

November 29, 2023

Kandalaa Distributors: Rating downgraded to [ICRA]BB(Stable)

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term fund-based – Cash credit	10.00	10.00	Downgraded to [ICRA]BB(Stable) from [ICRA]BB+(Stable)
Total	10.00	10.00	

*Instrument details are provided in Annexure-I

Rationale

The rating action on Kandalaa Distributors is on account of a change in the analytical approach owing to the cross-default linkages of the entities in the Kandalaa Group. ICRA came to know about the cross-default linkage recently that has triggered the change in the analytical approach. To arrive at the rating, ICRA has carried out a consolidated analysis of the Kandalaa Group, comprising Kandalaa Distributors, Kandalaa, Kandalaa Prints and Sribalaji Hitechexim Projects Private Limited against the earlier standalone analysis of Kandalaa Distributors. The rating action factors in the consolidated financial risk profile of Kandalaa group being weaker than the standalone financial risk profile of Kandalaa Distributors.

The rating takes into consideration the established track record of the Kandalaa Group in the pharmaceutical distribution and jewellery retail business. ICRA notes Kandalaa Distributors' established relationship with the principals and its status as the sole superstockist/clearing and forwarding agent (CFA) in the regions allocated to it in the Karnataka market. The principals include reputed pharmaceutical companies such as British Biologicals, Hegde & Hegde LLP, MSD Pharmaceuticals Ltd., Albert David Ltd., among others. The rating draws comfort from its established relationship with a large client base and a wide product portfolio.

The rating continues to favourably factor in the established market position of Kandalaa's standalone showroom in Bengaluru and the extensive experience of its promoters in the jewellery retail sector, which is expected to aid its operations over the medium term.

The rating is, however constrained by its thin margins owing to the trading nature of operations and high geographical concentration risk. Further, the rating continues to be constrained by the Group's average financial risk profile, characterised by stretched coverage indicators. The capital structure remains leveraged due to the high working capital requirements. The rating also considers the competition in the pharmaceutical distribution and jewellery retail business. Besides, the rating notes that Kandalaa, Kandalaa Prints and Kandalaa Distributors are partnership firms, which increases the capital withdrawal risk, as witnessed in the previous years.

The Stable outlook on the [ICRA]BB rating reflects ICRA's opinion that the Kandalaa Group will continue to benefit from its extensive track record of operations and an established market position.

Key rating drivers and their description

Credit strengths

Established track record of the Group in pharmaceutical distribution and jewellery retail business - Kandalaa Distributors was set up in 1992. The firm has a track record of more than three decades in the pharmaceutical distribution business as a CFA/super stockist for various pharmaceutical companies in Karnataka. KD caters to a large number of customers in the Karnataka (especially Bengaluru) market, which are a mix of wholesalers/sub-stockists, medical retail chains etc.

Kandalaa has an established presence in the Bengaluru region, with the entity operating its jewellery showroom in a prominent location for around a decade. Further, the vast experience of the promoters in the gold jewellery industry coupled with its focus on providing ornament designs that suit the specific tastes and preferences of the customers enabled the company to establish a loyal customer base, which has driven its revenues over the years through repeat purchases.

Established relationships with pharmaceutical companies and wide product portfolio – Kandala Distributors has been able to establish strong relationships with its suppliers. It is the sole super stockist/C&F agent for the regions allocated to it in Karnataka for many of its supplier brands. Its association with reputed pharmaceutical companies such as Albert David Ltd., British Biologicals Pvt Ltd, Hegde & Hegde provides stability to the revenues.

Kandala Distributors is responsible for maintaining a stock of various pharma companies and forwarding the required stock keeping units (SKUs) to the stockists on request. It has a wide product portfolio of about 1,500 SKUs of different pharmaceutical companies and caters to more than 500 stockists and retailers in the Karnataka region.

Credit challenges

Low operating margins and stretched coverage indicators –The Group’s operating margins continue to be low due to the relatively low margins in major entities - Kandala Distributors and Kandalaa. The Group financial risk profile is marked by stretched coverage indicators, with a total debt/OPBITDA of 7.2 times and interest coverage of 1.3 times in FY2023. The Group’s gearing was weak at 3.9 times as on March 31, 2023. However, ICRA notes a significant portion of the debt as on March 31, 2023, is in the form of interest-bearing unsecured loans from promoters and relatives with no scheduled repayment.

