November 29, 2019 (Revised)

Bhartiya International Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long-term – fund-based facilities	50.65	36.23	[ICRA]BBB+ (Stable); reaffirmed
Short-term – non-fund-based facilities	137.35	157.45	[ICRA]A2; reaffirmed
Short term-fund based/ non-fund based facilities	30.00	--	--
Long-term/ Short-term – fund-based/non-fund based facilities	123.00	360.00	[ICRA]BBB+ (Stable)/[ICRA]A2; reaffirmed
Long-term/ Short-term – fund-based facilities	293.20	--	--
Total	**634.20**	**553.68**	

**Instrument details are provided in Annexure-1*

Rationale

The rating reaffirmation factors the steady operational profile of Bhartiya International Limited (BIL) characterised by its long and successful operating history of more than two decades and integrated nature of its operations spanning across designing, manufacturing and marketing activities. Besides, presence of experienced promoters and a professional management team has facilitated establishment of a large base of active and reputed clientele, providing it repeat business. This is corroborated from the fact that BIL has been able to sustain growth in its revenues (compound annual growth rate of ~6% between FY2015 and FY2019) in recent years, while India's leather garment exports have been witnessing headwinds in the form of subdued demand trends in the key markets (mainly Europe), competition from other low-cost nations, as well as from alternative product segments (non-leather). Further, the rating continues to factor BIL's comfortable financial profile characterised by adequate debt coverage metrics and its demonstrated ability of getting timely enhancements in working capital limits to support its increasing scale of operations. ICRA notes that an increase in finance costs owing to the elevated debt levels, as well higher borrowing costs resulted in a moderation in its interest cover in FY2019. Nevertheless, the same remained adequate at ~1.9 times. Nonetheless, BIL's credit profile continues to be tempered by its working capital-intensive nature of operations, given the seasonality inherent in its key segment (viz. leather garments), a long operating cycle, integrated operations (leather tannery as well as garmenting) and a multi-location manufacturing base. While the improvements in working capital cycle and margins (operating margins improved from ~7.1% in FY2018 to ~8.7% in FY2019 and remained steady in H1 FY2020) over the past one-and-a-half years have facilitated an improvement in the cash flow generation, a tangible and sustained improvement on these fronts remains crucial for the company's credit profile.

Further, the rating continues to be constrained by the company's high dependence on the leather segment as well as high client and geographical concentration risks. The leather segment remains exposed to industry risk arising from waning consumer preference for animal skins, as well as growing protests against their use. Being an export-oriented company, BIL is also exposed to foreign exchange risk. The risk is, however, partly mitigated by 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 steady profitability over the years.

The Stable outlook reflects ICRA's expectation that a strong operational profile and steps being taken by the company to diversify its presence across segments will help it sustain a comfortable growth in its turnover and a gradual improvement in operating margins in the near-to-medium term. Besides, ICRA expects a further gradual contraction in BIL's gross operating cycle, to shore up its liquidity profile, resulting in reduced dependence on debt and helping maintain comfortable coverage metrics.

Key rating drivers and their description

Credit strengths

Extensive operating history in the leather apparel business, with an established track record of attracting repeat business from 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 standalone 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 has been providing repeat business. Its ability to get repeat business, together with the addition of new renowned customers like Coach, Chloé, Ralph Lauren and Reiss in the recent years, reflects favourably on its operations.

Strong operational profile - 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 consolidated revenues declining to an estimated ~60% in FY2019 from ~82% in FY2014.

Experienced promoter group, supported by professional management team – BIL's promoter Mr. Snehdeep Agarwal has over two decades of relevant experience in the leather product manufacturing and export business, which has helped the company establish a strong customer base over the years. The promoter group is actively involved in the operations of the company and is supported by a professional management team for heading various operational roles such as sales and marketing, designing, procurement and finance.

Credit challenges

Stretched operating cycle; entails high reliance on working capital borrowings and constrains debt coverage metrics - Given the integrated nature of operations, multi-location manufacturing base, seasonal availability of raw leather 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. In addition to high inventory levels, an increase in receivable turnover period resulted in a stretched operating cycle for BIL in FY2018. However, BIL reported a correction in the receivable turnover period in FY2019, resulting in reduction in gross working capital cycle (GWC) to 300 days in FY2019 from ~318 days in FY2018. In this context, ICRA notes that the risk of inventory obsolescence remains low given BIL's practice of procurement of inventory against estimated orders, and the long shelf life of tanned leather. Further, the company has been taking various steps to reduce the GWC, which include efficient management of inventory with increasing focus on the finished leather segment, and faster conversion of receivables (from non-recourse factoring arrangements). Nevertheless, a sustained and tangible improvement on this front remains crucial for its credit profile, as high working capital intensity, together with increasing scale of operations entails increased dependence on debt.

However, BIL's ability to get timely enhancements in working capital limits from the Bankers in the past, provides comfort on its financial flexibility. Further, 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 ~1.5 times and an interest cover of ~1.9 times in FY2019.

Continued high geographic and customer concentration risk lead to susceptibility of revenues to demand trends in key markets, 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 its regional presence, Europe still accounts for ~60% of BIL's revenues, exposing it to the risk from adverse regional development as well as change in demand trends in these markets. The risk is particularly higher, given that the top five customers account for more than ~40% of its consolidated sales. Besides, it remains exposed to industry risks such as intense competition from international suppliers, waning consumer preference for animal skins, as well as growing protests against their use.

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 by its 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.

