Asian Star Company Limited

February 04, 2019

Ratings

Facilities*	Amount (Rs. crore)	Rating[1]	Rating Action
Long term/Short term Bank Facilities	1154.00	CARE A-; Stable/ CARE A2+ (Single A Minus; Outlook: Stable/ A Two Plus)	Reaffirmed
Total Facilities	**1154.00 (Rupees Eleven thousand one hundred and fifty four crore only)**		

**Details of instruments/facilities in Annexure-1*

Detailed Rationale & Key Rating Drivers

The reaffirmation in the ratings assigned to the bank facilities of Asian Star Company Limited (ASCL) factors in the experience of its promoters, the company's strong business profile with international marketing setup, its association with the world's leading diamond mining companies and its established relationship with the customers.

These rating strengths are, however, tempered by ASCL's thin profitability, its moderate capital structure and debt coverage indicators, working capital intensive operations of the company, and susceptibility of the profitability to volatility in the prices of rough diamonds and foreign exchange fluctuations. The rating also factors in the intense competition and fragmented nature of cut and polished diamond (CPD) industry.

The ability of the company to effectively manage its working capital cycle, and maintain its liquidity profile and capital structure, debt protection metrics and improve its profitability margins remain the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters

Mr. Dinesh T. Shah, Chairman of ASCL, has over 41 years of experience in the G&J industry. Mr. Vipul Shah, CEO & MD also has vast experience in the G&J industry. He has been instrumental in establishing ASCL's global network and in developing ASCL's jewellery business. He is assisted by a team of well qualified and experienced directors, who are actively involved in various functions of the business.

Strong business profile with international marketing setup

ASCL has sales exposure in both domestic and international markets. Rough diamonds are procured at group level and are cut and polished in the manufacturing facility of ASCL in Surat, Gujarat, and then sold across the globe. During FY18, ASCL consolidated sales mix constituted 57% of CPD, 28% of rough diamonds and 14% of diamond studded jewellery (15% in FY17).

The total operating income increased by 11.87% i.e. to Rs.3911.39 crore in FY18 on account of increased sales from foreign subsidiaries primarily from rough diamond trading through its UAE subsidiary, Asian Star DMCC (ASD).

ASCL caters to diversified customers in the domestic as well as overseas market. Hong Kong, UAE and USA remain the major export destinations accounting for 52% of the total revenues in FY18. The company also has its presence across countries like USA, China, Japan and European countries. However, their share continued to remain low. Besides its subsidiaries in USA, Hong Kong and UAE, ASCL has 16 marketing arms spread across Asia, Europe and America. These marketing arms have enabled ASCL to establish its customer base across 40 countries.

Established relationship with customers

ASCL has a diversified customer base with exposure to jewellery manufacturers and retailers and has developed long standing relationship with jewellery manufacturers and retailers. Titan Company Limited is the largest customer of ASCL.

Sourcing of rough diamonds from world's leading diamond mining companies

ASCL has rough supply contracts with all the major mining companies i.e. DTC sight-holder contract of the De Beers Group since 1993 and Alrosa Alliance Member of Russian based rough diamond mining company Alrosa Company Ltd. It is also a part of Select Diamantiaries List of the Rio Tinto group as well as a Dominion Preferred Purchaser of Dominion Diamond Corporation, a Canada-based rough diamond mining company. Meanwhile, during FY18 ASCL has also explored sourcing of diamond from Angola, through Sodiam (trading subsidiary of Endiama, E.P) to diversify its sourcing.

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

Majority of purchases are made at the group level from DTC and miners as compared to secondary market. ASD, which is a DTC sight holder of Alrosa, procures rough diamonds from miners and secondary market, and supplies to ASCL. Apart from procuring rough diamonds, ASCL also procures polished diamonds for meeting specific requirements of customers. In FY18, purchase from miners constituted 50.61% of total rough diamond procurement. In addition to this, the company also procured roughs from secondary suppliers/open market in addition to direct procurement from diamond mining companies.

Key Rating Weaknesses

Marginal growth in revenue along with thin profitability margins

ASCL reported an increase in total operating income by 11.87%, from Rs.3496.38 crore in FY17 to Rs.3905.03 crore in FY18. During FY18, ASCL on a standalone basis contributed 70% to consolidated revenues as compared to 77% in FY17. ASCL on a standalone basis reported a marginal increase of 1.19% in FY18 its total operating income, from Rs.2705.06 crore in FY17 to Rs.2737.60 crore in FY18. This is a result of declined revenue contribution from UAE region from 34% in FY17 to 19% in FY18 as an outcome of decreased demand due to enforcement of value added tax (VAT) in Dubai from January 01, 2018.

During FY18, ASD, reported significant increase in revenue and profitability. ASD is involved in trading of mainly rough diamonds. This led to improvement in overall PBILDT margin to 4.85% in FY18. However, PBILDT margin in CPDs continues to remain thin due to the limited value addition and intense competition in the industry. Further, PAT margin improved to 2.60% in FY18.

Moderate capital structure and debt coverage indicators

Overall gearing ratio improved to 0.86 times as on March 31, 2018 (as compared to 1.16 times as on March 31, 2017) on account of reduction in working capital utilization as compared to FY17 and reduced loan from promoters. The company had total debt of Rs.844.35 crore as on March 31, 2018 out of which Rs.144.32 crore was loan from promoters. These loans from promoters are non-interest bearing and repayable on demand. Total Debt/ GCA and interest coverage ratios improved to 11.71x and 4.31x as on March 31, 2018 vis-à-vis 6.87x and 4.73x as on March 31, 2017 respectively as a result of improvement in GCA and PBILDT.

