SHREE GANESH JEWELLERS LIMITED

Rating

Facilities	Amount (Rs. crore)	Rating[1]	Remarks
Long-term Bank Facilities	27.64	CARE BB	Assigned

Rating Rationale

The rating is constrained by modest scale of operations with geographical concentration risk, high volatility in income and profitability margins, stretched working capital cycle, moderately high gearing ratio and significant exposure in group companies by way of corporate guarantee and investments. The rating also takes into account competition from players in the organized and the unorganized sector and vulnerability of margins to gold price fluctuation. The rating, however, favorably factors in the experience of the promoters, long track record of operations and established brand image in Ludhiana market.

Going forward, SGJL's ability to effectively manage its working capital requirement and improve its profitability and leverage ratios would remain the key rating sensitivity.

Background

SGJL was incorporated in year 1997 with the purpose of carrying out business of manufacturing and trading of gold jewellery, diamond/precious stones, gold bars/coins etc. The company has been promoted by Deepak Fasteners Ltd (DFL) and Mr Kailash Chander Kalra, Mr Sanjeev Kalra and Mr Deepak Kalra. DFL holds 49.75% of total equity in SGJL and is engaged in manufacturing and export of fasteners.

Credit Risk Assessment

Experienced promoters and long operational track record

SGJL is running a retail store in the name of 'Ganpati Jewellers' in Ludhiana for more than a decade. All the directors in the company have vast experience in varied fields. The directors are also running other companies like 'DFL' which is engaged in manufacturing and export of fasteners since the year 1990 and 'Deepak Fibres Ltd' which is engaged in manufacturing/trading of clothes/fabrication clothes since 1997. In 1997, the directors of DFL decided to diversify from their main line of business of manufacturing of fasteners, and entered into jewellery business. Over a span of almost 15 years, the directors managed to establish a strong brand image of SGJL in Ludhiana market. The total income had increased from Rs.40.61 crore in FY08 (refers to the period April 1 to March 31) to Rs.177.21 crore in FY10.

Modest scale of operations with geographical concentration risk

SGJL is engaged in the manufacturing and retailing of gold and diamond-studded jewellery, precious stones etc. SGJL has a very small manufacturing unit located at Ludhiana where the company only manufactures bangles and does casting work. For other work related to making of jewellery, the company gets it produced through contract manufacturers. Apart from selling jewellery, SGJL is also into trading of gold bars/coins which it purchases from traders in cities like Mumbai, Jaipur, Surat and Ahmedabad. Since the operations are highly concentrated to Ludhiana market, it substantially increases the business risk of SGJL and limits its scale of operations too.

High volatility in income and profitability margins

The income and profitability margins (PBILDT and PAT margin) of SGJL had registered a fluctuating trend in the last three years (FY09-FY11). The same was mainly because of fluctuating income from trading business related to sales of gold bars. In FY11, the trading business contributed Rs.70.39 cr i.e almost 62% to the total sales of the company as compared to Rs.139.62 cr i.e 80% to the total sales in FY10. The increased trading operations of gold bars resulted in increase of approximately 140% in total income in FY10. Further, the profitability margins in the last three years had been fluctuating mainly on account of volatility in trading income of gold bars which are generally traded at lower margins than jewellery.

High gearing and significant exposure in group companies by way of corporate guarantee and investments

The overall gearing ratio of SGJL had been continuously deteriorating since FY09 end. The same was mainly because of higher utilization of working capital bank borrowings owing to high inventory requirement. Further, the company had extended

[1] *Complete definition of the ratings assigned are available at www.careratings.com and other CARE publications*

corporate guarantee of Rs.289.70 crore to various banks for loans availed by DFL and has also made an investment to the extent of Rs.10.66 crore in various group companies. The adjusted gearing on considering the above works out to be high at 24.56x as on March 31, 2011. These huge exposures in group companies are likely to have an adverse impact on the credit profile of SGJL in case of any guarantee invocation or weak operational performance of the group companies. Further, though there are cross corporate guarantees among these companies however SGJL's risk increases in the light of the fact that its operations are modest as well as concentrated in nature.

