

Future Lifestyle Fashions Limited (Revised)

November 11, 2020

Ratings

Bank Facilities	Amount (Rs. crore)	Rating	Rating Action
Long-term - Proposed Term Loan	175.00	CARE C (Under Credit watch with Negative Implications) (Single C) (Under Credit watch with Negative Implications)	Revised from CARE BB (Double B); Continues to be on Credit watch with Negative Implications
Long-term Bank Facilities – Term Loan	339.39		
Long-term fund based bank facilities – CC	550.00		
Short-term Bank Facilities – LC/BG	475.00	CARE A4 (Under Credit watch with Negative Implications) (A Four) (Under Credit watch with Negative Implications)	Continues to be on Credit watch with Negative Implications
Total	1,539.39 (Rs. One thousand five hundred thirty nine crore and thirty nine lakh only)		
Non-convertible Debenture Issue	350.00	CARE D (Single D)	Revised from CARE BB (Double B); Continues to be on Credit watch with Negative Implications
Proposed Non-convertible Debenture Issue	150.00	CARE C (Under Credit watch with Negative Implications) (Single C) (Under Credit watch with Negative Implications)	

**carved out of working capital limits*

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision of ratings assigned to the bank facilities and instruments of Future Lifestyle Fashions Limited (FLFL) is on account of delay in servicing of its interest and principal due (subsequent to exercise of put option) on November 09, 2020 on its Non-convertible Debentures (NCD) bearing ISIN INE452007047. NCD issued by the company on November 9, 2017 carried Put and Call option at the end of 3rd and 4th year from issue which was exercised by two of the investor. While one of the investor agreed to defer the payment to February 01, 2021 the other investor rejected the proposal for deferment. The default is primarily on account of poor liquidity position. Consequently, the ratings for other facilities and instruments have also been revised.

The other issues raised by CARE in its press release dated October 15, 2020, viz weakened credit profile of the company on account of slower than envisaged ramp up of sales, unavailability of additional working capital limits/COVID lines from lenders further deteriorating its stretched liquidity position continue to constrain the ratings. Inadequate cash flows continue to put stress on liquidity position of the company.

FLFL applied for the One Time Restructuring (OTR) facility vide its letter dated September 17, 2020 to all its lenders, under RBI guidelines issued on August 6, 2020. Further FLFL did not made debt repayments that were due on September 30, 2020 to its lenders as the OTR process has been initiated. Since the application for OTR has been made before the due date, CARE has not treated the same as default in line with the criteria issued on 'Analytical treatment for one-time restructuring due to COVID-19 related stress', issued on September 29, 2020. As per the discussion with some of the lenders, the OTR has been invoked on November 02, 2020 and ICA shall be signed within 30 days from the date on invocation. The successful implementation of restructuring remains a key rating monitorable.

The ratings continues to be tempered by moderate return on capital employed, refinancing risk, high operating cycle coupled with susceptibility to economic cycles and increasing competition in the fashion retail industry. The ratings also factor in stretched liquidity position of the Future Group which could impact the financial flexibility of the company.

The ratings continue to be on credit watch with negative implications on account of the company's announced scheme of arrangement with FEL and OTR application. CARE will continue to monitor the progress on said scheme of arrangement and OTR application and will resolve the watch once clarity emerges on the same.

Rating Sensitivity Factors

Positive factors

- Improvement in credit profile of FLFL post end of pandemic on back of strong sales growth and increased contribution from private brands.
- Improvement in capital structure through equity infusion/monetisation of brands leading to overall gearing (post adoption of IndAS116) below 1.00x

Negative factors

- Weakening in liquidity position resulting from extended closure and enhancement in working capital limits
- Increase in working capital intensity or weakening of debt credit metrics on account of larger than anticipated debt funded capex leading to overall gearing (post adoption of IndAS116) above 2.00x.

Detailed description of the key rating drivers

Key Rating Weaknesses

Deterioration of debt coverage metrics on the back of COVID19: FLFL's financial risk profile has weakened on account of disruption in operations caused by temporary shutdown of operations on the back of COVID19 pandemic. As on March 31, 2020, the capital structure has deteriorated to 1.68x as against 0.64x as on March 31, 2019 on account of net losses, increase in debt and adoption of IndAS 116. Similarly debt coverage metrics such as interest coverage ratio and total debt to GCA have also deteriorated to 3.45x and 11.65 respectively.

