March 22, 2021

Mirza International Limited: Ratings reaffirmed at [ICRA]A- (Negative)/ [ICRA]A2+

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund Based – Term Loan	27.45	24.68	[ICRA]A- (Negative); reaffirmed
Fund Based – Working Capital Facilities	436.10	420.0	[ICRA]A- (Negative); reaffirmed
Non-fund Based – Working Capital Facilities	16.45	35.05	[ICRA]A2+ ; reaffirmed
Long term-unallocated	-	0.27	[ICRA]A- (Negative); reaffirmed
Total	**480.0**	**480.0**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of the ratings factors in the company's established market position as one of the leading leather footwear exporters in India, its backward-integrated manufacturing operations that increase its cost competitiveness, along with its experienced promoter and management team. Moreover, the ratings derive comfort from the reduction in leverage to ~Rs. 258.0 crore as on January 31, 2021 from Rs. 388.8 crore as on March 31, 2020 due to the improved cash flow arising from the release of working capital particularly in Q3 FY2021, which coupled with unutilised working capital lines, led to healthy liquidity buffer available with the company. The ratings favourably factor in the established position of the company's Red Tape brand in the domestic market, along with diversified brand portfolio including brands such as Red Tape Athleisure, Bond Street, Mode, and Oaktrak. With rapid expansion in the domestic market, the share of domestic sales has risen to 65% in 9M FY2021 compared with 58% in FY020 and as low as 0% in FY2017. The launch of more brands, along with diversification in the product offerings, which includes sports shoes, casual shoes and apparel, has facilitated in the expansion and diversification of the clientele and product offerings. ICRA notes that MIL is gradually reducing the share of the wholesale/ multi-brand outlet (MBO) segment owing to the high working capital-intensive nature of the segment. The same, coupled with rise in focus on online and exclusive business outlets (EBOs) led to rise in the cumulative sales contribution of these two segments over the last three years. The company has also strengthened its domestic retail network via own stores as well the franchisee stores, with 273 EBOs, increased from 222 as of March 2020. The ratings are further strengthened by the large and diversified customer base in the export market, with repeat orders from reputed clients such as Steve Madden and Marks & Spencer, etc, reflecting positively on its track record. Further, MIL has a policy of 100% hedging of export receivables since FY2011, which insulates it from adverse movements in foreign exchange. Since FY2021, the company has started 100% hedging of imports as well, vis-à-vis 50% earlier, which reduces the forex exposure for the client.

However, the ratings remain constrained by the adverse impact of the Covid-19 pandemic, which has led to significant decline in revenues and accruals for the current year. The revenues for 9M FY2021 declined by 27% to Rs. 736.2 crore vis-à-vis Rs. 1,011.8 crore in 9M FY2020, while the operating profitability dipped to 10.6% in 9M FY2021 from 13.6% in 9M FY2020. ICRA notes that, despite the reduction in leverage, the lower accruals impacted the debt coverage indicators in YTD FY2021 as evidenced by the reduction in interest cover to 2.3 times in 9M FY2021 from 3.9 times in 9M FY2020. The ratings remain constrained by the continued tepid demand in the export market exacerbated by the lockdowns imposed in MIL's main market, United Kingdom (UK), to contain the spread of the pandemic including the new UK variant of Covid-19 virus. The ratings also factor in the low capacity utilisation of the tanneries due to muted demand for finished leather, leading to continued losses in leather segment since FY2019. The ratings continue to be constrained by high working capital intensity (46% in FY2020) owing to significant investments in inventory and receivables. The ratings also continue to be impacted by the intense competition in the leather footwear industry, geographical concentration in exports (particularly to UK), and vulnerability of profits to adverse movements in raw material prices and changes in rates of export incentives / duty remission rates, especially given that the company currently imports most of the non-leather footwear and garments, which are sold in the domestic market. ICRA has noted that MIL plans to construct a corporate office, and has a fresh sanctioned loan for the same.

ICRA has also noted the discontinuation of the Merchandise Exports from India Scheme (MEIS), under which MIL claimed Rs. 21.39 crore in FY2020. MEIS is to be replaced with Remission of Duties or Taxes on Export Products (RoDTEP). The rates and certain key points for RoDTEP are yet to be finalised, and the same would remain a monitorable. The profitability may be impacted in case of adverse changes in rates under the scheme.

