Arvind Fashions Limited

January 08, 2025

Facilities/Instruments	Amount (₹ crore)	Rating[1]	Rating Action
Long-term bank facilities	17.19 (Reduced from 20.51)	CARE A; Stable	Reaffirmed
Long-term/Short-term bank facilities	160.00	CARE A; Stable/ CARE A1	Reaffirmed
Short-term bank facilities	17.50	CARE A1	Reaffirmed

Details of instruments/facilities in Annexure-1.

Rationale and key rating drivers

Ratings assigned to bank facilities of Arvind Fashions Limited (AFL) continue to derive strength from AFL being part of the Ahmedabad-based Lalbhai group, which has a track record of over a decade in apparel brands and retail business, AFL's strong brand portfolio of owned and licensed international brands, PAN-India retail presence across multiple sales channel and diversified revenue mix; despite concentrated towards men's wear. Rating further considers satisfactory return on capital employed (ROCE), capital structure and debt coverage indicators, which are expected to remain healthy due to controlled working capital cycle and improvement in profitability. Post sale of its loss-incurring licensed brand 'Sephora', profitability and ROCE improved in FY24 (FY refers to April 01 to March 31).

However, rating strengths are tempered by its modest profitability as some of AFL's brands operate at sub-optimal scale particularly, 'Arrow' and 'Flying Machine' and its presence in a highly competitive fashion retail industry, which is vulnerable to changes in fashion trends, consumer preferences and economic cycles. Ratings also factor in current weak consumer spending impacting value segment of apparel retail which limits revenue growth in the near term.

Rating sensitivities: Factors likely to lead to rating actions

Positive factors

- Double digit growth in its total operating income (TOI) along with improvement in its profit before interest, lease rentals, depreciation, and taxation (PBILDT) margin to more than 16% and ROCE of over 20% on a sustained basis.
- Sustained improvement in its total debt to PBILDT (TD/PBILDT) below 2x.
- Maintaining gross working capital cycle at ~180 days on a sustained basis and company maintaining adequate liquidity cushion.

Negative factors

- Decline in its PBILDT margin below 10% on a sustained basis leading to moderation in its TD/PBILDT above 3.5x and ROCE below 12%.
- Significantly lower-than-envisaged cash flow from operations.

Outlook: Stable

Stable outlook reflects that AFL is likely to maintain its market position supported by strong brand portfolio. AFL's financial risk profile is also likely to sustain in the medium term with expectations of improved scale of operations and profitability with no major debt funded capex plan.

Analytical approach: Consolidated

CARE Ratings Limited (CARE Ratings) considered AFL's consolidated financials for its analytical purpose, which includes financials of its subsidiaries/joint venture (JVs), where it has operational and managerial linkages, and they are engaged in same line of operations. Subsidiaries/JVs consolidated in AFL are listed under **Annexure-6.**

Detailed description of key rating drivers:

Key strengths

Part of the Ahmedabad-based Lalbhai Group with experienced and qualified management

AFL is a part of the Ahmedabad-based Lalbhai group, which was founded by Late Kasturbhai Lalbhai in 1931. The group is a diversified conglomerate having presence in textile, apparel retailing, engineering, waste water treatment and real estate businesses. Arvind Limited (Arvind; rated 'CARE AA-; Stable/ CARE A1+'), the group's flagship company is one of the India's leading vertically integrated textile companies, having presence of over eight decades in the industry. Post its demerger from Arvind; AFL got separately listed on stock exchanges on March 08, 2019. The Lalbhai family of Arvind is the largest shareholder in AFL.

[1]Complete definition of ratings assigned are available at www.careedge.in and other CARE Ratings Limited's publications.

Sanjay Lalbhai is the Chairman of AFL while his sons, Punit Lalbhai and Kulin Lalbhai, are non-Executive Directors on the company's board. AFL's management team includes Shailesh Chaturvedi (Managing Director and Chief Executive Officer [CEO]) and Girdhar Chitlangia (Chief Financial Officer). AFL's board comprises eminent industry experts, including Nilesh Shah.

Strong brand portfolio of own and licensed international apparel brands

AFL discontinued many of its loss-incurring brands in the last few years. The company completed closure of most of its loss-incurring brands and decided to focus on its five key brands (Tommy Hilfiger, U.S. Polo, Arrow, Flying Machine and Calvin Klein) with an aim to improve its profitability. Licenses of existing international apparel brands are long term/perpetual. Existing brands have been major revenue drivers for the company in the last few years and are expected to continue in the medium-to-long term. Historically, higher growth momentum of some of these brands led to healthy PBILDT margin thus driving AFL's overall profitability.

