September 09, 2019

Kalyan Jewellers India Limited: Ratings reaffirmed; outlook revised to Stable from Positive

Summary of rating action

Instrument*	Previously Rated Amount (Rs. crore)[1]	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	253.00	253.00	[ICRA]A- (stable); reaffirmed outlook revised from positive to stable
Long term / short term - Fund based	2,777.00	2,777.00	[ICRA]A- (stable) / [ICRA]A2+; reaffirmed; outlook revised from positive to stable
Short term - Fund based / Non-fund based (sub limits)	(1,465.00)	(1,465.00)	[ICRA]A2+; reaffirmed
Medium term – Fixed deposit	525.00	525.00	MA- (stable); reaffirmed; outlook revised from positive to stable
Total	**3,555.00**	**3,555.00**	

**Instrument details are provided in Annexure-1*

Rationale

The ratings remain supported by KJIL's established presence and the vast experience of its promoters in the domestic gold jewellery retail industry, diversified geographical presence across India, favourable product mix with rising revenue share from the margin-accretive studded jewellery, and strong hedging practices. The ratings favourably consider the presence of private equity (PE) player, Highdell Investment Limited (Warburg Pincus Group) with ~30% shareholding in KJIL, providing comfort on systems and governance, and long-term favourable demand for the gold jewellery retail industry. The revision in the rating outlook to Stable from Positive factors in KJIL's weaker-than-expected financial performance in FY2019 (revenues down by ~10% YoY), affected by factors like floods in Kerala, the management's revamping of low-margin product segments in key markets like Tamil Nadu, slower-than-expected ramp-up of the new stores in non-South markets, subdued jewellery demand due to elevated gold prices and intense competition in most of the regions from both organised and unorganised players. In FY2019, KJIL added 14 new stores, primarily in non-South markets, which resulted in a sharp rise in overheads like rental and advertisement costs. Increase in operating costs amid fall in revenues consequently impacted KJIL's net profits in FY2019. While the earnings profile was impacted, ICRA notes that KJIL's debt levels have reduced despite addition of new stores. Notably, the stock requirements in the new stores were largely met through rationalising inventories in the existing stores. The ratings also remain constrained by the company's exposure to regulation-related risks (which impacted the retailers' performance in the past), inherently stiff competition in the industry with consequent pricing pressures on retailers and continuing cautious stance of lenders to the gems and jewellery sector. The ratings also consider KJIL's moderate debt coverage indicators, high working capital intensity and low return on capital employed (RoCE) levels.

[1] *100 lakh = 1 crore = 10 million*

The Stable outlook on the medium-term and long-term ratings reflects ICRA's opinion that KJIL will benefit from the strong management and business profile characterised by a well-diversified presence (both in terms of geography and products). Nevertheless, improvement in earnings profile and stock rotation will be critical monitorables going forward.

Key rating drivers and their description

Credit strengths

Vast experience of promoters and presence of PE player - KJIL has been involved in the gold jewellery retailing business for nearly three decades. The promoters' vast experience and commitment to business has supported KJIL in establishing a strong presence across the country. Further, the presence of Highdell Investment Limited (the Warburg Pincus Group) provides additional comfort on systems and governance. KJIL received the follow-on funding of Rs. 500 crore from the PE in April 2017. The proceeds were used for store expansions (both India and overseas), giving KJIL a diversified geographical presence, apart from improving its liquidity position and capital structure.

Strong business profile - KJIL is one of the largest players in the domestic jewellery retail business with 104 showrooms spread across 18 states and two union territories (as of March 2019). With the company setting up 21 new stores in non-South markets between FY2016 and FY2019, the revenue share of the region increased to ~33% in FY2019. KJIL's product diversity also improved with increasing sale of margin-accretive studded and diamond jewellery across the non-South markets. Rising share of studded jewellery sales coupled with the management's change in strategy to revamp its low-margin product segments is expected to result in margin expansion going forward.

Favourable long-term demand – The higher number of auspicious days this year is likely to offset the likely dip in the near-term gold jewellery demand due to the sharp rise in gold prices (up over 20% in last three months). The medium-to-long term demand outlook, however, remains favourable supported by cultural underpinnings, evolving lifestyle, growing disposable income, favourable demographic dividend and growing penetration of the organised sector. Increasing regulatory restrictions aimed towards greater transparency and higher compliance costs have resulted in a churn in unorganised segment, benefiting the organised players. KJIL is well positioned to tap the incremental demand, given its wide presence, brand name and strong hedging practices.

Credit challenges

Subdued performance in FY2019 - KJIL's earnings in FY2019 were affected by factors like floods in Kerala, the management revamping the low-margin product segments in markets like Tamil Nadu, slower-than-expected ramp-up of the new stores opened in non-South markets, subdued jewellery demand due to elevated gold prices and Intense competition in most of the regions from both organised and unorganised players. In FY2019, KJIL added 14 new stores, primarily in non-South markets, which resulted in a sharp rise in overheads like rental and advertisement costs. Increase in operating costs amid fall in revenues consequently impacted the company's net profits in FY2019. While the earnings profile was impacted, ICRA notes that KJIL's debt levels have reduced despite the addition of new stores. The stock requirements in the new stores were largely met by rationalising inventories in its existing stores. The profitability and debt indicators, however, remained moderate owing to lower operating profits. Going forward, favourable earnings profile and higher stock rotation will be critical for improving the credit profile of the company.

