October 26, 2020

Kalyan Jewellers India Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previously Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Term Loans	253.00	85.00	[ICRA]A- (stable); reaffirmed
Long term / short term - Fund based	2,777.00	2,945.00	[ICRA]A- (stable) / [ICRA]A2+; reaffirmed
Short term - Fund based / Non-fund based (sub limits)	(1,465.00)	(1,390.00)	[ICRA]A2+; reaffirmed
Medium term – Fixed deposit	525.00	525.00	MA- (stable); reaffirmed
Total	**3,555.00**	**3,555.00**	

**Instrument details are provided in Annexure-1*

Rationale

The reaffirmation of ratings considers KJIL's diversified geographical presence across India, strong brand repute, favourable product mix with rising revenue share from the margin-accretive studded jewellery and strong hedging practices. The ratings also favourably consider the vast experience of promoters in jewellery retail industry and presence of private equity (PE) player, Highdell Investment Limited (Warburg Pincus Group) with ~30% shareholding in KJIL, providing comfort on systems and governance and long-term favourable demand for gold jewellery retail industry. The ratings also consider the working capital-intensive nature of business, high competition from organized and unorganized players, vulnerability of earnings to the volatility in gold prices and the inherent regulatory risks in the gems and jewellery industry.

KJIL's revenues grew by 5.4% YoY during FY2020 supported by higher realizations amidst rising gold prices while volumes declined due to subdued consumer sentiments and competition. The growth was also affected by the outbreak of Covid-19 pandemic in March 2020 leading to contraction in footfalls across its stores. KJIL's operating margins (adjusted for Ind AS 116) recovered to 6.5% in FY2020 following a contraction in preceding year; the margin expansion was supported by realization-led inventory gains and increased focus on high margin products. Despite improved earnings, KJIL's debt metrics are moderate with Adjusted Total outside liabilities to tangible networth of 1.6x and interest cover of 2.0x in FY2020 while ROCE levels remain low due to the slower ramp up of new stores launched in the recent years. The average working capital utilisation, as a percentage of sanctioned limits, was high at ~93% in the last one year. At consolidated level, the revenues grew by 3.4% in FY2020 with operating and net margins of 5.8% (adjusted for Ind AS 116) and 1.4% respectively. The adjusted Total outside liabilities to tangible networth was 2.1x and interest cover was 1.8x in FY2020.

ICRA expects KJIL's revenues in FY2021 to be negatively impacted by the Covid-19 pandemic-related shutdown of its stores in most part of Q1, covering the critical Akshaya Tritiya season. While the company has resumed operations in most of its stores, its sale volumes are expected to fall at a sharper rate (in line with industry) because of the lockdown measures in its key markets and reduction in discretionary spending by customers amidst elevated gold prices. To counter the impact on earnings, KJIL has undertaken cost reduction measures and intends to reduce its selling and rental expenses significantly during FY2021. While the upcoming festive season is likely support KJIL's performance in H2 FY2021, it will remain sensitive to the duration and breadth of Covid-19 before an eventual containment.

ICRA also notes that KJIL has filed a DRHP for public issue and intends to raise ~Rs. 1,750 crore (includes Rs. 1,000 crore through fresh issue of shares and Rs. 750 crore through offer for sale). From the proceeds, ~Rs. 750 crore (net of expenses) is expected to be deployed for working capital requirements and store expansion purposes and balance would be used for general corporate purposes.

The Stable outlook on the medium-term and long-term ratings reflects ICRA's opinion that KJIL will benefit from its business profile characterised by its diversified presence (both in terms of geography and products) and formal hedging practices. Nevertheless, improvement in earnings profile and debt metrics will be critical monitorables going forward.

Key rating drivers

Credit strengths

Extensive experience of promoters and presence of PE player - KJIL has been involved in gold jewellery retailing business for nearly three decades. The promoters' vast experience and commitment to business has supported KJIL in establishing a strong presence across the country. Further, the presence of Highdell Investment Limited (Warburg Pincus Group) provides additional comfort on systems and governance. The proceeds raised from PE was used for store expansions (both India and overseas), giving KJIL a diversified geographical presence, apart from improving its capital structure.

