May 08, 2020

Indian Terrain Fashions Limited: Ratings reaffirmed; outlook revised to Negative

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based Working Capital Facilities	30.00	30.00[1]	[ICRA]A-(Negative) / reaffirmed; outlook revised to Negative from Stable
Short-term fund-based Working Capital Facilities	11.50	11.50	[ICRA]A2+; reaffirmed
Short-term non-fund-based Working Capital Facilities	8.00	8.00	[ICRA]A2+; reaffirmed
Unallocated limits	10.50	10.50	[ICRA]A- (Negative)/ [ICRA]A2+ / re-affirmed; outlook revised to Negative from Stable
Total	**60.00**	**60.00**	

**Instrument details are provided in Annexure-1*

Rationale

The revision in the long-term rating outlook of Indian Terrain Fashions Limited (ITFL) is in line with ICRA's negative outlook for the sector, given the expected adverse impact of the Covid-19 outbreak on the retail industry. ICRA expects ITFL's operating performance to remain under pressure in the coming months because of the prevalent weak demand conditions. Revenues and earnings are expected to decline by around 20% in FY2021. ITFL had shut down all its retail stores and manufacturing facilities after the Government of India (GoI) imposed the nationwide lockdown following the outbreak of Covid-19. While the stores are anticipated to reopen gradually in the coming days across most of the locations, demand recovery is likely to take a long time, given that discretionary consumer spending is expected to remain at a relatively lower level than the preceding fiscal. The earnings and liquidity position of retailers are likely to remain under pressure during the major part of H1 FY2021 as receivables cycle elongates further and companies resort to reducing inventory levels at higher discounts. ICRA, however, considers the invocation of the force majeure clause by most retailers, including ITFL, and the company's ongoing negotiations to convert existing rental arrangements to variable (as a percentage of revenues), which should help reduce their rental costs in the coming months. ICRA would continue to monitor the developments in this regard and will conclude the rating action once greater clarity emerges.

ITFL's operating performance has been constrained in the recent past by the tepid domestic consumption levels and temporary business disruption due to transition towards distribution model in the multi-brand outlets (MBO) channel. While revenues are estimated to have declined by 5% in FY2020, operating margins are likely to have moderated to around 9.5% owing to an increase in marketing spends and discounts extended. Selling expenses have remained high because of modest demand conditions, continuing expansion across markets and increasing competition in the branded apparel business from several established brands. ITFL's working capital intensity remains high, characterised by high receivables position, with its debtor days increasing to around 240 in the recent quarters on the back of an extended credit enjoyed by its channel partners. However, the same is likely to improve over the medium term, supported by

[1] *The long-term fund-based working capital facility has been carved out from the reduction in limits of other facilities rated*

better collection from the MBO channel with the recent shift to the distribution model from the direct sales model. Despite the high working capital funding requirements, the ratings are supported by ITFL's adequate credit metrics and liquidity position. ITFL has availed moratorium on scheduled payment obligations from its lenders for the period March-May 2020 as a part of the Covid-19 regulatory package announced by the Reserve Bank of India (RBI). Key ratios including adjusted debt[2] to operating profits and debt service coverage ratio (DSCR) are estimated to be at around 1.5 times and 2.5 times, respectively in FY2020. ICRA expects ITFL's performance to improve over the medium term, supported by its established presence in the domestic men's branded apparel segment and continued efforts taken to improve business diversity and reduce receivables position.

Key rating drivers and their description

Credit strengths

Established market presence in the domestic men's wear segment – ITFL's flagship brand, Indian Terrain, enjoys strong recall in the men's casual wear segment, especially in South India, with a long presence of over two decades. The company has a strong multi-channel distribution network of more than 170 exclusive brand outlets (EBO), 380 large format stores (LFS) and 1,400 MBOs encompassing over 2,000 points of sale in about 250 cities. While the EBOs allow the company additional flexibility in promotion and brand building, enabling direct engagement with customers, the MBO channel helps the company expand its geographical presence with minimal investments. ITFL also generates around 10% of sales through the 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 volume growth over the medium term.

Comfortable debt protection metrics – Despite an increase in working capital intensity and some moderation in earnings, ITFL's financial profile is characterised by a conservative capital structure with adequate credit metrics. Key ratios including total outside liabilities to tangible net worth, adjusted debt to operating profits and DSCR are estimated to be at around 0.7 times, 1.5 times and 2.5 times, respectively in FY2020.

