Spacewood Furnishers Private Limited

May 31, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long term Fund-based-Working Capital Facilities	32.50	43.50	[ICRA]BBB-downgraded from [ICRA]BBB, outlook revised to Negative from stable
Long term, unallocated	2.50	0.00	-
Non-fund Based Facilities	22.76	21.26	[ICRA]A3 downgraded from [ICRA]A3+
Total	**57.76**	**64.76**	

*Instrument details are provided in Annexure-1

Rating action

ICRA has revised the long-term rating to [ICRA]BBB- (pronounced ICRA Triple B minus) from [ICRA]BBB (pronounced ICRA Triple B) for the Rs. 43.50-crore (enhanced from Rs. 32.50-crore) long-term facilities of Spacewood Furnishers Private Limited (SFPL or the company)[1]. ICRA has also revised the short-term rating for the Rs. 21.26-crore non-fund based limits (reduced from Rs. 21.76 crore) to [ICRA]A3 (pronounced ICRA A three)[2] from [ICRA]A3+ (pronounced ICRA A three plus). The outlook on the long-term rating has been revised to Negative from Stable.

Rationale

The revision in ratings considers the sharp decline in the operating profit margins of the company over the past two fiscals, given the higher overheads required to manage the home furniture segment and its stretched receivable position. This along with its high inventory levels has impacted the liquidity position as evidenced from SFPL's high utilisation of working capital limits. The revision in rating outlook also factors in the expected pressure on the company's profitability and liquidity position, going forward, given its high overheads and stretched receivable position. ICRA notes that a sizeable portion of SFPL's receivables are from its subsidiary, Modern Living Solutions (MLS), which has been stretching the payments given its weak financial position, and timely recovery of the same will remain crucial for the improvement in its liquidity position. Further, the ratings continue to remain constrained by the company's weak debt coverage indicators; vulnerability of its profitability to fluctuations in the prices of its raw materials and foreign exchange rates in the absence of any firm hedging policy. The ratings also take note of its exposure to significant competition from the unorganised and organised sectors and also cheaper imports, which have a significant bearing on the company's profitability.

The rating, however, continues to factor in the extensive experience of the promoters in the furniture industry, technical support provided by the Japan-based Sumitomo Group, which holds a 26% stake in the company through its subsidiary Sumitomo Forestry (Singapore) Private Limited. The rating also favourably factors in the wide product portfolio of the company as also its presence across various sales media providing visibility and its reputed and diversified customer base.

[1] *100 lakh = 1 crore = 10 million*

[2] *For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications*

Outlook: Negative

ICRA expects the company's operating profitability to remain under pressure, given the high overheads required to manage the home furniture segment. The rating may be downgraded if the company continues to report weak profitability and/or the working capital cycle weakens further, thereby constraining the financial profile of the company. The outlook may be revised to Stable if the financial profile is strengthened because of improved profitability and working capital cycle on the back of faster recovery of receivables and reduction in inventory levels.

Key rating drivers

Credit strengths

Extensive experience of the promoters in the modular furniture industry; investment by the Japan-based Sumitomo Group in the form of 26% equity stake in SFPL - SFPL was established in 1996 by Mr. Kirit Joshi and Mr. Vivek Deshpande. Both the promoters have more than two decades of experience in the domestic modular furniture industry. The Japan-based Sumitomo Group through its subsidiary, Sumitomo Forestry (Singapore) Company Limited (Sumitomo Forestry) in FY2016 has invested Rs. 72.00 crore in the company acquiring ~26% stake. The investment proceeds have been used for setting up the pre-hung door unit in technical collaboration with Sumitomo Forestry and capacity expansion with the buffer parked in liquid mutual funds.

Diversified product profile - The company's operations remain sub-divided into five verticals namely, office furniture / table tops, pre-laminated boards, kitchen and pre-vinyl shutters, bedroom home furniture and doors, wherein it offers a diverse range of products. Bedroom and home furniture sales continued to dominate SFPL's revenue mix in FY2017 and FY2018 (~40% of the total sales) as in FY2016 followed kitchen and PVC shutters, wherein the sales have remained almost constant in FY2016 and FY2017 (~30% of the total sales). In FY2018, it also has forayed in the pre-hung doors segment and has garnered ~Rs. 10.00-crore revenues from this segment.

