

Kapotex Industries Private Limited

March 07, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. Crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term loans	4.80	3.68	[ICRA]B+(Stable); downgraded from [ICRA]BB(Stable)
Long-term Fund-based and Non-fund based facilities	(3.50)	(3.50)	[ICRA]B+(Stable); downgraded from [ICRA]BB(Stable)
Short-term Fund-based facilities	5.00	5.00	[ICRA]A4; reaffirmed
Short-term Non-fund based	7.85	5.60	[ICRA]A4; reaffirmed
Total	17.65	14.28	

*Instrument details are provided in Annexure-1

Rating action

ICRA has revised the long-term rating of [ICRA]BB (pronounced ICRA double B) to [ICRA]B+ (pronounced ICRA B plus) to the Rs. 3.68-crore¹ (earlier Rs. 4.80 crore) term loan facility of Kapotex Industries Private Limited (KIPL or the company)². The outlook on the long-term rating is Stable. ICRA has re-affirmed the [ICRA]A4 (pronounced ICRA A four) rating to the Rs. 5.00-crore short-term fund-based facility and the Rs. 5.60-crore (earlier Rs. 7.85 crore) short-term non-fund based facility of KIPL. The cash credit facility of Rs. 1.50 crore, which is a sub-limit within the fund-based facility of Rs. 5.00 crore and the Capex Letter of Credit of Rs. 2.00 crore, which is a sub-limit of the term loan, have been rated at [ICRA]B+.

Rationale

The revision in the long-term rating takes into account the sharp deterioration in the financial profile of KIPL as indicated by a decline in revenues and profitability on account of a change in the product mix of the company as well as a slowdown in demand, which in turn has led to the weakening of coverage indicators. The operating income declined from Rs. 22.30 crore in FY2016 to Rs. 14.76 crore in FY2017, with erosion in margin to 8.88% in FY2017 from 11.94% in FY2016 following inventory losses. The gearing also deteriorated to 1.12 times as on March 31, 2017 compared to 0.49 times as on March 31, 2016 following debt-funded capex incurred by the company. Increase in debt levels has also led to weaker coverage indicators as reflected by the Total Debt/OPBDITA of 7.69 times as on March 31, 2017 over 1.57 times as on March 31, 2016. The ratings also take into account, the stretched liquidity position of the company with working capital intensity of 47% as on March 31, 2017 and the susceptibility of the margins to the competitive pressure from international players.

¹100 lakh = 1 crore = 10 million

² For 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 incorporate the established experience of the directors of KIPL in the wool yarn business, and the operational efficiencies likely to arise from its forward integration initiative and its present diversified customer base.

Outlook: Stable

ICRA believes KIPL will continue to benefit from the extensive experience of its promoters. The outlook may be revised to Positive if KIPL is able to operate the newly set up plant at healthy utilisation levels, post commissioning, report healthy growth in revenue and profitability, as well as efficiently manage its working capital requirement. The outlook may be revised to Negative if the company is not able to ramp up the operations post commissioning of the new unit, and also if its inflow of orders remains low, or the stretch in the working capital cycle weakens liquidity further.

Key rating drivers

Credit strengths

- **Long experience and technical qualification of the promoters in the wool/textile industry** – KIPL was established in 2008 by Mr. Rajiv Kapur and Mr. Varun Kapur who are technically qualified and have a wide experience in the field of manufacturing and marketing of woolen yarns for the carpet industry. Mr. Rajiv Kapur has an experience of more than three decades in this industry, which has helped the company to establish its relationship with a few big players in the rugs and carpets industry in the international market.
- **Diversified customer base** - With an increase in the share of low grade wool yarn, there have been additions to the existing client base of the company, resulting in a diversified client profile as indicated by the top three customers, accounting for ~30% of the total sales in FY2017 compared to ~46% of the total sales in FY2016. The company has also established relationship with some of its customers which has led to repeat business.

