

June 12, 2019

Sri Dhanalakshmi Cotton & Rice Mills Pvt. Ltd.: Ratings reaffirmed

Summary of rated action

Instrument	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund-based limits	113.00	106.34	[ICRA]A- (Stable); reaffirmed
Short Term - Fund based limits	8.00	8.00	[ICRA]A2+; reaffirmed
Long Term - Unallocated limits	0.84	7.50	[ICRA]A-(Stable); reaffirmed
Total	121.84	121.84	

**Instrument details are provided in Annexure-1*

Rationale

The ratings reaffirmation favourably factors in the extensive experience of promoters in the cotton industry. Besides, operational efficiency arises from the integrated nature of Sri Dhanalakshmi Cotton & Rice Mills Pvt. Ltd.'s (SDC) work comprising spinning, weaving and oil extraction & refining, along with captive hydel power and windmill. The ratings also consider the location-specific advantage of the company's plant as it is located in Guntur district of Andhra Pradesh, a prominent cotton-growing belt, resulting in easy access to all the raw materials. SDC has an established market presence in the cotton seed oil industry and is one of the largest cotton seed oil extractors in India. The ratings further consider low gearing, comfortable coverage indicators and liquidity position, as reflected by moderate utilisation of working capital limits in FY2019. ICRA also notes that SDC's operating income rose by 12% to Rs. 570.3 crore in FY2019 because of improved demand from the cotton seed oil division due to better availability of cotton seed, which is expected to improve further, going forward.

The ratings, however, remain constrained by low return indicators over the past few years due to subdued profitability margins in all the divisions. Although the operating margins improved to 6.8% in FY2019 amid better absorption of fixed overheads with increasing scale and improved captive power generation, the margins still remain low because of thin profitability margins in the cottonseed oil division (which accounted for 47% of revenues in FY2019). Further, SDC's revenues and profitability are exposed to availability and seasonality of cotton, regulatory and agro-climatic risks associated with crop harvest affecting production and realisations as witnessed during the last three years. The ratings are also constrained by the availability of the cottonseed along with its seasonality in the cotton oil division, leading to volatility in revenues and profitability of the company as witnessed in the past. Besides, there is high customer concentration risk in the fabric division and the top five customers accounted for over 85% of the division's sales during the last three years.

Outlook: Stable

The Stable outlook reflects ICRA's expectation that SDC will continue to benefit from the extensive experience of its promoters in the cotton industry while captive power generation will support the overall operating profitability. The outlook may be revised to Positive if a substantial growth in revenue and profitability strengthens the financial risk profile. The outlook may be revised to Negative if revenues and margins fall significantly or a decline in cash accruals or a stretch in the working capital cycle weakens liquidity.

Key rating drivers

Credit strengths

Extensive experience of promoters in the cotton industry - The promoters of the company have more than four decades of experience in the cottonseed oil industry. The company is one of the largest cottonseed oil extractors in India with 600 MTPD of seed processing capacity, 280 MTPD solvent extractor and 50 MTPD of refining. Later, the company diversified vertically into spinning and weaving, with spinning capacity of 85,200 spindles and weaving capacity of 120 looms. The company also has hydel power capacity of 6.2 MW and windmill capacity of 15.3 MW. Moreover, SDC has established relationships with suppliers and customers, resulting in repeat orders.

Integrated nature of operations - The revenue profile of the company is diversified with vertically integrated operations comprising spinning, weaving, oil extraction and refining along with captive hydel power and windmill, resulting in operational efficiency. Further, ~37% of the yarn requirements of the fabric divisions were met through in-house production, while ~37% of total power requirement was met by captive power generation in FY2019, supporting operating margins to an extent.

Healthy capital structure and comfortable coverage indicators - The capital structure of SDC was comfortable with a gearing of 0.3 times as on March 31, 2019 and is expected to remain comfortable, going forward, due to absence of major capex plans. The coverage indicators were also comfortable with interest coverage at 7.4 times, NCA/Total Debt at 40% and Total Debt/OPBDITA at 1.8 times as on March 31, 2019. The liquidity position was satisfactory with an average working capital utilisation of ~30% in FY2019.

Proximity of the plant to cotton growing areas - SDC has location-specific advantage as the plant is located near the major cotton growing belt of Guntur, Andhra Pradesh, resulting in easy access to all raw materials.