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 and accessories; despite skewed towards men's wear. The company has a dedicated team for its adjacent categories (footwear, inner wear, kids wear, women wear and accessories), which has supported revenue of ~₹600 crore from adjacent categories in FY24. Adjacent categories account for over 15% of the revenue for some brands. Going forward, the management plans to increase its sales in adjacent categories within its existing brands to improve demographic presence. In FY24, AFL launched women wear line under U.S. Polo through online channels.

Wide distribution network with presence across multiple sales channels

AFL has a strong distribution network with 931 exclusive brand outlets (EBOs) and over 9,000 multi brand outlets (MBOs) having total retail space of 10.72 lakh square feet (LSF) as on March 31, 2024. AFL's brands are sold through multiple sales channels such as retail store network, through wholesale to MBO and large departmental stores and through online retailers like Flipkart, Myntra and Amazon in addition to its own website NNNOW.com and uspoloassn.in. 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 the online inventory. As on March 31, 2024, nearly 90% stores were omni-channel enabled, which supported AFL to achieve sales of ~₹965 crore from online channel in FY24 contributing ~23% (FY23: ~22%) of its consolidated sales.

Sustained improvement in profitability and ROCE

AFL reported an aggregate net profit of ₹218 crore in the last 12 quarters ended Q2FY25. AFL witnessed gradual increase in share of full price sales across brands and lower discounting, improvement in performance of 'Arrow' brand, discontinuation of loss-making brands and benefits of operating leverage aided improvement in profitability in recent past.

In FY24 and H1FY25, AFL's consolidated sales and profitability impacted by slowdown in demand mainly for value segment due to inflationary pressures and consumer shift towards offline shopping. Despite challenging demand environment, AFL could increase its revenue in FY24 and H1FY25 on y-o-y with improvement in profitability supported by increase in share of full price sales across brands and lower discounting and discontinuation of loss-incurring brand 'Sephora'.

In H1FY25, AFL's revenue grew by 10% over H1FY24 (excluding sales of Sephora brand) with over 100 bps improvement in PBILDT margin despite muted demand scenario and higher advertising and marketing spend. AFL's revenue is expected to grow by ~8-10% in the near-to-medium term supported by strong market position of its apparel brands, increase in sales from adjacent categories, addition of new stores (mainly across tier-2 and tier-3 towns through franchisee stores), improvement in performance of 'Flying Machine' brand, and increase in store efficiency. Operating profitability is mainly a function of sales volume, being very high gross margin (~50%) business. Growth in sales supported by steps taken by management to rationalise costs is expected to improve overall profitability to 13-15% (post-Ind AS 116 basis) in near to medium term. With improvement in profitability and improvement in operating cycle and release of capital employed in loss-incurring operations, AFL achieved ROCE of ~16% in FY24 and is expected to reach ~25% by FY26.

Satisfactory capital structure and debt coverage indicators

AFL's capital structure marked by overall gearing ratio (including lease liability) and total outside liabilities to tangible net worth (TOL/TNW) remained satisfactory and largely stable at 1.37x (PY: 1.55x) and 2.31x (PY: 2.74x), respectively, as on March 31, 2024. In November 2023, AFL sold its entire stake in Arvind Beauty Brands Retail Limited (ABBRL; retailing Sephora brand) to Reliance Beauty and Personal Care Limited at enterprise value of ₹213 crore.

Despite extra ordinary cashflow from sale of equity stake in ABBRL, total debt (including lease liability and acceptances) level of AFL remained largely stable as on March 31, 2024, against March 31, 2023, mainly due to increase in gross operating cycle and reduction in creditors in the year.

With improvement in operating performance and reduction in debt level, CARE Ratings expects AFL's debt coverage and leverage indicators to improve in FY25. Overall gearing (including lease liability) is expected to fall below unity by March 2026. Debt coverage indicators marked by TD/PBIDLT, which improved in FY24 to 2.73x (PY: 3.09x), is expected to improve and remain below 2.5x in FY25. TOL/TNW is also likely to improve in FY25.

Liquidity: Strong

AFL's operations 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, AFL has taken steps to improve inventory turnover and collection period. The company's gross operating cycle, which elongated to nearly 400 days in FY21 mainly due to COVID-19 pandemic, improved to 197 days in FY24 (FY23: 174 days) supported by steps taken by the management to improve collection period, inventory turnover and store efficiency.

