

Jayshree Company Private Limited

Ratings

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

Details of Facilities/Instruments in Annexure 1

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

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of JSCP takes into account deterioration in the overall financial risk profile of the company amid decline in Total Operating Income (TOI) and sharp fall in profitability leading to moderation in debt service coverage indicators of the company in FY22 (Audited; FY refers to the twelve-month period ending mid-July). Amid sluggish demand scenario, the company's financial performance in FY23 is likely to remain suppressed, with uptick in margins year-on-year owing to slightly softened input prices to be offset by lower income levels and increased funding cost. The ratings also factor in JSCP's exposure to volatile interest rate, raw material price volatility risk, vulnerability to changes in fashion trends and obsolescence risk associated with inventory. The ratings also factor in JSCP's presence in competitive nature of industry and foreign exchange fluctuation risk associated with procurement of raw materials.

The ratings, however, derive strength from experienced promoters & established track record of operations, established brand presence & distribution network and stable demand outlook of footwear industry over the medium term.

Going forward, the ability of the company to profitably scale up its operations, manage its working capital requirements to support the growth in operations while improving its coverage indicators would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Elongated operating cycle resulting in working capital intensive nature of business

The operations of the company are working capital intensive in nature marked by high inventory holding at the end of FY22. Average inventory holding period elongated to 152 days at the end of FY22 from 97 days at the end of FY21. The company, being in the highly competitive footwear industry, has to maintain adequate raw material inventory for smooth running of production of different varieties of footwear. Furthermore, it is critical for the company to maintain the minimum levels of finished goods inventory (wide range of designs, shape, sizes and color) to meet the immediate demand of its customers. These factors resulted in high inventory holding at the end of FY22. Also, the company imports its raw materials majorly through Usance Letter of Credit, generally with credit period of 90-120 days. Being in a highly competitive industry, the company has to extend generous credit period to its dealers leading to an average collection period at around 95 days during FY22 (PY: 73 days). Consequently, net operating cycle of the company was high at 226 days in FY22, which increased from 150 days in FY21. A highly elongated operating cycle leads to reliance of the company on the bank finance for meeting its working capital needs.

Highly suppressed profitability along with decline in income levels in FY22

JSCP's TOI declined 16.78% year-on-year to Rs. 555 Mn during FY22 mainly on account of muted demand scenario during FY22. PBILDT margin declined sharply by 1,283 bps to 11.86% in FY22 as the company was not able to fully pass on the increase in input prices. Amid declining PBILDT coupled with increase in interest expense, PAT margin declined by 1,369 bps to 1.52% during FY22. Gross Cash Accruals (GCA) of the company declined by ~67% to Rs. 46 Mn during FY22. Overall gearing of the company stood moderate at around 1.15x at the end of FY22 which deteriorated from 1.03x at the end of FY21, mainly on account of increase in bank borrowings of the company. Consequently, JSCP's interest coverage ratio deteriorated to 3.03x during FY22 from 18.77x during FY21. Furthermore, JSCP's total debt/GCA deteriorated to 6.76x during FY22 from 1.95x during FY21.

During 9MFY23 (Unaudited, refers to the nine-month period ended mid-April 2023), JSCP reported TOI of Rs. 380 Mn with PBILDT margin to 19.35%.

Raw material volatility risk and foreign exchange fluctuation risk

Ethyl Vinyl Acetate Copolymer (EVA), Low Density Polyethylene Polymer and Poly Vinyl Chloride (PVC) Resin are the major raw materials for JSCP which are majorly imported from different countries and procured domestically. The prices of the JSCP's raw materials are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. Raw material cost contributed more than 70% of the total production cost of the company during FY21 and FY22. JSCP's overall profitability hugely depends on raw material prices and the company's ability to pass through the changes to the customers. While increase in raw material prices could be sudden and substantial, the company's ability to immediately pass through the changes could be limited, particularly in a competitive market, also reflected by the substantial drop in PBILDT margins in FY22. Hence, the company's overall profitability remains highly exposed to the volatility in input prices.

Furthermore, a substantial portion of JSCP's procurement is imported from India, China, and other countries. Foreign supplies other than from India, is invoiced in USD. In contrast, the company's income is majorly from the domestic market. With initial cash outlay for procurement in foreign currency and majority of sales realization in domestic currency, the company is exposed to the fluctuation in foreign currency exchange rates. Since, the company does not hedge its foreign exchange exposure, JSCP is exposed to any sharp depreciation in the value of Nepalese rupee against USD which may impact its cash accruals.

Vulnerability to changes in fashion trends and obsolescence risk associated with inventory with its presence in highly competitive footwear industry

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 in risk of inventory becoming obsolete if it does not meet the taste and preferences of the customers. This could adversely impact the financial profiles of entities operating in the business segment.

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

Exposure to volatile interest rate

JSCP had Rs. 22 Mn as finance cost in FY22, which increased from Rs. 9 Mn in FY21, thus squeezing its net profitability. JSCP's interest expenses are based on a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. Thus, funding taken by the company is exposed to volatile interest rate.

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). Mr. Anuj Poddar and Mrs. Rubi Agrawal are the directors holding 100% of total share capital of the company. Mr. Anuj Poddar, is also the partner in Jayshree PU Tech (CARE NP BB-/A4, manufacturer of PU shoes) and Jayshree Polymers Private Limited (manufacturing of PU, PVC and sports footwear), with more than two decades of experience in related business. Mrs. Rubi Agrawal, has considerable business experience in footwear industry. The experience of the promoters in footwear industry bodes well for the overall business prospects of the company in an increasingly competitive industry. Furthermore, the BoD are supported by an experienced team across various functions. The company has an established track record of operations of more than three decades in the manufacturing of footwear products in Nepal.

Established distribution network and brand presence

JSCP has an increasing presence across nation reaching major towns and cities of Nepal. At the end of mid-January 2023, the company had around 27 dealers across the country. The strong marketing network across all major cities in the country provides a ready market for its products. Furthermore, the company, along with other group companies, sells its products under the brand name "Magic", which is an established name in the footwear segment in the domestic market.

Stable demand outlook of footwear industry over medium term

The footwear manufacturing business in Nepal is increasing in high numbers over the past years after pandemic. There is a growing demand for locally-made, high-quality footwears that is fashionable and affordable in the market. Nepal's proximity to large footwear markets like India and China also make it easy for the procurement of raw materials. Manufacturers like JSCP could benefit from the increasing demand for locally manufactured footwears in the country over the medium-term.

About the Company

Jayshree Company Private Limited (JSCP) was incorporated on June 26, 1983. The company manufactures slippers and sandals. As on mid-July 2022, it had total production capacity of 12 Mn pairs per annum. The manufacturing facility is located in Biratnagar, Nepal.

Financial Performance

(Rs. Million)

For the period	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	575	667	555
PBILDT Margin (%)	19.14	24.69	11.86
Overall Gearing (times)	0.76	1.03	1.15
Total Outstanding Liabilities/ Tangible Net Worth (times)	1.00	1.29	1.25
Interest Coverage (times)	9.45	18.77	3.03
Current Ratio (times)	2.70	1.44	1.91

Total Debt/Gross Cash Accruals (times)	1.72	1.95	6.76
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A: Audited

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 Loan	67.22	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limits	273.00	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non-Fund Based Limits	259.78	CARE-NP A4 [A Four]
Total		600.00	

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