Liquidity position: Adequate

Although high working capital intensity has resulted in consistently high utilisation of working capital limits (averaging at more than 95% in FY2019 and 7M FY2020), there is adequate cushion available in the form of unencumbered cash balances to meet any temporary mismatches. Going forward, BIL's cash accruals are expected to remain steady, and capex requirements marginal. The estimated cash profits are expected to remain comfortable against the repayment obligations, as well as margin for working capital.

Rating sensitivities

Positive triggers – ICRA could upgrade BIL's rating if the company demonstrates a sustained and tangible improvement in working capital intensity, which results in an improvement in its liquidity profile, viz., higher cushion available in working capital limits (fund-based limit utilisation averaging at less than 75% vis-à-vis drawing power, on a sustained basis). Besides, a significant improvement in profitability alongside a reduced dependence on debt, which results in improved debt servicing indicators, could be positive triggers. Specific credit metrics that could be considered for a rating upgrade include interest cover of more than 3.5 times, on a sustained basis.

Negative triggers – Negative pressure on BIL's rating could arise if a further stretch in working capital cycle results in deterioration in liquidity profile. Besides, decline in profitability, which results in a pressure on debt servicing indicators could also be a downgrade trigger. Specific credit metrics that could result in a rating downgrade include an interest cover of less than 2.0 times, on a sustained basis. Further, any sizeable debt-funded capex or investment undertaken by the company, which results in a deterioration of BIL's financial profile may also be downgrade triggers.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Textiles Industry - Apparels Liquidity Analysis of Entities in the Non-Financial Sector
Parent/Group Support	None
Consolidation/Standalone	For arriving at the rating, ICRA has considered the consolidated financials of BIL. As on March 31, 2019, the company had 10 subsidiaries, which are all enlisted in Annexure-2.

About the company

Initially incorporated as Bhartiya Galecha Industries Private Limited in January 1987, Bhartiya International Limited (renamed 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 overseas markets like Spain, France, Austria, Italy, Switzerland, the US and Canada. The company's manufacturing facilities are located in Bangalore, Chennai and Nellore (Andhra Pradesh). It is backward integrated with its own tannery facilities in Chennai. As 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. Besides leather products, the company also trades in textile apparels for which designing, raw material procurement and marketing activities are done in-house, while manufacturing is outsourced to manufacturers in China and Bangladesh.

Key financial indicators (audited)- Consolidated

	FY2018	FY2019	H1 FY2020*
Operating Income (Rs. crore)	710.5	753.4	417.7
PAT (Rs. crore)	18.6	19.0	21.1
OPBDIT/OI (%)	7.1%	8.7%	9.6%
RoCE (%)	8.0%	8.4%	9.6%
Total Outside Liabilities/Tangible Net Worth (times)	1.5	1.3	1.4
Total Debt/OPBDIT (times)	7.2	5.9	5.3
Interest Coverage (times)	2.2	1.9	3.2
DSCR	1.7	1.5	2.4

** Based on abridged financials reported by the company.*

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
					29-Nov-2019	31-Aug-2018	22-Dec-2017	13-Sep-2017	15-Mar-2017
1	Fund-based facilities – Term Loans	Long Term	36.23	36.23	[ICRA]BBB+ (Stable)	[ICRA]BBB+ (Stable)	[ICRA]A(Stable)	[ICRA]A(Stable)	[ICRA]A(Stable)
2	Non-fund-based facilities – Letter of Credit/ SBLC	Short Term	157.45	--	[ICRA]A2	[ICRA]A2	[ICRA]A1	[ICRA]A1	[ICRA]A1
3	Fund-based/Non-fund-based facilities	Long-term/ Short Term	360.00	--	[ICRA]BBB+ (Stable) / [ICRA]A2	[ICRA]BBB+ (Stable) / [ICRA]A2	[ICRA]A(Stable) / [ICRA]A1	[ICRA]A(Stable) / [ICRA]A1	[ICRA]A(Stable) / [ICRA]A1

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 click here

Annexure-1: Instrument details

ISIN	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loan 1	Mar-2019	9.8%		29.84	[ICRA]BBB+(Stable)
NA	Term Loan 2	May-2019	9.8%		6.39	[ICRA]BBB+(Stable)
NA	Short-term non-fund-based limits	Apr-2019	--	NA	157.45	[ICRA]A2
NA	Short-term/long-term fund-based working capital limits	Apr-2019	--	NA	360.00	[ICRA]BBB+(Stable)/ [ICRA]A2

Source: Bhartiya International Limited

Annexure-2: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
Bhartiya Global Marketing Ltd.	100.00%	Full Consolidation
J&J Leather Enterprises Ltd.	88.95%	Limited Consolidation
Bhartiya International SEZ Ltd.	100.00%	Full Consolidation
Bhartiya Urban Infrastructure Ltd.	100.00%	Full Consolidation
Bhartiya Fashion Retail Ltd.	100.00%	Full Consolidation
Ultima S. A	100.00%	Full Consolidation
Design Industry Ltd.	100.00%	Full Consolidation
Design Industry China Ltd.	100.00%	Full Consolidation
Ultima Italia SRL	100.00%	Full Consolidation
World Fashion Trade Ltd.	100.00%	Full Consolidation

Source: BIL's Annual Reports; ICRA research

Corrigendum:

Document dated November 29, 2019 has been corrected with revisions in PAT figures for FY2018 and FY2019 in Key Financial Indicators given on Page 4. PAT figures stand corrected to Rs. 18.6 crore and Rs 19.0 crore for FY2018 and FY2019 respectively, from Rs 19.0 crore and Rs 28.2 crore earlier.

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About ICRA Limited:

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