Arvind Fashions Limited

March 20, 2017

Ratings

Facilities	Amount (Rs. Crore)	Ratings[1]	Rating Action
Long term/ Short term Bank Facilities	50.00	**'CARE AA (SO); Stable/ CARE A1+ (SO)' [Double A (Structured Obligation); Outlook: Stable]/ [A One Plus (Structured Obligation)]**	**Assigned**
Long term Bank Facilities	175.00	**'Provisional CARE AA (SO); Stable' [Double A (Structured Obligation); Outlook: Stable]**	**Assigned**
Short term Bank Facilities	75.00	**'Provisional CARE A1+ (SO)' [A One Plus (Structured Obligation)]**	**Assigned**
	300.00 (Rupees Three Hundred Crore Only)		

Details of instruments/facilities in Anneuxre-1

 # The above bank facilities are backed/proposed to be backed by the unconditional and irrevocable corporate guarantee of Arvind Limited (Arvind; rated: CARE AA; Stable / CARE A1+)

Detailed Rationale& Key Rating Drivers

The ratings for the various bank facilities of Arvind Fashions Limited (AFL) are based on the credit enhancement in the form of unconditional and irrevocable corporate guarantee of Arvind.

The ratings of Arvind continue to derive strength from the wide experience of its promoters, long-standing operational track record of Arvind as an integrated textile manufacturer having a presence across the textile value chain and the strong growth potential associated with its diversified brand portfolio spread across all customer and product segments supported by widespread retail distribution network. The ratings further continue to factor sustained growth in the scale of operations with stable operating profitability margin despite volatile cotton prices and forex rates, gradual diversification in revenue mix and shift in its business profile as indicated by the increasing contribution of non-denim textiles and brands & retail sales to its revenue stream thereby reducing its dependence on the cyclical denim business. Moreover, the ratings also factors in pre-payment of long-term loans and significant reduction in the debt-level as on December 31, 2016 consequent to the extraordinary cash flow of nearly Rs.1,000 crore generated through 10% equity stake dilution in its brands and apparel business subsidiary (Q3FY17) and liquidation of investment in shares (Q2FY17) resulting into substantial savings on interest charges and improvement in leverage, debt-coverage and debt service coverage ratios.

The long-term rating, however, continue to be constrained on account of Arvind's working capital intensive nature of operations, susceptibility of its profitability to volatile cotton prices and forex rate fluctuation, subdued profitability of its brands and retail business albeit improving year on year and its presence in the cyclical and competitive textile and apparel industry.

The ability of Arvind to maintain the growth momentum in scale of operations while managing raw material price fluctuation and working capital requirement, to improve the profitability of its brands and retail business and maintain improved capital structure and debt coverage indicators would be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths of Guarantor

Wide experience of the promoters in textile industry along with competent management

Arvind, the flagship company of the Ahmedabad based Lalbhai group, is currently led by next generation entrepreneurs of the Lalbhai family under the leadership of Mr Sanjay Lalbhai. Mr Sanjay Lalbhai, aged 67 years, is the *Chairman and*

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

Managing Director of Arvind and looks after the overall operations of the company and has a total work experience of nearly 35 years. Further, the next generation of the Lalbhai family, Mr Punit Sanjay Lalbhai and Mr Kulin Sanjay Lalbhai, have also been inducted on the board at executive directors. Mr Jayesh Shah, *Whole-time-Director and CFO*, is a Chartered Accountant and looks after finance activities with total work experience of over two decades. The management team of Arvind also consists of experienced professionals who have guided the company successfully through various economic cycles. Over the years, Arvind has seen shift from having a family centric management to a professionally managed company facilitating healthy and steady growth of operations through various strategic initiatives.

Diversified revenue stream and product portfolio along with complete vertical integration
Arvind has significantly diversified its revenue base in different segments over the past. Further, Arvind's textile business operations are vertically integrated across the complete value chain from fabric to garments to branded apparel to retail. This integrated setup gives Arvind significant operational flexibility and ability to rationalize costs by managing dependence on outsourced vendors. During FY16, textiles division contributed 60% *(63% during FY15)* of Arvind's total operating income; whereas brands & retail division contributed 32% *(30%)*.

Strong and diversified brand portfolio providing opportunity to grow healthy in fast growing apparel market
Over the years, Arvind has continuously increased its focus on brands and retail business in order to reduce its revenue dependence on highly cyclical and commoditized textiles business. The income from Arvind's brands & retail division have grown from Rs.732 crore in FY10 to Rs.2,740 crore in FY16.