Exposed to intense competition – The presence of a large number of players due to the low entry barriers in the pharma distribution business intensifies competition in the segment, thereby putting pressure on the margins. Nevertheless, Kandala Distributors’ established presence in Bengaluru provides competitive advantage to some extent.

However, Kandalaa’s jewellery retail operations are confined to its single showroom in Bengaluru, exposing it to geographical concentration risk. Its established brand presence in the region and customer base supported its performance over the years, but it remains exposed to increasing competition from organised and unorganised players, limiting pricing flexibility and margins.

Inherent risk associated with partnership firms – Kandalaa, Kandala Distributors and Kandalaa Prints are exposed to the risks associated with a partnership firm, including capital withdrawal risk, which can adversely impact their capital structure.

Liquidity position: Stretched

The repayment of the existing loans, along with an elongated working capital cycle, would continue to exert pressure on the Group’s liquidity. The high average utilisation of the working capital limits provides limited buffer. Further, the group liquidity profile may be impacted if financial support is extended to Kandalaa Prints, which has substantial debt repayment obligations over the medium term and for which Kandalaa has already extended corporate guarantee.

The Group promoters and related parties have infused funds in the past in the form of unsecured loans to support the liquidity requirements. The promoter’s contribution in case of any cash flow mismatch will remain crucial to support the company’s liquidity.

Rating sensitivities

Positive factors – A sustained growth in the Kandalaa Group’s scale of operations and earnings coupled with an improvement in the working capital cycle, resulting in better debt protection metrics and liquidity position, may result in an upgrade.

Negative factors – Pressure on the rating will emanate from any sharp fall in the Group’s earnings or an elongation in the working capital cycle, which would result in a deterioration of the coverage metrics and liquidity position. A specific credit metrics that could lead to a rating downgrade includes a consolidated DSCR below 1.1 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not Applicable
Consolidation/Standalone	For arriving at the rating, ICRA has carried out consolidated analysis of the Kandalaria Group, comprising Kandala Distributors, Kandalaria, Kandalaria Prints and Sribalaji Hitechexim Projects Private Limited

About the company

Kandala Distributors is a partnership firm formed in 1992 and is involved in the distribution of pharmaceutical products. The firm is a super stockist/clearing and forwarding agent of pharmaceutical companies and caters to stockists all over Karnataka. The firm trades in over 1,500 branded drugs with supplies from pharmaceutical companies like British Biologicals, Hegde & Hegde LLP, MSD Pharmaceuticals Ltd, Albert David Limited, among others. It used to operate from four warehouses in Bengaluru. However, it has now shifted its operations to Harohalli, Ramanagara, Karnataka. The Group consists of sister concern, Kandalaria, which is a jewellery retail outlet; Kandalaria Prints which is a packaging firm; and Sribalaji Hitechexim Projects Private Limited which is the lessor for the warehouse leased to Kandala Distributors.

Kandalaria, established in 2011 by Mr. K.G. Subbaraj, is a partnership firm involved in the retailing of gold and diamond jewellery. The firm operates a single retail showroom at Jayanagar in Bengaluru, which was set up in October 2011. The firm's retail store sells both readymade and customised jewellery.

Kandalaria Prints, established in 2020, is an integrated packaging firm located at Harohalli. Its capacity includes conventional printing & UV printing.

Key financial indicators

Consolidated	Standalone		Consolidated	
	FY2022	FY2023*	FY2022	FY2023*
Operating income	182.1	203.6	331.1	417.2
PAT	1.1	0.9	-0.4	-1.7
OPBDIT/OI	1.6%	1.5%	4.1%	3.6%
PAT/OI	0.6%	0.4%	-0.1%	-0.4%
Total outside liabilities/Tangible net worth (times)	3.0	3.8	4.4	5.6
Total debt/OPBDIT (times)	3.3	4.9	6.1	7.2
Interest coverage (times)	1.6	1.6	1.3	1.3

