

February 26, 2021

Bhartiya International Limited: Long-term rating downgraded to [ICRA]BBB and short-term rating reaffirmed; Outlook revised to Stable and rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – fund-based facilities	36.23	86.23	[ICRA]BBB(Stable); downgraded from [ICRA]BBB+(Negative), with revision in outlook
Short-term – non-fund-based facilities	157.45	157.45	[ICRA]A2; reaffirmed
Long-term/ Short-term – fund-based/non-fund based facilities	360.00	360.00	[ICRA]BBB(Stable)/[ICRA]A2; long-term rating downgraded with revision in outlook, short-term rating reaffirmed
Total	553.68	603.68	

*Instrument details are provided in Annexure-1

Rationale

The downgrade in long-term rating of Bhartiya International Limited (BIL) factors in a moderation in its credit profile owing to slower than expected pick-up in the export demand for leather apparel and accessories. As the pandemic impact still prevails in the key export markets, and global economic recovery is still in early stages, the apparel/retail sales (including leather and accessories) are yet to see a sustained improvement to pre-Covid levels. While revising the outlook on BIL's long-term rating to Negative, ICRA had earlier factored in a sharp contraction in demand in H1 FY2021, followed by a gradual recovery in performance during H2 FY2021, with revenues reaching pre-Covid levels by Q3 FY2021. Despite the sequential recovery reported after a steep contraction in Q1 FY2021, reinstatement of lockdowns in some of the key markets (particularly UK and the EU) towards the end of Q3 FY2021 has delayed the recovery, and resulted in continued uncertainty on orders and offtake for BIL. Given the sizeable inventory holding requirements of the business and a long lead time involved in inventory planning for the estimated order book, the company's inventory level remains high despite uncertainty on orders. Together with lower scale this year, this has translated into a further increase in working capital intensity as reflected by NWC/ OI to 99% in H1 FY2021, from 62% in H1 FY2020. In this context, access to additional lines of credit (including corporate loan of Rs. 50 crore as well as additional facilities being availed under the ECLGS¹ facility) have supported BIL's liquidity profile in the current fiscal, despite heightened challenges amid the pandemic. Additional debt is, however, also resulting in increased repayment obligations for BIL from FY2022 onwards, thus resulting in a moderation in its coverage metrics.

The ratings continue to draw comfort from BIL's strong operational profile characterised by its long and successful operating history of more than two decades, integrated nature of its operations across designing, manufacturing and marketing activities and strong positioning in the market as a leading exporter of leather garments in the country. Besides, its experienced promoters and a professional management team have facilitated the establishment of a large base of active and reputed clientele, providing it repeat business. The ratings, however, continue to be constrained by the company's high dependence on the leather sector as well as high client and geographical concentration risks. The leather sector remains exposed to industry risk arising from waning consumer preference for animal skins, as well as growing protests against their use. Being an export-oriented company, BIL is also exposed to foreign exchange risk. The risk is, however, partly mitigated by a natural hedge, given

¹ Emergency credit Line Guarantee Scheme announced by Reserve Bank of India, for providing guaranteed collateral free additional credit to companies, in the form of working capital term loan facility

its import requirements as well as its policy of entering into forward contracts for a part of the exposure, which has helped the company report steady profitability over the years.

The Stable outlook reflects ICRA's expectation that a sustained recovery in turnover together with steps taken by the company to control its costs will help it cushion the impact on profit margins and report adequate coverage metrics, despite moderation expected from the previously envisaged levels.

Key rating drivers and their description

Credit strengths

Extensive operating history in the leather apparel business, with an established track record of attracting repeat business from export markets - BIL is one of the largest exporters of leather apparel from India, with a long operating history of over two decades. Over the years, the company has established a strong customer base of reputed international entities such as All Saints, Esprit, Levis Strauss and Okaidi, which has been providing repeat business. Its ability to attract repeat business as well as new renowned customers, even during the pandemic year, reflects favourably on its operations.

Strong operational profile - BIL runs integrated operations in the leather business with in-house designing, tannery and manufacturing facilities. Further over the years, the company has focused on diversifying its operations across related product categories (such as accessories, textile apparels, PU leather products, finished leather and outerwear, among others) as well as customers and geographies (increasingly focusing on North American and Asian markets). This has helped the company reduce its geographical concentration to some extent, as reflected in EU's (including the UK) share in its consolidated revenues declining to an estimated ~54% in FY2020 from ~82% in FY2014 (on a comparable basis). Within EU, the company's customer base is diversified across markets.