Susceptibility of profitability margins to volatility associated with raw material prices

ASCL is dependent on imports to meet its requirement of rough diamonds which contribute 65% of total diamond purchase, with 99% of total rough diamond purchase being imported. The profitability margins of ASCL are susceptible to the price of rough diamonds and C&P which are market driven and volatile in nature. Manufacturers in the midstream segment of the CPD industry have limited bargaining power vis-à-vis both the diamond mining companies as well as the jewellery retailers who earn larger part of the profitability in the value chain.

Susceptibility to foreign exchange rates fluctuation

The company earns 60% of its revenue from exports in FY18 and is subject to foreign exchange fluctuations. As ASCL enjoys natural hedge on most of its foreign exchange exposure. The company enters into hedging by way of forward contracts, in case exports are not enough to cover imports. Despite hedging contracts, commodity price and foreign exchange fluctuation are moderate risks to the profitability of the company.

Intense competition and fragmented nature of the CPD industry

India is the world’s largest centre for cutting and polishing of diamonds. However, the CPD industry in India is highly fragmented with the presence of numerous unorganized players in addition to the large integrated G&J manufacturers leading to a high level of competition. The Indian CPD industry is primarily export-oriented and is characterized by working capital intensive operations and thin profitability.

Liquidity:

As per Audit Report of FY18, ASCL had overdrawn an amount of Rs.4.14 crore of its working capital facility obtained from the bank. The overdrawal was for 5-7 days. As per the management, the overdue amount was repaid by the company between April 3, 2018 and April 6, 2018 with the last curing on April 6, 2018. The management has also clarified these working capital facilities pertained to dollar denominated post shipment loans which were availed against exports and were outstanding as the export realizations were delayed by a few days. The company wanted to repay the dollar denominated loans using the dollar denominated receivables and not out of the INR balance available with the company. *As the overdrawal period was less than 30 days, the ratings have not been downgraded to ‘default grade’ by CARE.*

ASCL’s operations are working capital intensive as rough diamond procurement is mainly on advance payment or cash basis whereas it has to extend credit to its customers for sale of polished diamonds. ASCL provides a credit period of 90 days to its customers on an average; however creditor period is less as it has to make upfront payments to rough diamond supplier because it procures a large part of its rough diamond requirement directly from mining companies. Average creditor days have further reduced from 35 days in FY17 to 27 days in FY18 on account of increased purchases

from DTC and miners. ASCL has to make advance payments to few of its secondary market suppliers as well. Further, the company maintains inventory levels for approximately 2 months out of which finished goods inventory is one month. ASCL's operating cycle stood at 113 days in FY18 in line with 113 days in FY17. There has been a build-up of inventory and receivables position in the last three years. Further, the consolidated free cash/bank balance has declined over the last 3 years, and is envisaged to decline to significantly low levels by March 31, 2019 by the company on account of build-up of receivables and inventory. Further, predominant portion of the free cash is available in ASHK which is engaged in jewellery/diamond trading. As per the management large portion of this is not repatriable into India.
To fund the operations, ASCL uses bank lines comprising post-shipment credit (PSC) and Export Packing Credit (EPC). ASCL's average working capital limit utilization was 65% during the twelve months ended November 2018 (peak utilisation of 79% during the same period).

Analytical approach:
CARE has analysed the consolidated financials of ASCL owing to the operational and financial linkages between the entities. The details of the entities which have been consolidated with ASCL in the analysis are as under:

Sr. No.	Name of entity	Relationship with ASCL
1	Asian Star Jewels Pvt. Ltd.	Wholly owned subsidiary
2	Asian Star DMCC (ASD)	Wholly owned subsidiary
3	Asian Star Company Ltd. (USA)	Wholly owned subsidiary
4	Asian Star Trading (Hong Kong) Ltd. (ASHK)	Wholly owned subsidiary
5	Shah Manufacturers	Associate Company

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

About the Company
ASCL was set up as a partnership firm in 1971 by the Shah and Kothari families. In the year 1990, the management control of the company was vested with the Shah family and in 1995 it was subsequently converted to a public limited company. In 1996, ASCL was listed on the BSE. ASCL is a recognized Four Star Trading House. ASCL's primary business involves CPDs of less than one carat. The company also manufactures diamond-studded gold and platinum jewellery. ASCL is partially integrated across the G&J value chain from procurement of rough diamonds, diamond cutting & polishing to jewellery manufacturing and distribution directly to retailers across the globe. The company also has windmills in Maharashtra, Kerala and Tamil Nadu.
In H1FY19, ASCL merged its subsidiary ASJPL with it vide NCLT order dated September 03, 2018 w.e.f. April 01, 2017.

Brief Financials (consolidated) (Rs. crore)	FY17 (A)	FY18 (A)
Total operating income	3496.38	3911.38
PBILDT	134.26	181.83
PAT	64.09	101.84
Overall gearing (times)	1.16	0.86
Interest coverage (times)	4.39	5.25

A: Audited

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 Instruments/Facilities

Name of the Instrument	Date of Issuance	Coupon Rate	Maturity Date	Size of the Issue (Rs. crore)	Rating assigned along with Rating Outlook
Fund-based-LT/ST	-	-	-	1154.00	CARE A-; Stable / 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 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017	Date(s) & Rating(s) assigned in 2015-2016
1.	Fund-based-LT/ST	LT/ST	1154.00	CARE A-; Stable / CARE A2+	-	1)CARE A-; Stable / CARE A2+ (05-Dec-17)	1)CARE A- / CARE A2+ (07-Sep-16) 2) CARE A- / CARE A2+ (15-Jan-16)	1)CARE A- / CARE A2+ (07-Jan-15)

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