September 18, 2023

Ethos Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fixed Deposits	10.00	10.00	[ICRA]A (Stable); reaffirmed
Proposed Working Capital	75.00	125.00	[ICRA]A (Stable); reaffirmed/assigned for enhanced amount
Total	**85.00**	**135.00**	

**Instrument details are provided in Annexure-I*

Rationale

The rating reaffirmation factors in ICRA's expectations that Ethos Limited (Ethos) will continue to witness significant traction in the sales and average realisations. Buoyant demand in the near to medium term coupled with ongoing store network expansion augur well for the company's business prospects and are expected to strengthen the company's market position. Moreover, the company's credit metrics have improved with better profitability on a growing scale with limited external debt in its books. Consistent increase in the exclusive arrangements with the brands and growing scale across segments will continue to support the company's margin profile. ICRA expects Ethos' credit metrics to be healthy, led by negligible leverage and benefits accruing from its retail network expansion despite Ethos' plan to bring additional working capital debt to support its endeavour to expand the store network. The rating continues to favourably factor in Ethos' position as the largest organised luxury watch retailer in the country. The ratings are further supported by stable performance of the parent company, KDDL Limited (KDDL), led by its healthy operating and financial performance, strong revenue visibility reflecting in the robust order book both at the domestic as well as exports divisions.

The ratings, however, are constrained by the inherently working-capital intensive nature of company's business. The company needs to maintain adequate inventory across various watch segments so as to maintain the brands' standards of displaying products to its customers. Inventory requirements are expected to increase further in terms of value as the company is planning to scale up its retail presence. Nevertheless, ICRA notes that the company is shoring up its inventory primarily through equity funds in the medium term, in line with the specified purpose of IPO funds, thus limiting debt levels. Additionally, the company is exposed to forex fluctuation risk, with a substantial share of its products is imported. Moreover, the company is exposed to competition from domestic players and international markets in the retail segment. Also, its ability to expand its store network depends on the timely availability of store space from developers.

The Stable outlook on the [ICRA]A rating reflects ICRA's expectation that Ethos will maintain its healthy market position and expand its presence further through more store launches, diversification in product mix and its established relationships with brands.

Key rating drivers and their description

Credit strengths

Established market position in watch retail segment – Ethos is the largest organised luxury watch retailing company in the country and operates currently through 60 stores spread across 23 cities in India. The company is engaged in retailing most of the global reputed brands such as Omega, Rolex, Rado, IWC, and Bvlgari, among others. Moreover, the company enjoys an exclusive distribution relationship with several brands including Jacob & Co., H. Moser & Cie, Bovet, and Oris, etc.

Expanding network augurs well for company's business prospects – The company achieved revenue growth of ~35% from Rs. 587 crore in FY2022 to Rs. 789.6 crore in FY2023. In addition, the company witnessed significant traction in the high luxury segment, which has been growing for the past couple of years. The company also witnessed a significant Same Store Sales Growth (SSSG) of ~30% in FY2023, which resulted in operating leverage reflecting in strong profitability of Ethos Limited. Further, its increasing portfolio of exclusive brand sales augurs well for further growth and profitability. Ethos' store network is expected to undergo healthy expansion with plans of opening 40 additional stores by FY2025. The company is expanding into tier-II and III cities as well, apart from increasing its presence in tier-I cities. Further, the company is trying to expand its luxury offerings by foraying into the luxury luggage and international branded jewellery business, which is expected to bring incremental growth, going forward. Buoyant demand in the near to medium term, coupled with ongoing store network expansion, augur well for the company's business prospects and are expected to strengthen its market position. Its ability to expand its store network, which depends on the timely availability of store space from developers will remain critical for the planned growth, going forward.

Improvement in financial risk profile, coverage metrics to remain healthy – With continued increase in the top line and sustained healthy profitability, the company's overall financial risk profile has been improving steadily. Supported by high value-added sales and economies of scale, the company posted operating margin of 15.7% and net profit margin of 7.6% in FY2023, which improved from 14.1% of operating margin and 4.0% of net margin in FY2022. This apart, the gearing improved to 0.19 times as on March 31, 2023 from 0.70 times as on March 31, 2022 largely on account of limited debt dependence and better internal accrual generation. The coverage indicators remained healthy in absence of any major external debt reflecting in improvement in interest coverage and TD/OPBIDTA. The company plans to raise moderate level of working capital limits and ICRA expects its coverage metrics are expected to remain healthy, supported by steady growth and profitability.

