Falcon Yarns Private Limited

September 21, 2022

Ratings

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long Term Bank Facilities	42.76 (Reduced from 56.94)	CARE BBB; Stable (Triple B; Outlook: Stable)	Reaffirmed
Short Term Bank Facilities	2.50 (Reduced from 3.50)	CARE A3+ (A Three Plus)	Reaffirmed
Total Bank Facilities	**45.26 (₹ Forty-Five Crore and Twenty-Six Lakhs Only)**		

Details of facilities in Annexure-1.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Falcon Yarns Private Limited (FYPL) continue to derive strength by FYPL's experienced and resourceful promoter group and proximity of its manufacturing unit to a cotton growing region with established relations with customers and suppliers. The ratings also take cognizance of significant growth in FYPL's total operating income (TOI) during FY22 (refers to the period from April 01 to March 31), its moderate capital structure, comfortable debt coverage indicators and adequate liquidity.

The ratings, however, continue to remain constrained on account of FYPL's concentrated customer base and its presence in an intensely competitive, fragmented, and cyclical cotton spinning industry with associated regulatory risks. The ratings also factor decline in FYPL's profitability due to high volatility in raw cotton prices, an inherent risk in the spinning segment of the textile value chain. This apart, near term headwinds in the cotton yarn spinning industry primarily due to higher cotton and cotton yarn prices may adversely impact the production, sales volume, and profitability of cotton spinners like FYPL.

Rating Sensitivities

Positive Factors - Factors that could lead to positive rating action/upgrade:

- Significant volume driven growth in scale of operations along with improvement in PBILDT margin and return on capital employed (ROCE) to more than 11% and 20% respectively, on a sustained basis.

Negative Factors- Factors that could lead to negative rating action/downgrade:

- Decline in scale of operations to below Rs.220 crore with decline in PBILDT margin to below 7.00% on a sustained basis.
- Deterioration in overall gearing beyond to 1.2 times and total debt/ GCA to more than 3 years on sustained basis.
- Any large-sized debt funded capex adversely affecting FYPL's capital structure and liquidity.

Detailed description of the key rating drivers

Key Rating Strengths

Significant growth in TOI:

FYPL's TOI grew by approximately 60% y-o-y to Rs.300.47 crore during FY22 owing to growth in sales volume and improvement in sales realisation by 5% and 54% respectively. Furthermore, TOI during Q1FY22 (Prov.) stood at Rs.76.68 crore with continued traction in sales realisation. However, scale of operations continues to remain moderate.

Moderate capital structure and comfortable debt coverage indicators:

Capital structure of FYPL improved during FY22, marked by an overall gearing of 0.66 times as on March 31, 2022 (P.Y. end: 0.79 times), on account of accretion of profits to reserves. It is expected to improve further going forward due to sizeable yearly debt repayment obligations of around Rs.14 crore over next two years ended FY24 and no major capex plans.

Debt coverage indicators also improved marked by Interest coverage and Total Debt/ Gross Cash Accruals of 5.34 times (FY21: 4.82 times) and 2.38 years respectively in FY22 (FY21 end: 2.63 years) due to reduction in debt levels.

Resourceful promoter group, along with healthy financial risk profile of FYPL's major shareholder:

FYPL is a part of the Falcon group of Rajkot (Gujarat) which has vast experience in the field of submersible pump and motor industry through its flagship company, Falcon Pumps Private Limited (FPPL). FPPL has a strong pan-India distribution network for pumps with more than 1300 dealers. Apart from above, the promoter group also has vast experience in other business segments such as pipes, cables and wires through their other group companies. FPPL holds 39% stake in FYPL as on March 31, 2022, providing good financial flexibility as it does not have any long-term debt obligations along with comfortable capital structure and debt coverage indicators. Also, the well-established 'Falcon' brand further strengthens the business risk profile of FYPL.

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE Ratings Ltd.'s publications

Established relationship with customers and suppliers:
Over a short span of around 5 years since commencement of operations, FYPL has developed healthy relation with its customers which facilitate it in securing repeat orders from them. FYPL sells cotton yarn to its customers located in Gujarat as well as outside Gujarat. FYPL has established a trading arm – Fair Deal to sell cotton yarn to its customers located outside Gujarat (to avail SGST subsidy benefit). Further, FYPL has also developed healthy relations with its suppliers. For last three years ending March 2022, the purchases of FYPL from its Top 5 suppliers stood at ~40-45% indicating moderate supplier concentration risk.