AFL has strong liquidity at a consolidated level marked by undrawn working capital limits, unencumbered cash and bank balance and positive cashflow from operations. In FY24, cash flow from operations stood at ₹278 crore (FY23: ₹149 crore). On a standalone level, AFL's average utilisation of fund-based working capital limits stood at ~58% for 12 months ended September 2024, while average utilisation of fund-based limits of Arvind Lifestyle Brands Limited (ALBL; its major subsidiary) stood at 64% for the same period. As on September 30, 2024, AFL had unutilised working capital limits of over ₹350 crore apart from cash and bank balance of ~₹150 crore, providing adequate liquidity cushion. CARE Ratings expects cash accruals of over ₹200 crore against relatively low term debt repayment obligation of ~₹25 crore due in FY25, providing liquidity cushion.

Key weaknesses

Operating performance exposed to economic down-cycles

Retail clothing and apparel industry has heavy dependence on disposable income of its customer segment and is susceptible to economic cycles because of discretionary purchases. Retail clothing and apparel industry is facing subdued demand for value segment and online channel, which had an impact on its overall performance.

The Indian economy has been experiencing a slowdown currently, coupled with high inflation and continued high interest rates. This has led to reduced disposable income, making consumers more cautious about their spending. There has been a noticeable shift in consumer spending towards other lifestyle avenues, such as travel and electronics, rather than apparel. This shift is partly due to changing consumer preferences and the need to prioritise essential over discretionary spending. After an initial surge in spending post-pandemic, driven by pent-up demand, growth rate in retail sales slowed down. This deceleration is evident across segments, including apparel.

Highly competitive branded apparel retail industry, exerting pressure on profitability margins

The apparel retail sector in India is highly competitive with presence of many domestic and international brands and foray of large corporates including TATA group, Reliance group and Aditya Birla group. AFL faces tough competition from private label brands of its established distributors. Some of AFL's brands are still at nascent stage and operate at sub-optimal scale, which results in moderate profitability. 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.

Being in the retail business, AFL has to continuously invest to revamp its existing stores and for opening new stores. The company is focusing on franchisee led expansion, limiting its capex requirements. With expectations of generating higher free cash flow, further improving ROCE and return on equity. AFL has planned capex of ~₹100-120 crore per annum in FY25-FY27, which is expected to be funded through internal accruals.

Environment, social, and governance (ESG) risks

Parameter	Compliance and action by the company
Environment	• AFL shifted 80% of its electricity consumption in the corporate office to renewable sources and has plan to shift 50% of its energy consumption in warehouse operations to renewable sources by 2025. The company introduced motion sensor lights in their warehouse premises. These lights automatically adjust illumination levels based on occupancy, reducing electricity consumption by up to 30%. • AFL introduced certain stock-keeping units (SKUs), which has a blend of sustainable cotton and manufactured using non-hazardous chemicals in the washing process.
Social	• AFL introduced 'responsible sourcing guidelines' for its finished goods vendors, which contain minimum sustainability and compliance standards that its vendors are expected to meet and good practices that may be adopted. • AFL is focusing on increasing productivity of employees by building their skillsets and technical knowledge.
Governance	• AFL's board of directors consists of 50% independent directors (6 of 12). • There are separate Codes of Conduct for Board Members and senior management personnel.

Parameter	Compliance and action by the company
	• Policies, including whistle blower policy, is in place, considering the requirement.

Applicable criteria
Consolidation
Definition of Default
Liquidity Analysis of Non-financial sector entities
Rating Outlook and Rating Watch
Financial Ratios – Non financial Sector
Retail
Short Term Instruments
Wholesale Trading

About the company and industry
Industry classification

Macroeconomic indicator	Sector	Industry	Basic industry
Consumer Discretionary	Consumer Services	Retailing	Distributors

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 part of the Ahmedabad-based Lalbhai group and earlier used to be a 90% subsidiary of Arvind. Post business restructuring undertaken within the Arvind group, AFL was demerged and separately listed on the stock exchange on March 08, 2019. Arvind's shareholders became AFL's shareholders post demerger. Through its one wholly owned subsidiary, one JV and two step-down subsidiaries, AFL 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 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 U.S. Polo 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
Value Fashion Retail Limited – wholly-owned by ALBL	Non-operational

Brief Consolidated Financials (₹ crore)	FY23 (A) ^	FY24 (A)	H1FY25 (UA)
Total operating income	4,421	4,259	2,243
PBILDT	472	525	292
PAT from continuing operations	88	107	59
PAT from continuing operations and discontinued operations	87	137	59
Overall gearing (times) @	1.55	1.37	NA
Interest coverage (times)	3.05	3.36	3.81