Widespread distribution network
Arvind has one of the largest retail networks in the textile apparel space in the country. Over the years, Arvind has widened its retail distribution footprints. As on March 31, 2016, Arvind had 1,049 stores *(which include The Exclusive Brand Outlets, Arvind Exclusive Stores and Megamart Retail Stores, 951 as on March 31, 2015)* and retail space aggregating 16.80 lakh square feet (lsf) (15.90) apart from 1,566 key account counters in multi brand outlets.

Sustained growth in the scale of operations along with stable profitability
The total operating income of Arvind, which shown increasing trend over the past, registered a compounded annual growth rate (CAGR) of nearly 17.50% during the past three years ended FY16 largely led by strong operational performance by the company in textile as well as brands & retail division. Further, during FY16, the total operating income grew by 9% over the previous year largely on the back of 16% growth in revenue from brands & retail division and 24% in the garment division.
Despite of volatile cotton prices and dollar exchange rate, the PBILDT margin of Arvind remained stable in the narrow range of 13-14% over past five years ended FY16 mainly on account of vertically integrated operations supported by the diversified revenue stream.
The total operating income grew further by nearly 17% y-o-y during 9MFY17 and stood at Rs.6,771 crore. However, the PBILDT margin declined by nearly 150 bps y-o-y during 9MFY17 largely on account of loss of nearly Rs.65 crore in Arvind Internet business which is at the initial stage of e-commerce platform. Further, the PBILDT margin also impacted due to demonetization during Q3FY17 and increase in the share of revenue from low margin brands and retail business.

Significant reduction in the debt-level as on December 31, 2016 consequent to the pre-payment of long-term loans from extraordinary cash flow
During Q2FY17 and Q3FY17, Arvind generated extraordinary cash flow of nearly Rs.1,000 crore by way of equity dilution and liquidation of investment in shares which was largely used for pre-payment of long-term loans apart from reduction in working capital borrowings. This has led to significant reduction in the debt-level as on December 31, 2016 against the projected level resulting into substantial savings on interest charges and improvement in solvency, debt-coverage and DSCR ratios for the period.

Improved leverage and debt-coverage indicators for 9MFY17
Considering extraordinary cash flow through both the above transactions, Arvind has made pre-payment of long-term loans of Rs.720 crore and the balance funds were utilised towards the reduction in working capital borrowings.

Subsequent to that, the total debt of Arvind reduced to Rs.3,071 crore as on December 31, 2016 on consolidated basis as against Rs.4,215 crore as on March 31, 2016 leading to improved overall gearing of 0.89 times as on December 31, 2016. The net-worth base also increased to Rs.3,432 crore as on December 31, 2016 against Rs.2,470 crore as on March 31, 2016. *Further, management has stated that the total debt is likely to be Rs.3,125 crore (as on Mar-17) and there should be a slight reduction to this amount of debt till Mar-18. There are no plans as of now to increase the size of absolute debt in a near term.*

Key Rating Weaknesses of Guarantor

Vulnerability of operating margin to volatility in cotton prices and foreign exchange fluctuation

Cotton and cotton yarn are the key raw materials for Arvind. Being the agriculture based input; the operations of Arvind are vulnerable to its inherent risks associated with agri-based inputs prices.

Arvind also earns revenue from the international market as during FY16 Arvind earned 24% *(26% during FY15)* of consolidated operating income from export sale; whereas import on the other side is negligible. Hence, Arvind is a net exporter and is exposed to adverse fluctuation in foreign currency exchange rates. However, Arvind generally enters into derivative contracts depending on the company's hedging policy which partially mitigates the forex risk.

Analytical approach: Since the bank facilities and instruments of AFL are guaranteed or proposed to be guaranteed by Arvind, CARE has considered the operational and financial performance of Arvind.

Applicable Criteria

Rating Methodology - Wholesale Trading
Financial ratios – Non-Financial Sector
CARE's Policy on Default Recognition
Criteria on assigning Outlook to Credit Ratings
Criteria for Short Term Instruments
Rating Methodology: Factoring Linkages in Ratings

About the Company

Incorporated in January 2016 as Arvind J&M Limited, the name of the company was changed to AFL in October 2016. AFL is a 90% subsidiary of Arvind and balance 10% is held by Multiples, Private Equity firm founded by Ms Renuka Ramnath.