FLFL's investments in nurturing brands offer it opportunities to unlock value over a period of time and provide it with the financial flexibility to raise funds whenever needed. The company also has demonstrated track record of raising funds from marquee investors like Blackstone, L-Catterton and Aion Capital which has invested funds in FLFL or promoter level entity.

Improvement in FY19 Operational Performance but ROCE remains moderate; further expected to contract due to COVID-19 lockdown: Footfalls in the stores of FLFL have increased by 19% in FY19 with an improvement in conversion rate as well. However, the average transaction size and average selling price declined by 5% and 2% respectively over FY18 on account of increase in contribution from the discount format store (Brand Factory).

During FY20, the operational performance was impacted due to outbreak of COVID-19 and subsequent lockdown imposed in the nation. The company, in FY20, reported net loss of Rs. 53 crore on total income of Rs. 6,362 crore as against net profit of Rs. 189 crore on a total income of Rs. 5,755 crore in FY19.

The company maintains large inventory and with increasing contribution from 'Brand Factory' the company's profit margins have remain modest. ROCE has improved over the years, however, the same is expected to moderate on account of addition of new stores and increasing contribution from 'Brand Factory'.

Post lifting of lockdown CARE expects recovery to be slow and gradual which is likely to result in moderation in debt coverage indicators and ROCE. Due to nation-wide lockdown and subsequent extensions, the company has reported a PAT loss of Rs. 616 crore on total revenue of Rs. 520 crore in H1FY21.

Refinancing risk: Non-Convertible debentures (NCD) issued by the company (ISIN INE452O07047) on November 9, 2017 carries Put and Call option at the end of 3rd and 4th year from issue. Two investors have exercised the Put option. FLFL had requested the investors to extend the date of payment of annual interest and principal which has been agreed by one of the Debenture holders. The other investor rejected the deferment proposal. Due to ongoing stress on liquidity position the company could not service principal payment of Rs.100 crore and interest payment of Rs.30.93 crore on its NCDs aggregating to Rs.350.00 crore.

Significant shares pledged/encumbered by the promoter: The total shares pledged/encumbered by promoters as on September 11, 2020 continue to remain high at 99.51%.

Blackstone has invested a total of Rs. 1,750 crore or USD 250mn in holding company of FLFL, Ryka Commercial Ventures Private Limited (Ryka). As a part of the deal, 6% of equity shares of FLFL held by Ryka have been acquired by Blackstone for an amount of Rs. 545 crore. The balance amount (Rs. 1,205 crore) is issued as NCD by Ryka and subscribed by Blackstone entity. The structure is backed by the security by way of encumbrance (Non-Disposal Undertaking) sale of shares of Ryka and FLFL (held by Ryka) and pledge will be created only upon the occurrence of the event of defaults.

As per the management, there is no recourse to the cash flows of FLFL and the NCD is a zero coupon instrument with payment at the end of five years.

The share price has also witnessed a significant decline. Share price has fallen by 38% to Rs. 73.35 as on November 11, 2020 as against closing of Rs. 119.25 on August 13, 2020. Market capitalisation has declined from Rs. 2,406 crore to Rs. 1,480 crore.

High Working Capital Cycle: FLFL has low receivables period like other retailers, however the inventory days are higher on account of bought out stock arrangement for its private brands which leads to higher working capital requirement. Also, the retailing of private brands coupled with the distribution business leads to an extended inventory requirement. The company has a relatively high working capital cycle.

Inventory carrying risk is partially mitigated through the 'Sale or Return' (SOR) model adopted by the company. This provides FLFL the right to return unsold stock to the vendor at determined frequency. The same minimises the inventory carrying risk for the company and help it with better working capital management. The company procures 50%-60% of inventory on SOR basis.

Acquisition of Koovs and investment towards digital business: The Board of FLFL in FY19 approved the investment in equity shares of Koovs plc. for GBP 15.3 million (approx. Rs.140.00 crore) for 30% stake. Koovs plc (company incorporated in England) is a supplier of branded fashion garments and accessories for sale by a third party through Koovs.com website principally in India. The company has till June 2019 invested Rs. 85 crore in Koovs and holds 25.8% of ordinary share capital. However, on account of continued losses reported by Koovs, FLFL in Q4FY20 had impaired its investment to the tune of Rs. 84 crore (which is reported as exceptional item).