The outlook on the long-term rating continues to be Negative, given the continuing pressure on debt protection indicators due to YoY decline in sales as well as accruals owing to the Covid-19 pandemic. Further, the prolonged tepid demand and lockdowns in the main export market had a sustained adverse impact on the segment and MIL's accruals. The pace and timing of pickup in demand would remain a key monitorable.

Key rating drivers and their description

Credit strengths

Experienced management – MIL has a long track record in domestic and global footwear market as the company was incorporated in 1979 as a private limited company. At present, the manufacturing capacity is spread across its five manufacturing units in Kanpur and Noida (Uttar Pradesh). Since FY2018, the company has been aggressively expanding in the domestic market with ramp up of its exclusive business outlets (EBOs), along with launch of brands for sale of shoes and garments. MIL has a customer base of more than 150 clients, including reputed clients such as Etablissements Cleon, Steve Madden, Marks & Spencer, etc.

Established position of MIL's Red Tape brand in domestic market – MIL's domestic sales include selling finished leather to its vendors. It also sells footwear and garments under the Red Tape brand through its own chain of stores across India, and through various retail stores such as Shoppers Stop, Metro Shoes, Lifestyle, Reliance Retail, Regal Shoe, Big Bazaar, etc (albeit the company is exiting this line of business), and through ecommerce sites like Amazon, Flipkart, etc. Additionally, MIL has launched brands like Red Tape Athleisure, Bond Street, and Mode in FY2018 and FY2019. Further, it has made additions in the product offerings to include sports shoes, casual shoes, and garments, thereby expanding its customer base.

Reduction in debt and healthy liquidity buffer available with MIL in YTD FY2021 – The company has witnessed reduction in leverage to ~Rs. 258.0 crore as on January 31, 2021 from Rs. 388.8 crore as on March 31, 2020 due to the improved cash flow arising from release of working capital particularly in Q3 FY2021. This, coupled with unutilised working capital lines, has led to healthy liquidity buffer available with the company.

Backward-integrated nature of operations with leather tanneries and complete footwear manufacturing facilities – MIL has backward-integrated operations with the presence of leather tanneries and complete footwear manufacturing facilities, most of which are concentrated near Kanpur. This ensures quality control and helps to capture the value addition across the supply chain, along with enabling the company to fulfil orders in a timely manner, while maintaining the quality of the products.

Credit challenges

Impact of Covid-19 pandemic – The ratings remain constrained due to the impact of Covid-19 pandemic, which led to a significant decline in revenues and accruals for the current year. The revenues for 9M FY2021 dipped by 27% to Rs. 736.2 crore vis-à-vis Rs. 1011.8 crore in 9M FY2020, while the operating profitability stood at 10.6% in 9M FY2021 from 13.6% in 9M FY2020. The same has also impacted the debt coverage indicators in YTD FY2021. Additionally, the continued tepid demand in the export market is exacerbated by the lockdowns imposed in MIL's main market, UK, to contain the spread of the new UK variant of Covid-19 virus. The timing of pickup in demand would remain a monitorable.

Moderation in debt protection indicators – While the total debt declined in 9M FY2021 due to contraction in the scale of operations, there has been moderation in the debt protection indicators during this period, given the reduction in accruals led by the adverse impact of Covid-19 and sustained tepid demand in the export market. MIL's interest cover decreased to 2.3 times in 9M FY2021 from 3.9 times in 9M FY2020 and 3.8 times in FY2019.

Elevated working capital intensity – MIL's working capital intensity remained elevated owing to significant investments in inventory and receivables. Additionally, owing to the elongated working capital cycle in the domestic market and rise in the proportion of sales from the same, it witnessed elevated working capital intensity with net working capital/operating income at 46% in FY2020. The same remained high in YTD FY2021 due to increased blockage given the Covid-19 pandemic.

Vulnerability of profits to adverse movements in raw material prices and export incentives – MIL is a manufacturer of leather and leather products. Its operations are dependent on procuring quality animal skins at competitive prices. As an exporter, MIL enjoys export incentives and interest subvention under various schemes run by the Government of India (GoI). There has been discontinuation of the MEIS, under which MIL claimed Rs. 21.39 crore in FY2020. MEIS is to be replaced with RoDTEP. The rates and certain key points for RoDTEP are yet to be finalised and the same would remain a monitorable. The profitability may be impacted in case of adverse changes in rates under the scheme. Additionally, any adverse change in raw material availability or prices, or in the GoI's regulations, may adversely affect the company's profitability.

