Arvind Fashions Limited

March 14, 2022

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	52.08	**CARE A-; Stable (Single A Minus; Outlook: Stable)**	**Reaffirmed; Outlook revised from Negative to Stable**
Long Term / Short Term Bank Facilities	145.00	**CARE A-; Stable/ CARE A2+ (Single A Minus; Outlook: Stable/ A Two Plus)**	**Reaffirmed; Outlook revised from Negative to Stable**
Short Term Bank Facilities	17.50	**CARE A2+ (A Two Plus)**	**Reaffirmed**
Total Bank Facilities	**214.58 (Rupees Two hundred fourteen crore and fifty-eight lakh only)**		

Details of facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Arvind Fashions Limited (AFL) continue to derive strength from AFL being part of the Ahmedabad based 'Arvind Lalbhai' group which has a track record of over a decade in the apparel brands and retail business, AFL's strong brand portfolio of owned and licensed international brands, its pan-India retail presence across multiple sales channel and diversified revenue mix; albeit concentrated towards men's wear. The ratings also favourably factor equity/non-debt fund infusion during FY21 (refers to the period April 01 to March 31) and 9MFY22, the proceeds from which have been utilized for funding of its losses as well as towards reduction of its consolidated debt and creditors; and shoring up its liquidity. Further, the ratings also take cognizance of expectation of improvement in profitability and return on capital employed (ROCE) post discontinuation of operations of most of its loss-incurring apparel brands along with benefit of operating leverage and saving in interest and finance cost. Furthermore, the latest round of equity/non-debt fund infusion during H1FY22 has enabled AFL to create adequate liquidity cushion as a safeguard against intermittent disruptions caused by various waves of the Covid-19 pandemic such as the one caused by the Omicron variant in January 2022 which may have an impact on its performance in Q4FY22 to an extent.

The ratings are, however, constrained on account of sizable net losses incurred by AFL during FY20, FY21 and H1FY22 due to losses from discontinued operations apart from adverse impact of Covid-19 on continuing operations whereby the losses have remained higher than envisaged; albeit funded through equity/ non-debt fund infusion. AFL's modest profitability margins and return indicators compared to its peers and its presence in a highly competitive fashion retail industry which is vulnerable to changes in fashion trends/consumer preferences and economic cycles further constrain its ratings.

Outlook: Stable

The revision in the outlook on the long-term rating of AFL from 'Negative' to 'Stable' reflects recovery in its operational performance during Q3FY22 and expectation of continued improved performance on y-o-y basis in the medium term. The improvement in operational performance was driven by growing online sales along with improving footfalls in stores supported by festive demand. With significant jump in sales and discontinuation of operations of loss-incurring brands and benefits of operating leverage, AFL achieved PBILDT margin of 10.40% in Q3FY22 and registered a net profit of Rs.18 crore after reporting net losses for past 10 quarters till Q2FY22. Its debt coverage indicators also improved during Q3FY22 on the back of improvement in its operational performance as well as due to significant reduction in debt level.

Rating Sensitivities

Positive Factors – Factors that could lead to positive rating action/upgrade:

- Significant improvement in its PBILDT margins to more than 14% and ROCE of more than 18% on a sustained basis
- Sustained improvement in its total debt to PBILDT below 4 times
- Gross working capital cycle improving to around 180 days on sustained basis along with company maintaining adequate liquidity cushion

Negative Factors – Factors that could lead to negative rating action/downgrade:

- Its profitability margins, debt coverage indicators and ROCE remaining under sustained pressure going forward even after the discontinuation of its loss-incurring apparel brands
- Any severe impact on the fashion retail sector due to ongoing Covid-19 pandemic and its concomitant impact on AFL's profitability, debt coverage and liquidity indicators

[1]Complete definition of the ratings assigned are available at www.careedge.in and other CARE publications