Source: Firm, ICRA Research; * Provisional numbers; All ratios as per ICRA's calculations; Amount in Rs. crore PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Amount rated (Rs. crore)	Current rating (FY2024)		Chronology of rating history for the past 3 years			
			Amount outstanding (Rs. crore)	Date & rating in FY2024	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	
				Nov 29, 2023	Aug 12, 2022	July 30, 2021	-	
1	Cash credit	Long term	10.0	-	[ICRA]BB (Stable)	[ICRA]BB+ (Stable)	[ICRA]BB+ (Stable)	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Cash credit	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	Cash credit	NA	NA	NA	10.00	[ICRA]BB(Stable)

Source: Company

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Kandala Distributors	Rated Entity	Full Consolidation
Kandalaa	Group Entity	Full Consolidation
Kandalaa Prints	Group Entity	Full Consolidation
Sribalaji Hitechexim Projects Private Limited	Group Entity	Full Consolidation

Source: Company

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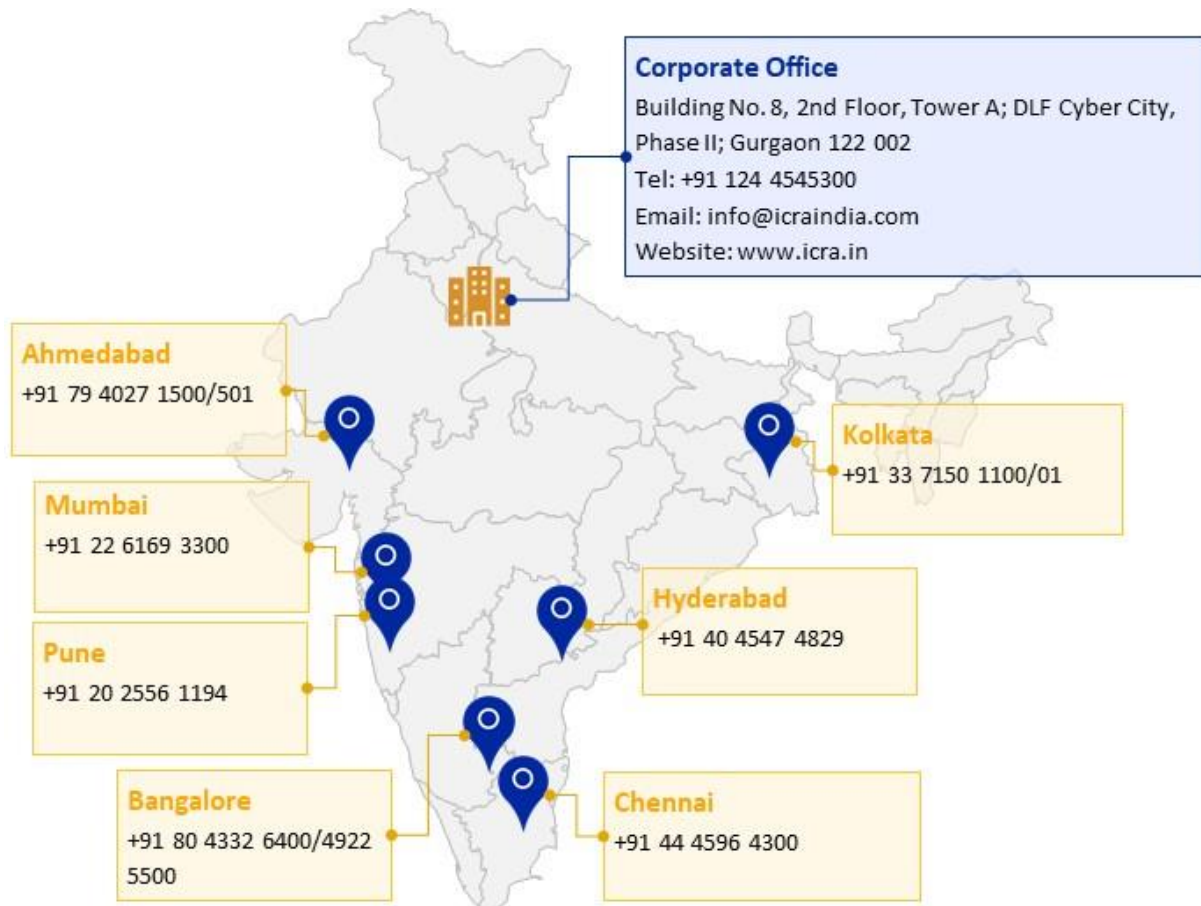
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