FLFL in Q2FY20, launched its digital business through the website 'brandfactoryonline.com'. For FY20, it reported a turnover of Rs. 19 crore and operating losses of Rs. 25 crore. The fall was primarily on account of platform building cost, trial run cost and one time set up cost.

The ability of the company to ramp up businesses and generate envisaged returns through stipulated investments remains key rating monitorable.

Deterioration in credit profile of Future Group

The share price of various Future Group entities has witnessed a steep decline. The weakening of market capitalization has impacted the financial flexibility of the group.

Intensifying competition: FLFL faces intense competition from other brick and mortar retailers like Lifestyle International, Shoppers Stop Limited, Aditya Birla Fashion, Trent Limited etc. The company also faces competition from online retailers like Amazon, Flipkart, Myntra. Heightened competition from both brick and mortar and online players could impact overall SSSG of FLFL. However, with its diverse offering with presence in premium and discount formats would support FLFL over the medium term.

Key Rating Strengths

Experienced promoters and expected support from PE Investors: FLFL is part of the Future Group, which is one of the largest retailers in India. Mr Kishore Biyani, founder of Future group is Managing Director of FLFL. The promoters of FLFL are involved in the management of the business, defining and monitoring the business strategy for the company, and have been successful in building and scaling up in both value retail and fashion retail. Furthermore, the promoters are supported by a strong management team, having significant experience in the retail industry. FLFL is backed by PE investors such as Blackstone, LCatterton, PremjiInvest and Aion Capital.

Established pan-India presence of various operationally profitable formats: As on September 30, 2020, FLFL distribution network includes 338 stores having a retail space of 7.7 million sq. ft. FLFL's fashion retail business is led by two major retail chains – Central and Brand Factory. These outlets contribute nearly 88% of the total retail sales for FY19. FLFL sells the premium apparel segment through Central while the low priced apparels are sold through Brand Factory. Central alone contributes 50% of the total sales in FY19. The company further operates EBOs and is also into distribution business wherein it is selling its brands from other MBOs (Multi Brand Outlets) falling outside Future Group Retail network. The key formats 'Central' and 'Brand Factory' are the major contributors to the EBDITA of the company.

Established and diversified lifestyle fashion brand portfolio: FLFL is associated with various brands in apparel, footwear, accessories, home fashion and luggage via three formats: (i) Own/Private Brands, (ii) Licensed Brands held directly by FLFL and (iii) Investments in various companies holding Brand licenses. FLFL brands contributed 39% of total sales in FY19 whereas the balance was by third party brands. These brands are sold through Central and Brand Factory as well as through EBOs and MBOs.

FLFL's investments in nurturing such brands offer it opportunities to unlock value over a period of time. During FY17, FLFL had transferred its investments in various companies holding brand licenses to "FLFL Lifestyle Brands Ltd. (FLBL)" and divested 51% stake to raise Rs.450 crore. During FY20 the company had bought back investment by PE player in 'Future Speciality Retail Limited' at ~Rs.350 crore.

The company is expected to benefit from the focus on brands along with increase in retail space in the medium term.

Robust supply chain infrastructure in place: FLFL has a robust supply chain infrastructure in place which helps in achieving better operational efficiencies. The inventory management system enables it to offer and display correct merchandise assortments in the right mix, style, colour and fashion at various price points on the shelves as per the regional taste and preference. The sales trends are also regularly monitored to optimise inventory levels.

The company's warehousing and logistic requirements are managed by Future Supply Chain Solutions Limited, which is a part of the Future Group. FLFL has mother warehouses at various locations in each zone which feeds the regional warehouse which in turn provides services to the stores across all the locations. Better inventory management led to inventory days declining to 126 days in FY19 as against 135 days in FY18. However, on account of temporary closure of stores during last week of FY20, inventories couldn't be liquidated leading to rise in inventory days to 154 in FY20.

Industry Outlook

In view of the COVID19 outbreak and lowering of the discretionary spending by the consumers in these times of economic downturn, the outlook for the Indian players in retail sector is 'Negative' in the short to medium term. The impact on demand, which is expected to remain muted at least for the next three or four quarters, will be more in case of players with presence in non-essential items and luxury segments. However, the expected support from the government in terms of financial stimulus packages and wage support subsidy as well as rental waivers from the mall-owners which would help the retailers to bring down their fixed costs, will reduce the impact on their credit profile to an extent. The retailers with presence in essential commodities continue to have some cash flows to support their fixed costs.