Credit challenges

Moderation in operating performance in recent quarters; likely to remain under pressure in H1 FY2021 – ITFL's operating performance has been under pressure in the recent quarters because of modest domestic consumption and high marketing expenses amid intense competition. In line with the industry, ITFL's revenues and earnings are expected to be adversely impacted in the coming quarters, owing to the prevalent tepid demand conditions following the Covid-19 outbreak. This is likely to result in moderation in coverage metrics and liquidity position during the major portion of H1 FY2021.

High working capital intensity – Apparel retail business inherently entails high working capital requirements towards stocking garments across a wide product range and high credit enjoyed by distribution channel partners. Its receivables position is stretched because of an extended credit enjoyed by the MBO, large format stores (LFS) and e-commerce channel partners. ITFL's receivable cycle has increased steadily to more than 240 days over the last 12 months. Nevertheless, ITFL's adequate liquidity position provides some comfort.

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[2] *Total debt adjusted for cash and liquid investments held and for vendor bills discounted*

Liquidity position: Adequate

ITFL's liquidity position remains adequate, supported by relatively stable earnings from operations in the recent quarters (albeit at lower levels than FY2019) and cash reserves held, despite the incremental working capital funding requirements witnessed. The company had cash equivalents (free cash reserves and liquid investments) of around Rs. 20 crore as on March 31, 2020 (down from ~Rs. 35 crore as on March 31, 2019). High working capital intensity and reduction in earnings constrained the company's free cash flows in FY2020. Despite the expected pressure on operating cash flows in the near term, low repayment obligations and adequate cash reserves held are likely to support the liquidity position of the company.

Rating sensitivities

Positive triggers – Given the Negative outlook, an upgrade in the ratings is unlikely in the near term. However, the outlook may be revised to Stable if there is a strong recovery in volumes and earnings in the coming quarters and if the working capital intensity reduces, which would consequently result in an improvement in ITFL's credit metrics and liquidity position.

Negative triggers – Pressure on ITFL's ratings may emerge if there is a sustained pressure on revenues and earnings in the coming quarters following the Covid-19 outbreak, or if there is an elongation in its working capital cycle, which would adversely impact its credit metrics and liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating methodology for Entities in the Indian Textiles 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 were commenced in 2000 under Celebrity Fashions Limited (CFL), which was demerged into a separate company with effect from 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 the flagship, Indian Terrain brand. 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 30.1% stake in ITFL as of December 31, 2019, of which 67% has been pledged as collateral towards the bank facilities enjoyed by the company. The operations are currently managed by Mr. Charath Narsimhan, the Managing Director of ITFL.

Key financial indicators (audited)

	FY2018	FY2019
Operating Income (Rs. crore)	401.5	422.4
PAT (Rs. crore)	25.4	25.7
OPBDIT/OI (%)	11.9%	12.0%
RoCE (%)	19.9%	19.0%
Total Outside Liabilities/Tangible Net Worth (times)	0.8	0.8
Total Debt/OPBDITA (times)	0.8	0.7
Interest Coverage (times)	6.8	6.0
DSCR	6.0	4.4

Source: ITFL and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

			Rating (FY2021)			Rating History for the Past 3 Years			
		Type	Amount Rated	Amount Outstanding	Current Rating 08-May, 2020	FY2020		FY2019	FY2018
						Feb 11, 2020	Aug 20, 2020	-	
1	Fund based-Cash Credit	Long Term	30.00	-	[ICRA]A- (Negative)	[ICRA]A- (Stable)	-	-	
2	Fund-based – Working Capital limits	Short term	11.50	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	-	
3	Non-Fund-based – Working capital limits	Short term	8.00	-	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	-	
4	Unallocated / Proposed limits	Long term/ Short Term	10.50	-	[ICRA]A- (Negative)/ [ICRA]A2+	[ICRA]A- (Stable)/ [ICRA]A2+	[ICRA]A- (Stable)/ [ICRA]A2+	-	

Amount in Rs. crore; Source: ITFL

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	Cash Credit	-	-	-	30.00	[ICRA]A-(Negative)
NA	Standby line of credit	-	-	-	5.50	[ICRA]A2+
NA	Ad-hoc WC limit	-	-	-	6.00	[ICRA]A2+
NA	LC (WC)	-	-	-	8.00	[ICRA]A2+
NA	Unallocated	-	-	-	10.50	[ICRA]A-(Negative) / [ICRA]A2+

Source: ITFL

Annexure-2: List of entities considered for consolidated analysis – Not applicable

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