Liquidity position: Adequate

The liquidity position is **adequate** as reflected by the unutilised portion of the working capital limits. MIL reported an average utilisation of 56% of the sanctioned working capital limits of Rs. 464.0 crore and 72% of the drawing power for the 15-month period that ended in January 2021. The company has limited long-term debt with Rs. 27.2 crore outstanding as on January 2021, of which ~Rs. 4.6 crore is due in Q4 FY2021 and Rs. 16.7 crore in FY2022. Further, it has buffer from unencumbered cash and equivalents of Rs. 14.7 crore as on December 31, 2020.

Rating sensitivities

Positive factors – The outlook on the long-term rating may be changed in case of sustained improvement in accruals and working capital intensity while maintaining the current leverage.

Negative factors – The ratings may be downgraded in case the interest coverage ratio falls below 3 times on a prolonged basis. Moreover, higher-than-expected debt-funded expansion, additional stress on its working capital cycle of the company, and slower than expected recovery from Covid-19 will be credit negatives.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in Footwear Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	Consolidated

About the company

Mirza International Limited (MIL) was incorporated in 1979 as a private limited company promoted by Mr. Irshad Mirza and his son Mr. Rashid Mirza. Initially, its operations were limited to manufacture and sale of processed leather through its own tannery unit in Kanpur. However, in 1990, MIL established an integrated shoe factory at Unnao, Kanpur. At present, the manufacturing capacity is spread across its five manufacturing units in Kanpur and Noida. Besides the above manufacturing capacities, the company outsources the production of footwear to other vendors. The promoters together hold a 70.19% stake in the company. It has expanded presence in the domestic market since FY2019, which contributed to 57% of the top line in FY2019. The various brands of MIL include Red Tape, Red Tape Athleisure, Bond Street, MODE, and Oaktrak.

Key financial indicators (audited)

Mirza International Limited (Consolidated)	FY2019	FY2020
Operating Income (Rs. crore)	1,151.7	1,261.2
PAT (Rs. crore)	48.8	47.7
OPBDIT/OI (%)	12.47%	13.62%
PAT/OI (%)	4.24%	3.78%
Total Outside Liabilities/Tangible Net Worth (times)	1.0	1.2
Total Debt/OPBDIT (times)	3.1	2.3
Interest Coverage (times)	4.2	3.8

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

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, 2020 (Rs. crore)	Date & Rating in	Date & Rating in FY2020	Date & Rating in FY2019			Date & Rating in FY2018
					Mar 22, 2021	Dec 13, 2019	Mar 5, 2019	Feb 25, 2019	Oct 8, 2018	Aug 30, 2017
1	Fund Based – Term Loan	Long-term	24.68	24.68	[ICRA]A-(Negative)	[ICRA]A-(Negative)	[ICRA]A-(Stable)	[ICRA]A-(Stable)	[ICRA]A (Negative)	[ICRA]A (Stable)
2	Fund Based – Working Capital Facilities	Long-term	420.0	--	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	-	[ICRA]A (Negative)	[ICRA]A (Stable)
3	Non-fund Based – Working Capital Facilities	Short term	35.05	--	[ICRA]A-(Negative)	[ICRA]A-(Negative)	[ICRA]A-(Stable)	[ICRA]A-(Stable)		
4	Long term-unallocated	Long-term	0.27	--	[ICRA]A-(Negative)	-	-	-	-	-

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 click here

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	Fund Based – Term Loan	FY 2018-19	NA	FY2022-23	24.68	[ICRA]A-(Negative)
NA	Fund Based – Working Capital Facilities	-	NA	-	420.0	[ICRA]A2+
NA	Non-fund Based – Working Capital Facilities	-	NA	-	35.05	[ICRA]A-(Negative)
NA	Long term-unallocated	-	NA	-	0.27	[ICRA]A-(Negative)

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	LTHL Ownership	Consolidation Approach
Mirza (H.K) Limited	100%%	Full Consolidation
Mirza Bangla Limited	99.9%	Full Consolidation

Source: *MIL annual report FY2020*

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About ICRA Limited:

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