February 21, 2020

Khadim India Limited: Ratings downgraded to [ICRA]BBB+/ [ICRA]A2; Outlook revised to Negative; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based – Cash Credit	110.00	125.00	[ICRA]BBB+; Rating downgraded from [ICRA]A and outlook revised to Negative from Stable
Non-Fund based – Letter of Credit/ Bank Guarantee	38.00	0.00	-
Non-Fund based – Letter of Credit/ Bank Guarantee/ Derivative	0.00	41.50	[ICRA]A2; Rating downgraded from [ICRA]A1
Non-Fund based – Letter of Credit/ Bank Guarantee[1]	0.00	(17.00)	[ICRA]A2; Rating downgraded from [ICRA]A1
Fund based – Purchase Bill Discounting/ Short Term Loans	22.50	37.50	[ICRA]A2; Rating downgraded from [ICRA]A1
Total	**170.50**	**204.00**	

**Instrument details are provided in Annexure-1*
[1]Sublimit of Cash Credit

Rationale

The downward revision in the ratings and a change in the long-term rating outlook primarily considers the significant decline in profits and cash accruals of Khadim India Limited (KIL) in FY2019 and 9M FY2020 (unaudited) primarily on the back of a decline in the proportion of high-margin retail sales to total sales, and an increase in the overall cost of the company vis-a-vis its realisation. The revisions also consider an increase in the working capital intensity of business in FY2019 and H1 FY2020 primarily due to accumulation of GST receivable and an increase in the inventory level of the company.

Meanwhile, the ratings derive comfort from the long experience of the promoters and its established track record in the footwear industry for around four decades. ICRA also notes the company's strong market presence, and a pan-India network of 911 retail stores and 576 distributors (as on September 30, 2019) supply Khadim's products. However, it continues to remain exposed to high geographical concentration risk with ~65% of the revenues contributed by East India. The ratings also derive comfort from the diversified product portfolio of the company across multiple price points, catering to a wide customer base and various segments. The ratings also consider the conservative capital structure of the company despite an increase in the short-term borrowings in FY2019 and H1 FY2020 (unaudited).

The ratings, however, continue to be constrained by the highly fragmented industry structure, characterised by low value-additive nature of business and intense competition from a large number of players, which impacts margin. Besides, the overall profitability remains vulnerable to fluctuations in raw material prices.

The Negative outlook on the [ICRA]BBB+ rating reflects ICRA's opinion that low profits as well as cash accruals and high working capital intensity of business will continue to stretch the liquidity position of the company in the near term at least.

Key rating drivers and their description

Credit strengths

Established position of KIL in domestic market – KIL has been in the business of manufacturing footwear and accessories for around four decades and has an established track record in the footwear industry. The company has a pan-India network of 911 retail stores and 576 distributors (as on September 30, 2019), supplying Khadim's products. East India accounts for around 65% of its revenues, which exposes the company to high geographical concentration risk. However, its established presence in the market mitigates such risk to an extent. The company is also expanding to northern and western states and has also started selling its products online to reach a wider customer base.

Diversified product portfolio across multiple price points – KIL has a large product portfolio with various sub-brands at multiple price points, catering to the needs of a wide customer base. The company also caters to various segments – retail, distribution and institutional. The growth in the retail segment have remained subdued, however, the distribution and institutional sales have witnessed a steady increase, which led to a stable growth in the top line of the company over the past few years.

Conservative capital structure – The capital structure of the company remained conservative, as depicted by a gearing of 0.38 times and 0.50 times as on March 31, 2019 and September 30, 2019 (unaudited), respectively, on the back of a healthy net worth of the company. However, ICRA notes that an increase in the working capital requirements along with a decline in the cash accruals from the business resulted in an increase in short-term borrowings to Rs. 133.46 crore as on September 30, 2019 from Rs. 68.66 crore as on March 31, 2018.

Credit challenges

Significant decline in profits and cash accruals – The operating profit and cash accruals from the business witnessed a significant decline (YoY) in FY2019 and in 9M FY2020 (unaudited) mainly because of a decline in the proportion of (high-margin) retail sales to total sales. Further, the profitability of the company was adversely impacted due to an increase in the promotional and overall expenses vis-a-vis realisation. In 9M FY2020 (unaudited), the company reported a net loss of Rs. 8.61 crore against a top line of Rs. 613.65 crore. Given the weak demand scenario and an increase in overhead expenses, ICRA does not expect any major improvement in the same in the near term at least.

Increase in the working capital intensity of business – The working capital intensity of operations increased to 27% in FY2019 from 21% in FY2018 and continued to remain high at 27% in H1 FY2020 (unaudited) primarily due to an accumulation of GST receivable and an increase in the inventory level of the company. This resulted in a significant increase in the working capital requirement for the company, leading to negative cash flows from operations and a stretched liquidity position.