Intense competition limits pricing flexibility - Gold jewellery retail business is highly fragmented and competitive. The pricing flexibility of most of the players remain under pressure with subdued demand growth across the industry. This coupled with the limited value addition in the products keeps the operating margins lower. While KJIL is present in more regions than other retailers, the competition remains high particularly in the southern markets.

Regulatory risks and cautious lending environment – The jewellery retail industry has been witnessing increased regulatory intervention. This has impacted the operating environment and consequently the performance of jewellers, including KJIL over the last few years. Lending to the gems and jewellery sector continues to be cautious and more case-specific. The credit profile of jewellery retailers shall remain exposed to such regulation-related risks.

Liquidity position: Adequate

KJIL's liquidity is **adequate** with healthy cash flow from operations of ~Rs. 290-300 crore (as of March 2019) enabled by pruning of inventory across stores and free cash reserves of Rs. 90 crore. Against the sanctioned working capital lines of Rs. 2,550 crore, the average utilisation, however, is higher at over 97%. The company has a debt repayment obligation of ~Rs. 80 crore each in FY2020 and FY2021. ICRA expects KJIL to be able to meet its debt repayment commitments through internal accruals. In addition, the company has healthy financial flexibility with lenders.

Rating sensitivities

Positive triggers – ICRA could upgrade KJIL's rating if it demonstrates a sharp and sustained improvement in its earnings and debt coverage ratios. A faster stock rotation of above 2.5x on a sustained basis shall support turnaround in operations / earnings and consequently enable rating upgrade.

Negative triggers – Negative pressure on KJIL's rating could arise with further deterioration in earnings. Aggressive store expansions resulting in large increase in debt levels (or) slower rotation of stock (at less than 1.6x) with consequent impact on debt coverage metrics could also exert negative pressure on the company's rating.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Gold Jewellery Retail Industry
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

About the company

Kalyan Jewellers India Limited (erstwhile Kalyan Jewellers India Private Limited), managed by Mr. T.S. Kalyanaraman and his sons, is an established jewellery retail player in southern India, with a presence in the market for more than two decades. In December 2013, KJIL had expanded its footprint into the Middle Eastern market with six showrooms. As of September, the company has 32 stores in those geographies. The stores in the Middle East are operated under the entities, Kalyan Jewellers LLC (UAE), Kalyan Jewellers WLL (Qatar), and Kalyan Jewellers for Golden Jewelleries WLL (Kuwait). Highdell Investment Limited (Warburg Pincus Group) currently holds a 30% stake in KJIL. As of March 2019, the company had 104 showrooms in India spread over 18 states and two union territories.

Key financial indicators (audited)

Standalone	FY2018	FY2019
Operating Income (Rs. crore)	8,255.9	7,454.3
PAT (Rs. crore)	137.6	50.0
OPBDIT/OI (%)	6.2%	4.7%
RoCE (%)	10.0%	6.4%
Total Outside Liabilities/Tangible Net Worth (times)	2.2	1.8
Total Debt/OPBDIT (times)	5.9	7.5
Interest Coverage (times)	2.0	1.4
DSCR	1.3	1.1

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating 09-Sep-2019	FY2019 5-Nov-2018	FY2018 9-Oct-2017	FY2017 9-Sep-2016
1	Term Loans	Long term	253.0	161.1	[ICRA]A- (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Positive)	[ICRA]A- (Stable)
2	Fund based limits	Long Term / Short term	2,777.0	2,777.0	[ICRA]A- (stable) / [ICRA]A2+	[ICRA]A- (Positive) / [ICRA]A2+	[ICRA]A- (Positive) / [ICRA]A2+	-
3	Fund based / non-fund based (sub limits)	Short term	(1,465.0)	(1,465.0)	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
4	Fixed deposits	Medium term	525.0	525.0	MA- (stable)	MA- (Positive)	MA- (Positive)	MA- (Stable)
5	Fund based facilities	Long term	-	-	-	-	-	[ICRA]A- (Stable)
6	Fund based facilities	Short term	-	-	-	-	-	[ICRA]A2+

Amount in Rs. crore

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loans	FY2018	NA	FY2021	253.0	[ICRA]A- (stable)
NA	Long term / short term – Fund based	NA	NA	-	2,777.0	[ICRA]A- (stable) / [ICRA]A2+
NA	Short term fund based / non-fund based (sub limits)	NA	NA	-	(1,465.0)	[ICRA]A2+
NA	Medium term – Fixed deposit	NA	NA	-		MA- (stable)

Source: KJIL

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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