

Mirza International Limited

March 05, 2019

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund based -Term Loan	19.50	19.50	[ICRA]A- (Stable); Rating outstanding
Fund based - Working Capital Facilities	350.5	410.0	[ICRA]A- (Stable); Rating assigned/ outstanding
Non-fund Based Limits	-	50.5	[ICRA]A2+; Assigned
Total	370.0	480.0	

*Instrument details are provided in Annexure-1

Rationale

The ratings take into account the sharp decline in Mirza International Limited's (MIL) profitability in Q3FY2019 owing to substantial discounts offered for clearing the inventory and for expanding the customer base in the domestic market, disturbance in tannery production due to restrictions and uncertainties on account of Kumbh mela, and rise in cost of imports due to the adverse movement in exchange rates. Further, the exports were under pressure in 9MFY2019 on account of weak demand from its customers in the European region, MIL's largest export destination. The ratings are also constrained by the continuing stress in the working capital cycle due to significant investment in receivables and inventory for aggressive expansion in the domestic market. This also led to consistently high utilisation of working capital limits, resulting in lower cushion in case of exigencies. The ratings continue to be constrained by the increase in leverage due to higher working capital borrowings and term loans taken for construction of a new warehouse and corporate office-cum-showroom. This, coupled with the sharp drop in profitability, led to deterioration in debt protection indicators. Intense competition in the leather footwear industry, and vulnerability of profits to adverse movements in raw material prices and changes in duty drawback rates also constrain the ratings.

However, the ratings derive strength from the healthy top-line growth to Rs 307.38 crore in Q3FY2019 from Rs. 253.99 crore in Q3FY2018 and to Rs. 865.15 crore in 9MFY2019 from Rs. 746.53 crore in 9MFY2018. The company's established market position as one of the leading leather footwear exporters in India, its integrated manufacturing operations which increase its cost competitiveness, and its experienced promoters and management team also support the rating. Moreover, the rating derives comfort from the higher market share in the domestic footwear market, mainly due to the increase in sales of products under the in-house Red Tape brand, along with launch of brands like Red Tape Athleisure, Bond Street, and Mode. Launch of more brands, along with addition in the product offerings to include sports shoes, casual shoes and apparel, has facilitated in the expansion and diversification of the clientele and product offerings. Sales under the brands Red Tape and Bond Street surged 43% in 9MFY2019, contributing to 16% YoY growth in the overall revenues. Further, MIL has a policy of 100% hedging of export receivables since FY2011, which insulates it from adverse movements in foreign exchange. However, this is offset to some extent as 50% of the company's imports remains unhedged.

Outlook: Stable

MIL continues to be one of the leading leather footwear companies. The company has limited term debt obligations with outstanding term loans of Rs 28.1 crore as of December 31, 2018. The outlook maybe revised to Negative or the rating may be downgraded in case of higher-than-expected debt-funded expansion or additional stress in the profitability and working capital cycle of the company. The outlook may be revised to Positive or the rating may be upgraded if the profitability, leverage, working capital intensity and utilisation of the working capital facilities improve.

Key rating drivers

Credit strengths

Experienced promoters with long track record in leather footwear business - MIL was incorporated in 1979 as a private limited company. Initially, its operations were limited to manufacture and sale of processed leather through its own tannery unit in Kanpur (Uttar Pradesh). However, in 1990, MIL established an integrated shoe factory at Unnao, Kanpur. Currently, the manufacturing capacity is spread across its five manufacturing units in Kanpur and Noida (Uttar Pradesh).

Established position in export footwear market with diversified and large customer base - MIL has a customer base of more than 200 clients, including reputed clients like Establishments Cleon, Debenhams Retail, Steve Madden, Marks & Spencer etc. MIL has been conducting business with these clients over the past many years and has bagged repeated orders from the same, which reflects positively on its track record.

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

Healthy growth in turnover- The topline of MIL increased to Rs. 307.38 crore in Q3FY2019 from Rs. 253.99 crore in Q3FY2018 and to Rs. 865.15 crore in 9MFY2019 from Rs. 746.53 crore in 9MFY2018. This was owing to its increased focus on the domestic market and the increase in retail stores to 195 as of December 2018, compared with 159 as of March 2018, with increase in the number of large format online shops (~2500-4000 sq ft), along with substantial discounts it offered to expand the customer base.

