Sutlej Textiles and Industries Limited

December 31, 2020

Ratings

Bank Facilities	Amount (Rs. crore)	Rating	Rating Action
Long-term - Term Loan	757.04 (enhanced from 688.34)	**CARE A; Stable (Single A; Outlook: Stable)**	**Revised from CARE A+; Stable (Single A Plus; Outlook: Stable)**
Fund Based- LT/ST-CC/ EPC/PCFC	600.00	**CARE A; Stable/CARE A1 (Single A; Outlook: Stable/A One)**	**Revised from CARE A+; Stable/CARE A1+ (Single A Plus; Outlook: Stable/A One Plus)**
Non-Fund Based-ST-LC/BG	45.30 (enhanced from 45.00)	**CARE A1 (A One)**	**Revised from CARE A1+ (A One Plus)**
Total	**1,402.34 (Rs. One thousand four hundred two crore thirty four lakh only)**		
Proposed Commercial Paper Issue^	300.00	**CARE A1 (A One)**	**Revised from CARE A1+ (A One Plus)**

^Carved out of the sanctioned working capital limits of the company.

Detailed Rationale and Key Rating Drivers

The revision of ratings assigned to the bank facilities of Sutlej Textiles and Industries Limited (STIL) factor in the weakening of company's credit profile in FY20 on account of deteriorating operational performance and H1FY21 on the wake of COVID-19 pandemic, delays and cost overruns in setting up the margin accretive green fiber plant, and lower than envisaged performance in home-textile division.

The ratings continue to derive strength from strong business profile being amongst India's well established players in the value added dyed spun yarn/specialty yarn segment and experienced management in the Textile industry (especially spinning segment). The ratings also factor in moderate debt coverage metrics and comfortable liquidity position.

The ratings are further tempered by working capital intensive nature of operations, susceptibility to fluctuation in raw material/product prices and fluctuation in foreign exchange imparting volatility to profitability and cyclical & competitive and fragmented nature of the industry

Positive Factors

- PBILDT margins of 12% and more on sustained basis
- Sustained profitability in home textile business

Negative Factors

- Higher than envisaged debt levels due to funding of going capex and/or higher working capital requirements leading to deterioration of capital structure i.e total outside liabilities to total tangible networth to 1.25x and beyond.
- Further delays in commissioning of the green fibre plant resulting in lower than envisaged cash accruals.

Detailed description of the key rating drivers Key Rating Strengths

Experienced Management in Textile industry: Sutlej Textiles and Industries Limited (STIL) was part of the erstwhile K.K Birla Group which was incorporated in 1932. In 2011 after the family division it came under Ms Nandini Nopany faction. Mr C.S. Nopany, grandson of late Mr K.K. Birla and son of Ms Nandini Nopany is the Chairman of company. STIL is led by a team of experienced professionals led by Mr S K Khandelia (President & CEO) and Mr Updeep Singh (Deputy CEO) both having over more 25 years' experience in Textile industry.

Diversified customer base: STIL has a diversified large customer base with no single customer accounting for over 5% of gross sales. Its top ten customers contributed ~17% to FY20 gross sales (PY: ~ 23%). STIL sells its products both domestically as well as exports it across the globe and its customers are geographically diversified. During FY20, the share of exports to the total income decreased to ~33%. The decrease in exports is mainly on account of reduction in lower margin trading export.

Key Rating Weaknesses

Weakening business profile: The company's yarn division has been reporting reduced profitability since FY17, from 10.01% to 5.67% in FY20. The contraction in profitability is mainly on account of company unable to pass in the increased costs to its customers. Further, the home textile division continues to post losses. Losses in FY20 reduced to Rs. 33.76 crore as against Rs. 38.14 crore in FY19.

The ability of the company to turnaround its home textile division on a sustained basis and improvement in margins from yarn division remains critical from credit perspective.

