Arex Industries Limited

December 17, 2018

Ratings

Facilities	Amount (Rs. Crore)	Rating[1]	Rating Action
Long term Bank Facilities	32.24 (reduced from Rs.33.82 crore)	**CARE BBB; Stable (Triple B; Outlook: Stable)**	**Reaffirmed**
Long term/Short term Bank Facilities	5.50	**CARE BBB; Stable / CARE A3+ (Triple B; Outlook: Stable/ A Three Plus)**	**Reaffirmed**
Total	**37.74 (Rupees Thirty Seven Crore and Seventy Four Lakh Only)**		

Details of facilities in Annexure-1

Detailed Rationale& Key Rating Drivers

The ratings assigned to the bank facilities of Arex Industries Limited (AIL) continue to derive strength from wide experience of promoters with competent management in woven labels manufacturing business, AIL's long-standing track record with well established manufacturing setup with latest technology machines, established relationship with reputed customers, healthy profitability margins, comfortable debt coverage indicators and adequate liquidity, and favourable demand scenario for woven labels.

The ratings are however, constrained on account of AIL's small scale of operations due to the niche product segment, working capital intensive operation, its presence in highly fragmented and competitive label manufacturing industry, vulnerability of profitability margins to volatility in raw material prices and stabilization and saleability risk associated with the large sized recently commissioned debt funded project.

AIL's ability to grow its scale of operations while maintaining its healthy profitability margins as well as ramp up in production and sales volume of its recently commissioned green field project and realisation of envisaged benefits are the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Wide experience of promoters in woven labels manufacturing business: The promoters of AIL have more than 25 years of experience in the woven label manufacturing business. Mr. Dinesh Bilgi, MD & CFO is the founder promoter of AIL and looks after the day-to-day operations of the company. He is supported by his two sons, Mr. Neel Bilgi and Mr. Chirag Bilgi. Mr. Neel Bilgi has done his Master in Business Administration and has nearly 12 years of experience. He looks after the marketing function of the company. Mr. Chirag Bilgi has done his bachelor in Business Administration and has nearly 10 years of experience. He looks after the production and technical aspect of the company. Further, the promoters are well-supported by the second-tier management.

Long-standing track record of operation having established relationship with reputed customers: AIL is one of the largest players in the organized sector in this niche segment of woven labels in the country with state-of-the-art manufacturing technology. AIL has a well-established clientele which include most of the leading ready-made garment and home-textile manufacturers in India. Further, over the years, the company has diversified its customer base. However, the revenue from top 10 customers continues to remain high at 57% of total operating income in FY18.

Healthy profitability margins, comfortable debt coverage and adequate liquidity: PBILDT margin although declined by 283 bps at 21.54% during FY18, it continue to remain healthy of over 20%. The PBILT margin declined during FY18 largely due to increase in raw material cost and fixed overhead associated with commencement of new plant at Anjar. Despite decline in PBIDLT margin, the PAT margin remained stable during FY18 at 9.15%. The debt coverage indicators also remained comfortable marked by PBILDT interest coverage of over 7 times and total debt to GCA of around 5 years during FY18.

Adequate liquidity: The liquidity of the company remained adequate marked by steady cash accruals, strong current ratio at 1.81 times as on March 31, 2018 and moderate average working capital utilisation at 47% for the past 12 months ended October 2018.

Favorable Industry scenario albeit competitive: Fortune of textile label is closely linked to the growth prospect of the Indian readymade garment / apparel industry. Government of India (GOI) is increasingly focusing on policy to create jobs that are good for development. The growth would also be driven by the factors like rising disposable income, increased usage of plastic money leading to impulsive buying among the Indian consumers. Also, the increasing percentage of the youth in the country together with rising urbanization, rising mall culture, changing fashion trends and retail penetration

[1]*Complete definitions of the ratings assigned are available at www.careratings.com and in other CARE publications.*

would continue to support the growth. However, the label manufacturing sector is highly competitive and fragmented due to presence of large number of unorganized players.

Key Rating Weaknesses

Small scale of operation: During FY18, total operating income (TOI) of AIL grew by 8% over FY17 largely due to increase in sales volume. The gradual growth in TOI is primarily driven by increasing sales volume supported by increase in capacities. However, the scale of operation of the company continued to remain small marked by total operating income of Rs.37.74 crore during FY18 and tangible net worth of Rs.24.17 crore as on March 31, 2018. The scale of operations has remained small due to company's operations in a niche product segment having relatively limited market size. The small scale of operation restricts the financial flexibility of the company as well as restricts the bargaining power with its large customers.