Credit challenges

Working capital intensive business – Ethos' business is inherently working-capital intensive as it needs to maintain adequate inventory across various watch segments so as to maintain global standards of displaying products and thus offer a good customer buying experience. Moreover, the company needs to healthy inventory for normal business operations to manage its supply chain. The company's working capital intensity increased from ~33% in FY2022 to ~37% in FY2023. With a growing footprint of 40 planned new store addition in the near to medium term, along with increasing high-value and excusive brand sales, the overall inventory requirement will remain sizeable. However, the funding for the same will be mostly through the IPO route, internal accruals and plans to raise working capital debt.

Risk of fluctuating demand amid ongoing global scenario – The company's performance is directly dependent on demand fluctuations, which mainly rely on discretionary consumer spending as well as overall market sentiments. Demand in the retail business also remains prone to regulatory headwinds such as changes in Government policies regarding taxation. Further, the company is exposed to competition from domestic players and international markets in the retail business. ICRA notes that the company has also forayed into retailing jewellery and luggage from luxury brands, whose ramp up remains to be seen.

Moderate exposure to forex risks – The company is a net importer with approximately 40% of its watches being imported. The company receives periodic price revisions from brands and thus remains exposed to foreign currency fluctuation risk to an extent.

Environmental and Social Risks

Environmental: The company is into retailing of watches and the products do not harm the environment or is of any concern to the climate. Further, the company is spending a part of its earning on the corporate social responsibility causes throughout the year. The Company has taken some energy initiatives such as:

• Installation of LED lights, LED signage & power saving equipment like waterless urinals, sensor-based taps and aerators fitted taps etc. across the stores to reduce the electricity consumption.

• Optimum use of air conditioner (AC) at all office in order to reduce the electricity consumption.

The company has undertaken several initiatives to enhance process efficiency as well as to reduce the total consumption of paper. The company's recyclable or reusable wastes are limited to corrugated boxes, bubble wraps and papers. Further the company remains focused on reducing bulky packaging encouraging recycle and reuse.

Social: The Company has moderate dependence on human capital thus maintaining healthy employee relationships and a safe work environment remain essential for disruption-free operations. Retaining human capital, maintaining healthy employee relationships and a safe work environment remain essential for disruption-free operations. The company conducts training sessions for all employees to upgrade their knowledge and skills from time to time. The company prohibits employment or engagement of child force at workplace and expects that its vendors also follow the same. Retail stores and backend offices of the company are located at various malls across the country whereby adequate facilities are provided to the persons with disabilities. The company provides insurance, and regular health check-ups to ensure employee well being.

Liquidity position: Strong

The company's liquidity position is **strong** on account of the sufficient cash generation and available funds to address its capex and working capital requirements. There are modest repayments of Rs. 6.37 crore towards public deposits (as on March 31, 2023). The company had free cash levels of ~Rs. 224.22 crore as on March 31, 2023, which can be used towards store additions and working capital in line with the end-use defined in the IPO. Moreover, the company is in the process of availing additional working capital limits as a back-up funding for its growth plans, which lends further comfort.

Rating sensitivities

Positive factors – A significant improvement in the credit profile of the parent will be a trigger for the company's rating upgrade. Further, a sustained improvement in Ethos' scale through timely capex implementation, while sustaining its liquidity position, will be considered for a rating improvement.

Negative factors – Negative pressure on the ratings could emerge if there is a dip in demand, leading to pressure on revenues and profitability. Any stretch in the working capital cycle and pressure on liquidity may also warrant a rating review. Further, deterioration in the parent's credit profile can also lead to a rating downgrade. Debt/OPBIDTA higher than 1.8 times, on a sustained basis, might also lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Yes. KDDL Limited holds ~61.1% (~51.3% directly and ~9.7% indirectly through its subsidiary Mahen Distribution Limited) in Ethos Limited (as on March 31, 2023).
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Ethos. The list of companies consolidated are shared in Annexure-II.