Moderation in FY20 operational performance; FY21 to be significantly impacted due to COVID-19: STIL reported a moderate dip in total income by 7.63% to Rs. 2,431 crore in FY20. The decline in total income was primarily on account of nationwide lockdown in the month of March 2020 and reduction in trading activities.

In FY21, the operational performance of the company has been significantly impacted due to complete lockdown in most parts of the country till May 2020, subsequent extension of localised lockdowns and discretionary nature of the apparels (end use) and other products manufactured by the company. Curtailed operations and continued losses from home textile division will lead to reduced cash flows and thereby impacting its debt servicing capabilities.

***Moderation in debt coverage ratios; albeit improvement in capital structure*:** STIL's financial risk profile is characterised by moderate capital structure and debt coverage ratios. Debt coverage indicators such as total debt to GCA deteriorated to 6.39 times respectively as on March 31, 2020 from 5.55x as on March 31, 2019. Interest coverage ratio has remained range bound -4.00-4.25 in FY20 and FY19.

Overall gearing continued to be moderate and marginally improved to 0.93 times as on March 31, 2020 on account of accretion of profits to reserves and scheduled debt repayment. Going ahead, overall gearing is expected to improve marginally albeit continue to remain moderate on account of fresh debt to be taken for the company's capex plan and reimbursement of previous capex despite high schedule repayments in FY21

Delays in capex due to COVID-19: Polyester staple fibre by recycling of pet bottles (Green Fibre plant) is estimated to have total capacity of 120mtpd at an estimated capital outlay of around Rs. 189 crore (mix of debt and internal accruals). The outbreak of COVID-19 has delayed the commissioning of the green fibre plant by approximately 9-12 months which has resulted in cost overruns. The company in Oct 2020 has started the trial run of 30 mtpd and is expected to commission the balance 90 mtpd by Q4FY21. The company till December 1, 2020 has incurred Rs.199 crore towards the expansion and is expected to further incur around Rs. 30 crore towards the same. The new plant will be in close proximity to its existing plant in Baddi, HP and the project is estimated to service ~75% of the polyester fibre requirements and improve operating margin from FY 22 onwards.

Home textile division continues to incur losses: In FY20, STIL's home textile division continued to impact the company's overall profitability on account of lower turnover and high fixed costs. The division posted a loss of Rs. 33.76 crore in FY20 as against a loss of Rs. 38.14 crore in FY19.

The division in Q1FY21 in the wake of COVID-19 pandemic posted a loss of Rs. 14.47 crore which has narrowed down to a loss of Rs 8.51 Cr in Q2FY21. The ability of the management to turnaround the home textile division as envisaged remains critical from credit perspective.

Cyclical and fragmented industry: STIL operates in a cyclical and fragmented textile yarn industry marked by organised as well as unorganised players. Intense competition in the industry limits the pricing abilities of the players in the industry. However, the risk is partly mitigated as STIL is among a few exclusive spinners in India for specialty yarns such as modal, lycra, tencil and other value-added yarns in the country apart from being one of the prominent manufacturers of dyed cotton blended/mélange yarn in the country.

Raw material volatility: Major raw materials used by STIL include cotton, polyester, viscose, etc. STIL procures raw material such as cotton fibre, polyester staple fibre (PSF) and viscose staple fibre (VSF). Cotton prices are volatile in nature driven by various factors like, area under cultivation, yield for the year, government regulation and pricing, etc. On the other hand, polyester being a derivative of crude oil is continuously affected by the movement in crude oil prices.

However the raw material volatility risk is mitigated to certain extent as it largely follows order base production policy and due to STIL's leadership position in the market which helps it to pass on increase in raw material costs to its customers to some extent.

Susceptible to volatility forex rates: During FY2019-20, STIL exported goods worth Rs. 785 crore (~33% of gross sales). STIL being a net exporter is susceptible to the volatility in forex rates. Although, STIL hedges almost entire export at the time of booking the order, the ability of the company to successfully manage its foreign exchange exposure remains key monitorable.

