September 05, 2023

P. N. Gadgil & Sons Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long Term - Fund Based – Cash Credit	320.0	317.5	[ICRA]A+(Stable); reaffirmed
Fixed Deposits	50.0	50.0	[ICRA]A+(Stable); reaffirmed
Short Term – Interchangeable -Others	(55.0)	(55.0)	[ICRA]A1; reaffirmed
Total	**370.0**	**367.5**	

Instrument details are provided in Annexure-I

Rationale

The rating reaffirmation factors in the healthy improvement in the financial performance of P. N. Gadgil & Sons Ltd. (PNGSL/company) in FY2023, which is expected to sustain in the current fiscal. In FY2023, there was a sharp increase in PNGSL's scale (~79%) due to a significant increase in the bullion trading business. The bullion business was started in July 2021, and in FY2023, it achieved revenues of ~Rs. 6,871 crore. Going forward, the revenues from bullion sales are expected to remain in the range of Rs. 7,000-8,000 crore. On the other hand, jewellery business grew by ~30%, supported by higher volumes and realisations. While the bullion business has high volumes, its profit margins are very low, thus impacting the overall operating margins, which reduced to ~2% in FY2023 from ~3% in FY2022. However, the operating margin in the jewellery business is estimated to remain steady at 6-6.5%. Also, in Q1 FY2024, the margin has improved, aided by inventory gains. The debt coverage indicators also remain comfortable with an interest coverage of ~6.7 times in FY2023 and ~16.9 times in Q1 FY2024. Going forward, the debt coverage indicators are expected to continue to remain healthy, supported by higher absolute profits. The ratings continue to consider its superior brand equity in Pune (Maharashtra) as well as other cities in Maharashtra, and extensive experience of its promoters. Over the years, PNGSL has established a strong market position in the Pune jewellery retail market and expanded its operations to 22 other cities and towns in Maharashtra, Karnataka and Gujarat. Going forward, ICRA expects the financial risk profile of the company to remain comfortable, given the favourable stock rotation level and a favourable long-term demand outlook for organised jewellery players, including PNGSL.

The ratings are, however, constrained by the company's relative geographical concentration in the Pune market, despite expansion in other regions of Maharashtra in the recent years. The company's earnings remain vulnerable to fluctuation in gold prices as raw material cost constitutes about 90% of the operating cost. However, the company follows hedging practices to reduce this risk. Though the company's working capital management remains efficient, its sizeable inventory associated with gold deposit schemes (off balance sheet) affects the inventory turnover metrices to some extent. As a result, PNGSL's TOL/Inventory and TOL/TNW remain slightly elevated. The ratings also factor in the intense competition and a fragmented industry structure, which are likely to keep the margins under check. ICRA also notes the inherent regulatory risks in the industry, which impacted the retailers' performance in the past. In addition, the trading business volume has significantly increased in FY2023 and is expected to remain at a similar level in the coming years. While PNGSL has long established relationships with customers, the counterparty credit risk remains. However, the cash-and-carry mode of business limits the risk to a large extent.

The Stable outlook reflects ICRA's expectation that PNGSL will continue to benefit from favourable demand outlook for organised jewellery players and will generate healthy cash flows, relative to its debt service obligations.

Key rating drivers and their description

Credit strengths

Healthy financial position, debt coverage indicators remain comfortable – The company's financial profile is strong, supported by healthy return on capital employed and comfortable debt protection metrics. PNGSL's ROCE was comfortable at

17.5% in FY2023, notwithstanding a decline from the FY2021 level due to commencement of the low-margin trading business. The coverage metrics also remain comfortable with an interest coverage of ~6.7 times in FY2023 and ~16.9 times in Q1 FY2024. These metrics are expected to remain steady, going forward and the financial profile will continue to remain strong.

Favourable long-term demand outlook for organised jewellery retailers – The long-term outlook 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 are likely to result in a churn in the unorganised segment, thus benefiting the organised players. The firm is well positioned to tap the incremental demand, given its reputed brand and established market position.

Low working capital intensity – As inherent in the industry, the company needs to maintain a high inventory level across all its showrooms to display varied designs of jewellery. Nonetheless, PNGSL's working capital intensity at ~7% in FY2023 is better than most of its industry peers because of the high inventory turnover of over 3 times during the last 2-3 years, supported by efficient inventory management practices. Though the company's working capital management remains efficient, its sizeable inventory associated with gold deposit schemes of about 300 kg as on March 31, 2023, (off balance sheet) deteriorates the inventory turnover metrices to some extent. ICRA notes that PNGSL's TOL/Inventory and TOL/TNW remain slightly elevated, and going forward, it will be a key monitorable.

Strong brand equity and market position in Pune with increasing footprints in rest of Maharashtra – PNGSL has an established market position with a dominant share in the Pune jewellery retail market. With presence of over six decades, PNGSL has gained strong brand loyalty, despite increasing competition in the market. While the company's dependence on the Pune market remains high at present, the same is expected to reduce over the medium term following its steady expansion across new geographies in Maharashtra in FY2018-19.

