Bhartiya International Limited

August 31, 2018

Summary of rated instruments

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – fund-based facilities	40.65	50.65	[ICRA]BBB+ (Stable); downgraded from [ICRA]A(Stable)
Long-term – non-fund-based facilities	0.50	-	-
Short-term – non-fund-based facilities	176.85	137.35	[ICRA]A2; downgraded from [ICRA]A1
Short term-fund based/ non-fund based	--	30.00	[ICRA]A2; downgraded from [ICRA]A1
Long-term/ Short-term – fund-based/non-fund based^	123.00	123.00	[ICRA]BBB+ (Stable)/[ICRA]A2; downgraded from [ICRA]A(Stable)/[ICRA]A1
Long-term/ Short-term – fund-based facilities^	293.20	293.20	[ICRA]BBB+ (Stable)/[ICRA]A2; downgraded from [ICRA]A(Stable)/[ICRA]A1
Total	**634.20**	**634.20**	

*Instrument details are provided in Annexure-1

^These limits are interchangeable on long term and short-term scale. In case the limits are availed as short-term facilities, the short-term rating will be applicable and in case the limit is availed as long-term facility, the long-term rating will be applicable. The overall utilisation by way of long-term and short-term facilities cannot exceed the stated amount.

Rating action

ICRA has downgraded the long-term and short-term ratings outstanding for the Rs. 634.20-crore[1] bank facilities of Bhartiya International Limited (BIL) to [ICRA]BBB+ (pronounced ICRA triple B plus)[2] and [ICRA]A2 (pronounced ICRA A two) respectively, from [ICRA]A (pronounced ICRA A) and [ICRA]A1 (pronounced ICRA A one), respectively. The outlook on the long-term rating continues to be Stable.

Rationale

The rating downgrade reflects deterioration in BIL's financial risk profile owing to a significant increase in its working capital intensity. Besides a consistent year-on-year increase in the inventory turnover period witnessed over the past few years, protracted receivable cycle as well as sizeable amount blocked towards GST refunds and export incentive receivable over the past one year, has created pressures on the company's liquidity. As a result, BIL’s working capital borrowings and reliance on stretched payments to creditors increased considerably in H2 FY2018 and Q1 FY2019, despite steady accrual generation and limited debt repayment obligations.

The ratings, however, continue to derive comfort from BIL’s adequate debt coverage metrics, its demonstrated ability of getting timely enhancements in working capital limits as well as regular equity infusions over the years which have kept the company’s capital structure and current ratio comfortable. Further, the ratings continue to factor in BIL’s strong operational profile characterised by its successful operating history spanning more than two decades, integrated nature of its operations, experienced promoters and a professional management team, which has facilitated establishment of a

[1] 100 lakh = 1 crore = 10 million

[2] For complete rating scale and definitions, please refer to ICRA's website www.icra.in or other ICRA Rating Publications

large base of active and reputed clientele. Despite industry-wide pressures on leather garment exports due to subdued demand in key export markets, BIL has been reporting steady growth in its revenues on a YoY basis (as reflected in a compounded annual growth rate or CAGR of ~14% during FY2014-FY2018) supported by its operational profile.

The ratings, however, continue to be constrained by the company's high dependence on the leather segment as well as high client and geographical concentration risk. Although it has been taking initiatives to diversify its product profile, customer base and geographical presence, which is evident from the improvement in its business profile over the years, BIL remains exposed to concentration risk. This is reflected in the fact that the leather-based products, the European region and the top five customers account for ~85%, ~62% and 45% of its revenues, respectively. Moreover, it continues to be exposed to industry risk arising from the growing protests against the use of animal skins in its leather segment. Being an export-oriented company, BIL is also exposed to foreign exchange risk. The risk is, however, partly mitigated from a natural hedge, given 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 stable profit margins over the years.

In ICRA's view, BIL's ability to sustain a healthy growth in its revenues, while improving its profitability as well as prudently managing its working capital cycle and to achieve higher product, client as well as geographical diversification, will remain the key rating sensitivities. Further, any increase in investment in the Group's real estate operations or future consolidation of the fashion and real estate business lines will entail a re-assessment of the credit profile.

Outlook: Stable

The Stable outlook reflects ICRA's expectation of a sustained growth in BIL's turnover in FY2019 driven by leather and textile segments, steady operating margins as well as improvement in working capital intensity from the prevailing levels, with the release of funds blocked in GST refunds. The outlook may be revised to Positive in case of a significant improvement in profitability and working capital cycle, which reduces dependence on debt and improves financial flexibility. The outlook may be revised to Negative in case of lower-than-expected operating profits, further stretch in working capital cycle and/ or sizeable debt-funded capital expenditure or investment undertaken by the company.

