March 15, 2021

Nahar Industrial Enterprises Limited: Ratings reaffirmed; outlook revised to Stable

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term Fund-based – Cash Credit	630.00	630.00	[ICRA]BBB+ reaffirmed; Outlook revised to Stable from Negative
Long-term Fund-based – Term Loan	259.59	204.78	[ICRA]BBB+ reaffirmed; Outlook revised to Stable from Negative
Long-term Unallocated	50.00	40.00	[ICRA]BBB+ reaffirmed; Outlook revised to Stable from Negative
Short-term Non-Fund based	105.13	105.13	[ICRA]A2 reaffirmed
Total	**1,044.72**	**979.91**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in outlook to Stable from Negative reflects the improvement in demand conditions for spinning/ fabric segments, which is supporting a better than previously expected operational and financial performance for Nahar Industrial Enterprises Limited (NIEL) in H2 FY2021. After a steep contraction of ~60% YoY in Q1 FY2021, NIEL's revenues improved gradually with a growth of ~8% and ~7% in Q2 and Q3 FY2021, respectively. The steeper increase in yarn realisations vis-à-vis cotton cost also resulted in a significant improvement in contribution margin for domestic cotton spinners in recent months, supporting profitability in H2 FY2021. Besides, the cost rationalisation measures adopted by the company also supported an improvement in profit margins. While the strong recovery in H2 FY2021 is expected to partially offset the decline witnessed in revenues and profitability in H1 FY2021, the company's revenues and profit margins are expected to moderate for the full year FY2021, vis-à-vis FY2020, and debt coverage metrics are expected to remain modest. The ratings, however, continue to draw strength from the operational and financial flexibility available to the company as a part of the Ludhiana (Punjab) based Nahar Group. Nahar is one of the largest textile groups in the country with vertically integrated operations from spinning to garmenting. ICRA also continues to draw comfort from the demonstrated track record of timely funding support from NIEL's promoter group, healthy financial flexibility at the Group level and a comfortable liquidity cushion maintained in its fund-based working capital limits. Further, the ratings continue to derive comfort from NIEL's three decade-long track record in the textile business with an established market presence and distribution network, its large-scale operations, partial forward integration into weaving and presence in the sugar sector. This increases the value addition and diversification, while moderating the impact of cyclicality in the spinning industry.

The ratings, however, remain constrained by the commoditised nature of the company's products, which coupled with the fragmented industry structure result in limited pricing power, keeping profitability under check. Further, the ratings factor in the high working capital intensity of NIEL's operations because of the seasonal nature of cotton availability that requires stocking during the harvest season, keeping the leverage high and profitability vulnerable to volatility in cotton prices.

The Stable outlook on the company's long-term rating reflects ICRA's expectation of an improvement in profitability, supported by healthy capacity utilisation and steps taken by the company to improve operational efficiencies. Together with a YoY reduction in the company's scheduled repayment obligations and no major debt-funded capex plans, this is expected to help it report an improvement in its debt coverage metrics and reduce its dependence on the promoter group's funds to meet cashflow mismatches.

Key rating drivers and their description

Credit strengths

Extensive track record in textile business with established market presence and distribution network – NIEL has established a strong and widespread distribution network in the country, over its three-decade long operational presence in the textile sector. An established market presence has helped it achieve healthy production levels across product segments over the years, despite the moderation seen in recent years owing to the adverse spinning industry scenario in FY2020, followed by the pandemic impact in the current fiscal year.

Large-scale and integrated textile capacities; modest presence in sugar sector provides diversification benefits – NIEL is one of the leading yarn manufacturers in India, with an installed manufacturing capacity of about 2.2 lakh spindles and 7,600 rotors. Although NIEL phased out ~45,000 old spindles (equivalent to ~17% of its earlier spindle count of ~2.6 lakh) in FY2020, it remains among the largest yarn manufacturers in India (considering the average spindle count of ~28,000-30,000 per unit in India) with an available capacity of 2.2 lakh spindles. Further, its spinning operations are partially forward integrated into weaving (~30-40% of the yarn production is consumed in-house) with an installed capacity of 515 looms and fabric processing capacity of 58.4 million metres per annum. This increases the extent of value addition in the company's operations. While the textile business remains its mainstay, NIEL is also present in the sugar sector with an installed cane crushing capacity of 4,000 tonne per day, along with a 16-MW co-generation power plant in Punjab. Even though the segment's contribution to the company's revenues is low at 9-12%, it provides diversification benefits.

