Rating Rationale

Jayshree Company Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating[1]	Rating Action
Long Term Bank Facilities	67.22	**CARE-NP BB+ [Double B Plus]**	**Assigned**
Short Term Bank Facilities	532.78	**CARE-NP A4+ [A Four Plus]**	**Assigned**
Total Facilities	**600.00**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB+' to the long term bank facilities and 'CARE-NP A4+' to the short term bank facilities of Jayshree Company Private Limited (JSCP).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of JSCP are constrained by its fluctuating scale of operations, elongated operating cycle, foreign exchange fluctuation risk and raw material price volatility risk, vulnerability to changes in fashion trends and obsolescence risk associated with inventory. The ratings are also constrained by the residual project implementation risk and its presence in competitive nature of industry.

The ratings, however, derive strength from experienced promoters & established track record of operations, established brand presence & distribution network and its moderate profitability margins and capital structure.

Going forward, ability of the company to sustain growth in the scale of operations while managing its working capital requirement and maintaining the profitability margins & capital structure will remain the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Fluctuating scale of operations

Company's total operating income (TOI) has been fluctuating over the past three years (FY18-FY20). TOI has registered growth in FY19 and decline in FY20. The decline in TOI was mainly on account of impact on the business operations of the company as Government of Nepal (GoN) imposed lockdown in Q4FY20. In 9MFY21, the company has booked total revenue of Rs. 542 Mn.

Elongated operating cycle

The operating cycle of the company is elongated and stood high at 111 days in FY20 (Audited, refers to 12 months' period ended mid-July 2020). Being a highly competitive business, the company has to extend credit period to its wholesalers / dealers and the average collection period remained high at around 62 days

[1]*Complete definitions of the ratings assigned are available at* www.careratingsnepal.com

during FY20. The company is required to maintain adequate inventory of raw material for smooth running of its production processes. Furthermore, it is critical for the company to maintain the minimum levels of finished goods inventory (wide range of designs, shape, sizes, color etc) to meet the immediate demand of its customers. This resulted in average inventory holding days of more than 70 days in last 3 financials years (FY18-FY20). Also, company imports its raw materials through Letter of Credit at sight or usance depending upon credit terms of the suppliers. All this leads to reliance of the company on the bank finance for meeting its working capital needs. However, working capital utilization level against drawing power remained at moderate level over the period for 12 months' period ended mid-April 2021.

Residual project implementation risk with exposure to project stabilization risk

JSCP is planning to undertake an expansion project by installing new machineries which will increase the production capacity by 6 Mn pairs per annum. The total cost is envisaged at Rs 166 Mn. which will be funded through a debt equity mix of 72:28. The debt for the same has been tied up and it is expected the commercial production will commence from early FY22 from the enhanced capacity. The company has incurred Rs 93 Mn. till April end 2021 and all the required plant and machineries has been procured and erected in the premises. Due to debt funding for the project, its capital structure is likely to deteriorate going forward. Though the capital expansion will increase the company's installed capacity, company remains susceptible to risk related to the stabilization and streamlining of production process from the enhanced capacity.

Foreign exchange fluctuation risk and raw material price volatility risk

The company is mainly importing material from abroad and its import procurement to raw material cost stood around 70% for last three FY's (FY18-FY20). The material is completely sold in the domestic market. With initial cash outlay for procurement in foreign currency and significant chunk of sales realization in domestic currency, the company is exposed to the fluctuation in exchange rates. Though, the company hedges part of its foreign payments through forward contracts; JSCP is exposed it to sharp depreciation in the value of Nepalese rupee against foreign currency for the unhedged portion which may impact its cash accruals.

Raw material constituted more than 60% of the total cost of production for the last 2 years (FY19-FY20). The company is exposed to the raw material price volatility risk due to the volatility experienced in the prices of Ethyl Vinyl Acetate Copolymer (EVA), Low Density Polyethylene Polymer, Poly Vinyl Chloride (PVC) Resin which are crude derivative. The general volatility in the crude oil prices also has an impact on the price of this product. They constitute a major component of the raw material and any adverse movement in raw materials price without any corresponding movement in finished goods price is expected to affect the profitability of the company.

