September 18, 2019

Reliance Chemotex Industries Limited: Ratings reaffirmed; Outlook revised to 'Positive'

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	19.47	13.76	[ICRA]BB+; Reaffirmed, Outlook revised to Positive from Stable
Cash Credit	33.00	33.00	[ICRA]BB+; Reaffirmed, Outlook revised to Positive from Stable
Standby Limit	3.00	2.00	[ICRA]A4+; Reaffirmed
Non-fund Based Limits	35.50	35.50	[ICRA]A4+; Reaffirmed
Unallocated Limit	31.95	38.66	[ICRA]BB+ / [ICRA]A4+; Reaffirmed, Outlook revised to Positive from Stable
Total	**122.92**	**122.92**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in outlook to 'positive' reflects the strengthening of networth and expected improvement in the Reliance Chemotex Industries Limited (RCIL)'s coverage indictors in the near term attributable to the full redemption of preference shares amounting to Rs. 23.08 crore in August 2019, leading to savings on dividend outflow (on preference shares) in the business. Also, the redemption of preference shares was fully funded by raising equity of Rs.23.16 crore through the rights issue in July 2019, thereby supporting the capital structure. ICRA notes that RCIL in the near term has planned for a debt funded capex of ~Rs 52 crore which will enable the company to manufacture various value-added yarn which command higher margin. Though the capex is debt funded, low interest rates under state policy scheme and ballooning repayment regime provides some comfort. However, commensurate returns and benefits from the capex in term of cost efficiencies would be the key monitorable in the near term. ICRA also notes that there is also a likelihood of reduction in power costs based on the tariff petition submitted by power DISCOM backed by textile company's representation to the regulator (Rajasthan Electricity Regulatory Commission) for reduction in tariff for power intensive industries like Textiles, which if approved is likely to lead to notable reduction in the power cost going forward. The ratings continue to reflect the extensive experience of the company's promoters in the textile industry, its diversified geographical presence and company's low working capital intensity of business driven by the prudent working capital management with favourable receivable cycle.

The ratings, however, remain constrained by the vulnerability of company's profitability to adverse fluctuations in the raw material prices, and limited bargaining power with its suppliers, in an intensively competitive manmade yarn industry which limits pricing flexibility. The ratings also take note of the company's exposure to foreign exchange rate risk given the presence of sizable exports in the business though the risk is mitigated to an extent by active forward hedging. The ratings also take note of the low DSCR of 1.02X as on March 31,2019 given the high repayment obligation which is tightly matched with the net accruals in FY2019, and average coverage indicators.

Key rating drivers and their description

Credit strengths

Established track record of promoters in the textile industry - The promoter, Mr. S.L. Shroff and family has been in textile business for over four decades. Over the years the company has established strong relationship with prominent suppliers in the domestic market. Furthermore, the company has developed a strong clientele in both domestic and international market which has diversified company geographical presence and has also resulted in repeat orders.

Comfortable capital structure which is further likely to improve in the current year due to full redemption of preference share and infusion of equity from rights issue - As on March 31, 2019 the company's capital structure remain comfortable as indicated by a gearing of 1.2X driven by controlled working capital borrowings. In August 2019, the company fully redeemed the preference shares amounting to Rs.23.08 crore leading to reduction in debt levels. Also, the redemption of preference shares was fully funded by raising equity of Rs.23.16 crore through the rights issue in July 2019, thereby strengthening the company's networth base which is likely to improve the capital structure in the near term.

Healthy growth in operating income backed by improved sale realisation and volumes coupled with improvement in operating profitability driven by favourable product mix - In FY2019, RCIL recorded a revenue growth of ~14% in the OI to Rs.324.4 crore in FY2019 from Rs.284.5 crore in FY2018 due to improvement in the sales volume and realisation. Further, with the increasing share of higher margin commanding value add yarn in the product mix and better absorption of fixed costs with increase in the scale of operation has enabled the company to improve its operating margin to 8.2% in FY2019 from 6.9% in FY2018.

Various benefit reaped under technology upgradation fund scheme (TUFS) of Central Govt. and good borrower scheme of Rajasthan State Industrial Development & Investment Cooperation - The company is eligible under various central & state government incentives such as interest subsidy benefits under TUF (Technology Upgradation Fund Scheme) and good borrow schemes that effectively reduces the interest cost and payback period to a large extent.

Credit challenges

Relatively average coverage indicators and debt protection metrics - The company's coverage indicators continue to remain relatively average, with interest coverage of 2.0X and TD/OPBDIT of 3.1X in FY2019 although it has improved from interest coverage of 1.6X and TD/OPBDIT of 4.8X in FY2018 due to improvement in the operating profitability. Further, the full redemption of preference shares amounting to Rs. 23.08 crore in August 2019, will lead to savings on dividend outflow in the business during FY2020.

Profitability vulnerable to raw material price movements, due to low bargaining power, power cost and forex fluctuations - The company's key raw materials include polyester staple fibre (PSF), viscose staple fibre (VSF) and acrylic fibre. The raw material procurement is mainly made from the domestic market. The raw material prices are primarily controlled by the large suppliers, offering RCIL limited bargaining power and pricing flexibility. Though the company is steadily diversifying its supplier base to improve it bargaining power. Also, VSF which forms ~60% of the raw material cost continue to chart stable price in comparison to prices of PSF which has remained volatile in the past. Being a net exporter, there is exposure to forex movements (Euro and US dollar). The company has a net foreign receivable position and primarily hedges its receivables through forward contracts. The active forex-hedging mechanism reduces the susceptibility of margins to unfavourable forex movement risks to a large extent.

