June 24, 2022

# Indian Terrain Fashions Limited: Ratings reaffirmed; outlook revised to Stable

## Summary of rating action

| Instrument* | Previous Rated Amount (Rs. crore) | Current Rated Amount (Rs. crore) | Rating Action |
|---|---|---|---|
| Long-term fund-based Working Capital Facilities | 37.50 | 37.50 | [ICRA]BBB+ reaffirmed; outlook revised to Stable from Negative |
| Short-term non-fund-based Working Capital Facilities | 8.00 | 8.00 | [ICRA]A2; reaffirmed |
| Long-term fund-based Term Loans | 6.83 | 9.99 | [ICRA]BBB+ reaffirmed; outlook revised to Stable from Negative |
| Unallocated limits | 7.67 | 4.51 | [ICRA]BBB+/[ICRA]A2 reaffirmed; outlook revised to Stable from Negative |
| **Total** | **60.00** | **60.00** | |

**Instrument details are provided in Annexure-1*

## Rationale

The ratings reaffirmation and revision in outlook reflects the expected improvement in the operating and financial performances of Indian Terrain Fashions Limited (ITFL) in the coming quarters, on the back of its established position in the men's branded apparel segment, and steady demand conditions as witnessed in the recent past. Post the impact of the pandemic-induced business disruptions on ITFL's performance in FY2021 and Q1 FY2022, the company's operations have improved gradually, supported by growth in discretionary spend and better footfalls across distribution channels. ITFL witnessed a revenue growth of 51% in FY2022 and is likely to grow further by around 35% in FY2023 backed by stable demand, proposed store expansion and healthy brand equity enjoyed by the 'Indian Terrain' brand. ITFL's operating margins have improved to around 11-12% in the recent quarters, backed by favourable pricing and better economics of scale with the recovery in demand. The overall operating and net margins were at 8.0% and -0.7%, respectively, in FY2022, limited by the modest performance in the beginning of the fiscal (the same is post net losses of around Rs. 30 crore incurred in FY2021). The expansion in operating margins in the near-term is likely to be limited due to the sharp increase in raw material prices. The operating margins for FY2023 are expected to be at ~11% and improve to around 13% over the medium term upon stabilisation of raw material prices.

ITFL's coverage metrics are also expected to improve in the current fiscal, backed by the growth in scale and operating profits in FY2023. The key metrics like interest coverage ratio is likely to improve to around 3 times for FY2023, post the operating losses incurred in FY2021 and modest levels of 1.4 times in FY2022. With expected steady growth in earnings from operations and proposed reduction in debt levels through focused efforts on reducing the receivables position, the interest coverage ratio is likely to improve to around 4 times over the medium term. The ratings also continue to factor in ITFL's high working capital intensity, characterised by its high receivables position on the back of an extended credit enjoyed by its channel partners. However, the working capital cycle is expected to improve over the medium term, with ITFL focusing on reducing its receivables position to around 180 days over the next 12-18 months. Despite the high working capital requirements, ITFL's liquidity position is expected to remain adequate, supported by the likely growth in earnings and recent fund infusion of Rs. 7.5 crore in Q1 FY2023, along with better collections. ICRA expects ITFL's performance over the medium term to be supported by its established presence in the domestic men's branded apparel segment and continued efforts made to improve business diversity and reduce its receivables position.

# Key rating drivers and their description

## Credit strengths

**Established presence in domestic menswear segment –** ITFL's flagship brand, 'Indian Terrain', enjoys strong recall in the men's casual wear segment, especially in South India, with a presence of over two decades. The company has a strong multi-channel distribution network of more than 220 exclusive brand outlets (EBO), 515 large format stores (LFS) and over 1,350 multi brand outlets (MBOs) across 140 cities. While the EBOs allow the company additional flexibility in promotion and brand building, enabling direct engagement with customers, the MBO channel helps ITFL expand its geographical presence with minimal investments. ITFL also generates around 15% of sales through e-commerce portals. Despite high dependence on the menswear segment, an established presence and favourable growth prospects for the branded apparel industry are likely to aid in the company's growth over the medium term.