Operational and financial flexibility as part of Nahar Group – NIEL is a part of the Ludhiana-based Nahar Group, which is one of the largest and oldest textile groups in the country with vertically integrated operations from spinning to garmenting and retailing. Other companies in the Nahar Group include Monte Carlo Fashions Limited[1], Oswal Woollen Mills Limited[2], Nahar Spinning Mills Limited, Nahar Capital and Financial Services Limited[3], Nahar Poly Films Limited and Vanaik Spinning Mills Limited. The Group has a demonstrated track record of extending regular and timely funding support across Group entities, depending on the requirements. For instance, the promoter group infused ~Rs. 39 crore in NIEL in FY2020 and Rs. 10 crore in Q1 FY2021 to ensure comfortable cash flows in light of performance pressures in the sector. With improvement being seen in its performance and cash accruals in H2 FY2021, in line with the overall industry trend, ICRA does not expect any major incremental funding requirements in the near term.

Credit challenges

Modest debt coverage metrics – Given the fixed as well as working capital intensive nature of operations, NIEL's dependence on debt, like other domestic spinning companies, has remained high over the years. However, given the limited outgo towards capital expenditure (capex) during the past couple of years, NIEL's term borrowings declined from a peak level of Rs. 642.2 crore as on March 31, 2014 to Rs. 160.4 crore (including proposed LRD loan of ~Rs. 35.0 crore) as on March 31, 2021 (E; estimated). This facilitated an improvement in the company's gearing ratio (Total Debt/Tangible Net Worth) to 0.9 time as on March 31, 2021(E) from 2.2 times as on March 31, 2014. Although the company's annual debt repayment obligations are scheduled to decline to ~Rs. 65 crore in FY2021 and further to Rs. 53 crore in FY2022 over more than Rs. 100.0 crore in FY2020, these remain sizeable. Together with a decline in revenues and profitability amid pressures on performance in recent years, this has resulted in a consistent weakening in the company's debt coverage metrics during the last three years. This is corroborated by an estimated decline in the interest coverage ratio and DSCR to 1.2 times and 0.6 time, respectively, in FY2021(E) from 3.6 times and 1.3 times, respectively, in FY2017. In this context, however, ICRA notes that the timely infusion

[1] *ICRA has ratings outstanding of [ICRA]AA-(Stable) and [ICRA]A1+ for Monte Carlo Fashions Limited*

[2] *ICRA has ratings outstanding of [ICRA]A-(Negative) and [ICRA]A2+ for Oswal Woollen Mills Limited*

[3] *ICRA has rating outstanding of [ICRA]A1+ for Nahar Capital and Financial Services Limited*

of funds by the promoter group companies has helped the company maintain an adequate liquidity profile, with an average cushion of ~Rs. 70-100 crore in its fund-based working capital limits.

Susceptibility of profitability to volatile cotton prices – Like other entities in the spinning sector, NIEL stocks cotton during the harvest season (from October to March) to meet a significant portion of its requirement during the off season. This stocking exposes the company to fluctuations in cotton and yarn prices during the non-harvest period, as the procurement cost is fixed, while yarn realisation fluctuates with cotton prices, which are driven by domestic and global factors. This was witnessed in FY2020 as well as FY2021, as a sharp decline in cotton yarn realisations during the first half of the fiscal years resulted in a pressure on the spinners' profitability, given the higher cost of cotton carried from the previous stocking season. Like last year, demand-led pressures resulted in a steep correction in cotton yarn realisations post conclusion of the harvesting and stocking season for cotton this year as well, which affected the contribution margin of spinners in H1 FY2021.

Commoditised nature of products and fragmented industry structure restricts pricing power and profitability – The spinning and weaving industries are highly fragmented with a significant share of the unorganised sector. While NIEL manufactures a wide variety of yarns and fabrics with varying levels of value addition, its product portfolio continues to be concentrated on medium-count yarns and low-to-medium, value-added mass segment fabrics. As a result, it has limited pricing power, which keeps its profitability under check.

Liquidity position: Adequate

Despite severe pressures on NIEL's profitability since FY2019 which have moderated its liquidity profile, the company's liquidity position remains **adequate**, primarily supported by the funding support from promoter group companies. The promoter group infused Rs. 39 crore and Rs. 10 crore in the company in the form of preference share capital in FY2020 and Q1 FY2021, respectively. With the improvement in the company's performance in recent months, ICRA does not expect any major incremental fund requirements from the promoter group in the near term. Adequate liquidity is reflected in the availability of adequate unutilised working capital limits with an average cushion of ~Rs. 67 crore over its drawing power in the six-month period ending February 2021. This is despite the increase in the company's working capital requirements during the second half of the fiscal on account of cotton stocking. ICRA also notes that the company's liquidity position in the near term is expected to be supported by a proposed LRD loan of Rs. 35 crore, which is to be availed towards reimbursement of capex incurred by the company in the past using internal accruals.

