

December 14, 2021

Hafele India Private Limited: Ratings reaffirmed; outlook revised to Positive, rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term /Short-term, Fund-based	30.0	0.0	-
Long-term/Short-term; Fund based/Non-fund Based	222.0	332.0	[ICRA]A+ (Positive) /[ICRA]A1; reaffirmed and outlook revised to Positive from Stable
Short-term, fund based	55.0	0.0	-
Long-term/Short-term interchangeable	(37.0)	0.0	-
Total	307.0	332.0	

*Instrument details are provided in Annexure-1

Rationale

The revision in the outlook to Positive factors in Hafele India Private Limited's (HIPL) significant improvement in the top line in CY2021, given the sharp recovery in 10M CY2021 (provisional numbers) because of strong demand, which is likely to drive the revenue profile in the near term. The operating margins for 10M CY2021 rose to 13% from 8% in CY2020, driven by higher top line as well as part continuation of Covid-induced cost rationalisations. Going forward, with the situation normalising, the company is likely to scale back any Covid-related cost curtailments, which is likely to moderate the margins from CY2021 levels. However, the operating margins are still expected to be at healthy levels and will remain a key monitorable from a rating perspective.

Strong demand conditions supporting faster inventory turnaround helped the company to improve its working capital cycle as the working capital intensity (net working capital as a percentage of operating income, NWC/OI) improved to 18% in 10M CY2021 from 31% in CY2020. This in turn led to lower working capital borrowing levels, strengthening the capitalisation and coverage metrics.

The ratings continue to derive comfort from the established position of HIPL's promoter group, Germany-based Hafele Holding GmbH (HHG), as well as its strong global brand presence in the premium architectural hardware and kitchen/furniture fittings industry. The ratings also derive strength from the professional management set-up as well as the operational expertise and financial flexibility enjoyed by HIPL by virtue of its strong parentage. The ratings favourably factor in HIPL's strong distribution network comprising dealers and exclusive franchisees.

The ratings, however, remain constrained by the stiff competition in the industry and the investments required to support the increased scale of operations that have kept the operating profit margins (OPM) range-bound. The ratings also remained constrained by the working capital-intensive nature of the business, driven by high inventory requirements. Moreover, there is a need to continuously invest in marketing initiatives for customer acquisition and retention. As around 89% of HIPL's (traded) products are imported, its OPM remains exposed to the fluctuations in foreign currency rates although these are mainly mitigated by hedging through forward contracts. Further, the gross margin remains vulnerable to rupee depreciation, though it attempts to pass it on to its customers through periodic price increases. ICRA notes the high concentration of HIPL's

revenues towards the BLUM's¹ range of kitchen fittings. Nonetheless, the rating agency draws comfort from HIPL's established relationship with the Hafele Group worldwide as exclusive distributors for BLUM's products.

The Positive outlook reflects ICRA's expectation that HIPL will continue to maintain its strong brand position in the fittings industry, which is expected to support its scale of operations, a strong liquidity profile and its healthy financial profile.

Key rating drivers and their description

Credit strengths

Strong brand presence in premium architectural hardware and furniture fittings segment; operational expertise and financial flexibility on account of strong parentage – HIPL is a wholly-owned subsidiary of the German firm, HHG, one of the leading players in architectural hardware and kitchen/furniture fittings segment, with a presence across six continents through 37 subsidiaries. HIPL enjoys access to the diversified product offering of HHG worldwide and enjoys a strong brand image in the premium segment. Its product range is considerably diversified vis-à-vis the competing brands. Besides operational expertise, the company benefits from the strong financial flexibility because of its parentage.

Significant improvement in operating performance expected in CY2021 – The company's revenues have improved significantly with the top line at Rs. 834.2 crore in 10M CY2021 against Rs. 599.6 crore in CY2020, driven by strong demand. This is likely to support the revenue base in the near term. The operating margins also improved to 13.0% in 10M CY2021 against 8.0% in CY2020 owing to the higher top line as well as part continuation of Covid-induced cost rationalisations. Although the margins are expected to moderate in CY2022 as the company is likely to scale back any Covid-related cost curtailments, they are expected to remain healthy and will remain a key monitorable. The improvement in the top line and margins and better inventory management during 10M CY2021 have ensured a healthy cash flow generation, leading to limited borrowing levels and notable improvement in the debt metrics as of provisional 10M CY2021.

Strong distribution network comprising dealers and exclusive franchisee – HIPL has a network of more than 500 dealers and exclusive distributors across India. The distributors further supply to sub-dealers, which primarily cater to the refurbishment market for products such as hinges and door handles. The franchisee network comprises 80 exclusive franchisees across India.

Healthy medium-term demand prospects – The aspirational consumption patterns of the upper-middle income groups and HNIs - HIPL's key customer segments - augur well for its demand prospects over the medium term. HIPL undertakes several initiatives to promote its brand presence, which has further improved secondary sales. The company has 11 design centres, with two each in Mumbai and Chennai, and one each in Kolkata, Pune, Bengaluru, New Delhi, Hyderabad, Dhaka, (Bangladesh) and Colombo (Sri Lanka), for customers to experience the functionality of the brand's products.

Credit challenges

Working capital-intensive nature of operations – The company's working capital intensity has remained high in the range of 30-40% on account of its large inventory requirements. It deals in more than 8,000 active stock keeping units (SKUs), most of which are imported. The high lead time necessitates large inventory holding. However, strong demand conditions leading to faster inventory turnaround along with lower debtor days helped the company to improve its working capital cycle as reflected in an improvement in NWC/OI to 18% in 10M CY2021 compared with 31% in CY2020. This in turn led to lower working capital borrowing levels, strengthening the capitalisation and coverage metrics. Hence, going forward, a judicious management of the inventory to keep the working capital borrowing levels under check will remain a key monitorable.