Key rating drivers

Credit strengths

Extensive operating history in the leather apparel business, with an established track record of getting repeat business in the export markets - BIL is one of the largest exporters of leather apparels from India, deriving its revenues mainly from the export of leather products (more than ~85% of its consolidated revenues) such as apparels, accessories and finished leather. It has a vast operating history of over two decades in the leather apparel business. Over the years, the company has established a strong customer base comprising reputed international entities such as All Saints, Esprit, Levis Strauss, Okaidi etc, which have been providing repeat business. Its ability to get repeat business, together with the addition of new renowned customers like Coach in the recent years, reflects favourably on its operations.

Integrated operations in the leather segment, with increasing focus on diversifying across product segments, customers and geographies - BIL has integrated operations in the leather segment with presence in in-house designing, tannery and manufacturing. Further over the years, the company has focused on diversifying its operations across related product categories (by adding products such as accessories, textile apparels, PU leather products, finished leather and outerwear etc.) as well as customers and geographies (increasingly focusing on the US and Asian markets). This has helped the company reduce its dependence on the European markets to some extent, as reflected in Europe's share in standalone revenues declining to ~62% in FY2018 from ~82% in FY2014.

Adequate debt coverage metrics supported by low term repayment obligations and range-bound profitability - With surplus capacities available in relation to its current scale of operations, the capex and hence long-term funding requirements of the company have remained low. As a result, with limited term repayment obligations and steady accruals supported by range-bound operating profitability, BIL's debt servicing indicators remain adequate, though modest, as reflected in a debt service coverage ratio (DSCR) of ~1.7 times and an interest cover of ~2.2 times in FY2018. With annual repayment obligations estimated to remain at ~Rs. 8-9 crore, the company's debt servicing indicators are likely to remain comfortable.

Credit challenges

High working capital intensity, with significant stretch in operating cycle witnessed over the past one year - Given the integrated nature of operations and 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, the requirement to procure similar quality leather for large customised orders and stock adequately for the next year's estimated order book, also keeps its inventory holding requirements high. There has been a consistent increase in BIL's inventory turnover period over the past few years, resulting in an increase in its NWC/ OI (Net Working Capital/ Operating Income) to ~64% in FY2018 from 42% in FY2014. This along with the increasing scale and moderate operating profitability resulted in modest/ negative cash flows from operations over the last five financial years. Even as the inventory turnover period continued to increase, a protraction in receivable cycle together with a sizeable amount blocked towards GST refunds and export incentives receivable, has stretched the operating cycle further during the past one year. Besides resulting in higher working capital borrowings, the company had to rely on stretched payments to creditors to tide over the liquidity pressures. Even though the insurance cover taken by BIL for receivables and letter of credit available against receivables from the new customers (added in FY2018) partially alleviates the credit risk, stretch in the working capital cycle has created pressures on its liquidity profile, corroborated by a consistently high utilisation of over 95% of the fund-based working capital limits over the past one year. ICRA notes that with the regularisation of GST refunds, the working capital situation is likely to ease from the prevailing levels. Nevertheless, the impact and extent of improvement in working capital cycle with the steps being taken by the company to efficiently manage the inventory levels, such as increasing focus on the finished leather segment, remains to be seen.

Susceptibility of revenues to demand trends in key buying regions, intense competition from international suppliers and risk of changing preferences - Although the company's increased focus on Asian and American markets is facilitating gradual diversification in regional presence, Europe still accounts for ~62% of BIL's revenues, thereby exposing it to the risk arising from adverse regional developments as well as change in demand trends in these markets. The risk is particularly higher, given that the top five customers account for ~45% of its consolidated sales. Besides, it remains exposed to industry risks such as intense competition from international suppliers as well as growing protests against the use of animal skins.

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 partly by natural hedge from imports and the use of foreign currency in its working capital limits as well as the company's hedging policy with respect to the usage 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, rate of export incentives etc, which could potentially impact the competitiveness of its products.

Analytical approach: For arriving at the ratings, ICRA has taken a consolidated view of the entity, comprising BIL, its ten subsidiaries[3] and two associates[4], owing to significant ownership, operational and financial inter linkages (BIL had a standby letter of credit amounting to Rs. 74.1 crore issued by its bankers in favour of its subsidiaries and corporate guarantee given to a bank for funding availed by its wholly-owned subsidiaries, amounting to Rs. 17 crore as on March 31, 2018). Most international subsidiaries primarily act as BIL's marketing arms in the international markets. Further, ICRA has applied its rating methodologies as indicated below.