Rating sensitivities

Positive factors – The ratings may be upgraded if there is a healthy recovery in the company's scale of operations, along with an improvement in its profitability, which results in an improvement in its debt-coverage metrics and makes it self-sufficient to fund its debt repayments and incremental working capital margin requirements on a sustainable basis. Further, efficient working capital management, which improves the company's liquidity position, could be a positive rating trigger.

Negative factors – The ratings could be downgraded if there is a sustained pressure on the company's sales growth and profitability. Additionally, NIEL's rating would be prone to a downgrade if a stretch in working capital cycle or a sizeable capex weakens its liquidity position, taking the average utilisation to more than 85% of lower of sanctioned limits or drawing power on a sustained basis and/or results in an increase in the company's leverage and deterioration in its debt protection metrics.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Textiles Industry - Spinning Rating Methodology for Entities in the Textiles Industry – Fabric Making Rating Methodology for Entities in the Sugar Industry
Parent/Group Support	Ratings factor in the financial flexibility from being a part of the established Ludhiana-based Nahar Group
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company.

About the company

Incorporated in 1983, NIEL is primarily involved in cotton spinning (with an installed capacity of about 2.2 lakh spindles and 7,600 rotors) and weaving (with an installed capacity of 515 air-jet looms and a fabric processing capacity of 58.4 million metres per annum). In addition, it runs a sugar unit with a capacity of crushing 4,000 tonnes of sugarcane per day. NIEL's manufacturing units are mostly located in Punjab, with spinning units in Lalru, Ludhiana (both in Punjab) and Bhiwadi (Rajasthan). The weaving and processing unit is based in Lalru and the sugar unit is in Amloh (Punjab).

NIEL is a part of the Ludhiana-based Nahar Group, one of the largest and oldest textile groups in the country with vertically-integrated operations from spinning to garmenting and retailing. The other major companies in the Nahar Group include Monte Carlo Fashions Limited, Oswal Woollen Mills Limited, Nahar Spinning Mills Limited and Nahar Capital and Financial Services Limited.

In FY2020, the company reported a net loss of Rs. 24.7 crore on an operating income (OI) of Rs. 1,572.7 crore, compared to a net loss of Rs. 21.6 crore on an OI of Rs. 1,866.2 crore in the previous year.

Key financial indicators (audited)

NIEL	FY2019	FY2020	9M FY2021
Operating Income (Rs. crore)	1866.2	1572.7	954.4
PAT (Rs. crore)	-21.6	-24.7	-49.3
OPBDIT/OI (%)	6.6%	6.0%	2.7%
PAT/OI (%)	-1.2%	-1.6%	-5.2%
Total Outside Liabilities/Tangible Net Worth (times)	1.6	1.3	NA
Total Debt/OPBDIT (times)	7.2	7.6	NA
Interest Coverage (times)	1.8	1.5	0.6

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation, NA: Not available

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021) Type	Amount Rated (Rs. crore)	Amount Outstanding as of Jan 08, 2021 (Rs. crore)	Date & Rating in		Chronology of Rating History for the past 3 years Date & Rating in FY2020	Date & Rating in FY2019		Date & Rating in FY2018
					15-Mar-21	19-May-2020	29-Nov-19	26-Nov-2018	19-Jul-2018	15-Sep-2017
1	Cash Credit	Long Term	630.00	--	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Negative)	[ICRA]A- (Negative)	[ICRA]A- (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
2	Term Loan	Long Term	204.78	204.78	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Negative)	[ICRA]A- (Negative)	[ICRA]A- (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
3	Unallocated Limits	Long Term	40.00	--	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Negative)	[ICRA]A- (Negative)	[ICRA]A- (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
4	Letter of Credit	Short Term	105.13	--	[ICRA]A2	[ICRA]A2	[ICRA]A2+	[ICRA]A2+	[ICRA]A1	[ICRA]A1
5	Commercial Paper	Short Term	-	--	-	-	-*	[ICRA]A2+	[ICRA]A1	-

**rating reaffirmed and withdrawn*

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 click here

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	Cash Credit	NA	NA	NA	630.00	[ICRA]BBB+(Stable)
NA	Term Loan	FY2011	NA	FY2033	204.78	[ICRA]BBB+(Stable)
NA	Unallocated Limits	NA	NA	NA	40.00	[ICRA]BBB+(Stable)
NA	Letter of Credit	NA	NA	NA	105.13	[ICRA]A2

Source: *Company*

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

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About ICRA Limited:

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