Industry Outlook

Cotton and cotton yarn

The Cotton Association of India (CAI) has projected cotton crop of 330 lakh bales for CS2019-2020, which is around 6% higher than the last season cotton crop of 312 lakh bales. However, on account of low demand (due to the Covid-19 pandemic), the prices of cotton fibre is expected to remain soft compared to the previous year.

The demand for cotton yarn is expected to decline significantly in H1FY21 leading to deterioration in the operational and financial performance of the companies engaged in the segment. Cotton yarn prices, which were already under pressure in FY20, are expected to decline further in FY21. However, cotton being a seasonal crop, major procurement by spinning mills happens till February/ March, thereby fixing their procurement costs. With yarn realization expected to decline, and majority of the procurement cost already fixed, the spread and profitability margins of the industry players are expected to witness a further deterioration. Also, with declining cotton prices, domestic spinners could be looking at inventory losses in the future. With major procurement of cotton almost done, majority players will be having limited cushion available in their working capital borrowings. Delay in payment from customers has also increased their reliance on the external borrowings. To address the liquidity concerns of the industry, some solace has been provided by the Reserve Bank of India (RBI) in the form of moratorium announced on the payment of term loan installment and interest on working capital borrowings along with easing of working capital financing. This will lead to many companies resorting to incremental working capital borrowings from banks.

CARE does not expect any major capacity increase in the industry in the next one year, with only a few large integrated players expected to undertake some capacity expansion. However, with declining profitability and increased working capital borrowings, CARE expects debt coverage indicators of the companies in the industry to remain under pressure at least in the next two quarters. Large companies having sufficient liquidity cushion in the form of cash & liquid investment and/ or unused working capital lines are expected to be better placed compared to their counterparts with limited liquidity cushion and holding large inventories.

Manmade Fibre/yarn

The demand for manmade fibre/ yarn is also expected to remain subdued due to low downstream demand. Also, exports will remain affected in the man-made fibre segment, which accounted for around 40% of the total man-made fibre production during FY19.

India is increasingly importing cheap apparel from Bangladesh, which sources cheap fabric from China. Not only is Bangladeshi apparel more affordable, but imports of clothing from Bangladesh also do not attract any duty under the South Asian Free Trade Agreement (SAFTA).

Decline in crude oil prices though will improve the liquidity position for MMF players but will also result in inventory losses. Synthetic fibre and yarn manufacturers are expected to benefit from removal of anti-dumping duty on purified terephthalic acid (PTA), the key raw material used to produce synthetic fibre and yarn, and lower PTA prices in FY21. While low raw material prices will ease some pressure on spinners' margins, sales revenues will continue to remain under pressure in FY21. Inverted duty at fabric stage has resulted in cloth manufacturers buying imported PSF and PFY. This is because unlike synthetic fabric, which attracts a GST of 5%, synthetic yarn attracts GST of 12%.

Liquidity Analysis: Adequate

The company's liquidity profile has been impacted on account of reduced cash accruals due to COVID-19 and high scheduled debt repayments. The liquidity profile, however, continues to be adequate as the company has headroom available in the form of undrawn working capital lines, moderate average utilisation of 52.46% for trailing 12 months Nov-2020 and envisaged GCA of Rs. 74.22 crore. The company has repaid Rs. 61.02 crore till December 1, 2020. The company has not availed moratorium on loans as allowed by RBI or any additional COVID limits.

Analytical Approach

For arriving at the ratings, CARE has considered the consolidated financials of STIL owing to financial and operational linkages with the subsidiary and common management.