After the control of the spread of the coronavirus and post the lock-down period, the spending as well as shopping patterns of the consumers are expected to change significantly. The consumers are likely to curtail their discretionary spending with reduced income in their hands as well as tendency to preserve cash. Also, more preference is likely towards online channels in order to avoid crowded spaces. In such times, the retailers with presence across the retail segments (grocery, apparel, appliances, accessories) as well as who have an omni-channel strategy with presence in both offline and online channels are expected to have a quicker recovery.

Liquidity: Stretched

Temporary closure of operations as directed by the governing authorities on the back of COVID19 outbreak has hampered the company's ability to generate cash flows. The company's working capital limits remain fully utilised. FLFL has availed moratorium on payments as per RBI package. The company has also applied to lenders for One Time Restructuring (OTR) facility under RBI guidelines issued on August 6, 2020. The liquidity profile of the company is stretched on account of reduced cash flows and short term financial liabilities and term loan repayments of Rs. ~280 crore (scheduled repayments prior to availing moratorium/OTR) due in FY21.

Analytical approach: Consolidated financials of FLFL along with its subsidiaries and joint ventures are considered for analysis due to strong operational linkages.

The list of entities consolidated is provided in Annexure – III.

Applicable Criteria

[Analytical Treatment for one-time restructuring \(OTR\) due to COVID-19 related stress](#)

[Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings](#)

[CARE's Policy on Default Recognition](#)

[Rating Methodology: Organised Retail Companies](#)

[Financial ratios – Non-Financial Sector](#)

[Criteria for Short Term Instruments](#)

[Rating Methodology: Consolidation and Factoring Linkages in Ratings](#)

[Liquidity Analysis of Non-Financial Sector Entities](#)

About the Company

Future Lifestyle Fashions Limited (FLFL) is a part of the Future Group (one of India's largest retailers). FLFL is in the business of managing the lifestyle fashion segment of the Future Group. It has a portfolio of fashion brands that cover a range of fashion categories including formal menswear, casual wear, active or sportswear, women's ethnic wear, women's denim wear, women's casual wear, footwear and accessories and are present across various price points. The company as on September 30, 2020 operate 338 stores having a retail space of 7.7 million sq. ft.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)	FY20 (Abg.)
Total operating income	4520	5755	6362
PBILDT	453	620	1055
PAT	126	189	-53

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)	FY20 (Abg.)
Overall gearing (times)	0.70	0.71	1.68
Interest coverage (times)	4.39	3.98	3.45

A: Audited; Abg: Abridged

Status of non-cooperation with previous CRA: Not Applicable

Any other information: Not Applicable

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

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-Term Loan	-	-	Jan 2025	339.39	CARE C (Under Credit watch with Negative Implications)
Fund-based - LT-Term Loan – Proposed	-	-	-	175.00	CARE C (Under Credit watch with Negative Implications)
Fund-based - LT-Cash Credit	-	-	-	550.00	CARE C (Under Credit watch with Negative Implications)
Non-fund-based - ST-Working Capital Limits	-	-	-	475.00	CARE A4 (Under Credit watch with Negative Implications)
Debentures-Non Convertible Debentures (Proposed)				150.00	CARE C (Under Credit watch with Negative Implications)
Debentures-Non Convertible Debentures INE452007047	November 10, 2017	8.70	09-11-2022	350.00	CARE D

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 2020-2021	Date(s) & Rating(s) assigned in 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018
1.	Fund-based - LT-Term Loan	LT	514.39	CARE C (Under Credit watch with Negative Implications)	1)CARE BB (Under Credit watch with Negative Implications) (15-Oct-20) 2)CARE BBB (Under Credit watch with Developing Implications) (13-Aug-20) 3)CARE A+; Negative (12-May-20)	1)CARE AA-; Positive (24-Dec-19)	1)CARE AA-; Positive (12-Dec-18)	1)CARE AA-; Stable (11-Jul-17)