Established brand equity and improving geographic diversification - KJIL is one of the largest players in domestic jewellery retail business with 107 showrooms spread across 19 states and two union territories (as of June 2020). With the company diversifying geographically into non-south markets over last five years, the revenue share of the region increased to ~33% in FY2020. KJIL's product diversity also improved with increasing sale of margin-accretive studded and diamond jewellery across the non-South markets. The company also has 30 stores in Middle East countries. Rising share of studded jewellery sales (~25%) coupled with the improving realizations supported the expansion in the company's margins during FY2020.

Favourable long-term demand– While the elevated gold prices and Covid-19 effect on discretionary spend shall impact the near-term gold jewellery demand, the long-term demand outlook however remains favourable supported by cultural underpinnings, evolving lifestyle, growing disposable income, favourable demographic dividend and growing penetration of the organised sector. Increasing regulatory restrictions aimed towards greater transparency including mandatory hallmarking from June 2021, need for social distancing and higher compliance costs are likely to result in a churn in the unorganised segment, thus benefiting the organised players including KJIL.

Credit challenges

Covid-19 led lockdown to result in sharp revenue contraction in FY2021 - KJIL's outlets were shut from end March to May 2020, owing to the lockdown imposed due to the Covid-19 pandemic. This resulted in minimal sales during the period, which also includes the Akshaya Tritiya season (which accounts for ~4% of annual gold jewellery demand), in line with other players in the industry. Amidst the low discretionary spending by consumers due to the sharp increase in gold prices, weak macroeconomic sentiments, loss of business due to complete lockdown, and uncertain economic situation due to the still evolving pandemic, KJIL is likely to witness ~20-25% contraction in revenues in FY2021. Nevertheless, KJIL has undertaken several cost saving initiatives towards advertisement and rental payouts, which coupled with inventory gains due to sharp appreciation in gold prices, could support the operating profits. ICRA will continue to monitor for any larger-than-expected contraction in demand stemming from sustained lockdowns.

Intense competition limits pricing flexibility - Gold jewellery retail business is highly fragmented and competitive. The pricing flexibility of most of the players remain under pressure with subdued demand growth across the industry. This coupled with the limited value addition in the products keeps the operating margins lower. While KJIL is present in more regions than other retailers, it continues to face competition from other established players in the southern markets and faces competition from local players in the non-south markets. That said, the company has been able to establish itself as a pan-India player over the last few years and has steadily witnessed an improvement in the margin-accretive studded jewellery segment, supporting its overall margins.

Moderate debt metrics – While the geographical diversification has led to improvement in the company's revenues from the margin-accretive studded jewellery segment, the rapid expansion (addition of 34 stores in the last five years) has resulted in increased stocking requirements and slower inventory turnaround as compared to industry. Consequently, the company's debt metrics remain moderate with Adjusted Total outside liabilities to tangible networth of 1.6x and interest cover of 2.0x in FY2020 while ROCE levels remain low due to the slower than expected ramp up of new stores launched in the recent years. At consolidated level, the adjusted Total outside liabilities to tangible networth was 2.1x and interest cover was 1.8x in FY2020.

Exposure to regulatory risks and cautious lending environment - Increased regulatory intervention in jewellery industry in the recent years has impacted the demand and supply scenario in the industry. Measures like 20/80 restriction on imports, mandatory disclosure requirement for purchases above threshold limits, restrictions on jewellery saving schemes, imposition of excise duty and GST, increase in import duty, demonetisation etc. have affected demand and supply in the past. While increasing supervision and a cautious lending environment has restricted fund flows to the sector.

Liquidity position: Adequate

KJIL's liquidity is **adequate** with healthy cash flow from operations of ~Rs. 300 crore during FY2020 and free cash reserves of ~Rs. 125 crore as on March 31, 2020. Against the sanctioned working capital lines of Rs. 2,555 crore, the average utilisation remains high at over 93% during the 12-month period ended August 31, 2020. This apart, KJIL received additional working capital limits and Covid-19 loan in current year thus supporting its liquidity profile. KJIL has debt repayment obligation of Rs. 56 crore in FY2021 and ~Rs. 150 crore in FY2022 (including repayment of Covid-19 loan) and capex requirements of Rs. 50-100 crore over the next two years. ICRA expects KJIL to be able to meet its near-term commitments through internal accruals. The company continues to enjoy healthy financial flexibility with lenders.