**Improvement in operating performance in recent quarters and conservative capital structure –** ITFL's revenues and earnings have witnessed steady growth in the recent past, backed by the recovery in demand across sales channels, focused marketing efforts undertaken and strong footfalls, with the demand having largely reached the pre-Covid levels by Q4 FY2022. The same was post the modest performance in FY2021 and H1 FY2022, because of the pandemic-induced demand disruptions across states and distribution channels. Further, ITFL's credit profile remains supported by its conservative capital structure notwithstanding the high working capital funding requirements in the business, ITFL's dependence on external debt has remained low over the years. Despite lower earnings and a consequent increase in the working capital requirements in the recent past, ITFL's capital structure remains at comfortable levels. The key ratios including gearing and total outside liabilities to tangible net worth (TOL/TNW) stood at around 0.6 times and 1.3 times, respectively, in FY2022.

## Credit challenges

**High working capital intensity** – The apparel retail business inherently entails high working capital requirements towards stocking garments across a wide product range in its outlets and high credit enjoyed by distribution channel partners. While ITFL's inventory turnover is comfortable with its sales distributed across channels, its receivables position remains stretched on the back of an extended credit enjoyed by the MBO, LFS and e-commerce channel partners. However, despite this, its receivables position has improved to some extent in the recent past with the recovery in demand. Nevertheless, an expected improvement in the working capital cycle and ITFL's adequate liquidity position provide some comfort.

**Exposure to consumer spending trends and intense competition, and resultant pressures on operating performance –** The branded men's wear segment is characterised by intense competition, with continuous expansion undertaken by a number of established brands across regions. The same mandates continued high marketing spend for retailers, limiting operating margins of market players. ITFL's sales, profitability and cash accruals, like any other apparel retailer, are closely linked to macro-economic conditions, consumer confidence and spending patterns, particularly considering the discretionary nature of its products. Besides, its sales remain vulnerable to the consumers' changing tastes and preferences, and the competition from other large, branded players in the menswear segment. ITFL's proposed entry into new markets, and an expected increase in sales promotion expenses are likely to limit its margin expansion over the medium term. However, an established presence and favourable growth prospects for the branded apparel industry are likely to aid in volume growth over the medium term. Also, the ongoing efforts to improve penetration in North and Central India are likely to reduce revenue concentration from the southern markets over the coming fiscals.

# Liquidity position: Adequate

ITFL's liquidity position is expected to remain adequate in the coming quarters, supported by growth in earnings from operations and free cash reserves, including liquid investments of Rs. 25 crore in end of May 2022. The average utilisation of its working capital limits over the last 12 months ending May 2022 stood at around 91%, given the high working capital requirements in the business. Given the limited debt repayment obligations and capital expenditure requirements over the next 12 months, ITFL's incremental working capital requirements are likely to be funded through cash accruals, which lends comfort to its liquidity position.

## Rating Sensitivities

**Positive factors –** The ratings may be upgraded if a sustained growth in revenues and earnings, coupled with improvement in the working capital cycle improves ITFL's debt protection metrics. A specific credit metric for an upgrade is if interest cover improves to more than 4 times, on a sustained basis.

**Negative factors –** Pressure on ITFL's ratings may emerge if there is a sustained pressure on revenues and earnings or deterioration in the working capital cycle, which would adversely impact its coverage metrics and liquidity position.

## Analytical approach

| Analytical Approach | Comments |
|---|---|
| **Applicable rating methodologies** | Corporate Credit Rating Methodology<br>Rating Methodology for Entities in the Textile Industry-Apparels |
| **Parent/Group support** | Not Applicable |
| **Consolidation/Standalone** | Standalone |

## About the company

ITFL, incorporated in 2009, is involved in retailing of readymade garments for men and boys. The apparel retail operations commenced in 2000 under Celebrity Fashions Limited (CFL), which was demerged into a separate company w.e.f. April 1, 2010. ITFL primarily caters to the mid-premium and premium segments, marketing a wide range of products including shirts, trousers, T-shirts, jackets, denims and sweaters under its flagship brand, 'Indian Terrain'. ITFL went public in 2011 and is listed on the Bombay Stock Exchange and the National Stock Exchange. The company was started by Mr. Venkatesh Rajagopal, who has over three decades of experience in manufacturing and retailing of apparels. The promoters held a 33.21% stake in ITFL as of June 30, 2021 (including outstanding convertible securities), of which 66.44% has been pledged as collateral towards the bank facilities enjoyed by the company. At present, the operations are managed by Mr. Charath Narsimhan, the Managing Director of ITFL.