Reputed and diversified customer profile - SFPL's customer profile comprises reputed customers like Future Retail Limited, Nilkamal Limited, Flipkart Limited, State Bank of India among others. The customer concentration has remained moderate in FY2018 with the top-five customers contributing close to 35% of the revenues almost in line with FY2017 (37% of the total revenues). The company garners revenues through various channels, such as retail outlets like Spacewood stores (managed by Modern Living Solutions Private Limited (MLS)), Pantaloons, e-commerce platforms like Flipkart, Urban Ladder etc which provides brand visibility. It has also entered in deferred credit advertisement with Benet Coleman and Company Limited against equity participation in order to further increase its brand visibility.

Credit challenges

Significant decline in operating profit margins in the last three fiscals, weak debt coverage indicators - Though the company has witnessed a moderate revenue growth in the last three fiscals, its operating profitability has been significantly impacted because of increased overheads to manage the increasing number of warehouses along with decrease in the share of project-based revenues, mainly from kitchen segment where margins are better as compared to retail sales. SFPL's operating profit margins (OPM), which were at ~11.7% in FY2015, declined sharply to 4.3% in FY2016 and 2.7% in FY2017, respectively. As per the provisional financials for 9M FY2018, the OPM continued to remain weak and stood at 2.9%. Accordingly, the net profit margins (NPM) have remained weak and stood at 1% in FY2017 as against 9.4% in FY2016. In 9M FY2018, the company has reported a negative profit before tax of Rs. 2.05 crore.

The company's capital structure has remained comfortable due to its healthy net worth base, with a gearing below 1 times as on March 31, 2017 and December 31, 2017. However, the debt coverage indicators have remained weak with an interest coverage of 1.3 times, total debt/OPBDITA of 7.1 times, NCA/TD of 8% as on December 31, 2017 as compared to an interest coverage of 1.0 times, total debt/OPBDITA of 7.4 times, NCA/TD of 12% as on March 31, 2017.

Stretched receivables and high inventory levels impacting the liquidity position - SFPL working capital intensity continued to remain high in FY2017 and 9M FY2018 as in the past and remained at 34% and 35%, respectively due to its stretched receivables and high inventory levels. The debtor days continued to remain stretched owing to delayed payments from some of the real estate clients and increased further to 150 days as on December 31, 2017 from 120 days as on March 31, 2017. A significant portion of the receivables are from its subsidiary MLS, which has continued to stretch the payments given its weak financial position. MLS accounted for 34% of the total receivables as on March 31, 2017. The inventory levels also remained on a higher side, given the high lead time involved in imports of raw material and the high stocking requirement because of multiple SKUs in the modular furniture segment. As on December 31, 2017, the inventory levels stood at 109 days as against 109 days as on March 31, 2017. SFPL's liquidity position has been impacted by its stretched receivables and high inventory levels as reflected by the high average monthly utilisation (88%) of working capital limits in FY2018. Nonetheless, liquid investments in the form of mutual funds to the tune of Rs. 13.00 crore as on March 31, 2017 have provided some support to the liquidity.

Vulnerability of profitability to fluctuations in raw material prices and foreign exchange rates - The company remains dependent on imports for its key raw materials (particle board and medium density fibre), as they are cheaper compared to the domestic market. Raw material imports formed 51% of the total purchases in FY2017 as compared to 54% in FY2016. It has minimal exports vis–a-vis significant imports, thus exposing it to foreign exchange fluctuation risks. SFPL does not enter into forward contracts to hedge the foreign exchange fluctuation risks. Further, given the high inventory levels, its profitability also remains vulnerable to any volatility in the prices of the key raw materials.

Intense competition mainly from the unorganised sector - Given the limited entry barriers, SFPL faces stiff competition from the unorganised players as well as from established brands and cheap imports, which limits the profitability in the modular furniture segment.

