September 26, 2022

Kanani Industries Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term/Short-term: Fund-based	24.00	24.00	[ICRA]B+(Stable)/[ICRA]A4; reaffirmed
Long-term/Short-term: Unallocated	1.00	1.00	[ICRA]B+(Stable)/[ICRA]A4; reaffirmed
Total	**25.00**	**25.00**	

^Instrument details are provided in Annexure-1

Rationale

The ratings of Kanani Industries Limited (KIL) continue to remain constrained by its modest scale of operations, its stretched liquidity position and a moderate financial profile, characterised by its thin operating profit margin (OPM). The ratings also consider the company's high geographical, customer and supplier concentration risks (at the standalone level), vulnerability of its profitability to fluctuations in foreign exchange (forex) rates and prices of polished diamonds, along with intense competition in the industry, which restricts its pricing flexibility.

The ratings, however, favourably factor in the extensive experience of the promoters of more than three decades in the Indian gems and jewellery industry as well as KIL's comfortable capital structure with a gearing of 0.4 times and total outside liabilities vis-à-vis its tangible net worth of 1.4 times as on March 31, 2022 (at the consolidated level).

The Stable outlook on the [ICRA]B+ rating reflects that KIL will continue to benefit from the extensive experience of its promoters.

Key rating drivers and their description

Credit strengths

Extensive experience of the promoters in gems and jewellery industry – KIL's operations are managed by the Mumbai-based Kanani family members, which have vast experience of more than three decades in the gems and jewellery industry. This has enabled the company to establish its position in the market.

Comfortable capital structure – The company's capital structure has remained comfortable over the years with a gearing of 0.4 times and total outside liabilities vis-à-vis the tangible net worth of 1.4 times as on March 31, 2022 due to low levels of external debt at the consolidated level and modest net worth.

Credit challenges

High working capital intensity of operations at the standalone level due to stretched receivables – At the standalone level, KIL extends a credit period of 175-180 days to its customers and avails a credit period of 60 days from its suppliers. The working capital intensity (net working capital vis-à-vis operating income) stood at 50% as on March 31, 2022 due to high receivables. Going forward, faster realisation of receivables remains critical to manage the working capital.

Moderate financial profile due to thin OPM – The financial profile continues to remain moderate owing to its thin OPM. During the last two years, the company's revenues were adversely impacted due to the pandemic. In FY2022, despite the improvement in demand conditions in the gems and jewellery industry, KIL witnessed a YoY reduction in revenues by 7% to Rs. 291.9 crore due to mobility in restrictions in the Hong Kong region, its key export market. There has been some pick-up in revenues in Q1 FY2023, aided by easing of restrictions. The OPM, however, remained thin at 1% in FY2022 and 1.6% in Q1 FY2023 (partly aided by exchange gains) owing to limited value addition. Thin profit margins led to a subdued financial profile, characterised by total debt-to-operating profit ratio of 8.3 times as on March 31, 2022 and net cash accruals vis-à-vis the total debt (NCA/TD) of 8% in FY2022. Going forward, the financial profile is likely to remain moderate, given the thin operating margin.

Susceptibility of margins to volatility in raw material prices and forex rates; intense competition in the industry – KIL's profit margins remain vulnerable to fluctuations in prices of diamonds, which in turn affect sales realisations. Any adverse movement in the prices of diamonds could impact its profitability, considering its limited ability to pass on the price hike owing to intense competition in the industry. Given the sizeable exports, the company's profitability remains exposed to fluctuations in forex rates. However, a natural hedge in the form of import of polished diamond mitigates the forex risk to a large extent. The studded jewellery industry is highly fragmented and is characterised by intense competition. KIL faces stiff competition from dominant unorganised players and established organised players.

High geographical, customer and supplier concentration at the standalone level – Hong Kong is the primary destination for the company's exports at the standalone level. Further, the operations of the subsidiary are also restricted to Hong Kong. At the standalone level, the top-five customers account for 85% of the total revenues, which exposes it to customer concentration risks. KIL's supplier concentration also remains high as it procures polished diamonds from a single supplier based out of Hong Kong.

Liquidity position: Stretched

The liquidity position of KIL remains stretched due to its modest cash flows on the back of thin profit margin and stretched receivables cycle (at the standalone level). The average utilisation of the working capital limit stood at 87% during the 18-month period ended in July 2022. KIL does not have any term loan repayment obligations and there are no capital expenditure (capex) plans. The company's free cash and bank balances stood at a modest level of Rs. 0.7 crore as on March 31, 2022. Going forward, the company's ability to improve its liquidity position by registering a significant growth in revenues and profitability and efficiently manage its working capital cycle remain key rating sensitivities.

Rating sensitivities

Positive factors – The ratings may be upgraded if the company is able to improve its liquidity position and significantly increase its scale of operations and profitability on a sustained basis.

Negative factors – The ratings may be downgraded if the revenues and/or the company's profitability decline on a sustained basis, leading to a deterioration in the financial risk profile or if a stretch in the working capital cycle impacts its liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	[Corporate Credit Rating Methodology](#)
Parent/Group Support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of Kanani Industries Limited, which includes the financials of its wholly-owned subsidiary, KIL International Limited (based out of Hong Kong). The entities considered for consolidation are enlisted in Annexure 2.

About the company

KIL was originally incorporated as Shivlaxmi Mercantile Company Limited on March 22, 1983 and was listed on the Bombay Stock Exchange (BSE) on May 16, 1984. It began manufacturing diamond-studded silver jewellery from January 2008 with exports to Hong Kong. KIL had set up a 100% wholly-owned subsidiary, KIL International Limited, to increase its presence in the Hong Kong market, which began operations from July 4, 2011 by trading in diamond and jewellery.

Key financial indicators (Consolidated)

	FY2021	FY2022
Operating Income (Rs. crore)	312.5	291.9
PAT (Rs. crore)	0.4	1.8
OPBDIT/OI (%)	0.6%	1.0%
PAT/OI (%)	0.1%	0.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.4	1.4
Total Debt/OPBDIT (times)	11.8	8.3
Interest Coverage (times)	1.5	3.5

PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; Source: Company, ICRA Research; All ratios as per ICRA's calculations

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2023)				Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2022	Date & Rating in FY2021	Date & Rating in FY2020
					26-Sept-2022	09-Dec-2021	08-Oct-2020	16-Jan-2020
1	Fund-based	Long-term / short-term	24.00	-	[ICRA]B+ (Stable)/ [ICRA]A4	[ICRA]B+ (Stable)/ [ICRA]A4	[ICRA]B+ (Stable)/ [ICRA]A4	[ICRA]B+ (Stable)/ [ICRA]A4
2	Unallocated	Long-term / short-term	1.00	-	[ICRA]B+ (Stable)/ [ICRA]A4	[ICRA]B+ (Stable)/ [ICRA]A4	-	-

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term / short-term – Fund-based	Simple
Long-term / short-term: Unallocated	Not Applicable

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 analysing 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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs Crore)	Current Rating and Outlook
NA	Long-term/short-term: Fund-based	-	-	-	24.00	[ICRA]B+(Stable)/[ICRA]A4
NA	Long-term/short-term: Unallocated	-	-	-	1.00	[ICRA]B+(Stable)/[ICRA]A4

Source: Company

Annexure-2: List of entities considered for consolidated analysis

Sr.	Company Name	Consolidation Approach
1	Kanani Industries Limited	Full consolidation
2	KIL International Limited	Full consolidation

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