

December 04, 2019

Fortune Foam Pvt. Ltd.: Long-term rating upgraded to [ICRA]BB- (Stable); Short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund Based TL	24.00	13.59	[ICRA]BB- (Stable); upgraded from [ICRA]B+ (Stable)
Long Term - Fund Based/ CC	7.50	18.00	[ICRA]BB- (Stable); upgraded from [ICRA]B+ (Stable)
Long Term / Short Term - Unallocated	0.50	0.41	[ICRA]BB- (Stable)/[ICRA]A4; Long term rating upgraded from [ICRA]B+ (Stable), short term rating [ICRA]A4 reaffirmed
Total	32.00	32.00	

*Instrument details are provided in Annexure-1

Rationale

The rating upgrade positively factors in expected improvement in operating profit margins in the medium term on the back of lower toluene di-isocyanate (TDI) and polyol prices and increased revenue contribution from mattress sales. The operating profit margins improved to 11.17% in 7MFY2020 and 6.40% in FY2019 from 5.91% in FY2018 owing to sharp reduction in prices of TDI and polyol since April 2018 which are the key raw materials required for manufacturing of PU (Polyurethane) foam. The revenues also increased over the years to Rs. 98.49 crore in FY2019 from Rs. 46.78 crore in FY2017 owing to increased sales of PU foam and addition of branded products, including mattresses and pillows to its product profile in FY2017. The ratings also factor in the extensive experience of the promoters in the PU foam industry and their continued financial support by promoters in the form of unsecured loans. However, the rating is constrained by the company's weak financial risk profile with gearing at 5.66 times, total outside liability/net worth at 7.54 times as on October 31, 2019 owing to low net worth levels and total debt/OPBDITA of 5.40 times in 7MFY2020 owing to high debt and modest profitability levels. Further, high repayment obligations and low cash accruals have resulted in debt service coverage ratio (DSCR) being less than one in the past three years with the shortfall met by timely infusion of unsecured loans from promoters. However, the DSCR is expected to improve going forward with improvement in profitability margins and revenues to improve marginally. The ratings are further constrained by high working capital intensive nature of operations owing to high inventory levels; highly competitive and fragmented nature of the PU foam industry owing to presence of large number of organised players constraining the pricing flexibility; and exposure of company's profitability to fluctuation in prices of polyol and TDI.

Key rating drivers and their description

Credit strengths

Increased scale of operation: The scale of operation had improved over the years to Rs. 98.49 crore in FY2019 from Rs. 46.78 crore and Rs. 12.40 crore in FY2017 and FY2016 respectively owing to improved sales of foam and addition of branded products including mattresses and pillows under the brand name Sleepkart in FY2017. Also, the company

reported operating income of Rs. 43.93 crore in 7MFY2020 and the same is expected to report a marginal growth of 1%-2% in FY2020.

Improved profitability margins: The company's operating profit margin has improved to 11.17% in 7MFY2020 from 6.40% in FY2019 and 5.91% in FY2018 owing to sharp reduction in prices of TDI and polyol since April 2018. The prices of TDI have reduced from 4500 USD/tonne in March 2018 to 1800 USD/tonne in March 2019. The TDI Prices have remained at ~1700 USD/tonne in 7MFY2020 and supported the company's profitability margins in FY2020. Further, the increasing share of mattress have supported the company's operating profit margins.

Credit challenges

Weak financial risk profile: The financial risk profile is weak with at 5.66 times, total outside liability/net worth at 7.54 times as on October 31, 2019 owing to low net worth levels and total debt/OPBDITA of 5.40 times in 7MFY2020 owing to high debt level and modest profitability levels. The company has a total debt of Rs. 16.02 crore as on October 31, 2019 comprising of term loan of Rs. 12.89 crore, interest free unsecured loans of Rs. 16.02 crore, working capital borrowing of Rs. 15.86 crore and vehicle loan of Rs. 0.59 crore.

