February 26, 2020

Alapatt Jewellery (House of Alapatt): Rating revised to [ICRA]B+(Stable) from [ICRA]BB-(Stable)

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based - working capital limits	5.50	5.50	[ICRA]B+(Stable); Downgraded from [ICRA]BB-(Stable)
Total	**5.50**	**5.50**	

^Instrument details are provided in Annexure-1

Rationale

The rating revision factors in Alapatt Jewellery (HOA)'s stretched financial profile with decline in margins in FY2019 owing to shift in revenue mix towards pure gold jewellery, which commands lower margins, and high capital withdrawals which resulted in stretched coverage indicators. The rating revision also factors in expected 25-30% revenue de-growth in FY2020 due to subdued demand owing to high gold prices. The rating considers high geographical concentration risk due to HOA's single-showroom presence, the increasing competition from other renowned jewellery retailers in the Cochin region, and the cannibalisation of sales among other family-owned Group entities sharing the 'Alapatt' brand name. The rating also factors the stretched liquidity position owing to working capital-intensive nature of operations due to high inventory levels. The rating considers exposure of HOA's revenues and margins to regulatory risks, affecting the industry demand. The rating is also constrained by risks associated with partnership firms, including the risk of capital withdrawals, as witnessed in last two financial years. However, the rating positively factors in the extensive experience of the promoters in the jewellery retail business spanning over two decades with HOA's established brand name and prominent store location in Cochin (Kerala) driving the footfalls.

The stable outlook reflects ICRA's belief that HOA will continue to benefit from its established brand and prominent store location.

Key rating drivers and their description

Credit strengths

Established brand and prominent store location drives footfalls – HOA operates out of a ~15000-sq. ft. showroom in Cochin's MG Road. The extensive presence of the Jose Alapatt Group since 1988 (and that of brand Alapatt for over six decades) in the Cochin market enables the firm in driving footfalls.

Credit challenges

Small scale of operations, geographical concentration risk due to single-showroom presence – HOA's scale is small with a revenue of Rs.42.8 crore in FY2019. Moreover, revenues are expected to witness a de-growth of 25-30% in FY2020 due to subdued demand owing to sharp rise in gold prices. With a single showroom presence in cochin, HOA faces geographical concentration risk along with intense competition from other jewellery retails in the region.

Weak financial profile with thin margins and stretched coverage indicators – HOA has weak financial profile deteriorated with decline in margins in FY2019 owing to shift in revenue mix towards pure gold jewellery, which commands lower margins, and high capital withdrawals. The coverage indicators were stretched with an interest coverage ratio of 1.0 time, NCA/Total debt ratio of -12.2% in FY2019.

Cannibalisation of sales among family-owned entities sharing Alapatt brand – The larger Alapatt Group is operated by the six Alapatt brothers and all the entities share the same brand name, Alapatt. The brand name enjoys significant equity in the region due to its six-decade long presence. However, the ambiguity owing to similar names (of the now separately-held family entities) has led to cannibalisation of sales among the different showrooms in Cochin region.

High working capital intensity and stretched liquidity position – HOA's working capital intensity was high at 48.4% in FY2019 owing to its high inventory holding. As inherent to the trading nature of the jewellery business, the firm requires a large quantum of gold ornaments in its showrooms to cater to the requirements of the retail customers. High working capital intensity and thin profits resulted in stretched liquidity position.

Increasing regulatory intervention – The jewellery retail industry has been witnessing an increased regulatory intervention, over the last five years, which impacted the operating environment and consequently the performance of jewellers (both manufacturers and retailers). The measures such as mandatory PAN card disclosure requirement for purchases over Rs. 2.0 lakh, currency demonetisation, import duty hikes and inclusion of the jewellery sector under the Prevention of Money Laundering Act (albeit for brief period) had its effect on both demand and supply.

Risk associated with partnership nature of firm – HOA is exposed to risks associated with partnership firms including the risk of capital withdrawal, as witnessed in the last two fiscals.

Liquidity position: Stretched

HOA's liquidity position is **stretched** with low retained cash flows and limited buffer in working capital limits against a repayment obligation of Rs.0.35 crore.

Rating sensitivities

Positive triggers – ICRA may upgrade the firm's rating if it demonstrates a sustained improvement in its revenues and margins. Specific credit metrics that could lead to an upgrade include improving its interest coverage ratio over 1.5 times on a sustainable basis.

Negative triggers – Negative pressure on the firm's rating could arise if lower than expected accruals, or increase in working capital intensity, or higher than expected capital withdrawals impacts the liquidity position.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Gold Jewellery Retail Industry
Parent/Group Support	Not applicable
Consolidation / Standalone	The ratings are based on standalone financial statements of the company

About the company

HOA is a Cochin-based partnership firm established by Mr. Jose Alapatt in 1994. It is involved in gold and diamond jewellery retailing through its ~15,000-square feet retail showroom located in Cochin. The firm meets its gold requirement through traders and melting of old gold exchanged by the customers and outsourcing the jewellery manufacturing to local goldsmiths. HOA meets its diamond jewellery requirement through diamonds procured from merchants based out of Mumbai and Bangalore.

HOA has reported an operating income (OI) of Rs.42.8 crore and net losses of -Rs.0.4 crore in FY2019, as against an OI of Rs. 37.5 crore and net profit of Rs. 0.2 crore in FY2018.

Key financial indicators (Audited)

	FY 2018	FY2019
Operating Income (Rs. crore)	37.5	42.8
PAT (Rs. crore)	0.2	-0.4
OPBDIT/ OI (%)	5.1%	2.8%
RoCE (%)	5.9%	3.4%
Total Outside Liabilities/Tangible Net Worth (times)	0.8	0.8
Total Debt/ OPBDIT (times)	5.0	8.4
Interest coverage (times)	1.6	1.0
DSCR	1.5	1.0

Source: HOA

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

	Instrument	Current Rating (FY2020)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	Rating	FY2019	FY2018	FY2017
					26-Feb-2020	31-Oct-2018	22-Jan-2018	21-Nov-2016
1	Fund based - working capital limits	Long Term	5.50	-	[ICRA]B+ (Stable)	[ICRA]BB- (Stable)	[ICRA]BB- (Stable)	[ICRA]BB- (Stable)

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	Working Capital limit	-	-	-	5.50	[ICRA]B+(Stable)

Source: HOA

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About ICRA Limited:

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