A: Audited; ^ including financials of ABBRL in continuing operations; UA: Unaudited; NA: Not available; Note: these are latest available financial results; @ 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: Annexure-2

Detailed explanation of covenants of rated instrument / facility: Annexure-3

Complexity level of instruments rated: Annexure-4

Lender details: Annexure-5

Annexure-1: Details of instruments/facilities

Name of the Instrument	ISIN	Date of Issuance (DD-MM-YYYY)	Coupon Rate (%)	Maturity Date (DD-MM-YYYY)	Size of the Issue (₹ crore)	Rating Assigned and Rating Outlook
Fund-based - LT-Term Loan	-	-	-	March 2026	17.19	CARE A; Stable
Fund-based-LT/ST	-	-	-	-	160.00	CARE A; Stable/ CARE A1
Non-fund-based - ST-Working Capital Limits	-	-	-	-	17.50	CARE A1

Annexure-2: Rating history for last three years

Sr. No.	Name of the Instrument/ Bank Facilities	Current Ratings			Rating History			
		Type	Amount Outstanding (₹ crore)	Rating	Date(s) and Rating(s) assigned in 2024-2025	Date(s) and Rating(s) assigned in 2023-2024	Date(s) and Rating(s) assigned in 2022-2023	Date(s) and Rating(s) assigned in 2021-2022
1	Fund-based-LT/ST	LT/ ST	160.00	CARE A; Stable / CARE A1	1)CARE A; Stable / CARE A1 (09-Aug-24)	1)CARE A; Stable / CARE A1 (05-Jan-24)	1)CARE A-; Positive / CARE A2+ (06-Dec-22)	1)CARE A-; Stable / CARE A2+ (14-Mar-22) 2)CARE A-; Negative / CARE A2+ (14-Dec-21) 3)CARE A-; Negative / CARE A2+ (06-Aug-21)
2	Fund-based - LT-Term Loan	LT	17.19	CARE A; Stable	1)CARE A; Stable (09-Aug-24)	1)CARE A; Stable (05-Jan-24)	1)CARE A-; Positive (06-Dec-22)	1)CARE A-; Stable (14-Mar-22) 2)CARE A-; Negative (14-Dec-21) 3)CARE A-; Negative (06-Aug-21)
3	Non-fund-based - ST-Working Capital Limits	ST	17.50	CARE A1	1)CARE A1 (09-Aug-24)	1)CARE A1 (05-Jan-24)	1)CARE A2+ (06-Dec-22)	1)CARE A2+ (14-Mar-22) 2)CARE A2+ (14-Dec-21) 3)CARE A2+ (06-Aug-21)

LT: Long term; ST: Short term; LT/ST: Long term/Short term

Annexure-3: Detailed explanation of covenants of rated instruments/facilities: Not applicable

Annexure-4: Complexity level of instruments rated

Sr. No.	Name of the 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: Lender details

To view lender-wise details of bank facilities please click here

Annexure-6: List of entities consolidated as on March 31, 2024

Sr. No	Name of the Company	Extent of consolidation	Rationale for consolidation
1	Arvind Lifestyle Brands Limited	Full consolidation	Operational and managerial linkages
2	PVH Arvind Fashion Private Limited (erstwhile Calvin Klein Arvind Fashion Private Limited) (JV)		
3	Arvind Youth Brands Private Limited (AYBPL) @		
4	Value Fashion Retail Limited*		

@Held by Arvind Lifestyle Brands Limited and Arvind Fashions Limited; Post conversion of Compulsory Convertible Preference Shares (CCPS), Flipkart to have 31.25% stake in AYBPL post
* Held by Arvind Lifestyle Brands Limited

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

Contact us

Media Contact	Analytical Contacts
Mradul Mishra Director **CARE Ratings Limited** Phone: +91-22-6754 3596 E-mail: mradul.mishra@careedge.in	Krunal Pankajkumar Modi Director **CARE Ratings Limited** Phone: +91-79-4026 5614 E-mail: krunal.modi@careedge.in
Relationship Contact Saikat Roy Senior Director **CARE Ratings Limited** Phone: 91 22 6754 3404 E-mail: saikat.roy@careedge.in	Akshay Dilipbhai Morbiya Assistant Director **CARE Ratings Limited** Phone: +91-79-4026 5619 E-mail: akshay.morbiya@careedge.in Naman Doshi Analyst **CARE Ratings Limited** E-mail: naman.doshi@careedge.in

About us:
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