Experienced promoter group, supported by professional management team – BIL's promoter, Mr. Snehideep Agarwal has over two decades of relevant experience in the leather product manufacturing and export business, which has helped the company establish a strong customer base over the years. The promoter group is actively involved in the operations of the company and is supported by a professional management team for heading various operational roles such as sales and marketing, designing, procurement and finance.

Credit challenges

Stretched operating cycle; entails high reliance on working capital borrowings- Given the integrated nature of operations, long operating cycle, multi-location manufacturing base, seasonality in sales and raw leather availability, as well as intense competition from other bulk buyers of leather in the international markets, the company needs to maintain a high raw material (leather) inventory to ensure smooth production throughout the year. In addition, its need to procure similar quality leather for large customised orders and stock them adequately for the next year's estimated order book, also keeps its inventory holding requirements high. The pandemic induced challenges have resulted in a further build-up in its inventory levels (amid sharp revenue degrowth in FY2021E), resulting in an increase in its GWC to over 420 days in FY2021E from 329 days in FY2020. ICRA notes that despite the interim spike in inventory levels, the risk of inventory obsolescence for raw material stocks remains low given the long shelf life of tanned leather. Besides, ICRA does not expect a stretch in receivables cycle for BIL, as it has managed to get access to factoring arrangements with some of its key buyers. Although BIL had been taking various steps to reduce the GWC, including increased focus on the finished leather segment to optimise inventory levels, a tangible improvement on account of this remains to be seen.

High dependence on debt, together with pressures on performance, to result in moderation in debt servicing indicators- An increase in working capital intensity resulted in an increase in debt outstanding in the books of the company to around Rs. 441 crore as on March 31, 2020 from Rs. 387 crore as on March 31, 2019. Despite lower turnover in the current fiscal, the dependence on debt is expected to remain high, although part of the short-term debt is expected to be replaced by long-term debt, providing a liquidity cushion. While ICRA expects the company's debt coverage metrics to remain adequate over the next two years (FY2021 and FY2022), these are likely to moderate vis-à-vis earlier expectations, as repayment obligations stand

increased owing to the incremental term debt being availed by the company to reduce working capital borrowings. Scaling up of operations, while maintaining/ improving profitability will remain crucial to maintain comfortable debt coverage metrics in the near to medium term, particularly given the sizeable repayment obligations from FY2023 onwards.

Continued high geographic and customer concentration risk lead to susceptibility of revenues to demand trends in key markets, intense competition from international suppliers and risk of changing preferences - Although the company's increased focus on Asian and North American markets is facilitating gradual diversification in its regional presence, dependence on key markets remains high with the EU, the US and the UK accounting for ~22%, ~23% and ~20% of its standalone revenues in FY2020. This exposes it to the risk from adverse regional development as well as change in demand trends in these markets. Further, BIL's top five customers account for more than ~50% of its standalone sales. BIL also remains exposed to industry risks such as intense competition from international suppliers, waning consumer preference for animal skins, as well as growing protests against their use.

Vulnerability of profitability to foreign exchange fluctuations and regulatory risks - Being an export-oriented entity, BIL remains exposed to currency risks on account of fluctuations in foreign currency movements. Though the forex risk is mitigated to some extent by its natural hedge from imports and the use of foreign currency in its working capital limits as well as the company's hedging policy for using of forward contracts, the same remains vulnerable to the management's discretion. Moreover, revenues and profitability remain susceptible to regulatory risks such as changes in duty structure and rate of export incentives, which could potentially impact the competitiveness of its products.

Liquidity position: Adequate

BIL's liquidity position in the current fiscal has been supported by a Rs. 50-crore corporate loan availed in Q1 FY2021 which also supported business continuity and turnaround, even while there were significant operational disruptions and heightened liquidity challenges owing to the pandemic. Thereafter, as operations ramped up, and business conditions improved sequentially, BIL's liquidity profile also improved. This is reflected by BIL's average WC utilisation (on a standalone basis) declining to ~89% in Q3 FY2021 over ~94% in H1 FY2021. As on January 31, 2021, BIL had a cushion of ~Rs. 67 crore in the form of undrawn limits and free cash/bank balances. Going forward, ICRA expects BIL's liquidity profile to remain adequate, with cash flows from operations remaining comfortable against the scheduled repayment obligations in FY2022 and its marginal capex requirements. Besides, access to additional lines of credit under the ECLGS, as well as free cash and bank balances are expected to provide further liquidity cushion.