					4)CARE AA-; Negative (17-Apr-20)			
2.	Fund-based - LT-Cash Credit	LT	550.00	CARE C (Under Credit watch with Negative Implications)	1)CARE BB (Under Credit watch with Negative Implications) (15-Oct-20) 2)CARE BBB (Under Credit watch with Developing Implications) (13-Aug-20) 3)CARE A+; Negative (12-May-20) 4)CARE AA-; Negative (17-Apr-20)	1)CARE AA-; Positive (24-Dec-19)	1)CARE AA-; Positive (12-Dec-18)	1)CARE AA-; Stable (11-Jul-17)
3.	Non-fund-based - ST-Working Capital Limits	ST	475.00	CARE A4 (Under Credit watch with Negative Implications)	1)CARE A4 (Under Credit watch with Negative Implications) (15-Oct-20) 2)CARE A3 (Under Credit watch with Developing Implications) (13-Aug-20) 3)CARE A1 (12-May-20) 4)CARE A1+ (17-Apr-20)	1)CARE A1+ (24-Dec-19)	1)CARE A1+ (12-Dec-18)	1)CARE A1+ (11-Jul-17)
4.	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (11-Jul-17)
5.	Commercial Paper- Commercial Paper (Carved out)	ST	-	-	1)Withdrawn (06-Aug-20) 2)CARE A1 (12-May-20) 3)CARE A1+ (17-Apr-20)	1)CARE A1+ (24-Dec-19)	1)CARE A1+ (12-Dec-18)	1)CARE A1+ (11-Jul-17)
6.	Debentures-Non Convertible Debentures	LT	-	-	-	-	-	1)Withdrawn (11-Jul-17)
7.	Debentures-Non Convertible Debentures	LT	150.00	CARE C (Under Credit watch with Negative Implications)	1)CARE BB (Under Credit watch with Negative Implications) (15-Oct-20) 2)CARE BBB	1)CARE AA-; Positive (24-Dec-19)	1)CARE AA-; Positive (12-Dec-18)	1)CARE AA-; Stable (11-Jul-17)

					(Under Credit watch with Developing Implications) (13-Aug-20) 3)CARE A+; Negative (12-May-20) 4)CARE AA-; Negative (17-Apr-20)			
8.	Fund-based - ST-Term loan	ST	-	-	-	-	1)Withdrawn (12-Dec-18)	1)CARE A1+ (11-Jul-17)
9.	Commercial Paper	ST	-	-	1)Withdrawn (06-Aug-20) 2)CARE A2+ (12-May-20) 3)CARE A1+ (17-Apr-20)	1)CARE A1+ (24-Dec-19) 2)CARE A1+ (23-Aug-19)	1)CARE A1+ (12-Dec-18)	-
10.	Commercial Paper	ST	-	-	1)Withdrawn (06-Aug-20) 2)CARE A2+ (12-May-20) 3)CARE A1+ (17-Apr-20)	1)CARE A1+ (24-Dec-19) 2)CARE A1+ (23-Aug-19)	-	-
11.	Debentures-Non Convertible Debentures	LT	350.00	CARE D	1)CARE BB (Under Credit watch with Negative Implications) (15-Oct-20) 2)CARE BBB (Under Credit watch with Developing Implications) (13-Aug-20) 3)CARE A+; Negative (12-May-20) 4)CARE AA-; Negative (17-Apr-20)	1)CARE AA-; Positive (24-Dec-19)	1)CARE AA-; Positive (12-Dec-18)	1)CARE AA-; Stable (11-Jul-17)

Annexure-3: Name of the companies consolidated with FLFL

Name of the Company	Relationship	Ownership as on March 31, 2019
Future Trendz Limited	Subsidiary	100.00%
Future Speciality Retail Limited	Subsidiary	99.96%
FLFL Business Services Limited	Subsidiary	100.00%

FLFL Travel Retail Bhubaneswar Private Limited	Joint Venture	51.00%
FLFL Travel Retail Guwahati Private Limited	Joint Venture	51.00%
FLFL Travel Retail West Private Limited	Joint Venture	51.00%
FLFL Travel Retail Lucknow Private Limited	Joint Venture	51.00%
FLFL Lifestyle Brands Limited	Joint Venture	49.02%
Clarks Future Footwear Private Limited	Joint Venture	1.00%
Holii Accessories Private Limited	Joint Venture	1.00%

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

Sr. No.	Name of the Instrument	Complexity Level
1	Debentures-Non Convertible Debentures	Simple
2	Fund-based - LT-Cash Credit	Simple
3	Fund-based - LT-Term Loan	Simple
4	Non-fund-based - ST-Working Capital Limits	Simple

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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