Liberty Shoes Limited

October 08, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating[1]	Rating Action
Long Term Bank Facilities	6.50	CARE BBB+; Stable (Triple B Plus; Outlook: Stable)	Assigned
Long Term Bank Facilities	165.40 (Enhanced from 135.00)	CARE BBB+; Stable (Triple B Plus; Outlook: Stable)	Revised from CARE A-; Negative (Single A Minus; Outlook: Negative) and outlook revised from negative
Short Term Bank Facilities	63.50 (Enhanced from 47.64)	CARE A2 (A Two)	Revised from CARE A2+ (A Two Plus)
Total Facilities	235.40 (Rs. Two Hundred Thirty-Five Crore and Forty Lakhs Only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities of Liberty Shoes Limited (LSL) takes into account elongated collection period and subdued operational performance of the company during Q1FY21 (refers to the period: April 01 to June 30) as reflected in sharp drop in sales and cash losses reported due to outbreak of Covid-19 pandemic adversely impacting the footwear and fashion industry with limited revenue visibility to recoup the operating losses during the remainder of the current year. The ratings are further constrained by low profitability margins, highly fragmented and competitive nature of the footwear industry and susceptibility of margins to volatility in raw material prices. The ratings continue to derive comfort from the long-track record of its promoters and established market position of LSL in domestic footwear industry. The ratings also factors in established brand image of the company, wide distribution network, comfortable capital structure and geographically diversified revenue stream.

Rating Sensitivities

Positive:

- Reduction in receivables below Rs. 90 crores on a sustained basis.
- Improvement in the PAT margin above 2.00% on a sustained basis and improved liquidity leading to lower dependence on working capital limits.

Negative:

- Decline in PBILDT margin below 6% on a sustained basis.
- Deterioration in operating cycle leading to stretched liquidity

Detailed description of the key rating drivers

Key Rating Strengths

Experienced promoters and management team

LSL is the flagship company of the Karnal (Haryana) based Liberty Group. The group is promoted by the Gupta and Bansal family and is engaged in footwear business for last six decades. The company is led by Mr. Adesh Kumar Gupta (Chief Executive Officer), who pioneered the use of Poly-urethane (PU) technology in the Indian footwear market. Mr. Gupta has more than three decades of experience in the footwear industry and is assisted by a management team having rich experience in the same line of business.

Reputed brand name and established position in Indian footwear industry

LSL has diversified product portfolio and enjoys good brand name in the footwear industry, which stems from the long successful track record. The company has wide spread presence in North India with increasing footprints in Southern part. LSL is spending substantially on the branding and promotional activities related to all its brands and also initial

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

marketing of fine fragrance products (Liberty Lifestyle). LSL has also developed number of popular sub brands such as Fortune, Warrior, Windsor, Senorita, Tiptop, Footfun, Prefect, Force-10, Gliders, Coolers, Aha, Leap7x, Healers and Lucy & Luke.

Widespread and diverse distribution network
LSL has wide and established distribution network comprising of about 150 distributors and 591 exclusive showrooms as on June 30, 2020 (both franchised and owned) spread across the country. LSL's sales are well diversified in terms of geography in North, South, East and West part of India with major contribution from North India. The company drives sales mainly from four channels viz. distributors, exclusive showrooms (franchised and company owned) and Institutional sales and is not highly dependent on any one of them. However, proportion of institutional sales is expected be higher in FY21 (refers to the period: April 01 to March 31) as retail sales got significantly impacted due to Covid-19 pandemic.

Comfortable capital structure albeit moderation in the overall gearing
The capital structure of LSL has been comfortable on account of high net-worth base owing to accretion of profits over the years. The overall gearing of the company stood at 1.25x as on March 31, 2020 from 0.65x as on March 31, 2019. The deterioration is mainly due to recognition of lease obligation as liability under IND AS 116 coupled with higher working capital utilization as on March 31, 2020. Consequently, total debt to GCA of the company also deteriorated to 9.46x for FY21 from 5.61 in FY19. The interest coverage ratio of the company has improved marginally to 2.88x for FY20 from 2.83x during FY19.

Key Rating Weaknesses
Declining profitability margins and weak operational performance during Q1FY21
The PBILDT margin of the company has further moderated to 6.32% in FY20 from 7.46% in FY18 (FY19: 6.95%) on account of increase in commission and freight outward charges. Further, the higher contribution from shoes in the lower price band led to a lower yield during FY20. PAT margin of the company improved to 1.69% in FY20 from 1.14% in FY19 mainly due to exceptional gain from sale of fixed assets of Dehradun plant. LSL reported total operating income of Rs. 652.50 crore for FY20 (PY: Rs. 602.78 crore). The operations of the company were severely impacted due Covid-19 lockdown resulting in lower total operating income of Rs. 51.35 crore in Q1FY21 against Rs. 168.25 crore in Q1FY20. The company has also reported net loss of Rs. 10.89 crore during Q1FY21. The stores sales (franchised and owned) contribute around 50% of the total operating income and the recovery marked by increase in footfall, conversion rate and growth in scale along with improvement in average selling price (ASP) shall be critical for the company to recoup the cash losses during Q1FY21 and full year recovery after having witnessed moderation in operations during H1FY21 (refers to the period from April 1 to September 30). In terms of institutional sales, the company has revenue visibility with sales orders to the tune of Rs.200 crore to be executed during H2FY21 (refers to the period from October 1 to March 31).

Elongated Inventory holding and collection period
The inventory holding period of the company stood high at 126 days in FY20 (PY: 127 days). The company has to maintain wide variety of inventory of finished goods across product category which results in high inventory holding for 100-120 days to meet any sudden spike in demand of a particular product. Consequently, the operating cycle of the company also stood high at 120 days in FY20 (PY: 120 days). Further, collection period of the company also elongated from 61 days in FY19 to 85 days in FY20 on account of dues from state government orders.