¹BLUM is an Austrian kitchen fittings manufacturer

High competitive intensity and investments to support scale of operation keep operating margins range-bound – The architectural hardware and furniture fittings industry is highly fragmented with several organised and unorganised players in the field. HIPL’s OPM has remained moderate and range-bound between 8% and 10.5% during the past four years ended CY2020 owing to the stiff competition in the industry as well as the investments undertaken (towards employees, sales, marketing and distribution activities) to support its increased scale of operations. As around 89% of HIPL’s (traded) products are imported and are mainly sold in the domestic market, its margins are exposed to the fluctuations in foreign currency rates. However, these are primarily mitigated by hedging through forward contracts. Further, its gross margin remains vulnerable to rupee depreciation, though the company attempts to pass it on to its customers through periodic revision in prices.

Business vulnerable to overall economic environment – HIPL’s business remains vulnerable to the overall economic environment as reflected in a sharp dip in the top line in CY2020 to Rs. 599.6 crore compared with Rs. 834.0 crore in CY2019 due to Covid-19 related disruption. This is also underpinned by the discretionary nature of product offering which the company deals with and the relatively premium segment it caters to.

Liquidity position: Strong

The company’s liquidity position is strong as reflected in a healthy cash flow from operations, unutilised limits of Rs. 233 crore as on September 30, 2021 and unencumbered cash and liquid investments of Rs. 46.5 crore as on October 31, 2021. Against this, the company has limited long-term debt repayments and is expected to incur minimal capex, supporting its liquidity position in the near to medium term.

Rating sensitivities

Positive factors – The ratings may be upgraded if there is a sustained improvement in the operating performance and liquidity position. Specific credit metrics that will result in a rating upgrade include the return on capital employed (ROCE) improving to above 20% on a sustained basis.

Negative factors – The outlook would be revised to Stable if there is a material weakening in the company’s revenues, profit margins and the working capital cycle, which impacts the overall financial/liquidity profile of the company. Sustained deterioration of the interest cover below 5 times will remain a negative rating trigger.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

About the company

HIPL, incorporated in 2003, is a 100% subsidiary of the German firm, HHG. While HIPL originally dealt in kitchen/furniture fittings and the architectural hardware product line of HHG, over the last four years, it has diversified into segments such as glass and sanitary fittings, sliding fittings, built-in appliances, lighting systems and kitchen slabs, among others.

HIPL has a product range of over 1,50,000 articles, which are either supplied under the in-house brand range or through other suppliers. The in-house brand range comprises nine brands, including Nagold (appliances), Ixconnect (connectors), Moovit (runner systems), Slido (sliding door solutions), Dialock (electronic locking and access control systems), Loox (lighting series), Officys (furniture fittings for offices) and EPC (customised client solutions). These products are assembled globally at Hafele

Germany and Hafele China before being supplied to various subsidiaries. HIPL deals in brands of over 1,500 suppliers such as BLUM (Austria), Bertazonni (Italy), and Blanco (Germany), etc. The company is present in Sri Lanka, Bhutan, Bangladesh and Nepal.

Key financial indicators (audited)

	CY2019	CY2020
Operating Income (Rs. crore)	839.3	605.4
PAT (Rs. crore)	47.6	16.7
OPBDIT/OI (%)	10.5%	8.0%
PAT/OI (%)	5.7%	2.8%
Total Outside Liabilities/Tangible Net Worth (times)	1.2	0.8
Total Debt/OPBDIT (times)	1.2	1.1
Interest Coverage (times)	6.8	4.4

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current Rating (FY2022)			Chronology of Rating History for the past 3 years					
		Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating on	Date & Rating in FY2021	Date & Rating in FY2020			Date & Rating in FY2019	
						14-Dec-2021	1-Oct-2020	26-Aug-19	31-May-19	27-Sep-18
1 Fund-based Limits	Long-term/ Short-term	0.0	-	-	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1
2 Fund-based / Non-fund Based Limits	Long-term/ Short-term	332.0	-	[ICRA]A+ (Positive)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1
3 Fund-based Limits	Short-term	0.0	-	-	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1
5 Interchangeable bank facilities	Long-term/ Short-term	0.0	-	-	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A+ (Stable)/ [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1	[ICRA]A (Positive) / [ICRA]A1

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/ Short-term- Fund-based / Non-fund Based Limits	Very Simple/ 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 analyzing 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, is available on ICRA's website: www.icra.in

Annexure-1: Instrument details

Bank Name	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. Crore)	Current Rating and Outlook
ICICI Bank	Fund-based / Non-fund Based Limits	NA	NA	NA	30.00	[ICRA]A+(Positive) /[ICRA]A1
HDFC Bank	Fund-based / Non-fund Based Limits	NA	NA	NA	117.00	[ICRA]A+(Positive) /[ICRA]A1
Kotak Mahindra bank	Fund-based / Non-fund Based Limits	NA	NA	NA	50.00	[ICRA]A+(Positive) /[ICRA]A1
HSBC Bank	Fund-based / Non-fund Based Limits	NA	NA	NA	35.00	[ICRA]A+(Positive) /[ICRA]A1
Standard Chartered Bank	Fund-based / Non-fund Based Limits	NA	NA	NA	60.00	[ICRA]A+(Positive) /[ICRA]A1
Yes Bank	Fund-based / Non-fund Based Limits	NA	NA	NA	40.00	[ICRA]A+(Positive) /[ICRA]A1

Source: Company

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

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