Favorable location of its manufacturing unit with proximity to cotton growing region:
The manufacturing facilities of FYPL are in Gondal district of Rajkot, Gujarat. Since Gujarat is India's major cotton producing belt, it helps FYPL to easily procure cotton from ginners in surrounding locality and offers FYPL locational advantage in terms of lower logistics expenditure (both on the transportation and storage) & ready availability of raw materials. Furthermore, proximity to select major Indian ports also aids its export-oriented sales profile.

Key Rating Weaknesses
Concentrated customer base:
FYPL has a concentrated customer base as Top five customers constituted around 75% of its FY22 sales (82% in FY21). Moreover, around 54% of the total sales were to a group entity Fairdeal, the trading arm of Falcon group, which also generated around 48% of its income from its Top five customers.

Decline in profitability due to steep increase in raw cotton prices:
FYPL's PBILDT and PAT margin declined by 505bps (to 6.17%) and 128 bps (to 2.75%) respectively in FY22 mainly due to steep increase in raw cotton prices, which accounted for around 88.74% of the total cost of sales (FY21: 82.77%). The prices of raw cotton are volatile in nature and depends upon factors like area under production, yield for the year, vagaries of the monsoon, international demand-supply scenario, inventory carry forward from the previous year and minimum support price (MSP) decided by the government. Collectively, these factors along with intense competition in the industry contribute to low bargaining power of yarn manufacturers like FYPL and volatility in profitability. Moreover, completion of eligibility period for interest subsidy and power tariff subsidy (FY22: Rs.6.32 crore) is also likely to impact its profitability.

Presence in highly fragmented and competitive textile industry:
India has the world's second largest spinning capacity, commanding a major share of the global yarn market. However, the textile industry in India is highly fragmented and dominated by a large number of medium and small-scale unorganized players, leading to high competition in the industry.

Industry outlook – near term headwinds:
Post first wave of Covid-19 pandemic, cotton spinners had gained momentum
supported by healthy export demand. With availability of low cotton inventory and improvement in operating efficiency, majority of cotton spinners reported all time high revenue and profitability during FY22. However, availability of raw cotton and its present elevated prices is posing a challenge. In the last 4-5 months till June 2022, the cotton prices have increased significantly due to lack of adequate availability of raw cotton in India. Government of India has allowed duty-free import of raw cotton till October 2022 to ensure adequate availability of cotton in domestic market. Presently, Indian raw cotton prices are 10-15% higher than international prices which is impacting the competitiveness of Indian spinning mills. Also, there is a shift in the demand from cotton yarn to blended/ manmade yarns due to the higher cotton prices.
Further, US and UK are the major cotton textile consuming nations globally which are facing a higher inflationary and rising interest rate scenario which may impact the demand temporarily. CARE Ratings expects that the sales volume and profitability of the industry players could be impacted adversely primarily in H1FY23 due to aforesaid near-term headwinds in the industry. However, it is expected that the cotton price shall fall from October 2022 with arrival of new cotton crop. On a long-term basis, Indian cotton spinners are expected to maintain stable demand growth and profitability supported by increasing urbanization, rising disposable income, China+1 strategy adopted by the major global retail players along with various incentives from government like Refund of Duties and Taxes on Exported Products (RoDTEP), Rebate of State and Central Taxes and Levies (RoSCTL) and Mega Integrated Textile Region and Apparel (PM MITRA) Parks etc.

Liquidity: Adequate
FYPL's liquidity remained adequate marked by moderate utilisation of working capital limits, lean operating cycle and healthy cash accruals vis-à-vis long-term debt obligations. Average utilisation of fund-based limits remained low at 5.53% during the trailing 12 months ended on August 2022. Operating cycle of FYPL continued to remain short at 7 days during FY22 (P.Y.: 8 days) due to low receivables and short inventory holding period. In FY22, cash flow from operation remained negative at Rs.3.06 crore mainly due to decrease in Trade payable and increase in inventory level. FYPL had unencumbered cash and bank balance of Rs.5.77 crore as on June 30, 2022.
As against expected gross cash accruals of over Rs.17-21 crore in FY23-25, FYPL has scheduled long term repayments of around Rs.14 crore annually, which signifies adequate liquidity cushion.

