

U.B. Cotton Private Limited

March 02, 2021

Ratings

Facilities/Instruments	Amount (Rs. crore)	Ratings	Rating Action
Long Term / Short Term Bank Facilities	37.00	CARE BBB; Stable / CARE A3+ (Triple B ; Outlook: Stable/ A Three Plus)	Reaffirmed
Total Bank Facilities	37.00 (Rs. Thirty-Seven Crore Only)		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The reaffirmation of ratings assigned to bank facilities of U.B. Cotton Private Limited (UBCPL) continues to derive strength from the experience of promoters in the cotton trading business, established and diversified base of reputed customers, prudent risk management practices, moderate capital structure and debt coverage indicators and adequate liquidity position.

The rating however is tempered, decline in scale of operations during FY20; albeit m-o-m pick-up in sales witnessed during 9MFY21 led by favorable pricing scenario of Indian cotton vis-à-vis International cotton, moderate operating cycle, susceptibility to regulatory policies, presence in highly competitive cotton trading sector and dependence on a single product coupled with seasonality in the business.

Rating Sensitivities:

Positive factors:

- Increase in PBILDT margin to more than 3.5% on a sustained basis
- Overall gearing less than unity on a sustained basis
- Operating cycle less than 2 months

Negative factors:

- Current ratio less than 1.2x
- Decline in Interest cover below 2x on continuous basis

Detailed description of the key rating drivers

Key Rating Strengths

Experienced Promoter and established track record

UBCPL is being currently directed by Mr. Udayan B. Thakkar (present Managing Director and third generation entrepreneur) and Mr. Kunal Udayan Thakkar (fourth generation entrepreneur). The promoter family has a track record of more than eight decades in the current line of business. Due to its long presence in the cotton trading segment, UBCPL has established itself as a preferred vendor for cotton exports for domestic textile mills. It has an established network of suppliers of cotton in the prime cotton growing region of the country and owns warehouses in Ahmedabad, Sri Ganga Nagar (Rajasthan), Maharashtra and Tamil Nadu.

Established and diversified base of reputed customers

UBCPL has been in the cotton trading business for about 2 decades and with long standing promoter experience, the company has been able to associate with major cotton ginneries and in some cases directly with the farmers. Over the years, the company has set up a strong distribution network and a diverse clientele. The company has presence in domestic as well as exports market through various dealers and distributors who have aided the company in garnering repeat orders. UBCPL exports cotton to China, Bangladesh, Hong Kong, Indonesia, Switzerland, etc. It also has a good distribution network to sell locally. The sales of UBCPL have seen minimal bad debts or provisioning of receivables which reflects good quality of its customers. The company has been receiving repeated orders from renowned customers over the years and confirmed orders from its reliable customers account for majority of sales.

Prudent risk management practices

The company follows conservative business model. UBCPL books transactions on a short term and back to back basis as a part of its conservative trading strategy, the same can be corroborated from the fact that its gross margins have been stable between 2% to 4% over the past 3 years.

Further, the company is primarily a cotton trader and is vulnerable to regulatory restrictions on cotton export which is linked to the demand supply scenario in the domestic market. UBCPL was able to maintain profitability even when exports were not viable in FY20 due to higher domestic prices of cotton, thus reflecting the flexibility in its trading strategy in line with fluctuation of cotton prices.

In order to mitigate the risks associated with foreign currency fluctuations, the company enters into forward contracts for all the export transactions to hedge its foreign currency risks. Though the payment terms differ from client to client, UBCPL has majority of export sales (approximately 85-90%) backed by LCs and remaining on Cash against Documents (CAD).

Moderate capital structure and Debt protection metrics

UBCPL's capital structure continues to be moderate. TOL/TNW as on March 31, 2020 improved to 1.51 times as against 1.62 times as on March 31, 2019. The overall gearing improved to 1.11x as on March 31, 2020 compared to 1.27x as on March 31, 2019. The improvement in gearing was mainly attributable to lower working capital borrowing requirement on account of lower sales especially in Q4FY20, due to the pandemic. The interest coverage ratio deteriorated to 1.72x in FY20 compared to 2.37x in FY19. Interest cost increased from Rs.3.55crore in FY19 to Rs.4.52crore during FY20 as UBCPL conducted 85% of sales in domestic market in FY20 which, required banking lines at higher interest rate compared to the financing it required for export sales in the previous fiscal.

