

Kitex Garments Limited

India Ratings Assigns Kitex Garments' Bank Facilities 'IND A'; Outlook Stable

India Ratings and Research (Ind-Ra) has rated Kitex Garments Limited's (KGL) bank facilities as follows:

DETAILS OF INSTRUMENTS

Instrument Type	Date of issuance	Coupon Rate (%)	Maturity Date	Size of Issue (million)	Rating assigned along with Outlook/ Watch	Rating Action
Fund-based working capital facilities	-	-	-	INR1820	IND A /Stable/IND A1	Assigned
Non -fund-based working capital facilities	-	-	-	INR 380	IND A/Stable/IND A1	Assigned
Proposed Fund Based Working Capital Limit	-	-	-	INR 240	IND A/Stable/IND A1	Assigned

ANALYTICAL APPROACH

Ind-Ra has taken a combined view of Kitex Garments Limited, its associate entity Kitex Childrenswear Limited (KCL) and its wholly-owned subsidiary, Kitex Apparel Parks Limited (KGL; 70% stake & KCL: 30%) while assigning of ratings, as these entities operate under same management and have strong financial linkages among them.

DETAILED RATIONALE OF THE RATING ACTION

The ratings reflect Kitex group's leading position in infant garment export business and its strong clientele. The improving export demand in the textile industry, especially from the US shall auger well for the group amid China-plus-one sourcing strategy and political instability at Bangladesh. Also, the scale of operations is expected to improve as group is undertaking a large debt-led greenfield capex to set up an integrated textile manufacturing unit where there is fair revenue visibility from the group's existing customers. However, the rating is constrained by the increasing leverage due to debt funding for the capex which shall peak in FY26 , high customer and geographical concentration and inherent industry risks.

List of Key Rating Drivers
Strengths

- Business Profile Strengths
- Improvement in Operational Performance
- Strong product profile supporting healthy margins
- Moderate Credit Metrics; Deterioration Likely over FY25-FY26

Weaknesses

- Continued Ongoing Large Debt-led Capex
- High Customer and Geographical Concentration
- Raw Material Price Volatility; Forex Risk

DETAILED DESCRIPTION OF KEY RATING DRIVERS

Business Profile Strengths: Kitex group has an operational track record of over three decades and is one of the leading exporters of infant garments. The company has longstanding relationships with large reputed international retailers such as William Carter, Gerber, The Children's Place etc. leading to repeat orders from these clients. It has added new customers such as Sam's club, GAP, Walmart to its client list in 1H FY25 which supports revenue visibility. The group is setting up its new

unit in Telangana that shall benefit from low-cost labour and easy availability of key raw material (raw cotton) for the new unit. The new facility shall largely cater to increased demand from the group's existing customers, providing fair revenue visibility for the incremental capacities as well.

Improvement in Operational Performance: Kitex group's revenue grew to INR8,278 million in FYP24 (FY23: INR6,930 million, FY22: INR9,768 million) aided by increase in sales volumes, despite lower realisations. Ind-Ra expects the revenue growth to continue in the medium term with gradual increase in demand from existing and new customers as the export demand is recovering, which will be supported further by capacity additions. Ind-Ra expects, with China-plus-one sourcing strategy and political instability in Bangladesh, Indian garment exporters are better placed to increase their market share in global exports, subject to availability of adequate capacities.

Strong product profile supporting healthy margins: The Kitex group is into infant garments which have a niche market in textile industry. Infant garments require more focus on quality of products and are highly customized which lead to high value addition reflecting in their healthy operating margins. Further, the demand of these products are less affected by industry downturns as it is relatively less discretionary compared to adult garments. Group's EBITDA margins recovered and stood at 18.9% in FY24 (FY23: 13.5%, FY22: 24.2%) owing to a reduction in the raw material cost and better absorption of fixed costs on higher sales volumes. The group also benefits from export incentives from the Government of India supporting the margins. Although the agency expects EBITDA margin to improve in FY25 on account of recovery in the textile industry, the margin is expected to moderate in FY26 and FY27 on account of higher fixed overheads due to initial stages of operations at KAPL.