Credit challenges

- **Decline in sales volumes following change in product mix, coupled with a global slowdown in the market leads to de-growth in revenues** - In FY2016, the company had reported a year-on-year decline in revenue on account of a change in the product mix. Coupled with this, the marginal decline in sales volume following slow demand conditions, had also contributed to the decline in revenues in FY2016. Demand continued to remain slow in FY2017 also and post the Brexit vote in June 2016, demand slowed down further in the U.K. and the European markets where most of its exports are made. Low valued export orders following the weakening of the British pound after the Brexit vote also dented the realisations in FY2017. The operating income (OI) has declined to Rs. 14.76 crore in FY2017 compared to Rs. 22.30 crore in FY2016. In the current fiscal also the company has reported lower sales.
- **Drop in profitability levels in FY2017 primarily on account of inventory losses incurred** - Operating Profit Margin (OPM) in FY2016 has marginally declined to 11.94% compared with 12.59% in FY2015 on account of the decline in average sales realizations as a result of the change in product mix. OPM in FY2017 declined further to 8.88% from 11.94% in FY2016 because of- inventory losses incurred coupled with high valued imports against low valued export orders post the Brexit vote.
- **Stretched liquidity profile because of high debtor and inventory levels and faster payment to creditors**- KIPL's working capital intensity has increased to ~47% in FY2017 over ~13% in FY2016. This is driven by the need to stock various types of wool following the seasonal availability of the same. In March 2017, some bulk purchases of raw material were also made as the prices were low, which has led to an increase in inventory levels as indicated by inventory days of 135 days as on March 31, 2017 compared to 129 days as on March 31, 2016. The extended credit period provided to the customers because of the slowdown in the market has led to an increase in debtor days from 31 days as on March 31, 2016 to 84 days as on March 31, 2017. Cash payment made to the suppliers of non-New Zealand wool has led to a significant decline in

payable days to 58 days as on March 31, 2017 from 135 days as on March 31, 2016.

- **Debt funded capex has led to a moderately leveraged capital structure and moderate debt coverage indicators as on March 31, 2017** - Total borrowings have increased to Rs. 10.08 crore as on March 31, 2017, from Rs. 4.18 crore as on March 31, 2016, following the additional term loan availed for funding the capex, coupled with an increase in unsecured loans and working capital borrowings. The capital structure of the firm remained moderately leveraged with a gearing of 1.12 time as on March 31, 2017 over 0.49 time as on March 31, 2016. With increase in debt levels, the coverage indicators have declined and remained moderate, as reflected by OPBDITA/ Interest of 3.15 times (4.97 times as on March 31, 2016) and Total Debt/OPBDITA of 7.69 times (1.57 times as on March 31, 2016) as on March 31, 2017.
- **Margins remain exposed to forex rate fluctuation risks, raw material price fluctuations and the stiff competition** - As the company earns its revenue primarily from exports, its margins are susceptible to foreign exchange rates fluctuations in the absence of any hedging policy. However, the risk is partly mitigated due to ~70% of the procurement being import dominated. Raw material cost constitutes a significant percentage of total expenses incurred, therefore, any increase in wool prices and inability to pass on the increase in raw material price could affect KIPL's profitability. However, with ~60% of the procurement being order-backed, this mitigates the raw material price fluctuation risk to an extent. KIPL faces stiff competition from overseas players in this sector from other international spinners. However, the company has an edge over international players in terms of lower labor costs.

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

Links to applicable criteria:

[Corporate Credit Rating – A Note on Methodology](#)

[Rating Methodology for Entities in the Textiles Industry – Spinning](#)

About the company

Kapotex Industries Pvt. Ltd. (KIPL or the company) had been incorporated on May 29, 2008, by Mr. Rajiv Kapur and Mr. Varun Kapur. The company manufactures and exports woollen yarn in the form of worsted spun yarn and carded yarn. The wool yarn manufactured by the company finds application in the manufacturing of rugs, floor coverings and carpets. KIPL's registered office is at Kurla, Mumbai, and its manufacturing unit is at the Gujarat Industrial Development Corporation (GIDC) area of Valsad, with an installed production capacity of 1,000 metric tonnes per annum. The company has set up another unit at GIDC, adjacent to the prevailing unit where dyeing operations will be carried out and two additional lines for carding has been installed.

In FY2017, KIPL reported a net profit of Rs. 0.48 crore on an operating income of Rs. 14.76 crore, as compared to a net profit of Rs. 1.24 crore on an operating income of Rs. 22.30 crore during the previous year.

