October 06, 2017

Kitex Garments Limited

Summary of rated instruments

Instrument	Rated Amount (in Rs. crore)	Rating Action
Term-loan facility	8.94 (reduced from 21.20)	[ICRA]AA- (Stable); re-affirmed
Short-term fund-based facilities	117.00	[ICRA]A1+; re-affirmed
Short-term non fund-based facilities	20.00	[ICRA]A1+; re-affirmed
Long-term/short-term unallocated	34.08 (revised from 21.82)	[ICRA]AA- (Stable)/ [ICRA]A1+; re-affirmed

*Instrument details are provided in Annexure-1

Rating action

ICRA has reaffirmed the long-term rating of [ICRA]AA-(pronounced ICRA double A minus) outstanding on the Rs. 8.94 crore term-loan facility (reduced from Rs 21.20 crore) of of Kitex Garments Limited ("KGL"/ "the Company")[1]. The outlook on the long term rating is 'stable'. ICRA has also re-affirmed the short term rating outstanding on the Rs. 117.00 crore fund-based facilities and the Rs. 20.00 crore non fund-based facilities of KGL at [ICRA]A1+ (pronounced ICRA A one plus). For the unallocated facilities of Rs. 34.08 crore (revised from Rs. 21.82 crore), a rating of [ICRA]AA- or [ICRA]A1+ would apply contingent upon the tenor of the availed facility.

Rationale

For arriving at the ratings, ICRA has consolidated the business and financial risk profiles of KGL and Kitex Childrenswear Limited (KCL, rated at [ICRA]AA-/Stable/[ICRA]A1+ and hereafter collectively referred to as "the Group"), owing to the common management and strong operational linkages.

The rating re-affirmation takes into account the established presence of the Kitex group in the infant wear export market backed by its track record and long standing relationship with leading international brands, its integrated manufacturing setup with a high level of automation enhancing operational efficiencies and its healthy financial profile characterized by a conservative capital structure and comfortable liquidity position. ICRA however notes that the business performance of the group has come under pressure during recent quarters owing to a slowdown in order inflows from its major customers, lack of new customer additions and loss of business from a few customers (scaling down of business with these retailers commenced from FY2016 on account of pricing and other specific reasons). Drop in revenues during FY2017, coupled with firm input costs and increase in fixed expenses impacted the profitability of the group. Going forward, the group's ability to grow volumes by new customer additions in the high value added infant wear segment would be a key moniterable. Further, despite a cumulative capital expenditure plan of about Rs 200 crore over the next three fiscals, steady earnings coupled with adequate cash balances are expected to result in the group remaining net debt negative during the period. The rating continues to factor in the relatively high customer concentration risk and limited pricing power, exposing the group's earnings to the risks of fluctuations in raw material prices and exchange rates which had impacted its earnings during FY2017. Nevertheless, these concerns are partly offset by the group's established market presence, strong operational efficiencies and a comfortable financial profile.

[1] *For complete rating scale and definitions, please refer to ICRA's website (www.icra.in) or other ICRA rating publications*

Key rating drivers

Credit strengths

- **Established presence in the infant wear export segment:** The Kitex group is amongst the largest exporters of infant wear from India, with a demonstrated track record and strong market position. Backed by the promoter's extensive experience in the apparel industry and long-standing relationship enjoyed with leading international brands based out of the US, revenues and earnings had recorded steady growth over the years. Presence in the niche infant wear segment, where stringent quality requirements and relatively complex manufacturing capabilities limits domestic competition, and continuous shift in sourcing by customers from other low cost countries to India owing to better compliance are expected to drive long term revenue growth
- **Integrated manufacturing facility:** The company has presence across knitting, processing and garmenting segments of the value chain, enhancing operational efficiencies; also, presence in value-added segment (printing and embroidery), coupled with strong operational infrastructure with high levels of automation supports better than average industry margins for the group
- **Healthy financial profile:** Kitex group enjoys strong financial flexibility, backed by its conservative capital structure with adequate coverage metrics and healthy cash balances (Rs 176 crore as on March 31, 2017) on the back of consistent earnings generated over the years. Despite the expenditure plan envisaged over the medium term, steady growth in earnings anticipated is likely to support the liquidity position with the group expected to remain net debt negative over the medium term

