Future Retail Limited

May 13, 2020

Ratings

Bank Facilities	Amount (Rs. crore)	Rating	Rating Action
Long-term - Term Loan	528.00	**CARE A- (Single A Minus) (Credit watch with negative implications)**	**Revised from CARE A+ (Single A Plus) Continues to be on credit watch with negative implications**
Long-term fund based bank facilities – CC	3250.00		
Short-term non-fund based bank facilities – LC/BG	2500.00	**CARE A2+ (A Two Plus) (Credit watch with negative implications)**	**Revised from CARE A1 (A One) Continues to be on credit watch with negative implications**
Total	**6,278.00 (Rs. Six thousand two hundred seventy eight crore only)**		
Non-Convertible Debenture Issue	199.00	**CARE A- (Single A Minus) (Credit watch with negative implications)**	**Revised from CARE A+ (Single A Plus) Continues to be on credit watch with negative implications**
Proposed Non-Convertible Debenture Issue	100.00		
Commercial Paper Issue	750.00	**CARE A2 (A Two) (Credit watch with negative implications)**	**Revised from CARE A1 (A One) Continues to be on credit watch with negative implications**
Commercial Paper Issue*	650.00	**CARE A2+ (A Two Plus) (Credit watch with negative implications)**	
Fixed Deposit Programme	700.00	**CARE A- (FD) (Single A Minus) (Credit watch with negative implications)**	**Revised from CARE A+ (FD) (Single A Plus) Continues to be on 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 Retail Ltd. (FRL) factors in weakening of business and financial risk profile on account of extended lockdown due to COVID19. CARE expects the recovery to be slow and gradual on account of extension of lockdown and given the discretionary spend by the customers towards non-essential items. FRL is currently been able to sell only lower margin essential items which has resulted in substantial decline in its monthly sales in March and April 2020.

The consumers are likely to curtail their discretionary spending with reduced income 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 omni-channel strategy with presence in both offline and online channels are expected to have a quicker recovery. Tie up with Amazon to increase its online presence and Big Bazaar, FBB positioned as 'Value For Money' is expected benefit FRL in faster recovery.

The ratings, however, continues to factor significant experience of promoters in retail industry. The ratings also derive strength from FRL's proven track record with a leading position in the organized retail business in India, pan-India presence across multiple formats and stable operational performance.

The rating strengths are tempered due to increase in debt levels, significant decline in market capitalisation which along with high promoter pledge is expected to significantly impact financial flexibility, high working capital cycle, refinancing risk and the intense competition in retail industry.

FRL is seeking a moratorium on payments from its lenders as part of the COVID19 - Regulatory Package announced by the RBI on March 27, 2020. As informed to CARE, in the anticipation of the said approval following the regulatory package by RBI some of the scheduled repayments were deferred by the company as at March 31, 2020. CARE has not recognised this instance as a Default as of now, as the same is permitted by the RBI as part of the relief measures announced recently. As per CARE's discussion with the bankers the approval for deferment has been approved/or is in the process for approval. Non-recognition of default in this case is as per the guidance provided by the SEBI circular SEBI/HO/MIRSD/CRADT/CIR/P/2020/53 dated March 30, 2020.

The ratings continue to be placed on watch negative on account of disruption in operations due to COVID19 which could impact the business risk profile resulting in lower operating cash flow. Disruption could also lead to increase working capital requirement which may impact the liquidity position; though the company is in discussion with the banks for enhancement in working capital lines. CARE will continue to monitor the situation and will resolve the watch once the exact implication of the situation on credit profile of FRL is clear.

Key Rating Sensitivities
Positive Factors

- Improvement in capital structure through divestment/equity infusion and reduction in debt resulting in overall gearing below 0.50x
- Stronger-than-anticipated business performance due to faster ramp-up of stores and/or due to savings in lease outflow while improving profitability between 8-10% and debt to EBITDA of 1.50x on a sustained basis
- Significant reduction in promoter pledge
- Reduction in inventory holding

Negative Factors

- Deterioration in ROCE below 15%.
- Delay in working capital enhancement/equity infusion resulting in stretch in liquidity
- Lower than anticipated increase in sales post end of lockdown

Detailed description of the key rating drivers
Key Rating Strengths
Experienced Promoters & Management: The promoters of FRL have been closely involved in the management of business and in defining & monitoring the business strategy for the company. Mr. Kishore Biyani, the founder and Group CEO of the Future group, is widely recognised as a pioneer of modern retail in India. Furthermore the promoters are supported by a strong management team having significant experience in retail industry.