Analytical approach: Standalone, along with comfort derived from Falcon Pumps Private Limited (FPPL) being its largest shareholder.

Applicable Criteria:
Policy on default recognition
Financial Ratios – Non financial Sector
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Credit Watch
Short Term Instruments
Cotton Textile
Manufacturing Companies
Factoring Linkages Parent Sub JV Group

About the Company
Incorporated in June 2015 by Mr. Dhirajlal Suvagiya, Mr. Kamalnayan Sojitra, Mrs. Meeraben Sojitra, Mr. Reechi Kotadia, Mr. Jagdish Kotadia and Mr. Bhargav Suvagiya, Rajkot, Gujarat based FYPL is engaged in manufacturing cotton yarn. The company commenced manufacturing operations from December 2016.
FYPL has an installed capacity of 7,500 MTPA (35,904 spindles) for manufacturing of hosiery combed cotton yarn in the range of 24-40 counts. FYPL has installed windmill plant with 2.6 MW capacity for captive consumption which will save power cost of the company.
FYPL is part of the Falcon Group, whose flagship company is FPPL which is engaged in manufacturing and distribution of submersible pumps and motors under the brand 'Falcon'. FPPL holds equity stake of 39% in FYPL as on March 31, 2022.

Brief Financials (Rs. crore)	March 31, 2021 (A)	March 31, 2022 (P)	June 30, 2022 (P)
Total operating income	188.13	300.47	76.68
PBILDT	21.10	18.53	NA
PAT	7.58	8.25	NA
Overall gearing (times)	0.79	0.67	NA
Interest coverage (times)	4.82	5.34	NA

A: Audited, P: Provisional; NA: Not Available

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Covenants of rated instrument / facility: Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3.

Complexity level of various instruments rated for this company: Annexure-4.

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (₹ crore)	Rating Assigned along with Rating Outlook
Fund-based - LT-Term Loan		-	-	November 30, 2027	32.76	CARE BBB; Stable
Fund-based - LT-Cash Credit		-	-	-	10.00	CARE BBB; Stable
Non-fund-based - ST-Bank Guarantee		-	-	-	2.50	CARE A3+

Annexure-2: Rating history for the last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022	Date(s) and Rating(s) assigned in 2020-2021	Date(s) and Rating(s) assigned in 2019-2020
1	Fund-based - LT-Term Loan	LT	32.76	CARE BBB; Stable	-	1)CARE BBB; Stable (01-Oct-21)	1)CARE BBB-; Stable (04-Sep-20)	1)CARE BBB-; Stable (16-Aug-19)
2	Fund-based - LT-Cash Credit	LT	10.00	CARE BBB; Stable	-	1)CARE BBB; Stable (01-Oct-21)	1)CARE BBB-; Stable (04-Sep-20)	1)CARE BBB-; Stable (16-Aug-19)
3	Non-fund-based - ST-Bank Guarantee	ST	2.50	CARE A3+	-	1)CARE A3+ (01-Oct-21)	1)CARE A3 (04-Sep-20)	1)CARE A3 (16-Aug-19)

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Not Applicable

Annexure-4: Complexity level of various instruments rated for this company

Sr. No.	Name of Instrument	Complexity Level
1	Fund-based - LT-Cash Credit	Simple
2	Fund-based - LT-Term Loan	Simple
3	Non-fund-based - ST-Bank Guarantee	Simple

Annexure 5: Bank Lender Details for this Company

To view the lender wise details of bank facilities please **click here**

Note on complexity levels of the rated instrument: CARE Ratings Ltd. has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About us:

Established in 1993, CARE Ratings is one of the leading credit rating agencies in India. Registered under the Securities and Exchange Board of India, it has been acknowledged as an External Credit Assessment Institution by the RBI. With an equitable position in the Indian capital market, CARE Ratings provides a wide array of credit rating services that help corporates raise capital and enable investors to make informed decisions. With an established track record of rating companies over almost three decades, CARE Ratings follows a robust and transparent rating process that leverages its domain and analytical expertise, backed by the methodologies congruent with the international best practices. CARE Ratings has played a pivotal role in developing bank debt and capital market instruments, including commercial papers, corporate bonds and debentures, and structured credit.

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