Vulnerability to changes in fashion trends and obsolescence risk associated with inventory

The footwear segment is driven by fashion trends and its target segment's aspirations. Therefore, their association with brands may change within a short span of time. Thus, manufacturers need to constantly innovate and adapt to the changing preferences of the target segment with its team of in-house designers who work on the upcoming season's collections and is expected to have the ability to adapt to the changing market trends.

Furthermore, companies need to manage their inventories according to fashion and changing trends. At times such fashion trends are short-lived, resulting into risk of inventory getting obsolete if it does not meet the taste and preferences of the customers. This could impact the financial profiles of entities operating in the business segment.

Competitive nature of industry

The footwear industry is intensely competitive and fragmented marked by the presence of both larger players with brand acceptability and numerous smaller players in the unorganized segment. The unorganized players in the industry do not have pricing power and are exposed to competition-induced pressures on profitability. The demand of footwear industry is also dependent upon the seasonal demand from the market.

Key Rating Strengths

Experienced promoters and established track record of operations

JSCP is a family run business and is managed under the overall guidance of its two-member Board of Directors (BoD) being Mr. Anuj Poddar and Mrs. Rubi Agrawal holding 100% share of the company. Mr. Anuj Poddar is the Director of the company with more than 2 decades of business experience and has involvement in various business sectors. He is also the director of Jayshree PU Tech and Jayshree Polymers Private Limited. By virtue of long experience of the promoters; the company has been able to attract experienced professionals from the industry, who adequately support the directors.

Established brand presence and established distribution network

JSCP has successfully established “Magic” as a brand name in footwear products in the domestic market. Additionally, the company has an established marketing and distribution network which comprises of 13 super distributors, more than 139 retailers and has a network of 11 retail stores (9 on franchise models and 2 are owned properties). JSCP has a strong marketing network across all major cities in the country which provides a ready market for its products.

Moderate financial profile

Despite the fluctuation in total operating income, PBILDT margin improved on y-o-y basis from 12.17% in FY18 to 19.14% in FY20 on account of change in product mix. The company has large product portfolio and profitability margins of the company are directly associated with quality and designing of product.

Better designed and superior quality products normally fetch better margins. Also, PAT margin of the company has shown an improvement trend which is in line with PBIDLT margin.

The company has moderate capital structure on account of conservative approach of promoters towards debt raising. On account of low debt levels and accretion of profit in the net worth, the overall gearing of the company stood moderate and stable at around 0.75x at the end of last 2 FYs (FY19 & FY20). Apart from overall gearing, other coverage indicators including total debt to GCA and Interest coverage ratios for the company stood comfortable at 1.70x and 9.45x for FY20 respectively (PY: 1.74x and 8.68x respectively).

Domestic footwear brands dominate market

Imported footwear is in decreasing trend as Nepal imported footwear of Rs 5.28 bn in FY20 as compared to import of Rs 7.51 bn done in FY19. This is mainly due to the production of quality and attractive designs footwear within the country which has led to decline in the import of foreign footwear. Also, footwear manufacturers are focusing on fulfilling internal demand for now which has resulted into decline in export by 15.19% in FY20 to Rs. 767 Mn. from Rs. 905 Mn. in FY19.

About the Company

Jayshree Company Private Limited (JSCP) was incorporated on June 26, 1983. The company manufactures slippers and sandals and as on mid-April 2021, it has total licensed capacity of 9.5 Mn pairs per annum. The manufacturing facility is located in Biratnagar, Nepal.

Brief financials of JSCP for last three years ending FY20 including 7MFY21 are given below:

(Rs. Million)

For the year ended Mid July	FY18 (Audited)	FY19 (Audited)	FY20 (Audited)	7MFY21 (Prov.)
Income from Operations	562	630	575	429
PBILDT Margin (%)	12.17	15.85	19.14	20.11
Overall Gearing (times)	1.04	0.74	0.75	0.85
Interest Coverage (times)	10.69	8.68	9.45	21.35
Current Ratio (times)	1.38	1.50	2.53	1.85
Total Debt/ Gross Cash Accruals (times)	2.56	1.74	1.70	2.60

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Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Term Loans	67.22	CARE-NP BB+
Short Term Bank Facilities	Working Capital Loans	273.00	CARE-NP A4+
Short Term Bank Facilities	Non-Funded Loans	257.00	CARE-NP A4+
Short Term Bank Facilities (Proposed)	Non-Funded Loans	2.78	CARE-NP A4+
Total		**600.00**	