October 28, 2021

Kalyan Jewellers India Limited: Long term and medium-term ratings upgraded; short-term rating reaffirmed

Summary of rating action

Instrument*	Previous rated amount (Rs. Crore)	Current rated amount (Rs. crore)	Rating Action
Long Term - Fund Based TL	85.00	166.00	[ICRA]A (Stable) upgraded from [ICRA]A-(Stable)
Long term / short term - Fund based	2,945.00	2,559.00	[ICRA]A (Stable) upgraded from [ICRA]A-(Stable); [ICRA]A2+ reaffirmed
Short Term - Interchangeable	(1,390.00)	(1,033.00)	[CRA]A2+ reaffirmed
Long term - Unallocated	0.00	305.00	[ICRA]A (Stable upgraded from [ICRA]A-(Stable)
Medium term - Fixed deposit	525.00	525.00	MA(Stable) upgraded from MA-(Stable)
Total	**3,555.00**	**3,555.00**	

**Instrument details are provided in Annexure-1*

Rationale

The long-term and the medium-term ratings upgrade reflects the expected improvement in performance of Kalyan Jewellers India Limited (KJIL) over the medium term, driven by favourable demand conditions and better business diversification. Besides, KJIL's capitalisation levels improved after the equity infusion of Rs. 750 crore (net proceeds) made through the initial public offering (IPO) in March 2021. Post the pandemic-induced business disruptions witnessed in the major part of H1 FY2021, KJIL's operating performance recovered strongly in the second half of the fiscal. Its diversified presence and strong market position in the domestic jewellery retail market and improved consumption levels seen in the industry owing to strong wedding-related demand supported its performance in H2 FY2021. KJIL's strong performance in the second half limited the YoY revenue decline to around 15% in FY2021 against the ~48% decline witnessed in H1 FY2021. Its revenues and earnings in FY2021 were also limited by the closure of six stores in the Middle East market and related one-time expenses because of the adverse impact of the pandemic. KJIL's operating margins remained at ~8.5% in FY2021, in line with the FY2020 levels, supported by the inventory gains and various cost reduction measures undertaken by the company. With favourable demand conditions continuing in the current fiscal (except during the second wave of the pandemic in May and June 2021), ICRA expects KJIL to register a revenue growth of more than 10% over the medium term. Growth in the coming quarters would also be supported by the proposed expansion of store network as well as a steady shift witnessed towards organised players in the industry. While ICRA expects KJIL's margins to witness some correction in FY2022 post the high margin seen in the preceding fiscals, it is expected to stabilise at around 8% over the coming fiscals driven by the focused initiatives undertaken to improve inventory turnover and share of studded jewellery.

The ratings continue to factor in the moderate coverage metrics and return indictors, limited by the high working capital requirements in the business and modest inventory turnover witnessed. Nevertheless, with the expected improvement in inventory turnover and lower interest costs, ICRA expects KJIL's interest coverage to improve to around 3.5 times over the next 12 to 18 months. Further, with the incremental working capital requirements being funded with the cash reserves held post the IPO and earnings from operations, KJIL's adjusted[1] total outside liabilities to the tangible net worth (TOL/TNW) and

[1] Total outside liabilities adjusted for cash and lease liabilities

adjusted total outside liabilities to inventory are likely to remain at comfortable to around 1.5 times and 80%, respectively in FY2022. The ratings also consider the intense competition, which limits pricing flexibility and exposes earnings to volatile gold prices and regulatory risks, which had impacted the retailers' performance in the past.

The Stable outlook on the rating reflects ICRA's expectations that the company's operational and financial performance will continue to benefit from the favourable demand conditions, its strong market position, improving business diversification and comfortable capitalisation levels.

Key rating drivers and their description

Credit strengths

Established market position – KJIL is one of the largest jewellery retailers in India with a strong brand name of Kalyan, enjoyed across the markets. Further, it has a diversified geographical presence with 40% of its revenues derived from non-South and Middle East markets. The company has been diversifying geographically to non-South markets over the last five years. KJIL's product diversity also improved with increasing sale of margin-accretive studded and diamond jewellery across the non-South markets. The vast experience of the promoters in the gold jewellery industry for three decades coupled with its focus on providing jewellery designs as per specific tastes and preferences of the customers enabled the company to establish its strong presence across the country and capture a loyal customer base. Further, the presence of Highdell Investment Limited (Warburg Pincus Group) and independent directors on the board post the recent IPO, complimented by a professional management team, provides additional comfort on systems and governance.

Growth prospects in jewellery segment owing to large industry size and fragmented market share – Increasing regulatory restrictions in the jewellery segment, aimed towards greater transparency and higher compliance costs have been resulting in a sizeable churn in the unorganised segment, thus benefiting organised players like KJIL over the years. Further, with the company's sizeable presence across India, and regulatory changes such as mandatory hallmarking of gold jewellery from Q2 FY2022 would further support the organised trade and provide better opportunities in the near term. Moreover, its expanding presence in the non-South markets and widening customer network through the jewellery savings scheme and My Kalyan stores have supported its revenue base.

Credit challenges

Moderate coverage metrics – The geographical diversification led to an improvement in the company's revenues from the margin-accretive studded jewellery segment. However, its rapid expansion resulted in increased stocking requirements and slower inventory turnaround compared to the industry. The same coupled with the pandemic impacted its operating performance. The company's coverage metrics remained at moderate levels, with an interest cover of around 2 times in FY2021. The ROCE levels remained modest with slower-than-expected ramp-up of new stores launched in the recent years. Nevertheless, KJIL's coverage indicators and return indicators are expected to improve with the expected improvement in inventory turnover and earnings in the coming quarters with no incremental debt to be availed for expansion (to be funded with cash reserves and earnings). Further, KJIL's capitalisation levels and liquidity position improved with the recent fund raising. The adjusted TOL/TNW improved to 1.5 times in FY2021 from around 2.1 times in FY2020.

