

July 04, 2019

## S.Mitul & Co.: Rating reaffirmed

### Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
<b>Fund-based - Short Term</b>			
PSC/EBRD	5.00	5.00	[ICRA]A4; Reaffirmed
Direct^	(5.00)	(5.00)	[ICRA]A4; Reaffirmed
PC/PCFC^	(1.50)	(1.50)	[ICRA]A4; Reaffirmed
PCFC (DDA /Collection Bill Backed)^	(5.00)	(5.00)	[ICRA]A4; Reaffirmed
Associate Bills^	(0.78)	(0.78)	[ICRA]A4; Reaffirmed
Unallocated Amount	5.00	5.00	[ICRA]A4; Reaffirmed
<b>Total</b>	<b>10.00</b>	<b>10.00</b>	

\*Instrument details are provided in Annexure 1

^Sublimit of PSC/EBRD

### Rationale

The rating remains constrained by the working capital-intensive nature of operations of S. Mitul & Co. (SMC), arising from its high inventory holding and stretched receivable cycle. ICRA, however, notes that a sizeable part of the working capital funding is met through SMC's own funds (partner's capital) and creditor funding in the business. The rating remains constrained by the firm's small scale of operations with fluctuating turnover and increased reliance on orders from the Group companies. This is attributable to the challenging operating environment in the cut and polished diamonds (CPD) industry, characterised by the persistent demand slowdown in the key export markets. Further, the rating remains constrained by the firm's susceptibility of profitability to volatility in rough diamond prices as well as foreign exchange fluctuation risks, as it significantly imports rough diamonds. However, the presence of a natural hedge (exports of polished diamonds) partly mitigates the forex risk. The rating is further constrained by the intense competition in the CPD business with the presence of both organised and unorganised players, and the risk of capital withdrawal inherent in partnership firms, which can have a material impact on the firm's credit quality.

The rating, however, continues to factor in the extensive experience of SMC's promoters in the CPD industry, the firm's established relationships with customers and sourcing arrangements with related parties, which ensure uninterrupted supply of rough diamonds.

### Outlook: Not applicable

### Key rating drivers

#### Credit strengths

**Extensive experience of promoters in diamond industry; support from professional management** - SMC benefits from the promoters' vast experience in the diamond industry, along with a professional management setup with an extensive experience in the CPD industry.

**Strong supplier network with rough diamonds sourced from related parties** - The firm has an established arrangement of sourcing from related parties, ensuring a steady supply of rough diamonds at competitive rates.

## Credit challenges

**Working capital intensive operations due to slow-moving inventory and elongated receivable cycle** - SMC's operations are working capital intensive in nature due to high inventory holding levels and liberal credit terms with customers (Group companies). Though the inventory levels moderated to 174 days in FY2019 from 477 days in FY2018 owing to higher offtake from the Group companies, the same remained high. The reduction in inventory levels contributed to the improvement in working capital intensity to 58% in FY2019 from 134% in FY2018; nevertheless, it remained high.

**Small scale of operations with top-line growth dependent on Group companies** - SMC shifted its focus from dealing in medium-to-high sized diamonds to small-to-medium sized diamonds due to an overall slowdown in demand in some key consuming markets. Further, its key customer profile mainly comprises Group companies/associates, which contributed to 95% of the total revenue share in FY2019 against 48% in FY2018. Though SMC's scale of operations remained small with a fluctuating trend, the operating income (OI) surged to Rs. 23.7 crore in FY2019 (estimated) from Rs. 13.4 crore in FY2018, following the increase in demand from the Group companies. Volumes sold witnessed a significant growth of 435% in FY2019, amid intense competition as well as declining realisations.

**Weak profitability inherent in low value-added nature of CPD business; susceptibility of margins to forex fluctuations and rough diamond prices** - The CPD industry is characterised by the persistent demand slowdown in the key export markets, putting pressure on sales volume and realisation, which resulted in weak profitability for the firm. With a major part of its purchases in the form of imports, its margins are further susceptible to exchange rate fluctuations. However, the risk is partially mitigated by a natural hedge through exports. SMC's operations also remain exposed to the volatility in rough diamond prices, affecting its pricing flexibility to a large extent.

