Sharma Industries (Jodhpur)

November 18, 2019

Ratings

Facilities	**Amount (Rs. crore)**	**Ratings[1]**	**Rating Action**
Long-term Bank Facilities	11.48	**CARE BBB; Stable (Triple B; Outlook: Stable)**	**Reaffirmed**
Short-term Bank Facilities	3.00	**CARE A3+ (A Three Plus)**	**Reaffirmed**
Total	**14.48 (Rupees Fourteen crore and forty-eight lakh only)**		

Details of instruments/facilities in Annexure-1

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Sharma Industries (Jodhpur) continue to derive strength from experienced and qualified management and its established track record of operations with renowned customer. The ratings, further, continue to derive strength from its healthy profitability margins, comfortable solvency position owing to moderate net-worth base as well as comfortable liquidity position.

These strength, however, continue to offset partially on account of its modest scale of operations with geographical and customer concentration risk in a competitive and fragmented nature of wooden industry, its constitution as a partnership concern and vulnerability of margins to raw material prices and foreign exchange rate. The ratings are, further, constrained on account of project implementation risk.

Rating Sensitivity

Positive Factors

- Sustained increase in scale of operations of the company with geographical and customer diversification
- Change in constitution from partnership concern to company resulting in eliminating the inherent risk of withdrawal of capital and dissolution of the firm
- Sustained improvement/maintaining of profitability margins over a period of time

Negative factors

- Any debt-funded project undertaken by the firm or withdrawal of capital by the partners which results in deterioration of solvency position
- Any deterioration in profitability due to foreign exchange rate fluctuation
- Any decrease in orders from its single customer

Detailed description of the key rating drivers

Key Rating Strength

Experienced and qualified management

Mr. Praveen Sharma and Mr. Manoj Sharma are graduates by qualification and have more than two decades of experience in the handicraft industry. Both look after the overall affairs of the firm. Further, each department of SIJ is looked after by experienced and qualified personnel. The tier-two management is supported by more than 100 employees to help the management to work efficiently and effectively.

Established track record of operations with renowned customer

Being present in the industry since 1982, the firm has established track record of operations in the handicraft industry. The firm generated 99% of its net sale in handicraft division from sale to Maisons Du Monde (MDM), France in FY19. The firm has a more than two decade of relationship with MDM and hence, continuously receives order from MDM. As on October 10, 2019, the firm has an order book position of USD $ 24,00,000 till December, 2019.

Increase in Total Operating Income (TOI) in FY19 although stood modest with customer and geographical concentration risk

During FY19, TOI of the firm has increased significantly by 29.10% over FY18 mainly due to increase in its product range by providing more variety in Chairs, wardrobe and other wooden items which ultimately increased its orders from MDM, France.

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

Further, the firm generated 77.45% of its TOI from handicraft division (75.13% in FY18) and 12.01% from power division in FY19 (16.17% in FY18) and balance relates to duty drawback as well as export incentive income and interest income on FDR (Rs.8.47 crore in FY19 as against Rs.6.58 crore in FY18). Furthermore, PBT margin for Handicraft division including other income stood at 22.85% in FY19 (against 27.38% in FY18) and PBT margin for power division stood at 72.39% in FY19 (against 33.10% in FY18). Till September 30, 2019, it has achieved TOI of Rs.28.10 crore from handicraft division.
The clientele base of the firm is skewed with MDM as the firm generates more than 95% of its income from MDM. This increases its dependency on orders received from MDM which is saddled with increased competition in the handicraft industry and growing demands and trend for India's handicraft around the world.

Healthy profitability margins with comfortable cash accruals
The profitability margins remained healthy with PBILDT and PAT margin of 37.61% and 21.75% respectively during FY19 as against 39.97% and 20.91% respectively in FY18. PBILDT margin of SIJ has witnessed continuous decreasing trend owing to higher raw material cost and job work and freight charges. Further, the firm registered a loss from foreign exchange of Rs.0.48 crore in FY19 as against income from exchange rate difference in FY18. Despite decrease in PBILDT margin in FY19, PAT margin has improved marginally by 83 bps in FY19 over FY18 owing to low interest and finance expenses as well as proportionate decline in depreciation cost as a percentage of TOI. Furthermore, GCA has also increased by 24.03% and remained comfortable at Rs.23.09 crore in FY19.

Comfortable solvency position owing to moderate net-worth base
Due to healthy profitability, the net-worth base of SIJ remained moderate at Rs.72.61 crore as on March 31, 2019. Due to high net-worth base along with scheduled repayment of term loans, the capital structure of SIJ remained comfortable and improved with overall gearing improved from 0.40 times as on March 31, 2018 to 0.27 times as on March 31, 2019.
Further, debt service coverage indicators of SIJ also remained comfortable with total debt to GCA of 0.86 times as on March 31, 2019, improved from 1.24 times as on March 31, 2018 mainly on account of decrease in total debt with increase in GCA level. The interest coverage ratio remained comfortable at 19.28 times in FY19.