Moderate Credit Metrics; Deterioration Likely over FY25-FY26: The combined gross interest coverage (operating EBITDA/gross interest expense) remained comfortable but reduced to 14.94x in FY24 (FY23: 14.26x; FY22: 36.01x) on increased interest costs while the net adjusted leverage (adjusted net debt including letter of credit (LC)/operating EBITDAR) stretched to 4.22x (-0.07x; -0.17x) on increased term loan drawdown for ongoing capex.. Till FY23, the group did not have any term debt and was availing only working capital facilities. However, the combined gross debt is likely to increase further during FY25-FY26 with additional term debt drawdown planned for. Accordingly, Ind-Ra expects the net adjusted leverage to peak in FY26 and then gradually reduce thereafter, when the incremental cash accruals from the new capex start accruing. Also, given the long repayment tenure of term loans starting from FY26, Ind-Ra expects the group's cash inflows will support timely servicing of debt with Debt service coverage ratio estimated to be more the 1.15 times over medium term.

Continued Ongoing Large Debt-led Capex: Currently, Kitex group has an annual production capacity of 258.6 million pieces which is anticipated increase by 124% to 579.3 million pieces by FY27. This expansion is being undertaken as a greenfield project under KAPL in Telangana. The new enhanced capacity will be having fully integrated garment manufacturing unit which will cost around INR 33,250 million. The project will be funded through debt fund of INR 23,275 million (INR20,230 million sanctioned; balance likely to be sanctioned by end-November 2024) and remaining INR9,975 million through internal accruals of the group. Till August 2024, the group has incurred INR13,257 million (around 40% complete) which was funded through term debt of INR 8,251 million and remaining INR 5,006 million through internal accruals

As per management, the project will be operationalized in two phases. In first phase, Warangal unit is expected to fully operationalize by April 2025 in which spinning mill is expected to operationalize by Dec'24. Second phase, Sitarampur unit is expected to operationalize by April 2026.

Considering the management has more than three decades of experience in the garment industry and ~87% of the required bank loans have already been tied-up, the operational risk and funding risk are low. However, the demand risk will be associated with the project as new project will more than double the existing capacity of the group and there was under utilisation of the installed capacities in past two fiscals due to slow down in the textile industry. Furthermore, Ind-Ra expects the group's net adjusted leverage shall increase further and will be at its peak in FY26 post disbursement of the required term loans and gradual increase in working capital requirement; and reducing gradually thereafter. Timely servicing of interest and principal will be key monitorables. The project shall also be eligible for Telangana state incentives which may offer additional liquidity cushion. However, the benefits have not been factored for the purpose of our current assessment.

High Customer and Geographical Concentration: The company maintains longstanding relationships with large reputed international retailers such as William Carter, Gerber, The Childrens Place LLC among others. It leads to repeat orders which supports continued revenue visibility. The top five customers contribute almost 100% to the overall group revenue, although the concentration risk is somewhat mitigated by the fact that the counterparties are associated with the company for more than 10 years. The group's sales to US-based customers accounted for about 92% of the total sales in FY24 (FY23: around 93%) indicating high geographical concentration. However, considering US is one of the largest importers of apparels, the Kitex group's concentration is likely to sustain given the nature of the industry.

Raw Material Price Volatility; Forex Risk: Kitex Group's margins are vulnerable to fluctuations in price of raw materials however, the company has been able to pass on the volatility to the customers, albeit with a time lag as pricing of the order book is done on quarterly basis. Furthermore, the company mainly deals in export of infant garments and is exposed to fluctuations in foreign exchange rates basis its receivables from customers which are mainly US dollar denominated.