About the company

Ethos Limited was incorporated in 2003 and is one of the subsidiaries of KDDL Limited. Ethos is engaged in retailing luxury watches. It retails ~60 premium and luxury watch brands such as Omega, Jaeger LeCoultre, Panerai, Bvlgari, H. Moser & Cie, Rado, Longines, and Tissot. The company currently runs 60 retail stores across 23 cities in India, including cities such as New Delhi, Mumbai, Bengaluru, Hyderabad, Chennai and Kolkata. Ethos was listed in Q1 FY2023 during May–June 2022.

Key financial indicators (audited)

Ethos consolidated	FY2021	FY2022	FY2023
Operating income	401.1	587.0	789.6
PAT	4.76	23.39	60.30
OPBDIT/OI	14.3%	14.1%	15.7%
PAT/OI	1.2%	4.0%	7.6%
Total outside liabilities/Tangible net worth (times)	1.45	1.14	0.38
Total debt/OPBDIT (times)	2.44	1.95	0.97
Interest coverage (times)	2.84	3.84	6.16

Source: Company, PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amounts in Rs. crore

Status of non-cooperation with previous CRA: CRISIL migrated the company's ratings to 'CRISIL FB+ (Stable) ISSUER NOT COOPERATING' on December 31, 2020; on best available information with the credit rating agency.

https://www.crisil.com/mnt/winshare/Ratings/RatingList/RatingDocs/Ethos_Limited_December_31_2020_RR.html

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 (Rs. crore) ^	Date & rating in FY2024		FY2023		FY2022	FY2021
					Sep 18, 2023	Aug 10, 2023	Oct 25, 2022	June 09, 2022	Dec 08, 2021	Dec-08-2020
1	Fund-based/Cash Credit	Long-term	0.00	0.00	-	-	[ICRA]A-(Stable); Withdrawn	[ICRA]BBB+(Positive);	[ICRA]BBB+(Positive);	[ICRA]BBB+ (Stable)
2	Fund-based/Term loan	Long-term	0.00	0.00	-	-	[ICRA]A-(Stable); Withdrawn	[ICRA]BBB+(Positive);	[ICRA]BBB+(Positive);	[ICRA]BBB+ (Stable)
3	Non-fund Based	Short-term	0.00	0.00	-	-	[ICRA]A2+; Withdrawn	[ICRA]A2	[ICRA]A2	[ICRA]A2
4	Unallocated	Long-term/Short-term	0.00	0.00	-	-	[ICRA]A-(Stable)/[ICRA]A2+; Withdrawn	[ICRA]BBB+(Positive)/ [ICRA]A2	[ICRA]BBB+(Positive)/ [ICRA]A2	[ICRA]BBB+(Stable)/ [ICRA]A2
5	Fixed Deposits^	Long-term	10.00	6.37	[ICRA]A(Stable)	[ICRA]A(Stable)	[ICRA]A-(Stable);	[ICRA]BBB+(Positive);	MA-(Positive)	MA- (Stable)
6	Proposed Working Capital	Long-term	125.00	00.00	[ICRA]A(Stable)	[ICRA]A(Stable)	-	-	-	-

Source: Company, ^outstanding as of March 2023

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fixed Deposits	Very Simple
Fund-based/ Proposed Working Capital	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	Fixed Deposits	NA	NA	NA	10.00	[ICRA]A(Stable)
NA	Fund-based/ Proposed Working Capital	NA	NA	NA	125.00	[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

Company Name	Ownership	Consolidation Approach
Ethos Limited	-	Full consolidation
Cognition Digital LLP	99.99%	Full consolidation
Silvercity Brands AG	100.00%	Full consolidation
Pasadena Retail Private Limited	50.00%	Full consolidation

Source: Company, Data as on March 31st 2023

ANALYST CONTACTS

Shamsher Dewan
91 124 4545 328
shamsherd@icraindia.com

Kinjal Shah
+91 22 6114 3442
kinjal.shah@icraindia.com

Sheetal Sharad
+91 124 4545 374
sheetal.sharad@icraindia.com

Nishant Misra
+91 124 4545 862
nishant.misra@icraindia.com

RELATIONSHIP CONTACT

L. Shivakumar
+91 22 6114 3406
shivakumar@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

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ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

Branches