Credit challenges

Low return indicators over last three years- The return indicators were low with ROCE at 7.0% in FY2019 due to subdued profitability margins. The operating margins declined from 7.6% in FY2016 to 5.5% in FY2018 because of weak profitability margins in the oil and weaving division. However, the same was supported to an extent by improved captive power generation in the last two years with the addition of a 6.3-MW windmill in March 2016. Although the operating margins improved to 6.8% in FY2019 because of improved performance of the oil division, the margins continued to remain modest.

High customer concentration risk in weaving division- The customer concentration risk is high in the fabric division with the top five customers accounting for over ~85% of the division's sales during the last three years. However, the same is mitigated to an extent as the customers are associated with the company over the years.

Exposed to the regulatory and agro-climatic risks- The company's revenues and margins are exposed to agro-climatic risks as availability and pricing of cotton are seasonal with cotton season running from mid-September to March every year. SDC is also exposed to regulatory risks with respect to the minimum support price (MSP) for raw cotton, which is decided by the Government every year. Prices remain volatile based on demand and supply, which mainly depends on China's procurement every year. The company's revenues and margins are also exposed to fluctuations in cotton and yarn prices, as witnessed during the last three years.

Liquidity position

SDC has a moderate debt repayment obligation of ~Rs. 7 crore over the next two years and the expected cash accruals remain comfortable. Also, the company did not incur any debt-funded capex during the last two years (FY2018 and FY2019). The repayment burden would ease going forward as the company does not have any major capacity expansion plans. The average working capital utilisation was low at 30% between April 2018 and April 2019 and has cushion available in the form of undrawn working capital limits.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Solvent Extraction (Edible Oil) Industry Rating Methodology for Entities in the Textiles Industry–Spinning Rating Methodology for Entities in the Indian Textiles Industry –Fabric Making
Parent/Group Support	Not applicable
Consolidation / Standalone	Standalone

About the company

Sri Dhanalakshmi Cotton & Rice Mills Pvt. Ltd. (SDC), located in Guntur, Andhra Pradesh was set up in 1977 and is managed by Mr. N. Raghava Rao, Mr. P. Raghava Reddy, Mr. P.V. Narayana, Mr. S. Hanumantha Rao and Mr. M. Lingaiah. The company, a closely-held business, is a diversified entity operating across oil extraction, cotton spinning, weaving, hydel power and wind power, all located in Guntur, Andhra Pradesh, a major cotton producing belt. The company also owns a 9-MW windmill in Tamil Nadu. SDC's spinning division (cotton yarn) has an installed capacity of 85,200 spindles, the cottonseed oil division has 600 MTPD of seed processing capacity, the solvent extraction division has a capacity of 280 MTPD, the refining division has a capacity of 50 MTPD, the fabric division has 120 looms, the hydel power division has a capacity of 6.2 MW and the wind mill has a capacity of 15.3 MW.

Key Financial Indicators

	FY2018	FY2019*
Operating Income (Rs. crore)	507.6	570.3
PAT (Rs. crore)	5.4	16.1
OPBDIT/ OI (%)	5.5%	6.8%
RoCE (%)	4.0%	7.0%
Total Debt/ TNW (times)	0.4	0.3
Total Debt/ OPBDIT (times)	3.4	1.8
Interest Coverage (times)	4.5	7.4

*Provisional

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2020)			Chronology of Rating History for the past 3 years			
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs Crore)	Date & Rating June 2019	Date & Rating in FY2019 June 2018	Date & Rating in FY2018 April 2017	Date & Rating in FY2017 April 2016	
1 Cash Credit	Long Term	83.50	-	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	
2 Term Loans	Long Term	22.84	22.84	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	
3 Non fund based	Short Term	8.00		[ICRA]A2+	[ICRA]A2+	[ICRA]A1	[ICRA]A1	
4 Unallocated	Long Term	7.50	-	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	

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	Cash Credit	-	-	-	83.50	[ICRA]A- (Stable)
NA	Term Loan-1	June 2016	-	March 2022	14.50	[ICRA]A- (Stable)
NA	Term Loan-2	November 2017	-	January 2023	8.34	[ICRA]A- (Stable)
NA	Letter of Credit	-	-	-	7.00	[ICRA]A2+
NA	Bank Guarantee	-	-	-	0.80	[ICRA]A2+
NA	CEL	-	-	-	0.20	[ICRA]A2+
NA	Unallocated	-	-	-	7.50	[ICRA]A- (Stable)

Source: SDC

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