Established pan-India presence of various operationally profitable formats: Future group has presence in retail (value, home and electronics retail), insurance (life and non-life through JV with the Generali Group) and retail support services (through various subsidiaries).
FRL is one of the leading retailers in India and occupies total retail space of 16.05msf as on Dec 31, 2019. Aggregately, the Future group has pan India presence in value retailing (Big Bazaar, Food Bazaar, Easyday, Nilgiris), lifestyle (Central, Brand Factory) & home retailing (HomeTown, eZone) and across various price points. The large scale of operations of Future group provides greater bargaining power with various suppliers & real estate developers.

Stable Operational Performance; moderation on account of COVID19 outbreak: The footfalls increased to 350 million in FY19 as compared to 340 million in FY18. Also, the conversion ratio increased to 66% in FY19 from 53% in FY18.
During FY19, FRL registered PBILDT and PAT of Rs. 1142 crore and Rs. 733 crore respectively on total operating income of Rs. 20183 crore as against PBILDT and PAT of Rs. 919 crore and Rs. 11 crore respectively on total operating income of Rs. 18492 crore. PBILDT margin improved to 5.66% as against 4.97% in FY18. The improvement in operating profits was on account of better same store sales growth, turnaround of convenience store (Easy Day), demerger of low margin hometown segment and rationalisation of E-Zone stores.
Post lifting of lockdown CARE expects recovery to be slow and gradual which is likely to result in moderation in operational as well as financial performance.

Divestment of stake in Future Coupons Limited (FCL): A promoter company, FCL, has entered into a share subscription agreement and shareholders' agreement with Amazon.com NV Investment Holdings LLC. Pursuant to these agreements, Amazon has made an equity investment in FCL for acquiring a 49% stake (Rs. ~1,500 crore) comprising both voting and non-voting shares. The funds raised through divestment has been infused in FRL and the same has been used for working capital requirements.

Acquisition of assets from FEL to be margin accretive; albeit leading to higher debt: Subsequent, to the equity infusion from Amazon, FRL raised USD 500mn (Rs. 3,560 crore) through debt which are to be utilised towards acquisition of retail infrastructure assets up to Rs. 4,000 crore of FEL in one or more tranches and deleverage FEL's balance sheet.
During FY19, the total lease outflow to FEL was Rs. 694.23 crore as against Rs. 759.40 crore in FY18. Post the completion of the transaction, FRL is expected to save Rs. 550-650 crore on lease rentals annually which will result in reduction of operating costs.

Raising fresh debt to fund the transaction has led to deterioration of capital structure. However, the ability of the company to achieve the envisaged margin accretion while maintaining the growth and profitability as envisaged remains the key rating monitorable.

Robust supply chain infrastructure in place: The company's inventory management module operates on state of art ERP system that is SAP R3. The sophisticated inventory management tools in the SAP allows the company to monitor, manage and control the inventory levels. This helps the company to manage the flow of inventory efficiently. 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. FRL 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.

Increase in reliance on group companies for purchase of goods & services; support to group company in terms of corporate guarantee: FRL's reliance on its group companies has shown an increasing trend from sourcing 8% of its total requirements in FY17 to 32% in FY19.
FRL is reliant on Future Enterprises Limited as it rents its retail assets from the latter (FY19: Lease rental Rs. 694 crore) and for purchasing goods (FY19: Rs. 3,142 crore). The company's warehousing and logistic requirements are managed by Future Supply Chain Solutions Limited (FY19: Rs. 557.88 crore).
Furthermore, FEL and FRL have also provided cross guarantees on behalf of each other for various borrowings to the tune of Rs. 5750 crore and Rs. 3583 crore respectively as on March 31, 2019.
Going ahead, with the proposed acquisition of retail assets from FEL, FRL's reliance on FEL is expected to come down and cross corporate guarantees between both the companies will also eventually be withdrawn.

Deterioration of debt coverage ratios; to accelerate due to COVID19: The overall gearing deteriorated to 1.30x as on March 31, 2019 from 1.19x as on March 31, 2018 on account of significant increase in working capital borrowings. Total debt to PBILDT and Interest coverage ratio remained broadly stable to 3.73x and 3.77x as against 3.32x and 3.68x respectively. Further, on account of launch of various private brands (in fashion and food category) and store addition of Easyday and Heritage, the company has invested in the base working capital requirement leading to high working capital levels.
Capital structure further deteriorated on account of higher debt raised to acquire lease assets from FEL, opening of new stores and increase in working capital requirements. Debt as on Feb 29, 2020 stood at Rs.7,241 crore (excl. acceptances on LC) as against Rs.2,657 crore as on Mar 31, 2019.
Average working capital utilisation including CP remained high at 83.64% for the past 12 months ending Feb-20.
Total scheduled term loan repayments over the next 2 years aggregate to Rs. 298.30 crore The Company's operations have been disrupted on account of COVID19 and is allowed to sell only essential grocery items which has resulted in weakening in its operating cash flows. Reduced cash flows and significant reliance on debt to fund its working capital requirements and meet its payment obligations, the company's capital structure and debt protection metrics are expected to deteriorate further.

