Precot Meridian Limited

August 13, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long-term Bank Facilities	137.76 (reduced from 181.62)	**CARE BB+; Stable (Double B Plus; Outlook: Stable)**	**Revised from CARE BBB-; Negative (Triple B Minus; Outlook: Negative)**
Short-term Bank Facilities	49.50	**CARE A4+ (A Four Plus)**	**Revised from CARE A3 (A Three)**
Long/Short-term Bank Facilities	158.50	**CARE BB+; Stable/CARE A4+ (Double B Plus; Outlook: Stable/A Four Plus)**	**Revised from CARE BBB-; Negative/CARE A3 (Triple B Minus; Outlook: Negative /A Three)**
Total Facilities	**345.76 (Rs. Three hundred forty five crore and seventy six lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of Precot Meridian Limited (Precot) takes into account the weak operating performance of the company with higher losses being reported year on year. The weak operating performance has led to a higher dependence on asset monetisation/promoter support to meet is debt service commitments in the past. Furthermore, with demand distortions caused by the Covid-19 pandemic, the cash flow from operations are expected to be weak in relation to the higher debt service commitments given the back ended nature of repayments.

The ratings continue to be constrained by Precot's relatively lower profitability margins in the spinning division and vulnerable to volatility in cotton/yarn price.

The ratings, however, derive strength from the company's long track record of operations of nearly six decades, long-standing experience of the promoters in the textile industry as well as the improvement of performance of Technical Textile Division.

Rating Sensitivities

Positive Factors

- Ability to improve profitability with PBILDT margins above 10% and report net profits, and generate adequate cash accruals with debt service coverage of more than 1.2x.
- Improvement in liquidity position with current ratio in the range of 1.3x-1.5x.

Negative Factors

- Sharp decline in the income levels and profits on account of an extended impact of the Covid pandemic
- Any large debt-funded capital expenditure leading to overall gearing above 1.5x.

Detailed description of key rating drivers

Key rating weaknesses

Decline in operating income and profitability during FY20: The operating income of the company had decreased by 8.36% in FY20 to Rs.729.61 crore from Rs.796.22 crore in FY19.The PBILDT margin declined from 8.13% in FY19 to 7.16% in FY20 on account of higher employee cost and raw material prices. On account of higher interest expenses on account of large debt availed in the past in TTD division, the company consistently reported net loss over past three years ended FY20. During FY20 Precot reported net loss of Rs.16.54 crore in FY20 as against net loss of Rs.8.28 crore in FY19.

Comfortable gearing however moderate debt protection metrics with continuous losses in the past: The overall gearing of the Company stood comfortable at 1.10x as on March 31, 2020 as against 1.14x as on March 31, 2019. However with lower accruals, the debt coverage indicators stood moderate with Total debt / GCA of 19.37x (PY: 15.35) as on March 31, 2020. The cash accruals decreased from Rs.23.09 crore in FY19 to Rs.16.20 crore in FY20

Volatility in raw material prices: During the past years, the market has seen volatility in cotton yarn production due to the unstable cotton prices and inconsistent cotton yarn export policy. The profitability of spinning mills depends largely on the prices of cotton and cotton yarn which are governed by various factors such as area under cultivation, monsoon, international demand-supply situation, etc. The cotton being the major raw material of spinning mills, movement in cotton prices without parallel movement in yarn prices impact the profitability of the spinning mills. The cotton textile industry is inherently prone to the volatility in cotton and yarn prices.

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

Key Rating Strengths

Established track record of the company: Precot with operational track record of nearly six decades is among the larger players in the spinning industry in Tamil Nadu.. Precot initially started with modest spindle capacity and gradually increased the capacity and has installed capacity of 1,95,451 spindles as on March 31, 2020, spread across six manufacturing units. The day to day operations are overseen by Mr. Ashwin Chandran, Chairman and MD of the company who is a qualified textile engineer from the UK and has nearly two decades of experience in the business.

Long-standing customer relationship with notable presence in export markets: The promoter group's long standing presence in textile business and established track record of Precot has helped the company to create strong customer base in domestic as well as export markets. Precot has a strong network of dealers/agents spread across India and export markets who facilitate the sale process of the company with key export markets being UK, US, Taiwan, Bangladesh etc

Improved performance in TTD Division: The income from TTD had increased from Rs.41.4 crore in FY17 to Rs.119 crore in FY20 at the CAGR of 30.20%. The PBILDT margin of TTD improved from 5.70% in FY19 to 14.36% in FY20 due to higher contribution of high margin products like Rolled and Finished goods. Though there has been improvement in TTD division, the TTD forms only 16% (PY: 12%) of Precot's total income in FY20, while spinning contributes to 80% (PY: 84%) of income which had not generated adequate accruals as anticipated for the year.