Liquidity

Liquidity Indicator - Adequate: The group's cash and cash equivalents stood moderate at INR725 million at FY24 (FY23: INR494 million; FYE22: INR1122 million). The average monthly maximum utilisation of its fund-based facilities was moderate at around 49% and non-fund-based facilities at 7% for the 12 months ending Aug'24. Further, group has longer tenor of repayment obligation with ballooning repayment structure which will lead to lower financial burden in the initial stages of operations. The group does not have any scheduled repayments for FY25, however, the repayments will start from FY26 amounting to INR 104 million. Further, the group will create Debt Service Reserve Account (DSRA) for principal and interest repayment obligation of one quarter which will support in case any shortfall.

The group's gross working capital cycle was stretched at 222 days FY24 (FY23: 184 days; FY22: 191 days) on account of increased inventory and delays in the receivable realization. The group has tied up long-term loans of INR20,230 million for the ongoing capex at KAPL (INR 8251 million availed till August 2024). Additional term loan requirement of INR 3045 million is likely to be sanctioned by end-November 2024. However, working capital limits for KAPL will be sanctioned before the operationalization of unit as and when required after that.

The group's combined free cash flow remained negative and stood at -INR6,769 million in FY24 (FY23: INR-683 million; FY22: INR-262 million) on the back of ongoing capex which started in FY22. Ind-Ra expects it to remain negative till FY27 on account of planned capex and increasing working capital requirement at KAPL.

RATING SENSITIVITIES

Positive: Improved business diversification, successful ramp up of the new asset's capacity with sizable EBITDA margins in KAPL, along with improved operational efficiency in the existing production capacity and working capital cycle, leading to the combined net adjusted leverage reducing below 2.5x on a sustained basis may lead to a positive rating action.

Negative: Lower than estimated profitability on a combined basis, any additional debt-led capex or any significant cost/time over run at KAPL leading to a stretch in liquidity may lead to a negative rating action.

Disclosures for CE Rating

NA

Disclosures for Provisional Rating

NA

ESG Issues

NA

Any Other Information

Standalone Performance: KGL recorded revenue of INR6,169 million during FY24 (FY23: INR5,570 million), EBITDA margin of 16.61% (11.49%) and interest coverage of 13.97x (14.32x). In FY24, the net leverage (including LC acceptances) stood at 0.29x (FY23: Net Cash).

About the Company

KGL is flagship company of the Kitex group which was incorporated in 1992. The company is engaged in manufacturing of infantwear garments with an installed capacity of 129.60 million pieces at its manufacturing facility at Kizhakkambalam unit in Kochi, Kerala. The company is listed in National Stock Exchange and Bombay Stock Exchange

KEY FINANCIAL INDICATORS - Combined

Particulars	Q1FY25	FY24	FY23
Revenue (INR million)	2,822	8,278	6,930
EBITDA (INR million)	723	1567	938
EBITDA margin (%)	25.63	18.93	13.53
Interest coverage (x)	22.92	14.94	15.07
Net leverage (x)		4.22	-0.07
Source: Company, Ind-Ra			

APPLICABLE CRITERIA

- Parent and Subsidiary Rating Linkage
- Rating Navigator - Textile Sector
- Evaluating Corporate Governance
- Short-Term Ratings Criteria for Non-Financial Corporates
- Corporate Rating Methodology
- The Rating Process

Status of Non-Cooperation with previous rating agency

Not applicable

RATING HISTORY

Instrument Type	Current Rating/Outlook		
	Rating Type	Rated Limits (million)	Rating
Fund-based working capital facilities	Long term/Short term	INR2060	IND A /Stable/IND A1
Non -fund-based working capital facilities	Long-/Short term	INR 380	IND A/Stable/IND A1

COMPLEXITY LEVEL OF THE INSTRUMENTS

Instrument type	Complexity Indicator
Fund-based working capital limits	Low
Non -fund-based working capital facilities	Low

For details on the complexity level of the instruments, please visit <https://www.indiaratings.co.in/complexity-indicators>.

ANNEXURE I- DETAILS OF INSTRUMENTS

Not applicable

ANNEXURE II- BANK WISE FACILITIES DETAILS

Please click here

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