of synthetic and blended yarn, including 100% polyester, 100% viscose, 100% acrylic, 100% bamboo viscose as well as polyester/viscose, polyester/acrylic, polyester/viscose/acrylic blended yarns. RCIL is promoted by Mr. S.L. Shroff and his son Mr. Sanjiv Shroff is at present the Managing Director of the company. The shares of RCIL are listed on the Bombay Stock Exchange since 2001. Based out of Mumbai, the company has a branch office in Kolkata and Delhi. Its manufacturing facility is located in Udaipur, Rajasthan and it has a current installed capacity of 53,280 spindles.

Mr. S.L. Shroff, the promoter and Chairman Emeritus, has an extensive experience of more than five decades in the textile industry. At present, Mr. Sanjiv Shroff manages the overall operations of the company and has over three decades experience in the textile industry. Mr. Shroff's sons - Mr. Rahul Shroff and Mr. Ameya Shroff are also a part of the management.

Two other companies held by the same promoter group are Modern Fibotex India Limited and Spell Fashions Private Limited, which manufacture and trade in fabric, primarily silk and shirts, respectively.

In FY2017, the firm reported a net profit of Rs. 6.70 crore on an operating income (OI) of Rs. 291.90 crore, as compared to a net profit of Rs. 2.53 crore on an OI of Rs. 257.13 crore in the previous year.

Key financial indicators (Audited)

	FY2016	FY2017
Operating Income (Rs. crore)	257.13	291.90
PAT (Rs. crore)	2.53	6.70
OPBDIT/ OI (%)	7.3%	7.8%
RoCE (%)	10.0%	12.9%
Total Debt/ TNW (times)	3.18	2.43
Total Debt/ OPBDIT (times)	6.03	4.19
Interest Coverage (times)	1.22	1.71
NWC/ OI (%)	15%	10%

Status of non-cooperation with previous CRA: As per CRISIL's press release dated October 31, 2017, RCIL's ratings of CRISIL BB/Negative/CRISIL A4+ to Rs. 96.8 crore bank facilities were reaffirmed and moved to ISSUER NOT CO-OPERATING category.

Any other information: None

Rating history for last three years:

Instrument	Current Rating (FY2018)			Chronology of Rating History for the past years			
	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
1 Term Loans	Long Term	30.03	30.03*	[ICRA]BB+ (Stable) February 2018	[ICRA]BBB- (Negative) February 2017	[ICRA]BBB- (Negative) June 2016	[ICRA]BBB (Stable) August 2015
2 Cash Credit	Long Term	33.00		[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)	[ICRA]BBB (Stable)
3 Standby Limit	Short Term	3.00		[ICRA]A4+	[ICRA]A3	[ICRA]A3	[ICRA]A3+
4 Non-fund based limits	Short Term	35.50		[ICRA]A4+	[ICRA]A3	[ICRA]A3	[ICRA]A3+
5 Unallocated Limit	Long and Short Term	21.39		[ICRA]BB+ (Stable)/ [ICRA]A4+	-	-	-

*as on December 31, 2017

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 Loans	FY2011	11.75%	FY2023	30.03	[ICRA]BB+(Stable)
NA	Cash Credit				33.00	[ICRA]BB+(Stable)
NA	Standby Limit				3.00	[ICRA]A4+
NA	Non-fund based limits				35.50	[ICRA]A4+
NA	Unallocated Limit				21.39	[ICRA]BB+ (Stable)/ [ICRA]A4+

Source: RCIL

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