Working capital intensive operation: AIL has to maintain large stocks of various coloured yarns as demand for any particular colour may arise depending on the customer requirements. Further, time for execution of order is also elongated on account of designing process involved before finalizing the order which elongates the operating cycle. Moreover, the company deals with the large customers where company needs to extend higher credit period which too results into higher working capital cycle.

Stabilization and salability risk associated with large sized recently commissioned debt funded expansion project: The company has recently concluded a large sized green-filed expansion project at Anjar, Dist: Kutch, Gujarat with a total cost of Rs.37.76 crore (as against envisaged cost of Rs.36 crore) which was being funded through the term debt of Rs.27 crore and balance through the internal accruals. The commercial production started from August 2018. The new manufacturing facility of AIL is constructed on lease land acquired from Welspun India Limited (WIL: rated: CARE AA; Stable/ CARE A1+) which is adjoining to the manufacturing facility of WIL located at Anjar. AIL has entered into an agreement with WIL for selling its product exclusively to WIL for a period of 10 years. WIL has agreed to off-take minimum 75% of the production capacity. Further, in case of WIL unable to off-take minimum production quantity and AIL's manufacturing facility remains un-utilised, WIL will reimburse all fixed cost associated with facility. This arrangement reduces the saleability risk to certain extent although dependency on single customer increases the concentration risk.

Vulnerability of operating margin to volatility in raw material prices and limited ability to pass on the increase in cost to its customers: Cotton yarn and synthetic tape/ yarn are the key raw materials for AIL, the prices of which depends upon the raw cotton and crude oil prices. Over the years, the prices of both these commodities have remained highly volatile mainly due to change in global demand supply scenario. Moreover, AIL has lower bargaining power vis-à-vis its customers as the labels account for a very low value of the final garment manufactured by its customers. This coupled with presence of unorganized sector restricts company's ability to pass on fluctuations in input costs to customers.

Analytical approach: Standalone

Applicable Criteria

[Criteria on assigning Outlook to Credit Ratings]
[CARE's Policy on Default Recognition]
[Criteria for Short Term Instruments]
[CARE's methodology for manufacturing Companies]
[Financial ratios – Non-Financial Sector]

About the Company

Incorporated in 1989, AIL is promoted by Mr. Dinesh Bilgi. AIL manufactures various types of woven labels of Satin and Taffeta quality in white or black warp-base, of different shapes, sizes and colors depending on the customer's requirement. The demand for these labels mainly arises from apparels/ ready-made garments and home textile segment of the textile industry along with footwear industry. The company has an installed capacity to manufacture 16,842 million picks meters of labels as on September 30, 2018 at its sole manufacturing facility in Kalol, Gujarat. The company also has two windmills having an aggregated power generation capacity of 1.60 MW located at Porbandar, Gujarat.

(Rs. Crore)

Brief Financials of AIL	FY17 (A)	FY18 (A)
Total operating income	35.04	37.74
PBILDT	8.54	8.13
PAT	3.22	3.45
Overall gearing (times)	0.61	1.24
PBILDT Interest coverage (times)	8.41	7.43

During H1FY19, as per un-audited results, AIL reported a net profit of Rs.1.39 crore on total operating income of Rs.19.97 crore with PBILDT margin of 24.54% as against total operating income of Rs.18.21 crore and net profit of Rs.1.22 crore with PBILDT margin of 21.75% during H1FY18.

Status of non-cooperation with previous CRA: ICRA has suspended its rating assigned to AIL vide press release dated September 26, 2016 on account of its inability to carry out a rating surveillance due to non-cooperation by the company and absence of requisite information from the Company.

Any other information: Not Applicable

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

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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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 - LT-Term Loan	NA	NA	March, 2027	32.24	CARE BBB; Stable
Fund-based - LT/ST -Cash Credit	NA	NA	NA	5.50	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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based - LT-Term Loan	LT	32.24	CARE BBB; Stable	-	1)CARE BBB; Stable (20-Dec-17)	1)CARE BBB; Stable (14-Dec-16)	1)CARE BBB (18-Nov-15)
2.	Fund-based - LT/ST - Cash Credit	LT/ST	5.50	CARE BBB; Stable / CARE A3+	-	1)CARE BBB; Stable / CARE A3+ (20-Dec-17)	1)CARE BBB; Stable / CARE A3+ (14-Dec-16)	1)CARE BBB / CARE A3+ (18-Nov-15)

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