Detailed description of the key rating drivers
Key Rating Strengths
Part of Ahmedabad based Arvind Lalbhai Group with experienced and qualified management
AFL is a part of the Ahmedabad based Arvind Lalbhai group which was founded by Late Mr. Kasturbhai Lalbhai in 1931. The group is a diversified conglomerate having presence in textile, apparel retailing, engineering, waste water treatment and real estate business. Arvind Limited (*Arvind; rated CARE AA-; Stable/ CARE A1+*), the flagship company of the group, is one of India's leading vertically integrated textile companies having presence of more than eight decades in the industry. Post its demerger from Arvind; AFL got separately listed on the stock exchanges on March 08, 2019. The Lalbhai family of Arvind is the largest shareholder in AFL while Multiples Private Equity fund managed by Ms. Renuka Ramnath; ex-MD and CEO of ICICI Ventures Ltd., holds nearly 9% equity stake in the company.
Mr. Sanjay Lalbhai is the Chairman of AFL while his sons, Mr. Punit Lalbhai and Mr. Kulin Lalbhai, are non-Executive Directors on the Board of AFL. The management team of AFL includes Mr. Shailesh Chaturvedi (Managing Director and Chief Executive Officer (CEO)) and Mr. Piyush Gupta (Chief Financial Officer). Further, the board of AFL comprises of eminent industry experts such as Mr. Nilesh Shah, Mr. Vallabh Bhansali and Ms. Nithya Easwaran.

Strong brand portfolio of own and licensed international apparel brands
AFL has a strong portfolio of own and licensed international apparel brands. The licenses are long term/perpetual in nature. AFL's brand portfolio is positioned across various price points and fashion styles although more focused towards casual wear. It also encompasses various segments like men's wear, women's wear, kids wear, inner wear, footwear, beauty and accessories; albeit it is skewed towards men's wear (~69% of its overall sales in FY21).
AFL discontinued many of its loss incurring growth/emerging brands during FY20 and FY21. Further, during H1FY22, AFL sold the assets of its loss incurring value retail 'Unlimited' business to V-Mart Retail Limited. The company completed closure of most of its loss incurring brands by end of September 2021. The company has decided to focus on its six key brands (Tommy Hilfiger, U.S. Polo, Arrow, Flying Machine, Calvin Klein and Sephora) with an aim to improve profitability. Turnaround in the performance of its 'Arrow' brand would be critical for the overall improvement in AFL's profitability. Going forward, the management of AFL plans to increase its sales in beauty brand, inner wear, footwear and kids wear segment in the medium term to improve its demographic presence. Moreover, the company has also forayed into masks, comfort-wear for work-from-home culture, in line with the current consumer requirements.

Wide distribution network with presence across multiple sales channels
AFL has a strong distribution network with 1,249 exclusive brand outlets (EBOs) and more than 3,700 key counters having total retail space of 19.45 lakh square feet (LSF) as on March 31, 2021. AFL's brands are sold through multiple sales channels such as its retail store network, through wholesale to Multi Brand Outlets (MBO) and large departmental stores as well as through online retailers like Flipkart, Myntra and Amazon in addition to its own website NNNOW.com. With a shift in the consumer behaviour towards online sales due to the outbreak of Covid-19 pandemic, the online channel has become a key growth driver for the company thereby increasing the reach of the brand portfolio of AFL. The online channel has been the fastest in recovering post unlock with 38% growth in overall online sales and 3.6 times sales through NNNOW.com along with marketplace. During Q3FY22, online sales had doubled as compared to Q3FY20, contributing more than 25% of the consolidated sales of AFL. AFL has integrated its offline stores and warehouse inventory to NNNOW.com and third-party online platforms to create 'one-view of inventory' which refers to access to the inventory of all the stores apart from online inventory. Further, AFL continued to shift its revenue from inventory and debtor led wholesale business to retail and online channel which significantly reduced wholesale channel contribution to total sales.

