

Liberty Shoes Limited

April 29, 2020

Ratings

Facilities	Amount (Rs. crore)	Rating ¹	Rating Action
Long-term Bank Facilities	135.00	CARE A-; Negative (Single A Minus; Outlook: Negative)	Reaffirmed; Outlook Revised from Stable to Negative
Short term Bank Facilities	47.64	CARE A2+ (A Two Plus)	Reaffirmed
Total	182.64 (Rupees one hundred eighty two crore and sixty four lakh only)		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Liberty Shoes Limited (LSL) continue to derive comfort from the long-track record of its promoters and strong 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. These strengths are however, partially offset by moderation in profitability margins, its susceptibility to the volatility in the raw material prices, highly fragmented and competitive nature of the footwear industry, and elongated inventory holding period.

Rating Sensitivities

Positive:

- Increase in Total Operating Income above Rs. 800 crore, PBILDT margin above 9% and PAT margin above 2.5% on a sustainable basis.

Negative:

- Decline in Total Operating Income below Rs.550 crore and PBILDT margin below 6% on a sustained basis.
- Deterioration in capital structure with overall gearing ratio deteriorating beyond 1.00x on a sustained basis.

Outlook: Negative

The outlook has been revised to 'Negative' as CARE Expects LSL's liquidation position to remain stretched amid loss of income and cash flows due to lockdown which may lead to reliance on external debt to meet its fixed obligations. The outlook may be revised to 'Stable' in case the company is able to revive growth in business, improve its profitability, cash flows and resultantly the liquidity position.

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 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 strong 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 promotion activities related to all its brands and also initial 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 600 exclusive showrooms as on December 31, 2019 (both franchised and owned) spread across the country. LSL's sales are well diversified in terms of

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

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.

Comfortable capital structure

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 improved from 0.99x as on March 31, 2017 to 0.65x as on March 31, 2019 (March 31, 2018: 0.72x). The interest coverage ratio of the company has improved to 2.83x in FY19 as compared to 2.60x in FY18 and 2.44x in FY17. The improvement in the interest coverage ratio and overall gearing is on the back of decrease in term debt and unsecured loans.

Key Rating Weaknesses

Moderation in profitability margins

The PBILDT margin of the company has moderated to 6.95% in FY19 from 7.46% in FY18 mainly on account of increase in the advertisement cost and commission paid to the franchisee. The high advertisement cost incurred mainly towards the newly introduced fine fragrance brand "Liberty Lifestyle". Further, the contribution of the low price shoes remained considerable during FY19 and 9MFY20, the margin from these shoes are comparatively low resulting in low overall margins albeit improving total revenue.

Elongated Inventory holding period

The inventory holding period of the company stood at 127 days in FY19 (PY: 134 days). The company has to maintain 100-120 days of inventory to meet any sudden spike in demand of a particular product, the company has to maintain wide variety of inventory of finished goods across product category which results in high inventory. Consequently, the operating cycle of the company also stood high at 120 days (PY: 130 days).

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/Industry Outlook (Source: msme.gov.in)

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. 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. The outbreak of COVID-19 has impacted the sales of the company as the revenue from stores (both owned and franchisee) has reduced for the month of March 2020, as all the malls and markets were closed.

Liquidity: Stretched

The temporary closure of business operations due to lockdown has squeezed LSL's liquidity with un-availed working capital limits reducing to around 10% as on April 19, 2020. The company has also curtailed non-essential expenditure to conserve cash through various initiatives including deferred payments to vendors and prudent measures to meet fixed overheads including rentals and salaries. It has applied to some of its working capital lenders for a moratorium in line extant RBI guidelines. Further the company has also been sanctioned ad-hoc working capital limit to the tune of Rs.6.50 crore (yet to be disbursed pending documentation). A prolonged lockdown and delay in resumption of business operations may further stretch the company's liquidity position and hence it shall remain key monitorable.

Analytical approach: Standalone

Applicable Criteria

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

[Criteria for Short Term Instruments](#)

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

[Rating Methodology-Manufacturing Companies](#)

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

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. LSL sells its merchandise through its pan India distribution network.

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

Brief Financials (Rs. crore)	FY18 (A)	FY19 (A)
Total operating income	544.36	602.78
PBILD	40.62	41.89
PAT	6.60	6.84
Overall gearing (times)	0.72	0.65
Interest coverage (times)	2.60	2.83

A: Audited

Status of non-cooperation with previous CRA: Nil

Any other information: NA

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-Cash Credit	-	-	-	135.00	CARE A-; Negative
Non-fund-based - ST-BG/LC	-	-	-	47.64	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 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	135.00	CARE A-; Negative	-	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	47.64	CARE A2+	-	1)CARE A2+ (31-Mar-20)	1)CARE A2+ (07-Jan-19) 2)CARE A2+ (29-Jun-18)	1)CARE A2+ (04-Jan-18)

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

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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