Links to applicable criteria:

Corporate Credit Rating Methodology
Rating Methodology for Entities in the Indian Textiles Industry- Apparels

About the company:

Initially incorporated as Bhartiya Galecha Industries Private Limited in January 1987, Bhartiya International Limited or BIL (name changed 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 countries like Spain, France, Austria, Italy, Switzerland, the US and Canada. The company's manufacturing facilities are located in Bangalore (Karnataka), Chennai (Tamil Nadu) and Nellore (Andhra Pradesh). It is backward integrated with its own tannery facilities located in Chennai (Tamil Nadu). As a part of the forward integration initiatives, the company has also established its own design house in Italy, the manufacturing for which is done in India. It also trades in textile apparels for which designing, raw material procurement and marketing activities are done in-house, while manufacturing is being outsourced to manufacturers in China and Bangladesh at present.

Key financial indicators - Consolidated (Audited)

	FY2017	FY2018
Operating Income (Rs. crore)	640.1	710.4
PAT (Rs. crore)	18.6	18.6
OPBDIT/OI (%)	7.01%	7.09%
RoCE (%)	9.39%	8.02%
Total Debt/TNW (times)	0.99	0.97
Total Debt/OPBDIT (times)	5.93	7.19
Interest Coverage (times)	2.44	2.18

Source: SIL's Annual Reports/ Financial Statements, ICRA research
Note: OI: Operating Income; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation; ROCE: PBIT/Avg (Total Debt + Tangible Net-Worth + Deferred Tax Liability - Capital Work - in Progress)

Status of non-cooperation with previous CRA: None

[3]Bhartiya Global Marketing Ltd, J&J Leather Enterprises Ltd, Bhartiya International SEZ Ltd, Bhartiya Fashion Retail Ltd, Bhartiya Urban Infrastructure Ltd, Ultima S.A. Switzerland, World Fashion Trade Ltd (Mauritius), Ultima SRL (Italy), Design Industry Ltd (Hong Kong), and Design Industry China Ltd

[4]Tada Mega Leather Cluster Pvt Ltd (~50% stake held by BIL) and Bhartiya Urban Infrastructure & Land Development Co Pvt Ltd (Since merged with Bhartiya City Developers Pvt. Ltd.)

Any other information: The financials for FY2018 have been reported as per IndAS, and accordingly, previous year financials have been restated.

Rating history for last three years:

	Instrument	Current Rating (FY2019)				Chronology of Rating History for the past 3 years			
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating	Date & Rating in FY2018	Date & Rating in FY2017	Date & Rating in FY2016	
					Aug-2018	Dec-2017	Mar-2017	Feb-2016	Jun-2015
1	Fund-based facilities –Term Loans	LT	50.65	44.84^	[ICRA]BBB+ (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
2	Fund-based/ Non-fund-based facilities	ST	30.00	--	[ICRA]A2	-	-	-	-
3	Non-fund-based facilities –Letter of Credit/ SBLC	ST	137.35	--	[ICRA]A2	[ICRA]A1	[ICRA]A1	[ICRA]A1	[ICRA]A1
4	Fund-based/Non-fund-based facilities^^	ST/LT	123.00	--	[ICRA]BBB+ (Stable)/ [ICRA]A2	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1
5	Fund-based-Working Capital	ST/LT	293.20	--	[ICRA]BBB+ (Stable)/ [ICRA]A2	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1	[ICRA]A (Stable)/ [ICRA]A1
	Total		**634.20**						

Note: LT: Long Term; ST: Short Term
^Outstanding as on March 31, 2018
^^Includes Packing Credit/Buyers' Credit/Letter of Credit

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	Sept-2015	NA	FY2029	50.65	[ICRA]BBB+(Stable)
NA	Working capital fund-based limits	--	--	--	293.20	[ICRA]BBB+(Stable)/ [ICRA]A2
NA	Fund-based/ Non-fund-based working capital facilities	--	--	--	30.00	[ICRA]A2
NA	Non-fund-based working capital limits	--	--	--	137.35	[ICRA]A2
NA	Fund-based/ Non-fund-based limits	--	--	--	123.00	[ICRA]BBB+(Stable)/ [ICRA]A2

^Includes LC and Bank Guarantee limit

Source: Bhartiya International Limited

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About ICRA Limited:

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