## Key financial indicators (audited)

| Indian Terrain Fashions Limited | FY2021 | FY2022 |
|---|---|---|
| **Operating income (Rs. crore)** | 222.5 | 336.3 |
| **PAT (Rs. crore)** | -30.8 | -2.2 |
| **OPBDIT/OI** | -15.3% | 8.0% |
| **PAT/OI** | -13.8% | -0.7% |
| **Total outside liabilities/Tangible net worth (times)** | 1.3 | 1.3 |
| **Total debt/OPBDIT (times)** | -3.5 | 4.1 |
| **Interest coverage (times)** | -2.2 | 1.4 |

*PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation*

## Status of non-cooperation with previous CRA: Not applicable

## Any other information: None

## Rating history for past three years

| | Instrument | Current rating (FY2021) | | | | Chronology of Rating History for the past 3 years | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | | Type | Amount rated (Rs. crore) | Amount outstanding as of Mar 31, 2022 (Rs. crore) | Date & rating in FY2023 | Date & rating in FY2022 | Date & rating in FY2021 | | | Date & rating in FY2020 | |
| | | | | | 24-Jun-22 | 30-Sep-21 | 26-Oct-20 | 20-Jul-20 | 08-May-20 | 11-Feb-20 | 20-Aug-19 |
| 1 | Cash Credit | Long Term | 37.50 | - | [ICRA]BBB + (Stable) | [ICRA]BBB + (Negative) | [ICRA]BBB + (Negative) | [ICRA]BBB + (Negative) | [ICRA]A- (Negative) | [ICRA]A- (Stable) | - |
| 2 | Fund-based – Working Capital limits | Short term | - | - | - | - | - | [ICRA]A2 | [ICRA]A2+ | [ICRA]A2 + | [ICRA]A2 + |
| 3 | Non-Fund-based – Working capital limits | Short term | 8.00 | - | [ICRA]A2 | [ICRA]A2 | [ICRA]A2 | [ICRA]A2 | [ICRA]A2+ | [ICRA]A2 + | [ICRA]A2 + |
| 4 | Fund based- Term Loan | Long Term | 9.99 | 9.99 | [ICRA]BBB + (Stable) | [ICRA]BBB + (Negative) | - | - | - | - | - |
| 5 | Unallocated / Proposed limits | Long term/ Short Term | 4.51 | - | [ICRA]BBB + (Stable)/ [ICRA]A2 | [ICRA]BBB + (Negative) / [ICRA]A2 | [ICRA]BBB + (Negative) / [ICRA]A2 | [ICRA]BBB + (Negative) / [ICRA]A2 | [ICRA]A- (Negative) / [ICRA]A2+ | [ICRA]A- (Stable)/ [ICRA]A2 + | [ICRA]A- (Stable)/ [ICRA]A2 + |

*Amount in Crores; Source: ITFL*

## Complexity level of the rated instruments

| Instrument | Complexity Indicator |
|---|---|
| Long-term fund-based Working Capital Facilities | Simple |
| Long-term fund-based Term Loan | Simple |
| Short-term non-fund-based Working Capital Facilities | Simple |
| Unallocated limits | NA |

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 analysing 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 are available on ICRA's website: www.icra.in

## Annexure I: Instrument details

| ISIN | Instrument Name | Date of Issuance | Coupon Rate | Maturity | Amount Rated (Rs. crore) | Current Rating and Outlook |
|---|---|---|---|---|---|---|
| - | Cash Credit | - | - | - | 37.50 | [ICRA]BBB+ (Stable) |
| - | Term Loan | FY2021 | - | FY2026 | 9.99 | [ICRA]BBB+ (Stable) |
| - | LC (WC) | - | - | - | 8.00 | [ICRA]A2 |
| - | Unallocated | - | - | - | 4.51 | [ICRA]BBB+ (Stable)/[ICRA]A2 |

***Source:*** *Company*

### Annexure II: List of entities considered for consolidated analysis – Not applicable

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