Credit weaknesses

- **High customer concentration risk:** Top three customers of the group contribute to more than 90% of volumes, which exposes revenues to vagaries in performance of its key customers as well as order cancellation and geo-political risks. Operating performance has been impacted during recent quarters resulting in revenue de-growth for the group by ~6% during FY2017, owing to lack of customer additions, stagnation in order inflow from existing customers and shift in product profile limiting realizations. Focused efforts towards customer additions supported by the marketing and design operations undertaken by the group in the US (through a joint venture between KCL and KGL) is likely to aid revenue growth over the medium term.
- **Limited pricing power** with established customers exposes earnings to fluctuations in raw material prices and exchange rates, as witnessed during FY2017 when the operating margins for the group fell by ~500 bps to 29%. The same coupled with the drop in export incentives and firm input costs are expected to restrict margin expansion in the near term despite the anticipated growth in orderbook / revenues in the coming quarters.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodology as indicated below:

Links to applicable criteria

Corporate Credit Rating Methodology
Rating Methodology for Indian Textiles Industry – Apparels

About the company:
Kitex Garments Limited was incorporated in the year 1992 and is currently managed by Mr. Sabu Jacob. The Company is a part of the larger Anna-Kitex Group, which has diversified interests in aluminium vessels, home appliances, spice trading and textiles. KGL is engaged in the manufacture and export of infant wear (less than 24 months) to apparel retailers based out of the US and UK. The Company has a fully integrated manufacturing facility at Kizhakkambalam (Kerala) with a facility to manufacture 2.7 lakh pieces per day and a fabric processing capacity of 42MTPD. KGL also supplies fabric to group entity Kitex Childrenswear Limited, which in turn holds 15.47% in the Company. To diversify its business profile and reduce dependence on its key customers, the Kitex group had established a marketing and design unit based out of the US during FY2015 (as a joint venture between KGL and KCL).

During FY2017, KGL reported a net profit of Rs. 83.8 crore on an operating income of Rs. 545.9 crore as against a net profit of Rs. 109.7 crore on an operating income of Rs. 545.8 crore during FY2016. For the quarter ended June 30, 2017, KGL reported a net profit of Rs. 18.0 crore on an operating income of Rs. 130.1 crore, as against a net profit of Rs. 21.1 crore on an operating income of Rs.119.3 crore for the similar period ended June 30, 2016.

Key financial indicators

Particulars	**FY2016**	**FY2017**
Operating income (Rs crore)	545.8	545.9
Operating profit before depreciation, interest, tax and amortization (OPBDITA in Rs crore)	188.8	175.3
Profit After Tax (Rs crore)	109.7	83.8
Operating profit margin (%)	34.6%	32.1%
Net Profit margin (%)	20.1%	15.3%
Return on capital employed (%)	39.4%	30.4%
Total Debt / Tangible Networth (times)	0.3	0.0
Total Debt / OPBDITA (times)	0.6	0.1
Interest coverage (times)	11.7	18.4
Net Working Capital /Operating Income (%)	14%	29%

Source*: Company, ICRA research*

Status of non-cooperation with previous CRA: Not applicable

Any other information: Not applicable

Rating history for the last three years:
Table:

Name of Instrument	Current Rating (September 2017)			Chronology of Rating History for the past 3 years		
	Type	Amount Rated (Rs. crore)	FY2018	FY2017	FY2016	FY2015
			Oct 2017	Aug 2016	July 2015	Aug 2014
Term-loan facility	Long-term	8.94	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]AA- (Stable)	[ICRA]A+ (Stable)
Short-term fund-based facilities	Long-term	117.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1
Short-term non fund-based facilities	Short-term	20.00	[ICRA]A1+	[ICRA]A1+	[ICRA]A1+	[ICRA]A1
Long-term/short-term unallocated	Long-term / Short-term	34.08	[ICRA]AA- (Stable)/ [ICRA]A1+	[ICRA]AA- (Stable)/ [ICRA]A1+	-	-

Complexity level of the rated instrument:
ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1

Instrument Details

Name of the instrument	Date of issuance	Coupon rate	Maturity Date	Amount rated (Rs. crore)	Current Rating and Outlook
Term-loan facility	-	-	April 2018	8.94	[ICRA]AA- (Stable)
Short-term fund-based facilities	-	-	-	117.00	[ICRA]A1+
Short-term non fund-based facilities	-	-	-	20.00	[ICRA]A1+
Long-term/short-term unallocated	-	-	-	34.08	[ICRA]AA- (Stable)/ [ICRA]A1+