Rating sensitivities

Positive factors – BIL's ratings could be upgraded if it demonstrates a sustained and tangible improvement in working capital intensity, which results in an improvement in its liquidity profile, viz., higher cushion available in working capital limits. Besides, a sustained growth in scale of operations along with an improvement in profitability and a reduced dependence on debt, resulting in improved debt servicing indicators, could be positive triggers. Specific credit metrics that could be considered for a rating upgrade include DSCR of more than 1.75 times, on a sustained basis.

Negative factors – Negative pressure on BIL's rating could arise if there is a deterioration in its liquidity profile owing to reasons including but not limited to, a further stretch in its working capital cycle, or a sustained pressure on demand and/or operating margins, which results in a higher than envisaged moderation in debt servicing indicators. Further, any sizeable debt-funded capex or investment undertaken by the company, which results in a deterioration in BIL's financial profile may also be a downgrade trigger.

The company also faces prepayment risk, given the possibility of debt acceleration upon the breach of rating linked covenants. Upon a failure to meet the covenant, if it is not able to get waivers from the lenders/ investors, or if the lenders/ investors do not provide adequate time to the company to arrange for alternative funding to pay-off the accelerated loans, the ratings would face a downward pressure.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Textiles Industry - Apparels Liquidity Analysis of Entities in the Non-Financial Sector
Parent/Group Support	None
Consolidation/Standalone	For arriving at the rating, ICRA has considered the consolidated financials of BIL. As on March 31, 2020, the company had 10 subsidiaries, which are all enlisted in Annexure-2 .

About the company

Initially incorporated as Bhartiya Galecha Industries Private Limited in January 1987, Bhartiya International Limited (renamed in July 1993) is a listed entity. It manufactures and exports leather garments and accessories (like wallets, hand bags, belts, etc). BIL is a recognised export house that derives its revenues mainly from the export of products to overseas markets like Spain, France, Austria, Italy, Switzerland, the US and Canada. The company's manufacturing facilities are located in Bengaluru (Karnataka), Chennai (Tamil Nadu) and Nellore (Andhra Pradesh). It is backward integrated with its own tannery facilities in Chennai. As part of the forward integration initiatives, the company has also established its own design house in Italy, whose manufacturing is done in India. Besides leather products, the company also trades in textile apparels for which designing, raw material procurement and marketing activities are done in-house, while production is outsourced to manufacturers in China and Bangladesh.

Key financial indicators (audited)

BIL Consolidated	FY2019	FY2020	9M FY2021 Prov.
Operating Income (Rs. crore)	753.4	720.7	405.7
PAT (Rs. crore)	19.0	24.7	4.4
OPBDIT/OI (%)	8.7%	8.8%	6.6%
PAT/OI (%)	2.5%	3.4%	-3.4%
Total Outside Liabilities/Tangible Net Worth (times)	1.3	1.6	NA
Total Debt/OPBDIT (times)	5.9	6.9	NA
Interest Coverage (times)	1.9	2.2	1.5

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

Source: BIL's financial statements

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Chronology of Rating History for the past 3 years						
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Jan 31, 2021 (Rs. crore)	Date & Rating in FY2021		Date & Rating in FY2020		Date & Rating in FY2019		Date & Rating in FY2018	
					Feb 26, 2021	May 26, 2020	Nov 29, 2019	Aug 31, 2018	Dec 22, 2017	Sep 13, 2017		
1	Fund-based facilities – Term Loans	LT	86.23	77.42	[ICRA]BBB (Stable)	[ICRA]BBB+ (Negative)	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)		
2	Non-fund-based facilities – Letter of Credit/ SBLC	LT	157.45	--	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A2	[ICRA]A1	[ICRA]A1		
3	Fund-based/Non-fund-based facilities	LT/ST	360.00	--	[ICRA]BBB (Stable)/ [ICRA]A2	[ICRA]BBB+ (Negative) / [ICRA]A2	[ICRA]BBB+ (Stable) / [ICRA]A2	[ICRA]BBB+ (Stable) / [ICRA]A2	[ICRA]A (Stable) / [ICRA]A1	[ICRA]A (Stable) / [ICRA]A1		