Rating sensitivities

Positive triggers – Sustained growth in scale of operations and earnings accompanied by better inventory management leading to improvement in debt indicators shall trigger a rating upgrade. Specific credit metrics that could lead to an upgrade of ratings are Adj. TOL/TNW less than 1.4x and interest coverage more than 5.0x on a sustained basis.

Negative triggers – Negative pressure will emanate with sharp deterioration in earnings or rise in debt levels or weakening of liquidity profile which shall be negative triggers. Key credit metrics leading to such rating action shall include Adj. TOL / TNW exceeding 2.0x and/or interest coverage being less than 3.0x on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Gold Jewellery Retail Industry
Parent/Group Support	NA
Consolidation / Standalone	The rating is based on consolidated financial statements of the company.

About the company

Kalyan Jewellers India Limited (erstwhile Kalyan Jewellers India Private Limited), managed by Mr. T.S. Kalyanaraman and his sons, is an established jewellery retail player in southern India, with a presence in the market for more than two decades. In December 2013, KJIL had expanded its footprint into the Middle Eastern market with six showrooms. As of September, the company has 30 stores in those geographies. The stores in the Middle East are operated under the entities, Kalyan Jewellers LLC (UAE), Kalyan Jewellers WLL (Qatar), and Kalyan Jewellers for Golden Jewelleries WLL (Kuwait). Highdell Investment Limited (Warburg Pincus Group) currently holds a 30% stake in KJIL. As of March 2020, the company had 107 showrooms across India.

Key financial indicators

Standalone	FY2019	FY2020
Operating Income (Rs. crore)	7,454.3	7,859.3
PAT (Rs. crore)	44.9	156.4
OPBDITA/ OI (%)	4.7%	6.5%*
RoCE (%)	6.3%	12.0%
Total outside liabilities/ TNW (times)	1.8	2.1
Total Debt/ OPBDITA (times)	7.5	5.0*
Interest coverage (times)	1.4	2.0*
DSCR (times)	1.1	1.7

*Source: KJIL; *indicates adjusted for IND-AS 116*

Consolidated	FY2019	FY2020
Operating Income (Rs. crore)	9,765.7	10,100.9
PAT (Rs. crore)	17.7	142.3
OPBDITA/ OI (%)	4.6%	5.8%*
RoCE (%)	6.2%	11.0%
Total outside liabilities/ TNW (times)	2.5	2.8
Total Debt/ OPBDITA (times)	6.6	4.9*
Interest coverage (times)	1.3	1.8
DSCR (times)	1.1	1.6

*Source: KJIL; *indicates adjusted for IND-AS 116*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)				Rating History for the Past 3 Years		
		Type	Amount Rated	Amount Outstanding	FY2021 26-Oct-2020	FY2020 9-Sep-2019	FY2019 5-Nov-2018	FY2018 9-Oct-2017
1	Term Loans	Long term	85.0	81.2	[ICRA]A- (Stable)	[ICRA]A- (Stable)	[ICRA]A- (Positive)	[ICRA]A- (Positive)
2	Fund based limits	Long term / Short term	2,945.0	NA	[ICRA]A- (stable) / [ICRA]A2+	[ICRA]A- (stable) / [ICRA]A2+	[ICRA]A- (Positive) / [ICRA]A2+	[ICRA]A- (Positive) / [ICRA]A2+
3	Fund based / non-fund based (sub limits)	Short term	(1,390.0)	NA	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+	[ICRA]A2+
4	Fixed deposits	Medium term	525.0	NA	MA- (Stable)	MA- (Stable)	MA- (Positive)	MA- (Positive)

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	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Term Loans	FY2018	NA	FY2023	85.00	[ICRA]A- (Stable)
NA	Long term / short term – Fund based	NA	NA	-	2,945.00	[ICRA]A- (Stable) / [ICRA]A2+
NA	Short term fund based / non-fund based (sub limits)	NA	NA	-	(1,390.00)	[ICRA]A2+
NA	Medium term – Fixed deposit	NA	NA	-	525.00	MA- (Stable)

Source: KJIL

Annexure-2: List of entities considered for consolidation (as of 31.03.2020)

Company name	Ownership	Consolidation Approach
Subsidiaries		
Kalyan Jewellers FZE	100%	Full consolidation
Kalyan Jewellers Inc.	100%	Full consolidation
Enovate Lifestyles P Limited	77%	Full consolidation

Source: KJIL

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About ICRA Limited:

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