January 16, 2020

Kanani Industries Limited: Long-term rating of [ICRA]B+(Stable) assigned; short-term rating reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Short-term Fund-based	25.00	0.00	-
Long-term/ Short-term Fund-based	0.00	25.00	[ICRA]B+ (Stable); assigned, [ICRA]A4; reaffirmed
Total	**25.00**	**25.00**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of ratings continues to be constrained by the company's weak financial performance as depicted by its stagnant revenues and thin profitability over the last five fiscals. Intense competition in the jewellery industry further restricts Kanani Industries Limited's (KIL) pricing flexibility. The ratings also take into account the company's high working capital intensive nature of operations (as indicated by net working capital (NWC)/operating income (OI) of 49% in FY2019) emanating from stretched receivables, with debtor days at 208 in FY2019. ICRA also notes the increased supplier concentration risk with purchases being done entirely from a single supplier in FY2019. Further, ICRA considers the susceptibility of the company's profitability to adverse fluctuations in raw material prices and foreign exchange rates.

The rating, however, favourably factors in the extensive experience of the promoters with more than 35 years of experience in the gems and jewellery industry as well as KIL’s comfortable capital structure with a gearing of 0.73 time as on March 31, 2019.

Key rating drivers and their description

Credit strengths

Extensive experience of the management in gems and jewellery industry - KIL's operations are managed by the Mumbai-based Kanani family, who 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 with a gearing of 0.73 times as on March 31, 2019 - The company's capital structure remained comfortable over the years with gearing of 0.73 and 0.50 time as on March 31, 2019 and September 30, 2019, respectively. The favourable capital structure was supported by the company's modest net worth position with a tangible net worth of Rs. 42.51 crore as on September 30, 2019.

Credit challenges

Financial profile characterised by stagnant revenues and thin profitability - The company's OI has remained stagnant over the past few years with a marginal growth of 3.08% registered in its operating income in FY2019 to Rs 83.14 crore from Rs 80.65 crore in FY2018. The company’s financial profile is also characterised by thin profitability as reflected from modest operating margins at 2.31% in FY2019 and 2.22% in H1 FY2020 and subdued net profit margins (NPM) at 0.68% in FY2019 and 0.90% in H1 FY2020.

High working capital intensity due to stretched receivables - The company provides a credit period of 180 days to its customers and avails a credit period of 30 to 60 days from its suppliers. The company's debtor days remained high at 208 days in FY2019 and 232 days in H1 FY2020, translating into high working capital intensity with NWC/OI at 49% in FY2019 and 46% in H1 FY2020.

Supplier base remains concentrated in FY2019 - The company's supplier concentration risk remained high with the entire purchase of polished diamonds being made from a single supplier, based out of Hong Kong in FY2019. Nevertheless, KIL's established relationship with the supplier mitigates the risk to an extent.

Susceptibility of margins to volatility in raw material prices and forex rates - Polished diamonds are the primary raw materials for KIL. Thus, the company's profitability remains vulnerable to the variations in polished diamond prices. Further, KIL has an inherent forex fluctuation risk due to its export-dominated sales profile and the absence of hedging mechanisms.

Intense competition from unorganised and organised players - The studded jewellery industry is highly fragmented and characterised by intense competition. KIL not only faces stiff competition from dominant unorganised players, but also from well-established organised players.

Liquidity position: Stretched

KIL had a free cash balance of Rs. 0.13 crore as on September 30, 2019. The average working capital utilisation stood at 92% during the 15-month period ended September 2019. Although the company does not have any capex plans or term loans outstanding as on date, the liquidity position remains **stretched** because of its high working capital intensity, low cash accruals and limited cushion available in the form of undrawn working capital limits.

Rating sensitivities

Positive triggers - The ratings may be upgraded if the firm is able to register increase in scale of operations and profitability on a sustained basis coupled with efficient management of receivables cycle.

Negative triggers - The ratings may be downgraded if scale of operations and profitability continue to decline on a sustained basis and if there is any further stretch in receivables cycle.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology
Parent/Group Support	Not Applicable
Consolidation/Standalone	Not Applicable

About the company

KIL was originally incorporated as Shivlaxmi Mercantile Company Limited on March 22, 1983 and, started manufacturing diamond-studded silver jewellery from January 2008. Polished diamonds are the company's primary raw material, procured mainly through imports while silver is purchased from the domestic market. KIL's sales primarily include exports to Hong Kong. To further increase its presence in the Hong Kong market, KIL has set up a 100% wholly-owned subsidiary, KIL International Limited, which began operations from July 04, 2011 by trading in diamonds and jewellery.

The company reported a net profit of Rs. 0.57 crore on an OI of Rs. 83.14 crore in FY2019 and a net profit of Rs. 0.38 crore on an OI of Rs. 42.44 crore in H1 FY2020 (provisional).

Key financial indicators (audited)

	FY2018 (Audited)	FY2019 (Audited)	H1 FY2020 (Provisional)
Operating Income (Rs. crore)	80.65	83.14	42.44
PAT (Rs. crore)	0.40	0.57	0.38
OPBDIT/ OI (%)	2.21%	2.31%	2.22%
RoCE (%)	2.52%	2.31%	2.55%
Total Debt/ TNW (times)	0.70	0.73	0.50
Total Debt/ OPBDIT (times)	16.32	16.05	11.40
Interest Coverage (times)	1.49	2.02	2.24
NWC/ OI (%)	49%	49%	46%

OPBDITA: Operating Profit before Depreciation, Interest, Taxes and Amortisation; PAT: Profit after Tax; RoCE: Return on Capital Employed
Source: Financial statements of KIL and ICRA research

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					16-Jan-2020	27-Dec-2018	15-Nov-2017	21-Jun-2016
1	Fund-based	Short-Term	-	-	-	[ICRA]A4	[ICRA]A4	[ICRA]A4; suspended
2	Fund-based	Long-Term/ Short-Term	25.00	-	[ICRA]B+ (Stable)/ [ICRA]A4	-	-	-

Amount in Rs. crore

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	Foreign Bills Purchased/Discounted/Rupee Advance against Collected Bills	NA	NA	NA	25.00	[ICRA]B+ (Stable)/ [ICRA]A4

Source: KIL

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
NA	NA	NA

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About ICRA Limited:

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