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	Term Loans	FY2019	-	FY2030	86.23	[ICRA]BBB(Stable)
NA	Short-term non-fund-based limits	-	-	-	157.45	[ICRA]A2
NA	Short-term/long-term fund-based working capital limits	-	-	-	360.00	[ICRA]BBB(Stable)/ [ICRA]A2

Source: Bhartiya International Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	BIL Ownership	Consolidation Approach
Bhartiya Global Marketing Ltd	100.00%	Full Consolidation
J & J Leather Enterprises Ltd	100.00%	Full Consolidation
Bhartiya International SEZ Ltd	88.95%	Limited Consolidation
Bhartiya Urban Infrastructure Ltd	100.00%	Full Consolidation
Bhartiya Fashion Retail Ltd	100.00%	Full Consolidation
Ultima SA, Switzerland	100.00%	Full Consolidation
Design Industry Ltd, Hong Kong	100.00%	Full Consolidation
Design Industry China Ltd	100.00%	Full Consolidation
Ultima Italia SRL	100.00%	Full Consolidation
World Fashion Retail Ltd, Mauritius	100.00%	Full Consolidation

Source: BIL's Annual Report

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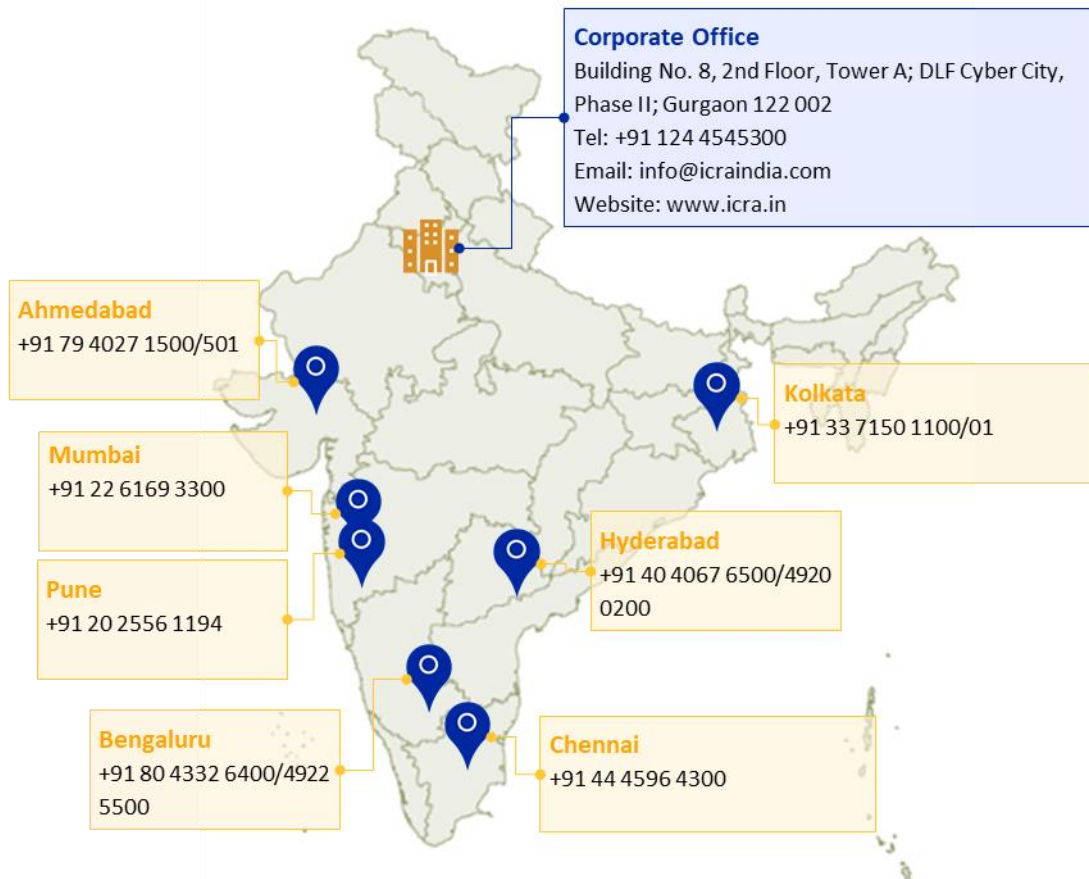
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