Arvind, through its wholly owned subsidiary, Arvind Lifestyle Brands Limited [ALBL; rated: CARE AA (SO); Stable and CARE A1+ (SO)], engaged in marketing and distribution of various local and global apparel brands in India. ALBL is a licensee of some of the reputed global brands like US Polo, Gant, Nautica, Elle, Cherokee, Ed Hardy, Hanes and Geoffrey Beene etc. ALBL was also holding the licenses of other apparel brands like 'Arrow', 'IZOD' and 'Flying Machine', however, under the business restructuring within the Arvind group, ALBL transferred the wholesale business of these three (i.e. 'Arrow', 'IZOD' and 'Flying Machine') brands to AFL since November 01, 2016. Now, AFL procures apparels of these brands from both overseas and domestic market and sells it in domestic market on wholesale basis. While ALBL continue to operate stores of these brands and sells in retail segment in India.

Moreover, under the business restructuring undertaken within the Arvind group, all the investments of brands and retail business are consolidated under AFL which was previously held by Arvind Brands and Retails Limited, wholly owned subsidiary of Arvind.

About Arvind (The Guarantor)

Arvind, the flagship company of the Ahmedabad-based Lalbhai group which was founded by the Late Mr Kasturbhai Lalbhai in 1931, is a diversified conglomerate having presence in textiles, apparel retailing, engineering and real estate businesses amongst others. Currently, the group is led by next generation of the Lalbhai family under the leadership of Mr Sanjay Lalbhai, Chairman & Managing Director, Arvind and Mr Sunil Lalbhai, MD of Atul Limited *(rated: CARE AA+ / CARE A1+).*

Arvind is one of the India's leading vertically integrated textile companies with the presence of more than eight decades in the industry. Arvind is among the largest denim and woven fabric manufacturers with an installed capacity of 108 million meters per annum (MMPA) and 132 MMPA respectively as on March 31, 2016. Apart from the denim and woven, Arvind also manufactures a range of cotton shirting, knits and bottom weights (Khakis) fabrics. Recently Arvind also has made foray in to technical textiles on its own and in joint venture with leading global players. Further, since the last three

years, Arvind also launched The Arvind Store, a store that offers Arvind's fabric, tailoring solution and key branded apparels.
Arvind has 13 manufacturing facilities located at Ahmedabad (5), Bangalore (7) and Kolhapur (1). During FY16 (refers to the period April 1 to March 31), Arvind (Consolidated) earned 60% *(63% during FY15)* of the total operating income from the textile manufacturing division, 32% *(30%)* from brands & retail division and the balance from others.

As per the audited results for FY16 (Consolidated), Arvind reported a PAT of Rs.365 crore on a total operating income of Rs.8,507 crore as against a PAT of Rs.338 crore on a total operating income of Rs.7,807 crore in FY15 (Consolidated). Further, during 9MFY17, Arvind reported PAT of Rs.222 crore on a total operating income of Rs.6,771 crore.

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

Note on complexity levels of the rated instrument: *CARE has classified instruments rated by it on the basis of complexity. This classification is available at www.careratings.com. Investors/market intermediaries/regulators or others are welcome to write to care@careratings.com for any clarifications.*

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About CARE Ratings:

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Annexure-1: Details of Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	-	-	-	50.00	CARE AA (SO); Stable / CARE A1+ (SO)
Fund-based - LT-Working Capital Limits	-	-	-	175.00	Provisional CARE AA (SO); Stable
Non-fund-based - ST-Letter of credit	-	-	-	75.00	Provisional CARE A1+ (SO)

Annexure-2: Rating History of last three years

Sr. No.	Name of the Bank Facilities	Current Ratings			Rating history			
		Type	Amount Outstanding (Rs. crore)	Ratings	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016	Date(s) & Rating(s) assigned in 2014-2015	Date(s) & Rating(s) assigned in 2013-2014
1.	LT/ST Fund-based/Non-fund-based-EPC / PCFC / FBP / FBD / WCDL / OD / BG / SBLC	LT/ST	50.00	CARE AA (SO); Stable / CARE A1+ (SO)	-	-	-	-
2.	Fund-based - LT-Working Capital Limits	LT	175.00	Provisional CARE AA (SO); Stable	-	-	-	-
3.	Non-fund-based - ST-Letter of credit	ST	75.00	Provisional CARE A1+ (SO)	-	-	-	-

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