Key Rating Weakness
Project Implementation risk
SIJ is engaged in the business of manufacturing and export of handicraft items such as furniture, giftware, and accessories in wrought iron and wood which is a labour intensive industry. Thus the expansion of space increases the capacity for its manufacturing.
The firm is continuously adding new products with new designs. During FY19, the firm undertook a project for construction of new building with prospective to increase its storage capacity amounting to Rs.1.30 crore funded through internal accruals along with increase in its product range by providing more variety in Chairs, wardrobe and other wooden items.
Further, due to increase in demand from MDM, the firm has undertaken a project for construction of pre-fabricated G+ 2 steel structures with an envisaged cost of Rs.3.50 crore which envisaged to be funded through internal accruals in current year. It is expected to be completed in next 3-4 months. Till October 18, 2019 , the firm has paid advance of Rs.3.00 crore for fabricated structure

Competitive and fragmented nature of handicraft industry along with foreign exchange fluctuation risk and its constitution as a partnership concern
The key raw materials required by the wooden handicraft industry are sheesham and mango wood which is procured by SIJ from the domestic market and processes the same to make handicrafts items. Due to competitive nature of the industry, SIJ is exposed to the risk of inability to pass on the prices of raw material to its customers. Further, the firm is exposed to foreign exchange fluctuation risk as the firm derives 100% of its revenue from the export sales. SIJ does the hedging for 30% of its orders by way of forward contract and balance is kept un-hedged which exposes it to foreign currency fluctuation risk.
Further, its constitution as a partnership concern restricts its overall financial flexibility in terms of limited access to external funds for any future expansion plans. Further, there is inherent risk of possibility of withdrawal of capital and dissolution of the firm in case of death/insolvency of partners.

Liquidity: Strong
Liquidity is marked by strong accruals against repayment obligations and liquid investments with FDR of Rs.15.18 crore (against Rs.9.75 crore as on March 31, 2018) as well as cash and bank balance of Rs.4.90 crore as on March 31, 2019. The firm has nominal average utilization of 11.11% of its fund based limit for the last 12 months ending September, 2019. Its unutilized bank lines are more than adequate to meet its incremental working capital needs over the next one year. Further, it has generated Rs.21.20 crore from cash flow from operating activities in FY19 as against Rs.4.98 crore in FY18 mainly due increase in operating profit with lower working capital gap.

Furthermore, the current ratio and quick ratio remained comfortable at 4.75 times and 4.44 times respectively as on March 31, 2019 owing to negligible creditor outstanding against high current assets. However, due to low inventory and collection period, the operating cycle of SIJ remained negative at 8 days in FY19, improved from negative 77 days in FY18 owing to decrease in creditor period. The firm has adopted just in time inventory management and thus keeps low level of inventory which ultimately reduces the cost. Further, the firm receives 100% amount in advance for the order dispatched and after the shipment of the order the amount for next order is received. As on March 31, 2019, unsecured loans amounting to Rs.4.31 crore received from MDM against such advances. Furthermore, debtors of MDM stood at Rs.0.80 crore as on March 31, 2019

Analytical approach: Standalone

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

Background of the firm
Sharma Industries (Jodhpur) (SIJ) was formed in 1982 as a partnership concern by Sharma family. Later, in 2012, the new partners namely Mr. Laxmi Narayan Sharma along with his sons Mr Praveen Sharma and Mr. Manoj Sharma were admitted to the firm and shares profit & loss in the ratio of 50:25:25. However, Mr. Laxmi Narayan Sharma passed away in the month of July, 2019 and due to this, his wife joined the firm as a new partner with share of Mr. Laxmi Narayan Sharma was transferred to his wife Mrs. Kshitiz Sharma.
SIJ is engaged in the business of manufacturing and export of handicraft items such as furniture, giftware, accessories in wrought iron and wood. The plants of the firm are located at Jodhpur. Further, the firm is also into power generation through six wind mills and four solar plants having total installed capacity of 6.65 and 10.40 Mega Watt (MW) respectively as on March 31, 2019. The firm sells power to various State Electricity Boards (SEBs) and has operation and maintenance (O&M) agreements for wind mills and solar plant.

Brief Financials (Rs. crore)	FY18(A)	FY19(A)
Total Operating Income	62.35	80.50
PBILDT	24.93	30.28
PAT	13.04	17.51
Overall gearing (times)	0.40	0.27
Interest coverage (times)	15.09	19.28

A: Audited

Status of non-cooperation with previous CRA: CRISIL has conducted the review on the basis of best available information and has classified SIJ as "Not cooperating" vide its press release dated April, 2018

Any other information: None

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	-	-	July, 2027	11.48	CARE BBB; Stable
Fund-based - ST-EPC/PSC	-	-	-	2.00	CARE A3+
Fund-based - ST-Bills discounting/ Bills purchasing	-	-	-	1.00	CARE A3+

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 2019-2020	Date(s) & Rating(s) assigned in 2018-2019	Date(s) & Rating(s) assigned in 2017-2018	Date(s) & Rating(s) assigned in 2016-2017
1.	Fund-based - LT-Term Loan	LT	11.48	CARE BBB; Stable	-	1)CARE BBB; Stable (04-Jul-18)	-	-
2.	Fund-based - ST-EPC/PSC	ST	2.00	CARE A3+	-	1)CARE A3+ (04-Jul-18)	-	-
3.	Fund-based - ST-Bills discounting/ Bills purchasing	ST	1.00	CARE A3+	-	1)CARE A3+ (04-Jul-18)	-	-

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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