Near term debt funded capex likely to keep return indicators weak; adequate returns from ongoing capex critical for overall improvement in financial profile - RCIL has regularly invested in capex over the last few years and has another capacity expansion plan over the near term. The company is expected to incur a capex of Rs. 52.00 crore in two phases, which will be funded through a mix of debt and, unsecured loan from promoters and internal accruals. The phase I of said capex was initialled planned to be undertaken in FY2019, however, given the challenging market condition and the general election year in India dissuaded the company to go ahead with the capex. However, the said capex is likely to commence in the current year. Given the debt-funded nature of the capex, the external long-term debt levels are expected to rise in the near term. The planned capex to (modernise a part of the vintage spindles) is expected to be operational by FY2021 and will lead to better production efficiencies and output. ICRA draws comfort from the ballooning repayment schedule and low effective interest on the sanctioned loan, which enhances the overall project viability. However, lack of commensurate returns from the capex will negatively impact the key credit metrics.

Intense competition in the textile industry - RCIL faces competition from international as well as domestic yarn manufacturers. In the domestic market, there is intense competition and fragmentation, limiting the pricing power of the textile companies and affecting their margins.

Liquidity position: Adequate

The repayment for the next three fiscals are in the range of Rs. 5-8 crore. which is should be comfortably covered by the cash accruals going forward, though for FY2019, cash accrual was tightly matched with the repayment. Further, the working capital utilisation in the last 7 months remain at ~66% of sanctioned limits indicating adequate buffer of undrawn line of credit. Also, RCIL ‘s near term debt funded capex will have favourable repayment terms and subsidized interest rate which are likely to support the cash flows.

Rating sensitivities

Positive triggers - ICRA could upgrade RCIL’s rating if the company demonstrates a steady improvement in profitability by better management of overhead costs and generate healthy return from the capex which is expected to improve the return indicators in the near term. Improvement in adjusted interest coverage of over 3.5 times coupled with DSCR of over 1.5X on sustained basis shall trigger an upgrade revision.

Negative triggers - Negative pressure on RCIL’s rating could arise if, company’s if the operating margin weaken and any inability to generate commensurate return from its debt funded capex. Also, company’s inability to maintain interest coverage above 2.5 times and DSCR of 1.2X on sustained basis shall trigger a downward revision in ratings.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Indian textiles Industry - Spinning
Parent/Group Support	Not applicable
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company

About the company

Incorporated in 1977, RCIL manufactures synthetic and blended yarn. The company's product count ranges from Ne 6s to Ne 50s in single, double and multi-ply yarn. RCIL is promoted by Mr. S.L. Shroff. His son, Mr. Sanjiv Shroff, is the company's Managing Director at present. RCIL's shares have been listed on the Bombay Stock Exchange since 2001.

Based out of Mumbai, the company has branch offices in Kolkata and Delhi, while its manufacturing facility is in Udaipur, Rajasthan, with an installed capacity of 53,280 spindles.

In FY2019, the company has booked a net profit of Rs.4.1 crore on an operating income of Rs.324.4 crore against a net profit of Rs.2.6 crore on an operating income of 284.5 crore in FY2018.

Key financial indicators

	FY2018 (Audited)	**FY2019 (Audited)**
Operating Income (Rs. crore)	284.5	324.4
PAT (Rs. crore)	2.6	4.1
OPBDIT/OI (%)	6.9%	8.2%
RoCE (%)	8.4%	12.3%
Total Outside Liabilities/Tangible Net Worth (times)	2.2	2.3
Total Debt/OPBDIT (times)	4.8	3.1
Interest Coverage (times)	1.6	2.0
DSCR (exl. STD/prepayment)	0.8	1.0

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)				Chronology of Rating History for the Past 3 Years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of July 2019 (Rs. crore)		Date & Rating in FY2019	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2017
					18-Sep-19	03-Jan-19	15-Feb-18	10-Feb-17	24-Jun-16
1	Term Loans	Long Term	13.76	13.76	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)
2	Cash Credit	Long Term	33.00	-	[ICRA]BB+ (Positive)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	[ICRA]BBB- (Negative)	[ICRA]BBB- (Negative)
3	Standby Limit	Short Term	2.00	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A3	[ICRA]A3
4	Non-fund Based Limits	Short Term	35.50	-	[ICRA]A4+	[ICRA]A4+	[ICRA]A4+	[ICRA]A3	[ICRA]A3
5	Unallocated Limit	Long and Short Term	38.66	-	[ICRA]BB+ (Positive)/ [ICRA]A4+	[ICRA]BB+ (Stable)/ [ICRA]A4+	[ICRA]BB+ (Stable)/ [ICRA]A4+	-	-

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 Loans	FY2015	~12%	FY2019-2023	13.76	[ICRA]BB+(Positive)
NA	Cash Credit	NA	NA	-	33.00	[ICRA]BB+(Positive)
NA	Standby Limit	NA	NA	-	2.00	[ICRA]A4+
NA	Non-fund Based Limits	NA	NA	-	35.50	[ICRA]A4+
NA	Unallocated Limit	NA	NA	-	38.66	[ICRA]BB+(Positive) /[ICRA]A4+

Source: RCIL

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

Analyst Contacts

K. Ravichandran
+91 44 4596 4301
ravichandran@icraindia.com

Suprio Banerjee
+91 22 6114 3443
supriob@icraindia.com

Srinivas Menon
+91 22 6169 3354
srinivas.menon@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
communications@icraindia.com

Helpline for business queries:

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

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) 2556 0194/ 6606 9999