Net profit in Q3FY22 after reporting losses in last 10 consecutive quarters along with sizable reduction in debt level
Performance of AFL had remained subdued in Q1FY22 due to impact of second wave of Covid-19 pandemic as its sales were affected from the month of March 2021 onwards. However, gradual recovery in sales was witnessed from the month of July 2021 onwards whereby sales improved on Y-o-Y basis backed by growing online sales and gradual opening of stores along with improving footfalls supported by festive demand. With continued recovery in sales, total operating income during Q3FY22 grew by 30% on y-o-y basis. Moreover, PBILDT margin improved significantly to 10.40% in Q3FY22 supported by higher share of retail sales having higher gross margin, improving share of full price sales, more freshness in stock coupled with benefits of operating leverage. With improvement in PBILDT margin coupled with lower interest cost on the back of reduction in debt level, AFL registered net profit of Rs.18 crore after reporting net losses for the immediately trailing 10 quarters ended Q2FY22. Focus on profitable brands coupled with discontinuation of loss-incurring brands, expected improvement in performance of 'Arrow' brand, structural cost reduction of more than Rs.100 crore and saving in interest cost post sizable debt reduction is expected to improve overall profitability going forward. Moreover, with release of capital employed in loss incurring operations, ROCE of the company is also likely to improve going forward.
The company raised equity funding of Rs.1,260 crore apart from realizing Rs.167 crore from sale of its value retail 'Unlimited' business during the period of one and half years-ended September 30, 2021, the proceeds from which have been utilized for funding of its significant losses incurred on a continuous basis during FY20, FY21 and H1FY22 as well as towards reduction of its consolidated debt and creditors, and shoring up its liquidity. Such timely fund infusion has enabled AFL to successfully counter the challenging external operating environment. The gross debt level (excluding lease liability) reduced sizably from Rs.947 crore as on March 31, 2021 to Rs.467 crore as on December 31, 2021. With improving trend in performance from its core business operations coupled with reduction in debt level, the debt coverage and leverage indicators of AFL also improved during Q3FY22 and 9MFY22; albeit continued to remain moderate.

Liquidity: Adequate
Operations of AFL have been highly working capital intensive due to requirement of large inventory holding in its retail business and extension of credit to its wholesale/online channels. However, company has taken various steps to improve inventory turnover. Moreover, increase in online sales also results in faster inventory turnover.
Despite losses incurred during H1FY22, liquidity of the company at a consolidated level has remained adequate on the back of the latest round of equity/non-debt fund infusion of around Rs.567 crore in AFL towards end-H1FY22. On a standalone level, AFL's average utilisation of fund based working capital limits stood at around 64% during the trailing 12 months ended January 2022 while average utilisation of fund-based limits of Arvind Lifestyle Brands Limited (ALBL; its major subsidiary) declined to 62% for the same period (89% during the trailing 12 months ended October 2021). As on December 31, 2021, on an aggregate level, AFL and ALBL had unutilized fund-based working capital limits of over Rs.250 crore apart from unencumbered cash and bank balance of around Rs.36 crore thereby providing adequate liquidity cushion to safeguard against intermittent disruptions caused by the outbreak of further waves of the Covid-19 pandemic, if any. Further, the company has relatively moderate term debt repayment obligation of around Rs.47 crore due in FY23. CARE Ratings also factors in the promoters' strong commitment to provide need-based support to the company in case of any exigency.

Key Rating Weaknesses
Net losses incurred up to H1FY22 and expectation of lower than previously envisaged profitability and cash accruals during Q4FY22 due to some impact of the Omicron variant of Covid-19 pandemic
Performance of AFL remained subdued in Q1FY22 due to impact of second wave of Covid-19 pandemic as its sales were affected from the month of March 2021 onwards. This apart, losses incurred from various discontinued operations during H1FY22 also adversely impacted its profitability. Consequently, AFL on a consolidated level incurred a net loss of Rs.277 crore during H1FY22. Furthermore, profitability and cash accruals during Q4FY22 is also expected to remain lower than previously envisaged due to the impact of omicron wave of Covid-19. Largely on account of the losses incurred during H1FY22, AFL is expected to report net loss and cash loss in FY22 as well; albeit this is expected to be significantly lower than what it incurred in the preceding two years.