Credit challenges

Exposed to geographical concentration risk – The company is exposed to geographical concentration risk, with a major presence in Maharashtra. It derives 50-60% of its revenues from Pune and Nasik markets. However, owing to its long track record, the company has a strong customer base and market share in its core region, helping it reduce this risk. ICRA notes that with the launch of a new store in Tier 2 and Tier 3 cities of Maharashtra in FY2018-2019, and with the expected increase in revenue from these new stores over the medium term, the same will further reduce the company's reliance on the Pune market.

Profitability susceptible to fluctuation in gold prices – As common in the retail jewellery business, raw materials constitute over 90% of the operating cost. Gold jewellery sales account for ~90% of the firm's jewellery revenue, so its profitability remains susceptible to gold price movements. However, hedging practices adopted by the management reduce this risk to an extent.

Exposure to regulatory risks – Increased regulatory intervention in the jewellery industry in the recent years has impacted the demand and supply scenario in the industry. Measures like 20/80 restriction on imports, mandatory PAN disclosure requirement for purchases above the threshold limit, restrictions on jewellery saving schemes, imposition of excise duty and GST, increase in import duty, demonetisation etc. have affected demand and supply in the past. Increasing supervision and a cautious lending environment further restricted fund flows to the sector, thus hampering the store expansion plans and liquidity profile of the retailers.

Liquidity position: Adequate

PNGSL's liquidity is adequate with steady fund flow from operations, modest capex plans in the near term and low long-term debt repayment obligations. The cash and liquid investment of ~Rs. 58.5 crore as on June 30, 2023 and unutilised working capital limits (~40%) provide additional comfort to the liquidity. Overall, ICRA expects the firm to be able to meet its near-term commitments through internal as well as external sources of cash.

Rating sensitivities

Positive factors – ICRA could upgrade PNGSL's ratings if the company is able to significantly increase its sales volumes in the jewellery business, while maintaining its profit margins. Specific credit metrics that could lead to ratings upgrade include TOL/TNW of less than 0.75 times on a sustained basis.

Negative factors – The ratings could be downgraded if a substantial increase in the working capital requirements results in elevated level of debt, leading to a deterioration in the capital structure and debt coverage indicators. Specific credit metrics that could lead to a ratings downgrade include TOL / TNW exceeding 1.3 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	Standalone financials have been considered

About the company

PNGSL is involved in retail sale of gold, silver and diamond studded jewellery along with bullion trading. The company enjoys a long legacy of the P N Gadgil brand, which is more than 180 years old. The same was established by the Gadgil family members, who entered the gold jewellery business in 1832 at Sangli, Maharashtra under the name of Purushottam Narayan Gadgil Jewellers. As on March 31, 2023, the company has 29 stores of which 27 are in Maharashtra, and one each in Karnataka and Gujarat, with an aggregate carpet area of 99,597 sq. ft. The day-to-day activities are managed by CEO-Director, Mr. Amit Modak, who has vast experience of ~20 years in the jewellery sector, derivatives and Fx Markets. Other Promoters and Whole-Time Directors, Mr. Govind Gadgil and Dr. Renu Gadgil, also have vast experience in the sector.

Key financial indicators (audited)

PNGSL	FY2022	FY2023	Q1 FY2024*
Operating income	5649.9	10116.1	2485.4
PAT	102.7	111.6	65.5
OPBDIT/OI	3.1%	1.9%	3.7%
PAT/OI	1.8%	1.1%	2.6%
Total outside liabilities/Tangible net worth (times)	1.7	1.3	1.1
Total debt/OPBDIT (times)	3.1	2.3	1.1
Interest coverage (times)	5.8	6.7	16.9

*PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore; *Provisional data*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years					
		Type	Amount rated (Rs. crore)	Amount outstanding as of Mar 31, 2023 (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023		Date & rating in FY2022		Date & rating in FY2021	
					Sep 5, 2023	Sept 16, 2022	May 26, 2022	Nov 02, 2021	Oct 07, 2021	Oct 07, 2020	May 11, 2020
1	**Cash Credit**	Long-term	317.5	--	**[ICRA]A+ (Stable)**	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
2	**Interchangeable**	Short-term	(55.0)	--	**[ICRA]A1**	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1
3	**Fixed Deposit**	Long-term	50.0	16.0	**[ICRA]A+ (Stable)**	[ICRA]A+ (Stable)	[ICRA]A+ (Stable)	MAA- (Stable)	MAA- (Stable)	MA+ (Stable)	MA+ (Stable)

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term – Fund-based – Cash Credit	Simple
Short -term – Interchangeable – Others	Simple
Long-term – Fixed Deposit	Very 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 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: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Long-term- Fund Based – Cash Credit	-	-	-	317.5	[ICRA]A+(Stable)
NA	Short term - Interchangeable – Others	-	-	-	(55.0)	[ICRA]A1
NA	Fixed Deposit	-	7.5%	-	50.0	[ICRA]A+(Stable)

Source: Company

Please click here to view details of lender-wise facilities rated by ICRA.

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

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