Analytical approach: For arriving at the ratings, ICRA has applied its rating methodologies as indicated below**.**

Links to applicable criteria:

Corporate Credit Rating Methodology

About the company:

SFPL was established in 1996 by Mr. Kirit Joshi and Mr. Vivek Deshpande. SFPL is primarily involved in manufacturing modular furniture and pre-laminated boards. The company started off as a manufacturer of furniture and furniture components for larger OEMs such as Godrej and Wipro. Over the years, SFPL has moved from being a component manufacturer to a complete furnishing solution provider to OEMs and now directly to the end-user under its own brands. SFPL has its manufacturing facility at Nagpur and at present, its operations are structured around five business verticals viz, modular kitchen and shutters, home and bedroom furniture, office furniture, pre-hung doors and pre-laminated boards. SFPL forayed into furniture retailing in 2008-2009 through the launch of its "Tru Value" brand. However, SFPL subsequently rebranded the same as Alfa and augmented its product profile by adding modular kitchens in 2010-2011. During 2010-2011, the company also introduced two new brands viz, Life Style Furniture and Modern Living in the premium and luxury segment. SFPL has a 100% subsidiary named Modern Living Solutions Private Limited, which is in the business of operating furniture showrooms. The Japan-based Sumitomo Group through its subsidiary, Sumitomo Forestry (Singapore) Company Limited holds ~26% stake in SFPL.

In FY2017, the company reported a net profit of Rs. 1.8 crore on an operating income (OI) of Rs. 184.1 crore, as compared to a net profit of Rs. 16.3 crore on an OI of Rs. 173.2 crore in the previous year. As per the provisional financials for 9M FY2018, SFPL has recorded an OI of Rs. 164.7 crore and a loss of Rs. 2.0 crore at the PBT level.

Key financial indicators

	FY2016 Audited	FY2017 Audited	9M FY2018 (Provisional)
Operating Income (Rs. crore)	173.2	184.1	164.7
PAT (Rs. crore)	16.3	1.8	-2.0
OPBDIT/OI (%)	4.3%	2.7 %	2.9%
RoCE (%)	25.0%	4.8%	1.7%
Total Debt/TNW (times)	0.3	0.3	0.4
Total Debt/OPBDIT (times)	5.2	7.4	7.1
Interest coverage (times)	1.2	1.0	1.3

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years:

		Current Rating (FY2019)				Chronology of Rating History for the Past 3 Years		
	Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date &Rating May 2018	Date & Rating in FY2018 -	Date & Rating in FY2017 February 2017	Date & Rating in FY2016 October 2015
1	Cash Credit	Long Term	43.50	-	**[ICRA]BBB- (negative)**	-	**[ICRA]BBB (stable)**	**[ICRA]BBB (stable)**
2	Non-fund-based limits	Short Term	21.26	-	**[ICRA]A3**	-	**[ICRA]A3+**	**[ICRA]A3+**
3	Unallocated	Long term	-	-	-		**[ICRA]BBB (stable)**	**[ICRA]BBB (stable)**

Complexity level of the rated instrument:

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the 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	Cash Credit	NA	NA	NA	43.50	[ICRA]BBB- (negative)
NA	Non-fund-based limits	NA	NA	-	21.26	[ICRA]A3

Source: Spacewood Furnishers Private Limited.

ANALYST CONTACTS

Subrata Ray
+91 22 6114 3408
subrata@icraindia.com

Suprio Banerjee
+91 22 6114 3443
supriob@icraindia.com

Tushar Bharambe
+91 22 6169 3350
tushar.bharambe@icraindia.com

Shashikant Raut
+91 020 66096 9915
shashikant.raut@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

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

Helpline for business queries:

+91-124-2866928 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

For more information, visit www.icra.in

ICRA Limited

Corporate Office
Building No. 8, 2nd Floor, Tower A; DLF Cyber City, Phase II; Gurgaon 122 002
Tel: +91 124 4545300
Email: info@icraindia.com
Website: www.icra.in

Registered Office
1105, Kailash Building, 11th Floor; 26 Kasturba Gandhi Marg; New Delhi 110001
Tel: +91 11 23357940-50

Branches

Mumbai	+ (91 22) 24331046/53/62/74/86/87
Chennai	+ (91 44) 2434 0043/9659/8080, 2433 0724/ 3293/3294,
Kolkata	+ (91 33) 2287 8839 /2287 6617/ 2283 1411/ 2280 0008,
Bangalore	+ (91 80) 2559 7401/4049
Ahmedabad	+ (91 79) 2658 4924/5049/2008
Hyderabad	+ (91 40) 2373 5061/7251
Pune	+ (91 20) 6606 9999