Highly competitive branded apparel retail industry which exerts pressure on profitability margins
Apparel retail sector in India is highly competitive with presence of many domestic and international brands as well as foray of large corporates like TATA group, Reliance group and Aditya Birla group into apparel retail segment. AFL faces tough competition from the private label brands of its established distributors. Furthermore, large expansion by retailers lead to pressure on their PBILDT margin as earnings from existing stores do not adequately offset gestation losses from high proportion of new stores added. However, a strong brand portfolio could help AFL in managing the increasing competition in a better manner.
Being in the retail business, AFL has to continuously invest in order to revamp its existing stores as well as for opening of new stores. However, AFL did not incur any major capex in FY21 on account of disruption of operations due to outbreak of Covid-19 pandemic. AFL has also gradually increased its focus on franchisee stores from FY20 onwards whereby share of company operated stores in total stores decreased from 47% in FY19 to 29% in FY21. Also, most of the store expansion going forward is planned to be done through franchisee route, thereby further reducing capex requirements. AFL's profitability margins and return indicators have hitherto remained modest compared to many of its larger peers. Going forward, realization of envisaged benefits from completed capex along with lower gestation period of newly opened stores will also be crucial for the overall performance of the company and improvement in its return indicators.

Analytical approach: Consolidated; CARE has considered the consolidated financials of AFL for its analytical purpose, which includes the financials of its subsidiaries/JVs. The list of subsidiaries/JVs consolidated in AFL is placed in **Annexure-3.**

Applicable Criteria
Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Criteria for Short Term Instruments
Rating Methodology - Organized Retail Companies
Rating Methodology - Wholesale Trading
Financial ratios – Non-Financial Sector
Rating Methodology: Consolidation
Liquidity Analysis of Non-Financial Sector Entities

About the Company
AFL was originally incorporated in January 2016 as Arvind J&M Limited and its name was changed to its current form in October 2016. It is a part of Ahmedabad based 'Arvind Lalbhai' group and earlier used to be a 90% subsidiary of Arvind with the balance stake being held by Multiples Private Equity Fund. Post business restructuring undertaken within Arvind group, AFL got demerged and was separately listed on the stock exchange on March 08, 2019. Shareholders of Arvind became shareholders of AFL post demerger. AFL, through its two wholly owned subsidiaries, one joint venture (JV) and two step-down subsidiaries, is engaged in the wholesale and retailing of owned and licensed branded apparels in India. However, its wholly-owned subsidiary, ALBL, has major contribution to AFL's consolidated revenue, profitability and debt profile.

Brief details of various businesses conducted by AFL and its subsidiaries/JV:

Company Name	Business activities
AFL	Wholesale of licensed brand 'Arrow'
ALBL - 100% subsidiary of AFL	Wholesale and retailing of various international licensed brands and retailing of Arrow
Arvind Youth Brands Private Limited (AYBPL) – nearly 40% equity stake held directly by AFL and balance equity stake held by AFL through its 100% subsidiary ALBL	Wholesale and retailing of own brand 'Flying Machine'
PVH Arvind Fashion Private Limited (PAFPL) - 50% JV between AFL and PVH Corp, USA	Wholesale trading of 'Tommy Hilfiger' (TH) and 'Calvin Klein' branded apparels, accessories and retail trading for TH brand
Arvind Beauty Brands Retail Private Limited (ABBRPL) - 100% subsidiary of AFL	Retailing of beauty products under 'Sephora'
Value Fashion Retail Limited – wholly-owned by ALBL	Non-operational

Brief Consolidated Financials of AFL (Rs. crore)	FY20 (A)	FY21 (A)	9MFY22 (UA)
Total operating income	3,922	2,328	2,185
PBILDT	292	122	153
PAT	(399)	(596)	(259)
Overall gearing (times) @	4.46	3.18	NA
PBILDT Interest coverage (times)	0.99	0.54	1.51

A: Audited; UA: Un Audited; NA: Not available @ including lease liability in debt

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

Rating History for last three years: Please refer Annexure-2

Covenants of rated instrument / facility: Not Applicable

Complexity level of various instruments rated for this company: Please refer Annexure-4

Annexure-1: Details of Instruments / Facilities

Name of the Instrument	ISIN	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based-LT/ST		-	-	-	145.00	CARE A-; Stable/ CARE A2+
Fund-based - LT-Term Loan		-	-	March 2026	52.08	CARE A-; Stable
Non-fund-based - ST-Working Capital Limits		-	-	-	17.50	CARE A2+