Working capital intensive operations: The company's operations remain working capital intensive owing to high inventory levels. In addition to inventory of raw material and of semi-finished goods the company maintains inventory of mattresses and pillows having standard size. The inventory level had increased to 126 days in 7MFY2020 owing to increased inventory of PU foam as on October 31, 2019.

Profit margins vulnerable to volatile input prices: Raw material cost forms a significant portion of the total manufacturing cost and polyol and TDI are the major raw materials which are by-products of crude oil. Along with the price of crude oil, the prices of polyol and TDI are linked to the demand-supply conditions prevailing in the market and thereby impact margins of players like FFPL.

Operates in a competitive and fragmented industry: PU foam industry is intensely competitive and fragmented, which limits its pricing flexibility and bargaining power with customers. This puts pressure on the company's revenues and margins. FFPL's ability to garner market share across a range of products in an intensely competitive market will remain a rating sensitivity. In addition, intense competition in the industry and the price sensitive customer base influence the margins.

Liquidity position: Stretched

FFPL's liquidity position is stretched owing to low cushion available in the working capital limits. The average limit utilization is high at 90% over the past one year ending September 2019. Also, the company has yearly debt repayment of Rs. 4.96 crore in FY2020 and expected cash flows would be sufficient for servicing the obligations with improvement in operating margins.

Rating sensitivities

Positive triggers: ICRA could upgrade FFPL's rating if there is an improvement in company's scale of operations and profitability margins on sustained basis. Specific credit metrics that could lead to an upgrade of FFPL's rating is total debt/OPBDITA of less than 4.00 times, and DSCR of more than 1.20 times on sustained basis.

Negative triggers: Negative pressure on FFPL's rating could arise if there is any decline in revenues or profitability margins on sustained basis. A weakening of interest coverage ratio of below 2.00 times and average working capital utilization of greater than 95% could also exert negative pressure on the company's rating.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not Applicable
Consolidation/Standalone	Standalone

About the company

Fortune Foam Pvt. Ltd. (FFPL) was incorporated in 2003 and is engaged in the manufacturing of PU (Polyurethane) foam and EPF (Expanded Polyethylene Foam) used for making mattresses, pillows, cushions, leather jackets, roll foam for lamination of apparels. Besides foam, the company also manufactures mattresses and sells them under "Sleepkraft" brand. FFPL started its commercial production from August 2015. FFPL has manufacturing capacity of 6,000 MTPA for foam at its manufacturing facility located in Hyderabad.

Key financial indicators

	FY2018	FY2019	7MFY2020
Operating Income (Rs. crore)	79.73	98.49	43.93
PAT (Rs. crore)	0.15	1.07	1.86
OPBDIT/OI (%)	5.91%	6.40%	11.17%
RoCE (%)	6.72%	9.24%	12.06%
Total Outside Liabilities/Tangible Net Worth (times)	829.17	10.15	7.54
Total Debt/OPBDIT (times)	11.07	7.48	5.40
Interest Coverage (times)	1.37	1.66	2.40

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					04-Dec-2019	23-Aug-2018	19-May 2017	NA
1	Term Loan	Long Term	13.59	13.59	[ICRA]BB-(Stable)	[ICRA]B+(Stable)	[ICRA]B+(Stable)	NA
2	Cash Credit	Long Term	18.00	-	[ICRA]BB-(Stable)	[ICRA]B+(Stable)	[ICRA]B+(Stable)	NA
4	Unallocated	Long Term/Short Term	0.41	-	[ICRA]BB-(Stable)/A4	[ICRA]B+(Stable)/A4	[ICRA]B+(Stable)/A4	NA

Amount in Rs. crore

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	18.10.2014	11.60%	-	13.59	[ICRA]BB- (Stable)
NA	Cash Credit	-		-	18.00	[ICRA]BB- (Stable)
NA	Unallocated Limit	-		-	0.41	[ICRA]BB- (Stable)/A4

Source: Fortune Foam Pvt. Ltd.

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