Competitive domestic cotton prices and improved demand to aid cotton exports in the near to medium term

In FY20, Indian cotton prices were not competitive in the international market. However, with the easing of lockdown since July 2020, the trade is gradually returning to pre-Covid levels following the revival of demand from the buyers in international market, UBCPL is expected to regain the export business. The Cotton Corporation of India (CCI) and the Maharashtra State Co-Operative Cotton Growers Marketing Federation (MAHFED) were holding huge inventory of cotton during the previous cotton season and as they liquidated the stocks, the prices of Indian cotton became competitive in the international market. The same can be corroborated from the increase in cotton exports from India.

Key Rating Weaknesses

Product Concentration risk

UBCPL earns revenues from sale of a single product i.e. raw cotton and this exposes the company's revenue to volatility in the production, demand as well as prices of cotton. Furthermore, cotton trading is seasonal in nature with the peak season from December to March. The majority of sales occur during this period. Thus, the profit margins of UBCPL are susceptible to the risks related to trading in a single commodity as well as seasonal nature of business.

Decline in scale of operations during FY20

The company reported 40% decline in TOI from Rs.314crore in FY19 to Rs.188crore in FY20, due to decline in exports. However, UBCPL reported improvement in PBILDT margin from 2.68% in FY19 to 4.13% in FY20. The improved PBILDT margins were primarily due to higher income from import commission, which rose from Rs.4.25crore in FY19 to Rs.6.75crore in FY20. However, due to improved demand post easing of lock down from major cotton consuming neighbours namely China, Bangladesh, Vietnam etc., UBCPL's sales for 9MFY21 improved by 65% on a YoY basis to Rs.216crore as compared to Rs.131crore in 9MFY20. Despite covid related disruption in FY21, PBILDT margin remained largely stable during 9MFY21 (4.54% in 9MYFY21 vs 4.96% in 9MFY20).

Moderate operating cycle

The operating cycle deteriorated from 86 days as on March 31, 2019 to 102 days as on March 31, 2020 mainly due to the increase in collection period from 59 days to 109 days. The collection period was stretched as the payments have been delayed primarily due to COVID-19 and also due to the increased domestic sales wherein the credit period offered is ~90 days (vs ~45 days for export sales).

Inherent risk associated with the cotton trading industry

Due to low value addition and moderate capital requirements, the cotton trading industry in India is characterized by presence of large number of players. Further the company is vulnerable to regulatory restrictions on cotton exports. The operating margins in commodity trading business remain thin and susceptible to volatility in commodity prices. Given the low trading margins, UBCPL works on back to back basis, with major part of the inventory being hedged, and LC backed sales.

Liquidity: Adequate

The company reported a gross cash accrual of Rs.3.22 crore in FY20; compared to Rs.3.80crore in the previous year and the company has no scheduled repayment obligation. The average utilization of bank limits for the 12 months ending January 2021 was 46%, thus providing a sufficient headroom to accommodate fresh trade opportunities. Furthermore, the company had not availed any moratorium or additional covid loans during the lock down.

Analytical approach: Standalone.

Applicable Criteria

[Criteria on assigning 'Outlook' and 'Credit Watch' to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Criteria for Short Term Instruments](#)

[Financial ratios - Non-Financial Sector](#)

[Rating Methodology- Wholesale Trading](#)

[CARE's Policy on Liquidity Analysis of Non-Financial Sector Entities](#)

About the Company

Incorporated in May 2002, U.B Cotton Private Limited (UBCPL) is being promoted by the Thakkar family who are in the cotton business since 1930. The company is a member of CAI (Cotton Association of India) and engaged in the business of export and domestic trading of ginned cotton. The company's major export markets are Pakistan, Bangladesh, Thailand, Vietnam, Indonesia and Turkey. The company reported 40% decline in TOI from Rs.314crore in FY19 to Rs.188crore in FY20, due to decline in exports.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	313.97	187.74
PBILDT	8.42	7.75
PAT	3.16	2.65
Overall gearing (times)	1.27	1.11
Interest coverage (times)	2.37	1.72

A: Audited

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based/Non-fund-based-LT/ST	-	-	-	37.00	CARE BBB; Stable / CARE A3+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based/Non-fund-based-LT/ST	LT/ST	37.00	CARE BBB; Stable / CARE A3+	1)CARE BBB; Stable / CARE A3+ (06-Apr-20)	1)CARE BBB; Stable / CARE A3+ (04-Apr-19)	-	1)CARE BBB; Stable / CARE A3+ (13-Dec-17) 2)CARE BBB; Stable / CARE A3+ (20-Apr-17)

Annexure-3: Complexity level of various instruments rated for this company

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based/Non-fund-based-LT/ST	Simple

Note on complexity levels of the rated instrument: CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.

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