Working capital intensive operations

Being in retail business, the company has to maintain high levels of inventory of 100-120 days both in the form of gold bars and coins and also as finished good stock at its outlet. The same leads to working capital intensive operations. The maximum working capital utilization in the last 12 months ending August 2011 was at 96%. The creditor days of SGJL are low as it purchases gold from Bank of Nova Scotia mostly against cash. Further, since the company sells gold bars and jewellery against cash, the debtor's also were low.

Vulnerability of margins to gold price fluctuations

The prices of gold have experienced high volatility in the past one year. Therefore, any adverse change in prices of the same is likely to have a significant impact on SGJL's margins. However, the company tries to somewhat mitigate this risk by adopting inventory replenishment policy (it purchases the same quantity of gold as sold at the same day rate).

Competition from players in organized and unorganized sector

The Indian gems and jewellery industry is highly fragmented as majority of the market share is spread across a large number of unorganized players. Currently, the organised retail players in the jewellery space have only 5-7% share of the total jewellery market, but this is expected to increase to more than 10% in the near future. Increasing prices of gold and aggressive strategy of the modern retail players to increase their market share would further intensify the competition in the industry. Thus, increasing competition and high volatility in the gold prices would have an additional downside pressure on the profitability margins of jewellery companies like SGJL.

Industry outlook

The growth in the domestic G&J sector in India is expected to be driven mainly by higher disposable income, rising young population, higher number of working women and conscious marketing efforts of companies with greater focus on branding and organised retail. However, record high gold prices and high inflation may act as demand dampeners for G&J products - being a discretionary product. Further, because of the highly fragmented nature of the jewellery industry in India along with the share of unorganised segment being close to 95%, margins are expected to remain at modest levels.

Going forward, larger players with strong sourcing relationships for raw materials, those with geographically diversified clientele, with higher value addition and a more conservative forex/liquidity management policy, are likely to exhibit more stable credit profiles.

Prospects

The prospects of SGJL seem somewhat positive on account of its established brand image and marketing network in Ludhiana. However, considering the fluctuations in the gold prices, rising interest rates and increasing competition in the industry, the profitability margins might remain under pressure in the short to medium term. Further, the ability of SGJL to sustain profitable operations amidst strong competition from both organized and unorganized players would remain the key rating consideration.

Financial Performance

(Rs. crore)

For the period ended/ as on March 31	2009	2010	2011
	(12m, A)	(12m, A)	(12m, A)
Working Results			
Net Sales	74.02	177.21	114.13
Total Operating income	74.02	177.21	114.13
PBILDT	4.11	5.45	7.79
Interest	2.34	2.66	3.49

For the period ended/ as on March 31	2009	2010	2011
	(12m, A)	(12m, A)	(12m, A)
Depreciation	0.21	0.18	0.31
PBT	1.56	2.61	4.00
PAT (after deferred tax)	1.01	1.70	2.58
Gross Cash Accruals	1.21	1.88	2.88
Financial Position			
Equity capital	5.72	5.72	5.72
Net worth	8.86	10.54	13.14
Total capital employed	26.43	33.73	46.10
Key Ratios			
Growth			
Growth in Total income (%)	82.27	139.42	-35.60
Growth in PAT (after D.Tax) (%)	80.00	68.63	51.65
Profitability			
PBILDT/Total Op. income (%)	5.56	3.08	6.83
PAT (after deferred tax)/ Total income (%)	1.36	0.96	2.26
ROCE (%)	16.26	17.52	18.75
Solvency			
Long Term Debt Equity ratio (times)	0.46	0.38	0.63
Overall gearing ratio(times)	1.98	2.20	2.51
Interest coverage(times)	1.76	2.05	2.24
Term debt/GCA(years)	3.33	2.15	2.88
Total Debt/GCA(years)	14.48	12.34	11.43
Liquidity			
Current ratio(times)	1.18	1.17	1.26
Quick ratio(times)	0.09	0.21	0.06
Turnover			
Average collection period (days)	2	2	3
Average creditors (days)	31	13	15
Average inventory (days)	113	54	112
Operating cycle (days)	84	43	100

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