Annexure-2: Rating History of last three years

Sr. No.	Name of the Instrument/Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Rating	Date(s) & Rating(s) assigned in 2021-2022	Date(s) & Rating(s) assigned in 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019
1	Fund-based-LT/ST	LT/ST	145.00	CARE A-; Stable / CARE A2+	1)CARE A-; Negative / CARE A2+ (14-Dec-21) 2)CARE A-; Negative / CARE A2+ (06-Aug-21)	1)CARE A-; Negative / CARE A2+ (29-Sep-20) 2)CARE A-; Negative / CARE A2+ (30-Apr-20)	1)CARE A-; Stable / CARE A2+ (20-Feb-20) 2)CARE A; Negative / CARE A1 (15-Oct-19) 3)CARE A; Negative / CARE A1 (20-Sep-19)	1)CARE A+; Stable / CARE A1+ (02-Aug-18)
2	Fund-based - LT-Term Loan	LT	52.08	CARE A-; Stable	1)CARE A-; Negative (14-Dec-21) 2)CARE A-; Negative (06-Aug-21)	1)CARE A-; Negative (29-Sep-20) 2)CARE A-; Negative (30-Apr-20)	1)CARE A-; Stable (20-Feb-20) 2)CARE A; Negative (15-Oct-19)	-
3	Non-fund-based - ST-Working Capital Limits	ST	17.50	CARE A2+	1)CARE A2+ (14-Dec-21) 2)CARE A2+ (06-Aug-21)	1)CARE A2+ (29-Sep-20) 2)CARE A2+ (30-Apr-20)	1)CARE A2+ (20-Feb-20) 2)CARE A1 (15-Oct-19)	-
4	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	LT/ST	-	-	-	-	1)CARE AA- (CE); Stable / CARE A1+ (CE) (20-Sep-19) 2)Withdrawn (20-Sep-19)	1)CARE AA (SO); Stable / CARE A1+ (SO) (03-Dec-18)
5	Fund-based - LT-Working Capital Limits	LT	-	-	-	-	1)Withdrawn (20-Sep-19)	1)Provisional CARE AA (SO); Stable (03-Dec-18)
6	Non-fund-based - ST-Letter of credit	ST	-	-	-	-	1)Withdrawn (20-Sep-19)	1)Provisional CARE A1+ (SO) (03-Dec-18)
7	Commercial Paper	ST	-	-	-	-	1)Withdrawn (21-Aug-19)	1)Provisional CARE A1+ (SO) (03-Dec-18)

Annexure 3: List of Subsidiaries/JVs of AFL

Name of the Company	% share-holding of AFL as on March 31, 2021	Consolidation
Arvind Lifestyle Brands Limited	100%	Fully Consolidated
Arvind Beauty Brands Retail Private Limited	100%	Fully Consolidated
PVH Arvind Fashion Private Limited (*erstwhile Calvin Klein Arvind Fashion Private Limited*) (JV)	50%	Fully Consolidated
Arvind Youth Brands Private Limited*	100%	Fully Consolidated
Value Fashion Retail Limited*	100%	Fully Consolidated

**Held by Arvind Lifestyle Brands Limited*

Annexure-4: Complexity level of various instruments rated for this company

Sr. No	Name of instrument	Complexity level
1.	Fund-based - LT-Term Loan	Simple
2.	Fund-based - LT/ ST	Simple
3.	Non-fund-based - ST-Working Capital Limits	Simple

Annexure 5: Bank Lender Details for this company

To view the lender wise details of bank facilities please **click here**

Note on complexity levels of the rated instrument: CARE Ratings Ltd. has classified instruments rated by it on the basis of complexity. Investors/market intermediaries/regulators or others are welcome to write to care@careedge.in for any clarifications.

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About CARE Ratings Limited:
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With an established track record of rating companies over almost three decades, we follow a robust and transparent rating process that leverages our domain and analytical expertise backed by the methodologies congruent with the international best practices. CARE Ratings Limited has had a pivotal role to play in developing bank debt and capital market instruments including CPs, corporate bonds and debentures, and structured credit.

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