Susceptibility of margins to the volatility in the raw material prices and foreign exchange fluctuations
The main raw materials for LSL are PVC (Polyvinyl Chloride), Leather, PU Chemicals etc., the prices of which are linked with crude oil prices and remain volatile. LSL's profitability depends to a large extent on the movement in raw material prices. With intense competition in the footwear segment mainly on account of significant presence of the unorganized sector and availability of cheap imported products, it is not always possible to pass on the entire increase in raw material prices to the customers, which puts pressure on the company's profitability.

Fragmented and highly competitive industry
The domestic footwear industry is fragmented and is characterised by large number of unorganised players. The unorganised segment gains prominence in the Indian context due to its price competitive products, which are more suitable and attractive to the price conscious Indian consumer. But with increased household income, shifting consumer behaviour from saving to spending, increasing brand consciousness amongst Indian consumers, influx of

large number of global brands and penetration in tier – II and III cities by footwear companies, the organised retail in footwear market is rapidly evolving and expected to grow at a higher rate in the future.

Prospects

India is the third largest footwear consuming country in the world after China and USA, India is the second largest footwear producer in the world, with footwear production accounting for approximately 13 per cent of the global annual production – 16 billion pairs as compared to China, which produces over 60 per cent of the global production. However, the operational performance of the companies in footwear has been severely impacted post March 2020 as a result of outbreak of global pandemic given the closure of retail outlets and malls during the period of lockdown. Going forward, the recovery in demand is expected to be slow owing to closure of educational institutes, offices working on reduced staff strength, curtailed discretionary spending and weak consumer sentiments. The prospects of the company shall be governed by its ability to increase institutional sales in the interim period and ability to gradually increase digital footprints through online sales to compensate for loss of revenue due to lower footfall.

Liquidity: Adequate

The liquidity profile of the company derive comfort from unutilized fund based working capital limits of ~Rs. 43.40 crore (includes ad-hoc limits of Rs. 30.00 crore sanctioned to the company) as on September 28, 2020. The company has been granted moratorium for payment of interest from April to August, 2020 by one of its lender. The current ratio of the company stood comfortable at 1.31x (PY: 1.43x). The company generated cash accruals of Rs. 24.52 crore during FY20 against very minimal amount of scheduled debt repayment of Rs. 1.92 crore in FY20. There is no major capital expenditure planned except miniscule amount of repair and maintenance which will be funded through internal accruals. Its moderate cash accruals and unutilized bank limits provide it a cushion against fund mismatches, if any, as well as any adverse market scenarios. Average utilization of fund based working capital limits for the twelve months ending July, 2020 stood high at ~86%.

Analytical approach: Standalone

Applicable Criteria

Criteria on assigning 'outlook 'and 'credit watch' to Credit Ratings
CARE's Policy on Default Recognition
Rating Methodology-Manufacturing Companies
Criteria for Short Term Instruments
Financial ratios – Non-Financial Sector
Liquidity Analysis of Non-Financial Sector Entities

About the Company

Incorporated in September, 1986, LSL is the flagship company of the Karnal (Haryana) based Liberty Group. The group has presence in Indian footwear industry for the last six decades. LSL is engaged in the business of manufacturing and selling leather and non-leather footwear. The company has five manufacturing facilities located at Karnal (Haryana), Gharaunda (Haryana), Liberty Puram (Haryana), Paonta Sahib (Himachal Pradesh) and Roorkee (Uttarakhand) having a combined capacity of manufacturing 106 Lakh pairs of shoes per annum as on June 30, 2020. LSL sells its merchandise through its pan India distribution network.

Brief Financials (Rs. crore)	FY19 (A)	FY20 (A)
Total operating income	602.78	652.50
PBILDT	41.89	41.22
PAT	6.84	11.00
Overall gearing (times)	0.65	1.25
Interest coverage (times)	2.83	2.88

A: Audited

Status of non-cooperation with previous CRA: Nil

Any other information: NA

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

Covenants of rated instrument / facility: *Detailed explanation of covenants of the rated instruments/facilities is given in Annexure-3*

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

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-Cash Credit	-	-	-	165.40	CARE BBB+; Stable
Non-fund-based - ST-BG/LC	-	-	-	63.50	CARE A2
Fund-based - LT-Proposed fund based limits	-	-	-	6.50	CARE BBB+; Stable

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	-	-	-	1)Withdrawn (31-Mar-20)	1)CARE A-; Stable (07-Jan-19) 2)CARE A-; Stable (29-Jun-18)	1)CARE A-; Stable (04-Jan-18)
2.	Fund-based - LT-Cash Credit	LT	165.40	CARE BBB+; Stable	1)CARE A-; Negative (29-Apr-20)	1)CARE A-; Stable (31-Mar-20)	1)CARE A-; Stable (07-Jan-19) 2)CARE A-; Stable (29-Jun-18)	1)CARE A-; Stable (04-Jan-18)
3.	Non-fund-based - ST-BG/LC	ST	63.50	CARE A2	1)CARE A2+ (29-Apr-20)	1)CARE A2+ (31-Mar-20)	1)CARE A2+ (07-Jan-19) 2)CARE A2+ (29-Jun-18)	1)CARE A2+ (04-Jan-18)
4.	Fund-based - LT-Proposed fund based limits	LT	6.50	CARE BBB+; Stable	-	-	-	-

Annexure-3: Detailed explanation of covenants of the rated instrument / facilities: Nil

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

Sr. No.	Name of the Instrument	Complexity Level
1.	Fund-based - LT-Cash Credit	Simple
2.	Non-fund-based - ST-BG/LC	Simple

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

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