Key Financial Indicators (Audited)

Particulars	FY2016	FY2017
Operating income (Rs. crore)	22.30	14.76
PAT (Rs. crore)	1.24	0.48
OPBDIT/ OI (%)	11.94%	8.88%
RoCE (%)	21.63%	7.29%
Total Debt/ TNW (times)	0.49	1.12
Total Debt/ OPBDIT (times)	1.57	7.69
Interest Coverage (times)	4.97	3.15
NWC/ OI (%)	13%	47%

*OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortisation; PAT: Profit after Tax; NWC: Net Working Capital; RoCE: Return on Capital employed; TNW: Tangible Net Worth
Source: Financial statements of KIPL and ICRA research*

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for last three years:

Table:

S. No	Name of Instrument	Current Rating (FY2018)			Chronology of Rating History for the past 3 years			
		Type	Rated amount	Amount Outstanding	Date & Rating	Date & Rating in FY2017	Date & Rating in FY2016	Date & Rating in FY2015
			(Rs. crore)	(Rs. crore)				
					Mar-18	Dec-16	Oct-15	Sep-14
1	Term Loan	Long-term Fund-based	3.68	3.68	[ICRA]B+ (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)
2	Cash Credit	Long-term Fund-based	(1.50) [#]	-	[ICRA]B+ (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)
3	Capex Letter of Credit	Long-term Non-fund based	(2.00) [*]	-	[ICRA]B+ (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)	[ICRA]BB (Stable)
4	Export packing Credit/Packing credit in Foreign Currency/ Export Bill Discounting	Short-term Fund-based	5.00	-	[ICRA]A4	[ICRA]A4	[ICRA]A4	[ICRA]A4
5	Letter of Credit	Short-term Non-fund based	5.00	-	[ICRA]A4	[ICRA]A4	[ICRA]A4	[ICRA]A4
6	Bank Guarantee	Short-term Non-fund based	0.50	-	[ICRA]A4	[ICRA]A4	[ICRA]A4	[ICRA]A4
7	Credit Exposure Limit	Short-term Non-fund based	0.10	-	[ICRA]A4	[ICRA]A4	[ICRA]A4	[ICRA]A4

#Sub limit of Export Packing Credit/Packing credit in Foreign Currency/ Export Bill Discounting facility of Rs. 5 crore

*Sub-limit within the term loan

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

Name of the instrument	Date of issuance	Coupon rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
Term Loan	Dec-15	13.15%	Jan-21	3.68	[ICRA]B+(Stable)
Cash Credit				(1.50) [#]	[ICRA]B+(Stable)
Capex Letter of Credit	-	-	-	(2.00)*	[ICRA]B+(Stable)
Export packing Credit/Packing credit in Foreign Currency/ Export Bill Discounting	-	-	-	5.00	[ICRA]A4
Letter of Credit				5.00	[ICRA]A4
Bank Guarantee	-	-	-	0.50	[ICRA]A4
Credit Exposure Limit				0.10	[ICRA]A4

[#]Sub limit of Export Packing Credit/Packing credit in Foreign Currency/ Export Bill Discounting facility of Rs. 5 crore

*Sub-limit within the term loan

Source: KIPL

Contact Details

Analyst Contacts

K. Ravichandran

+91 44 45964301

ravichandran@icraindia.com

Suprio Banerjee

+91 22 61143443

supriob@icraindia.com

Rupa Pandey

+91 22 61143456

rupa.pandey@icraindia.com

Nijara Kalita

+91 22 61143455

nijara.kalita@icraindia.com

Relationship Contact

Jayanta Chatterjee

+91 80 4332 6401

jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani

Tel: +91 124 4545 860

naznin.prodhani@icraindia.com

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

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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.

For more information, visit www.icra.in

ICRA Limited

Corporate Office

Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002

Tel: +91 124 4545300

Email: info@icraindia.com

Website: www.icra.in

Registered Office

1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001

Tel: +91 11 23357940-50

Branches

Mumbai + (91 22) 24331046/53/62/74/86/87

Chennai + (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,

Kolkata + (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,

Bangalore + (91 80) 2559 7401/4049

Ahmedabad+ (91 79) 2658 4924/5049/2008

Hyderabad + (91 40) 2373 5061/7251

Pune + (91 20) 6606 9999

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