

March 22, 2022

Alukkas Enterprises Private Limited: Long-term rating upgraded to [ICRA]A(Stable)

Summary of rating action

Instrument*	Previous rated amount (Rs. Crore)	Current rated amount (Rs. crore)	Rating Action
Long term - Fund based facilities	49.55	49.55	Upgraded to [ICRA]A(Stable) from [ICRA]A-(Stable)
Total	49.55	49.55	

*Instrument details are provided in Annexure-1

Rationale

For arriving at the rating, ICRA has taken a consolidated view of Alukkas Enterprises Private Limited (AEPL) and other jewellery entities operating in the Group (collectively referred to as the Jos Alukkas Group), given the common management and strong operational and financial linkages among the entities. Details of various entities operating in the Group, which have been consolidated, are given in Annexure 2.

The ratings action reflects better-than expected performance of the Jos Alukkas Group in the recent quarters and the anticipated steady revenues and earnings over the medium term, driven by its strong market position in the southern states and proposed diversification initiatives. Despite the pandemic-induced business disruptions witnessed in H1 FY2021, the Group's revenues and earnings improved in FY2021, supported by the recovery in demand conditions in the second half and a healthy increase in gold prices. Thus, the Group registered only a marginal revenue decline of 2% in the fiscal, against a ~39% decline witnessed in H1 FY2021. Favourable gold prices resulting in inventory gains, and cost-control measures helped improve the operating margin to rise to 7.1% in FY2021 from 3.5% in the previous fiscal. In line with the healthy demand witnessed post the second wave of the pandemic, the Jos Alukkas Group is likely to register a revenue growth of more than 10% in FY2022. Growth over the medium term would be supported by the on-going store expansion as well as opportunities presented by a large share of unorganised players in the industry. The Group's operating margins are likely to stabilise at around 4% over the medium term. The same would be driven by the focused initiatives undertaken to improve the inventory turnover and an expected increase in the share of studded jewellery (the Group has set up new store in non-South market in the current year).

The ratings continue to positively consider the Group's comfortable financial profile. A steady growth in earnings and lack of any major expansion in the recent past led to an improvement in its debt protection metrics. Key credit metrics including the interest coverage and total outside liabilities to the tangible net worth (TOL/TNW) improved to around 9 times and 0.9 times, respectively in FY2021 and are expected to remain comfortable at around 6 times and 0.8 times, respectively in the current fiscal. The same is despite the moderation in earnings on the back of reduction in margins to steady-state levels and an increase in the debt levels to fund the ongoing store expansion. The ratings remain constrained by the Group's moderate operating profitability owing to low contribution from studded jewellery, high working capital requirements in the business and high geographical concentration risks as it derives the major portion of its revenues from the Tamil Nadu market. The ratings also factor in the intense competition and lack of hedging practices, which expose its earnings to volatile gold prices. The other concerns include risks inherent in the partnership firms (one entity in the Group has been constituted as a partnership firm) including the risk of capital withdrawal. Besides, the Group has extended financial support to other promoted-owned companies to the tune of Rs. 110 crore in the recent past. The regulatory risks had also impacted the retailers' performance in the past. ICRA expects no incremental support to be extended towards other promoter-owned companies, going forward.

The Stable outlook on the long-term rating reflects ICRA's expectations that Jos Alukkas' performance will continue to benefit from its strong market position, improving business diversification, and comfortable capitalisation levels.

Key rating drivers and their description

Credit strengths

Established market position – Jos Alukkas is among the largest organised jewellery retailers in South India with an established and dominant Jos Alukkas brand. The company has 47 stores and commands a strong market position in Tamil Nadu, Kerala and Karnataka (cumulatively contributes ~90% to sales), which supported its revenues over the years. The vast experience of the promoters in the gold jewellery industry for three decades coupled with its focus on providing jewellery designs as per specific tastes and preferences of the customers enabled the company to establish its presence and capture a loyal customer base. Its strong brand equity is illustrated by a steady revenue growth across the states despite entry of many large regional chains in the recent years. Incremental sales from the ongoing store expansion coupled with its established presence are expected to drive footfalls and revenues over the medium term.

Comfortable financial profile – The Group's financial profile remains comfortable, characterised by a conservative capital structure with adequate coverage metrics and liquidity position. The coverage metrics improved in FY2021 driven by a healthy growth in earnings, despite the high working capital requirements in the business. The leverage indicators and coverage metrics are likely to remain comfortable, despite the ongoing store expansion, supported by expected steady earnings from operations over the medium term. Further, the financial profile derives comfort from its adequate liquidity position and relatively limited dependence on external debt, reflected in the total outside liabilities to inventory ratio of around 55%.

Favourable growth prospects in jewellery segment for organised players – Increasing measures in the jewellery segment for greater transparency and higher compliance costs resulted in a sizeable churn in the unorganised segment, benefiting organised players such as the Jos Alukkas group over the years. Further, regulatory changes such as the mandatory hallmarking of gold jewellery from June 2021 have supported organised trade and would continue to provide better opportunities for the group which has an extensive presence in tier-2 and tier-3 markets.

Credit challenges

Earnings exposed to geographical concentration risks – The Group, being a South India-based jewellery retailer, derives over half of its revenues from Tamil Nadu and the balance from Karnataka, Andhra Pradesh, Telangana and Kerala, leading to geographical concentration risks. While dependence on the southern states is expected to remain high, its established brand presence and revenues from repeat customers coupled with proposed expansion into new regions within these large markets lend some comfort.