**Inherent risk associated with partnership entities** - Due to its partnership constitution, the firm is exposed to the risk of capital withdrawal by the partners, which could impact its capital structure.

**Intense competition from organised and unorganised players, inherent to CPD industry** - SMC not only faces intense competition from dominant unorganised players, but also from few well-established, organised players, who are similar in scale and size, which exerts pricing pressures.

## Liquidity position

SMC does not have any repayment obligations in the next three years. The firm reported negative fund flow from operations and free cash flows in FY2018, due to high operating cost with corresponding decline in turnover and stretched inventory levels. However, higher inventory off-take due to increase in orders from Group companies, along with an undrawn line of credit of Rs. 4.77 crore as on March 31, 2019, is expected to ease the liquidity position in FY2019.

## Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	<a href="#">Corporate Credit Rating Methodology</a> <a href="#">Rating Methodology for Entities in the Indian Gems &amp; Jewellery Industry—Cut &amp; Polished Diamonds</a>
Parent/Group Support	Not applicable
Consolidation/Standalone	Standalone

## About the company

Established in 2011, S. Mitul & Co. started as a partnership firm, promoted by Mr. Mitul Jhaveri and Mr. Somil Jhaveri. SMC cuts and polishes diamonds of small to medium sizes, ranging from 0.001 pointer to 1 carat, on a job-work basis. Its office is at the Bandra Kurla Complex (BKC), Mumbai.

SMC's group companies - C.J. Exporters (rated [ICRA]A4+ in Oct 2018) and C.J. Jewellers Pvt. Ltd. (rated [ICRA]A4 in July 2019) are engaged in the businesses of cut and polished diamonds (CPDs) and jewellery manufacturing respectively. In addition, the Group has overseas associates who act as marketing and distribution agents

In FY2018, SMC reported a profit before tax of Rs. 0.2 crore on an OI of Rs. 13.4 crore, compared to a net profit before tax of Rs. 0.3 crore on an OI of Rs. 16.6 crore in the previous year. The firm has an estimated revenue of Rs. 23.7 crore in FY2019.

## Key financial indicators

	<b>FY2017 Audited</b>	<b>FY2018 Audited</b>
Operating Income (Rs. crore)	16.6	13.4
PBT (Rs. crore)	0.3	0.2
OPBDIT/ OI (%)	1.9%	1.1%
RoCE (%)	3.5%	2.2%
Total Debt/ TNW (times)	0.1	0.0
Total Debt/ OPBDIT (times)	6.1	0.7
Interest Coverage (times)	1.5	0.7
NWC/ OI (%)	82.8%	135.1%

**Status of non-cooperation with previous CRA: Not applicable**

**Any other information: None**

## Rating history for last three years

Current Rating (FY2020)					Chronology of Rating History for the past 3 years		
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating Jul 2019	Date & Rating in FY2019 Oct 2018	Date & Rating in FY2018 May 2017	Date & Rating in FY2017
1 PSC/EBRD	Short term	5.00		[ICRA]A4	[ICRA]A4	[ICRA]A4	-
2 Direct*	Short term	(5.00)		[ICRA]A4	[ICRA]A4	[ICRA]A4	-
3 PC/PCFC*	Short term	(1.50)		[ICRA]A4	[ICRA]A4	[ICRA]A4	-
4 PCFC (DDA /Collection Bill Backed)*	Short term	(5.00)		[ICRA]A4	[ICRA]A4	[ICRA]A4	-
5 Associate Bills*	Short term	(0.78)		[ICRA]A4	[ICRA]A4	[ICRA]A4	-
6 Unallocated	Short term	5.00		[ICRA]A4	[ICRA]A4	[ICRA]A4	-

\*Sub-limit of PSC/EBRD

## 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](http://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	PSC/EBRD	-	-		5.00	[ICRA]A4
NA	Direct*	-	-		(5.00)	[ICRA]A4
NA	PC/PCFC*				(1.50)	[ICRA]A4
NA	PCFC (DDA/Collection Bill Backed)*				(5.00)	[ICRA]A4
NA	Associate Bills*	-	-		(0.78)	[ICRA]A4
NA	Unallocated				5.00	[ICRA]A4

\*Sublimit of PSC/EBRD

Source: SMC

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

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