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology-Manufacturing Companies
Rating Methodology for Manmade Yarn Manufacturing Sector
Rating Methodology-Cotton Textile Manufacturing

Criteria for Short Term Instruments
Financials Ratio-Non Financial Sector
Liquidity Analysis of Non-Financial Sector Entities
Rating Methodology: Consolidation

About the Company

Sutlej Textiles and Industries Limited (STIL) was incorporated in 2005 out of a corporate restructuring exercise in which the textile divisions of Sutlej Industries Ltd and Damanganga Processors Ltd were demerged to create a single cohesive company. STIL was part of the erstwhile K. K. Birla Group and after the family division it came under Ms Nandini Nopany. The company is currently managed by Mr C.S. Nopany (Chairman), grandson of late Mr. K.K. Birla and son of Ms. Nandini Nopany.

STIL is amongst India's leading producers of dyed spun yarn and value added/specialty yarn. It also manufactures fabrics and home textiles. As on March 31, 2020; STIL's spinning capacity was 420,840 spindles (vis-à-vis 418,680 spindles in FY2017-18), Home Textile Capacity was at 9.6 million meters p.a. as on March 20 (vis-à-vis 9.6 mmpa in FY17). Its manufacturing facilities are located in Bhawanimandi (Rajasthan), Kathua (Jammu & Kashmir), Daheli (Gujarat) and Baddi (Himachal Pradesh).

Further, during FY2017-18, STIL has Invested USD 4.5 Million (Rs. 30.64 crore) in Wholly Owned Subsidiary in USA. STIL Acquired Design, Sales, and Distribution (DS&D) business along with brand of American Silk Mills LLC (ASM) based at Plains, Pennsylvania.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	2632.19	2431.31
PBILDT	230.60	184.75
PAT	58.26	27.70
Overall gearing (times)	0.98	0.93
Interest coverage (times)	4.08	4.04

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	-	-	Jan-2029	757.04	CARE A; Stable
Fund-based - LT/ ST-CC/Packing Credit	-	-	-	350.00	CARE A; Stable / CARE A1
Non-fund-based - ST-BG/LC	-	-	-	45.30	CARE A1
Fund-based - LT/ ST-CC/Packing Credit	-	-	-	250.00	CARE A; Stable / CARE A1
Commercial Paper (Carved Out)	-	-	-	300.00	CARE A1

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	757.04	CARE A; Stable	-	1)CARE A+; Stable (03-Jan-20)	1)CARE A+; Stable (03-Dec-18) 2)CARE AA-; Stable (21-May-18)	1)CARE AA; Stable (11-Sep-17)
2.	Fund-based - LT/ ST-CC/Packing Credit	LT/ST	350.00	CARE A; Stable / CARE A1	-	1)CARE A+; Stable / CARE A1+ (03-Jan-20)	1)CARE A+; Stable / CARE A1+ (03-Dec-18) 2)CARE AA-; Stable / CARE A1+ (21-May-18)	1)CARE AA; Stable / CARE A1+ (11-Sep-17)
3.	Non-fund-based - ST-BG/LC	ST	45.30	CARE A1	-	1)CARE A1+ (03-Jan-20)	1)CARE A1+ (03-Dec-18) 2)CARE A1+ (21-May-18)	1)CARE A1+ (11-Sep-17)
4.	Fund-based - LT/ ST-CC/Packing Credit	LT/ST	250.00	CARE A; Stable / CARE A1	-	1)CARE A+; Stable / CARE A1+ (03-Jan-20)	1)CARE A+; Stable / CARE A1+ (03-Dec-18) 2)CARE AA-; Stable / CARE A1+ (21-May-18)	1)CARE AA; Stable / CARE A1+ (11-Sep-17)
5.	Commercial Paper-Commercial Paper (Standalone)	ST	300.00	CARE A1	-	1)CARE A1+ (03-Jan-20)	1)CARE A1+ (03-Dec-18) 2)CARE A1+ (21-May-18)	1)CARE A1+ (11-Sep-17)

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Commercial Paper-Commercial Paper (Standalone)	Simple
2.	Fund-based - LT-Term Loan	Simple
3.	Fund-based - LT/ ST-CC/Packing Credit	Simple
4.	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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