Deterioration in financial flexibility; considerable promoters' stake pledged: The promoters of FRL as of Sep 2018 had pledged 10.76 crore shares (46.03% of promoter stake) towards debt raised at promoter level. During the past year, the company's market capitalisation has declined significantly from Rs. 25,380 crore to Rs. 4,430 crore as on May 11, 2020. Falling market capitalisation coupled with rising debt has led to significant deterioration of debt to market-capitalisation from 0.11x as on March 31, 2018 to 0.19x as on March 31, 2019 to current level of ~1.97x.
However, in lieu of significant fall in share price, the promoters had to pledge additional shares taking the total to 52.28% of promoters' stake (as on Jan 6, 2020). As per the management, post the current steep fall in share prices, promoters' pledged stake as increased to ~90%.
Considerable reduction in market capitalisation and significant proportion of promoter's stake pledged hampers the company's flexibility to raise funds.

High Working Capital Cycle: FRL has low collection period which is inherent in the industry, however the inventory days are higher on account of bought out stock arrangement for its inventory which leads to higher working capital requirement. Inventory days have increased from 79 in FY17 to 85 in FY18 and 91 in FY19. Increase in inventory days and growth in operations has led to an increase in company's fund based average working capital utilisation (including CP) for the past 12 months ending Feb-20 to 83.64% as against 57.99% during the same period last year. The company's cash flow from operations was negative in FY19 and H1FY20.

Intensifying competition: Heightened competition from both brick and mortar and online players could impact overall SSSG of FRL. Competition from e-commerce players, remains a key threat. Also, change in FDI norms can lead to further competition. Currently, the government has allowed FDI in food processing sector. Apart from this, the government is also contemplating liberalising rules relating to multi-brand retail. This will open up foreign investments which may pose a threat to existing retail players like FRL, etc.

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 Position: Stretched

The company's liquidity has been severely impacted on account of lockdown measures. The company has applied to the lenders for moratorium as per RBI package. The company has applied to the bankers for enhancement in working capital limits and COVID19 emergency lines. Some banks have already released the additional working capital limits. The company has short term obligation of approximately Rs. 2,100-2,200 crore (incl. LC payments) due in May and June which is required to be refinanced. The timely release of additional working capital limits remains critical for meeting the short term repayment obligations .The company is also discussion for equity infusion which remains critical from liquidity perspective.

Analytical approach: Standalone, factoring the debt of FEL guaranteed by FRL.

Applicable Criteria

Criteria on assigning 'outlook' and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology: Factoring Linkages in Ratings
Rating Methodology: Organised Retail Companies
Financial ratios – Non-Financial Sector

About the Company

Future Retail Limited is the flagship company of the Future Group (one of India's leading retailers) and is engaged mainly in home & electronics retailing and value retailing. The company operates Big Bazaar, Easy Day, Foodhall among other format stores.

FRL as on Dec 31, 2019 operates 1,338 stores across 414 cities with retail space of 16.05msf. The company has signed a master franchise agreement with 7-Eleven, the world's largest convenience store chain, that will open and manage the brand stores in India. Future Retail's subsidiary SHME Food Brands will open newer stores as well as convert existing locations to the 7-Eleven brand. The project is currently under pilot stage.

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	18492	20183
PBILDT	919	1142
PAT	11	733
Overall gearing (times)	1.19	1.30
Interest coverage (times)	3.66	3.78

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

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
Non-fund-based - ST-BG/LC	-	-	-	2500.00	CARE A2+ (Under Credit watch with Negative Implications)
Fund-based - LT-Working Capital Limits	-	-	-	3250.00	CARE A- (Under Credit watch with Negative Implications)
Fund-based - LT-Term Loan	-	-	Aug 2024	528.00	CARE A- (Under Credit watch with Negative Implications)
Debentures-Non Convertible Debentures INE752P07013	03-Jun-19	10.65%	03-Jun-22	100.00	CARE A- (Under Credit watch with Negative Implications)
Debentures-Non Convertible Debentures INE752P07021	03-Jun-19	10.65%	03-Jun-23	99.00	CARE A- (Under Credit watch with Negative Implications)
Debentures-Non Convertible Debentures	April 30, 2019	10%	April, 2025	100.00	CARE A- (Under Credit watch with Negative Implications)
Fixed Deposit	-	-	-	700.00	CARE A- (FD) (Under Credit watch with Negative Implications)
Commercial Paper	-	-	7 days to 364 days	650.00	CARE A2+ (Under Credit watch with Negative Implications)
Commercial Paper	-	-	7 days to 364 days	200.00	CARE A2 (Under Credit watch with Negative Implications)
Commercial Paper	-	-	7 days to 364 days	250.00	CARE A2 (Under Credit watch with Negative Implications)
Commercial Paper	-	-	7 days to 364 days	300.00	CARE A2 (Under Credit watch with Negative Implications)