Fragmented and intensely competitive nature of the industry – The company faces intense competition from multiple branded footwear manufacturers as well as unorganised players, which limit its pricing flexibility and consequently, its ability to expand its operating margins.

Profitability remains susceptible to volatility in raw material prices – As footwear are raw material intensive operation, the profit margins remain susceptible to adverse fluctuations in the costs of raw materials. The company's ability to pass on the increased cost to the customers will remain a key determinant of the company's profitability, going forward.

Liquidity position: Stretched

High working capital requirements of the company resulted in high utilisation of its fund-based limits, as reflected by an average utilisation above 92% in the last 15 months. ICRA expects that the liquidity position of the company is likely to remain stretched on account of a decline in the cash accruals and an increase in the working capital intensity of operations, which in turn will restrict its financial flexibility to a large extent. However, absence of long-term debt service obligations would provide some cushion to the company's cash flows. As the company's business is expected to record a modest growth in the medium term, efficient management of working capital requirement would remain crucial, going forward.

Rating Sensitivities

Positive triggers – ICRA may revise KIL's long-term rating outlook if the company demonstrates a meaningful recovery in the margins, resulting in an improvement in cash accruals and liquidity position.

Negative triggers – Pressure on KIL's ratings may arise if there is any further weakening of profitability and/ or an increase in working capital intensity of operations.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Footwear Industry
Parent/Group Support	Not Applicable
Consolidation / Standalone	Ratings are based on the standalone financial statements of the company

About the company

Khadim's was founded in 1965, when Late S.P. Roy Burman acquired a single shoe store in Chitpur, Kolkata. Subsequently in 1981, the company was incorporated in the name of S. N. Footwear Industries Pvt. Ltd. Since then, it has grown from a single-shop entity to a company, having 911 retail outlets and 576 distributors for sale of footwear and accessories. In June 2005, the company's status was changed from a private limited company to a public limited company under the name, Khadim Chain Stores Limited. Further, in August 2005, the company's name was changed to Khadim India Limited (KIL). In November 2017, private equity investor, Reliance Alternative Investments Fund sold its stake through an IPO and the company got listed on the stock exchange.

Key financial indicators

	FY2018 (Audited)	FY2019 (Audited)	9M FY2019 (Unaudited)	9M FY2020 (Unaudited)
Operating Income (Rs. crore)	748.71	799.18	592.52	613.65
PAT (Rs. crore)	37.90	21.17	19.97	-11.37
OPBDIT/ OI (%)	10.49%	7.40%	8.04%	6.34%
RoCE (%)	22.53%	12.76%	-	-
Total Outside Liabilities/Tangible Net Worth (times)	0.82	0.91	-	-
Total Debt/OPBDIT (times)	0.87	1.85	-	-
Interest Coverage (times)	5.59	4.28	5.76	5.76
DSCR	3.56	3.80	-	-

Status of non-cooperation with previous CRA: Not Applicable

Any other information: None

Rating history for last three years

		Current Rating (FY2020)				Rating History for the Past 3 Years				
					Rating	FY2019		FY2018	FY2017	
	Instrument	Type	Amount Rated	Amount Outstanding	21-Feb-2020	28-Jan-2019	6-Aug-2018	-	15-Mar-2017	16-Aug-2016
1	Cash Credit	Long Term	125.00	-	[ICRA]BBB+ (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	-	[ICRA]A- (Stable)	[ICRA]BBB+ (Positive)
2	Letter of Credit/ Bank Guarantee/ Derivative	Short Term	41.50	-	[ICRA]A2	-	-	-	-	-
3	Letter of Credit/ Bank Guarantee[1]	Short Term	(17.00)	-	[ICRA]A2	-	-	-	-	-
4	Purchase Bill Discounting/ Short Term Loans	Short Term	37.50	-	[ICRA]A2	[ICRA]A1	[ICRA]A1	-	[ICRA]A2+	[ICRA]A2
5	Letter of Credit/ Bank Guarantee	Long Term	-	-	-	[ICRA]A (Stable)	[ICRA]A (Stable)	-	[ICRA]A- (Stable)	[ICRA]BBB+ (Positive)
6	Term Loan	Long Term	-	-	-	-	[ICRA]A- (Stable) withdrawn	-	[ICRA]A- (Stable)	[ICRA]BBB+ (Positive)

Amount in Rs. crore
[1]*Sublimit of Cash Credit*

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	-	-	-	125.00	[ICRA]BBB+ (Negative)
NA	Letter of Credit/ Bank Guarantee/ Derivative	-	-	-	41.50	[ICRA]A2
NA	Letter of Credit/ Bank Guarantee[1]	-	-	-	(17.00)	[ICRA]A2
NA	Purchase Bill Discounting/ Short Term Loans	-	-	-	37.50	[ICRA]A2

Source: Khadim India Limited
[1]*Sublimit of Cash Credit*

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

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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

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