Intense competition and exposure to regulatory risks – Certain adverse regulatory developments have impacted the domestic gold jewellery industry in the past. Restrictions on bullion imports and metal loan funding, mandatory PAN disclosure on transactions above a certain limit, and imposition of excise duty are some of the adverse regulatory developments that have taken place over the last four years. KJIL will remain exposed to the risks of any such future regulatory actions that may impact its business profile. Further, the jewellery retail business is highly fragmented and is exposed to intense competition from other organised and unorganised players, which limits its pricing flexibility and same store revenue growth to an extent. However, the company has been able to establish itself as a pan-India player over the last few years and has steadily witnessed an improvement in the margin-accretive studded jewellery segment over the years, supporting its overall margins.

Liquidity position: Adequate

KJIL's liquidity position is expected to remain adequate, supported by steady earnings from operations coupled with unutilised lines of credit enjoyed and adequate free cash balances. Cash buffer, including free cash reserves, liquid investments and unutilised working capital limits together stood at around Rs. 660 crore as on March 31, 2021. The average utilisation of its fund-based limits over the last 12 months ending June 2021 stood at around 90%. KJIL is expected to generate accruals of more than Rs. 400 crore in the fiscal against its funding requirements towards capital expenditure estimated at ~Rs. 100 crore in FY2022 along with Rs. 160 crore of debt repayments. The incremental working capital requirements to support the expansion are likely to be funded through a mix of surplus earnings and funds raised through IPO.

Rating sensitivities

Positive factors – The ratings may be upgraded if the company registers a sustained healthy growth in revenues and earnings, and improve its inventory turnover, which in turn would support improvement in its credit metrics and return indicators.

Negative factors –Pressure on KJIL's ratings may arise if there is a sustained pressure on the operating performance or a further deterioration in the working capital cycle, which would adversely impact its coverage metrics and liquidity position. Specific credit metrics that may lead to a rating downgrade include adjusted TOL / TNW exceeding 1.8 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in Gold Jewellery - Retail Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The rating is based on the consolidated financial statements of the company.

About the company

KJIL, managed by Mr. T.S. Kalyanaraman and his sons, is an established jewellery retailer in the domestic markets with a presence for more than three decades. The company had 117 showrooms in India as on September 30, 2021 of which 73 were in South India and the remaining 44 in non-South markets. In December 2013, the company had expanded its footprint to the Middle East market with six showrooms. KJIL had 30 showrooms in the Middle East as on September 30, 2021 after closing six showrooms in FY2021. The company was listed on the Bombay Stock Exchange and the National Stock Exchange in March 2021 with the promoter holding around 60% stake in the company, Highdell Investment Limited (Warburg Pincus Group) holding around 26% stake and public holding the rest.

Key financial indicators (audited)

KJIL (consolidated)	FY2020	FY2021
Operating Income (Rs. crore)	10,128.0	8,584.1
PAT (Rs. crore)	142.3	-6.1
OPBDIT/OI (%)	8.3%	8.8%
PAT/OI (%)	1.4%	-0.1%
Total Outside Liabilities/Tangible Net Worth (times)*	2.1	1.5
Total Debt/OPBDIT (times)*	3.4	3.2
Interest Coverage (times)	2.0	1.9

*Source: Company; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Net Debt: Debt adjusted for free cash reserves *adjusted for cash & cash equivalents and lease liability*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as on September 30, 2021 (Rs. crore)	Date & Rating in	Date & Rating in FY2021	Date & Rating in FY2020	Date & Rating in FY2019
					October 28, 2021	October 26, 2020	September 09,2019	November 05,2018
1	Term Loans	Long term	166.0	77.3	[ICRA]A (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)
2	Fund Based – Working Capital Facilities	Long term/Short term	2559.0	-	[ICRA]A (Stable)/ [ICRA]A2+	[ICRA]A- (Stable) / [ICRA]A2+	[ICRA]A- (Stable) / [ICRA]A2+	[ICRA]A- (Positive) / [ICRA]A2+
3	Fund-based/Non-fund Based (sublimit)	Short term	(1033.0)	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
4	Unallocated Limits	Long term	305.0	-	[ICRA]A (Stable)	-	-	-
5	Fixed Deposits Programme	Medium term	525.0	-	MA (Stable)	MA- (Stable)	MA- (Stable)	MA- (Positive)

Source: Company; Amount in Rs. Crore

Complexity level of the rated instrument

Instrument	Complexity Indicator
Term Loans	Simple
Fund Based – Working Capital Facilities	Simple
Fund-based/Non-fund based (sub limits)	Very Simple
Unallocated Limits	Not Applicable
Fixed Deposits Programme	Simple

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analyzing an entity's financial, business, industry risks or complexity related to the structural, transactional, or legal aspects. Details on the complexity levels of the instruments, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loans	FY2021	-	FY2023	166.00	[ICRA]A (Stable)
NA	Fund Based – Working Capital Facilities	-	-	-	2559.00	[ICRA]A (Stable)/[ICRA]A2+
NA	Fund-based/Non-fund based (sub limits)	-	-	-	(1033.00)	[ICRA]A2+
NA	Unallocated Limits	-	-	-	305.00	[ICRA]A (Stable)
NA	Fixed Deposits Programme	-	-	-	525.00	MA(Stable)

Source: *KJIL*

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidated approach
Kalyan Jewellers FZE	100%	Full Consolidation
Kalyan Jewellers Inc.	100%	Full Consolidation
Enovate Lifestyles P Limited	77%	Full Consolidation

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About ICRA Limited:

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