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-Working Capital Limits	LT	3250.00	CARE A- (Under Credit watch with Negative Implications)	-	1)CARE A+ (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE AA-; Negative (23-Oct-19)	1)CARE AA-; Stable (03-Oct-18)	1)CARE AA-; Stable (12-Oct-17) 2)CARE AA-; Stable (17-Aug-17) 3)CARE AA-; Stable (05-May-17)

						3)CARE AA-; Negative (23-Jul-19)		
2.	Commercial Paper	ST	650.00	CARE A2+ (Under Credit watch with Negative Implications)	-	1)CARE A1 (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE A1+ (23-Oct-19) 3)CARE A1+ (23-Jul-19)	1)CARE A1+ (18-Jan-19) 2)CARE A1+ (03-Oct-18)	1)CARE A1+ (12-Oct-17) 2)CARE A1+ (20-Sep-17) 3)CARE A1+ (17-Aug-17) 4)CARE A1+ (05-May-17)
3.	Non-fund-based - ST-BG/LC	ST	2500.00	CARE A2+ (Under Credit watch with Negative Implications)	-	1)CARE A1 (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE A1+ (23-Oct-19) 3)CARE A1+ (23-Jul-19)	1)CARE A1+ (03-Oct-18)	1)CARE A1+ (12-Oct-17) 2)CARE A1+ (17-Aug-17) 3)CARE A1+ (05-May-17)
4.	Commercial Paper	ST	200.00	CARE A2 (Under Credit watch with Negative Implications)	-	1)CARE A1 (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE A1+ (23-Oct-19) 3)CARE A1+ (23-Jul-19)	1)CARE A1+ (18-Jan-19) 2)CARE A1+ (03-Oct-18)	1)CARE A1+ (20-Nov-17) 2)CARE A1+ (12-Oct-17) 3)CARE A1+ (20-Sep-17) 4)CARE A1+ (17-Aug-17) 5)CARE A1+ (05-May-17)
5.	Commercial Paper	ST	250.00	CARE A2 (Under Credit watch with Negative Implications)	-	1)CARE A1 (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE A1+ (23-Oct-19) 3)CARE A1+ (23-Jul-19)	1)CARE A1+ (18-Jan-19) 2)CARE A1+ (03-Oct-18)	1)CARE A1+ (20-Nov-17) 2)CARE A1+ (12-Oct-17) 3)CARE A1+ (20-Sep-17) 4)CARE A1+ (17-Aug-17) 5)CARE A1+ (05-May-17) 6)CARE A1+ (20-Apr-17)
6.	Commercial Paper	ST	300.00	CARE A2 (Under Credit watch with Negative Implications)	-	1)CARE A1 (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE A1+ (23-Oct-19)	1)CARE A1+ (18-Jan-19) 2)CARE A1+ (03-Oct-18)	1)CARE A1+ (20-Nov-17)

						3)CARE A1+ (23-Jul-19)		
7.	Fund-based - LT-Term Loan	LT	528.00	CARE A- (Under Credit watch with Negative Implications)	-	1)CARE A+ (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE AA-; Negative (23-Oct-19) 3)CARE AA-; Negative (23-Jul-19)	1)CARE AA-; Stable (14-Mar-19) 2)CARE AA-; Stable (03-Oct-18)	1)CARE AA-; Stable (20-Nov-17)
8.	Fixed Deposit	LT	700.00	CARE A- (FD) (Under Credit watch with Negative Implications)	-	1)CARE A+ (FD) (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE AA- (FD); Negative (23-Oct-19) 3)CARE AA- (FD); Negative (23-Jul-19)	1)CARE AA- (FD); Stable (14-Nov-18)	-
9.	Debentures-Non Convertible Debentures	LT	199.00	CARE A- (Under Credit watch with Negative Implications)	-	1)CARE A+ (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE AA-; Negative (23-Oct-19) 3)CARE AA-; Negative (23-Jul-19)	1)CARE AA-; Stable (14-Mar-19)	-
10.	Debentures-Non Convertible Debentures	LT	100.00	CARE A- (Under Credit watch with Negative Implications)	-	1)CARE A+ (Under Credit watch with Negative Implications) (26-Mar-20) 2)CARE AA-; Negative (23-Oct-19) 3)CARE AA-; Negative (23-Jul-19)	1)CARE AA-; Stable (14-Mar-19)	-

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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