Credit challenges

Significant decline in profitability in Q3FY2019-The operating profitability of MIL almost halved to 9.7% in Q3FY2019 from 18.1% in Q3FY2018. Also, its net profitability margin dropped by two-third to 2.4% in Q3FY2019 from 8.2% in Q3FY2018 owing to the substantial discounts it offered to clear the inventory, disturbance in tannery due to Kumbh Mela, rise in cost of material imports due to adverse movement in foreign exchange rates, and weak consumer sentiment in Europe.

Debt-funded expansion in domestic market -Expansion in the domestic market (which has higher working cycle), investments to set up online shops and retail stores in FY2018 and 9MFY2019, and debt-funded construction of a warehouse led to an increase in total debt to Rs. 479.5 crore as of December 31, 2018 from Rs. 402.5 crore as of March 31, 2018.

Decline in available liquidity because of high utilisation of limits - Owing to the increased working capital intensity of operations, the utilisation of working capital limits remained elevated in the 12 months ending December 2018, reducing the liquidity cushion available with the company in case of exigencies. Further, MIL's working capital intensity remained elevated owing to significant investments in inventory and receivables.

Vulnerability of profits to adverse movements in exchange rate, raw material prices and export incentives- MIL is a manufacturer of leather and leather products and its operations are dependent on procuring quality animal skins at competitive prices. Also, as an exporter, MIL enjoys export incentives and interest subvention under various schemes run by the Government of India (GoI). Any adverse change in raw material availability/prices or in the GoI's regulations may impact the company's profitability.

Liquidity position

Continuous high utilisation of working capital limits over the 12-month period ended December 2018 has led to low buffer in case of exigencies. Nonetheless, the company has low term debt repayments, which will cushion its liquidity position to some extent, unless MIL undertakes additional debt-funded capex or requires debt for further investment in working capital. Further, MIL has unencumbered drawing power which can be utilised for increasing the working capital limits available from banks.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the 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, the operations of the company 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. Currently, the company has a manufacturing capacity of 64 lakh pairs per annum, which is spread across its five manufacturing units in Unnao, Kashipur & Greater Noida. Besides the above manufacturing capacities, the company outsources the production of footwear to other vendors, which exclusively cater to manufacturing footwear for Mirza International. The promoters together hold a 70.43% stake in the company.

In FY2018, the company reported a net profit of Rs. 78.42 crore on an operating income (OI) of Rs. 972.09 crore compared with a net profit of Rs. 71.74 crore on an OI of Rs. 935.68 crore in the previous year.

Key financial indicators (audited)

	FY2017	FY2018	9MFY2019 (Limited Review)
Operating Income (Rs. crore)	935.7	972.1	865.15
PAT (Rs. crore)	71.7	78.4	41.68
OPBDITA/ OI (%)	17.2%	17.9%	13.4%
RoCE (%)	15.7%	15.7%	-
Total Debt/TNW (times)	0.7	0.7	-
Total Debt/OPBDITA (times)	2.1	2.3	-
Interest Coverage (times)	6.2	7.0	4.6

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for last three years

Current Rating (FY2019)						Chronology of Rating History for the Past 3 Years			
Instrument	Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore)	Date & Rating March 2019	Date & Rating February 2019	Date & Rating October 2018	Date & Rating in	Date & Rating in	Date & Rating in
							FY2018 Aug, 2017	FY2017 Aug, 2016	FY2016 Jul, 2015
1 Fund Based Term Loan	Long Term	19.5	19.5	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
2 Fund based- Working Capital Facilities	Long Term	410.0	-	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A (Negative)	[ICRA]A (Stable)	[ICRA]A (Stable)	[ICRA]A (Stable)
3 Non-fund Based Limits	Short term	50.5	-	[ICRA]A2+	-	-	-	-	-

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 Loan 1	Feb 2018	NA	FY2022	19.5	[ICRA]A- (Stable)
NA	Fund based- Working Capital Facilities	NA	NA	-	410.0	[ICRA]A- (Stable)
NA	Non-fund Based Limits	NA	NA	-	50.5	[ICRA]A2+

Source: Mirza International Limited

Annexure-2: List of entities considered for consolidated analysis

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

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