Moderate operating profitability – Gold jewellery retailing business is very competitive with presence of large organised and unorganised players. This coupled with limited value addition, constrains pricing flexibility of the players, resulting in thin operating margins. Further, as the retail business is working capital intensive in nature with adequate inventory required to be maintained across stores, earnings remain exposed to volatility in gold prices. The Group's profitability has remained low over the years due to the Group's focus on the fast-moving low value-added gold jewellery and due to competition from established retailers in its key markets. However, customer loyalty driven by strong brand equity has augmented the sales volumes over years, resulting in stable profits.

Exposure to regulatory risks as well as risks inherent in partnership firms – Although certain regulatory measures have aided in the shift towards organised trade like the recent hallmarking initiatives, some adverse regulatory developments have impacted the domestic gold jewellery industry in the past. Restrictions on bullion imports and metal loan funding, mandatory PAN disclosure on transactions above a certain limit, and imposition of excise duty are some of the regulatory developments that have impacted the industry over the last decade. The Group remains exposed to the risks arising out of any such future regulatory actions that may impact its business profile. Moreover, one of the entities has been constituted as a partnership firm, so the Group is exposed to discrete risks including the possibility of capital withdrawal by the partners. Any significant capital withdrawal by the partners or incremental funding support to other companies managed by the promoters could adversely impact its credit profile and remain a key monitorable.

Liquidity position: Adequate

The Group’s liquidity position is expected to remain adequate, supported by steady earnings from operations coupled with unutilised lines of credit enjoyed and adequate free cash balances. Cash buffer, including free cash reserves, liquid investments and unutilised working capital limits together stood at around Rs. 140 crore as of February 2022. The average utilisation of its fund-based limits over the last 12 months ending February 2022 stood at around 85%, given the high inventory holding requirement in the business. Despite the expected increase in working capital requirements to fund store expansion, its cash flow position would be supported by cash accruals of around Rs. 200 crore per annum apart from the proposed enhancement in its working capital limits.

Rating sensitivities

Positive factors – ICRA could upgrade the Group’s ratings if there is a sustained healthy growth in revenues and improvement in its profitability on the back of better business diversification through store expansion and higher share of studded jewellery, while maintaining its comfortable debt protection metrics and liquidity position..

Negative factors – Pressure on the Jos Alukkas Group’s ratings may arise if there is a sustained pressure on the operating performance or any deterioration in the working capital cycle, which would adversely impact its coverage metrics and liquidity position. Specific credit metrics that may lead to ratings downgrade include an interest coverage of less than 5.0 times on a sustained basis. Further, any incremental cash outflow towards other companies owned by the promoters would also exert pressure on the ratings.

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	For arriving at the ratings, ICRA has consolidated the business and financial risk profiles of AEPL, Alukkas Gold Retail India Private Limited Alukkas Jewellery Thrissur (collectively referred to as the Jos Alukkas Group), owing to the common management and strong linkages between the entites

About the company

The Jos Alukkas Group of entities, with Mr. Jose Alukka as its Chairman, commenced jewellery retail operations in 2002 with a showroom in Thrissur, Kerala. The Group consisted of three entities, including AGR IPL, Alukkas Enterprises Private Limited (AEPL) and Alukkas Jewellery Thrissur (AJT) of which the latter one is a partnership firm. The Group is managed by the promoter’s three sons – Mr. Paul Alukka, Mr. Varghese Alukka and Mr. John Alukka. The Group’s operations are concentrated in Tamil Nadu, Kerala, Andhra Pradesh, Telangana and Karnataka. It has expanded its presence in non-South markets with its first store added in Pune in the current year. The Group has 47 stores across five states in South India and one in Pune as of February 28,2022.

Key financial indicators (audited)

Jos Alukkas Group (consolidated)	FY2020	FY2021
Operating Income (Rs. crore)	6716.3	6581.5
Adjusted* Operating Income (Rs. crore)	4,006.4	3,947.3
PAT (Rs. crore)	139.5	307.3
OPBDIT/OI (%)	3.5%	7.1%
Adjusted* OPBDIT/OI (%)	5.9%	11.9%
PAT/OI (%)	2.1%	4.7%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	0.9
Total Debt/OPBDIT (times)	2.3	1.1
Interest Coverage (times)	4.5	9.1

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

*Adjusted for vendor sales correspondence to bullion given to artisans for Job work

AEPL (standalone)	FY2020	FY2021
Operating Income (Rs. crore)	2,011.1	1,802.0
PAT (Rs. crore)	67.9	114.9
OPBDIT/OI (%)	4.6%	8.6%
PAT/OI (%)	3.4%	6.4%
Total Outside Liabilities/Tangible Net Worth (times)	0.5	0.4
Total Debt/OPBDIT (times)	0.4	0.3
Interest Coverage (times)	14.4	19.6

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Current Rating (FY2022)				Chronology of Rating History for the past 3 years				
	Type	Amount Rated (Rs. crore)	Amount Outstanding as on February 28, 2022 (Rs. crore)	Date & Rating in	Date & Rating in FY2021		Date & Rating in FY2020	Date & Rating in FY2019	
					December 14, 2020	October 30, 2020			
1 Fund Based – Working Capital Facilities	Long term	49.55	-	March 21, 2022 [ICRA]A (Stable)	December 14, 2020 [ICRA]A- (Stable)	October 30, 2020 [ICRA]A- (Stable)	July 17, 2019 [ICRA]A- (Stable)	April 06, 2018 [ICRA]A- (Stable)	

Source: Company; Amount in Rs. Crore

Complexity level of the rated instrument

Instrument	Complexity Indicator
Fund Based – Working Capital Facilities	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

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund Based – Working Capital Facilities	-	-	-	49.55	[ICRA]A (Stable)

Source: ARG IPL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Alukkas Enterprises Private Limited	-	Full Consolidation
Alukkas Jewellery Thrissur	-	Full Consolidation
Alukkas Gold Retail India Private Limited	-	Full Consolidation

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