Liquidity: Stretched - The liquidity is stretched marked by tightly matched accruals against the repayment obligations and modest cash balance of Rs.0.35 crore (PY: Rs.0.69 crore) as on March 31, 2020. The current ratio of the company was below unity at 0.85x as on March 31, 2020, mainly on account of higher bank borrowings to support the operations of the company. The working capital cycle stood high at 93 days in FY20 (PY: 94 days) on account of higher raw material inventory holding of around 3 months. The company has been sanctioned working capital limits of Rs.188 crore including bill discounting of Rs.30 crore and the average utilization of the same stood at 78.84% for the past 12 months ended June 2020. The company had availed moratorium for the interest and principal during the period March-August 2020 as a relief measure offered by the banks for Covid-19 crisis.

Covid Impact

Indian cotton spinning industry, which was already facing multiple headwinds such as low demand, unfavourable duty structure and fluctuating cotton fibre prices, is confronting another challenge in the form of Covid-19 pandemic. The demand distortions are expected to hurt the domestic textiles production as well. Cancellation of export orders has led to build-up of inventories with the textile companies. Also, unsold stock with the industry players may soon run out of fashion for the next season to come which will add to the industry's burden. The operations of the TTD division of Precot resumed during April 2020 and Spinning units resumed operations partially from May 2020. The ability of the company to generate adequate cash accruals amidst demand distortions arising from Covid-Pandemic remains key rating sensitivity.

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
CARE's methodology for manufacturing companies
Liquidity Analysis of Non-Financial Sector Entities

About the Company

Precot Meridian Limited (Precot) was established in 1962 as Premier Cotton Spinning Mills by the brothers, Mr. V. N. Ramchandran and Late Mr. N. Damodaran. Precot is into the business of spinning of yarn catering to both domestic and export markets. Precot commenced its operations in 1964 with an initial capacity of 12,096 spindles at Kanjikode, Kerala. The company's installed capacity as on March 31, 2020 was 1,88,640 spindles, 195 rotors and windmills of 4 MW.
The company has commissioned the commercial operations in its technical textile division (TTD) from June 2013, which is a 100% export-oriented unit, set up in an SEZ. Under this segment the company manufactures high end value-added cotton based products which includes products like sanitary napkins, baby wipes, wet wipes, etc., largely catering to the healthcare and hygiene sectors. The Spinning division contributed to 80% (PY: 84%) of income in FY20 while TTD contributed to 16% (PY: 12%) of the income in FY20.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	796.22	729.61
PBILDT	64.72	52.25
PAT	(8.28)	(16.54)
Overall gearing (times)	1.14	1.10
Interest coverage (times)	1.55	1.56

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 - LT-Term Loan	-	-	March 2024	137.76	CARE BB+; Stable
Fund-based - LT/ ST-CC/Packing Credit	-	-	-	158.50	CARE BB+; Stable / CARE A4+
Non-fund-based - ST-BG/LC	-	-	-	49.50	CARE A4+

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 - LT-Term Loan	LT	137.76	CARE BB+; Stable	-	1)CARE BBB-; Negative (18-Nov-19) 2)CARE BBB-; Stable (25-Jul-19)	1)CARE BBB-; Stable (21-Sep-18)	1)CARE BBB-; Stable (10-Jul-17)
2.	Fund-based - LT/ ST-CC/Packing Credit	LT/ST	158.50	CARE BB+; Stable / CARE A4+	-	1)CARE BBB-; Negative / CARE A3 (18-Nov-19) 2)CARE BBB-; Stable / CARE A3 (25-Jul-19)	1)CARE BBB-; Stable / CARE A3 (21-Sep-18)	1)CARE BBB-; Stable / CARE A3 (10-Jul-17)
3.	Non-fund-based - ST-BG/LC	ST	49.50	CARE A4+	-	1)CARE A3 (18-Nov-19) 2)CARE A3 (25-Jul-19)	1)CARE A3 (21-Sep-18)	1)CARE A3 (10-Jul-17)

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Term Loan	Simple
2.	Fund-based - LT/ ST-CC/Packing Credit	Simple
3.	Non-fund-based - ST-BG/LC	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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About CARE Ratings:
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