ICRA

RATING METHODOLOGY - GEMS & JEWELLERY (RETAIL)

MARCH 2022

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This rating methodology describes ICRA's approach to assessing the credit risk of jewellery retailers. It aims to help issuers, investors and other market participants understand ICRA's approach to analysing risks that are likely to affect the rating outcomes of the entities in the sector. This rating methodology updates and supersedes ICRA's earlier methodology note on this subject, published in February 2020. While this revised version incorporates a few modifications, ICRA's overall approach to rating entities in the sector remains materially similar.

Overview

India is the second largest gold jewellery market after China in terms of consumption. Buoyed by various socio-economic and cultural factors, the jewellery retail industry has had a long tradition in the country. Historically, the jewellery retailing business has been carried out by a large, fragmented base of small, unorganised family-owned businesses. However, over the past decade and a half, the sector has transformed with a continued and rapid rise in organised trade. Higher transparency and compliance requirements on the back of various regulatory measures, over the years, has resulted in increased formalisation of the sector. Factors like rising disposable income, changing demographics, vast product/ design collections and enhanced shopping experiences have benefited national and regional jewellery retail chains, supporting an improvement in their market shares. Further, the larger retailers have taken efforts to enhance diversification and implement robust risk management systems, which has strengthened their businesses as they have scaled up.

While organised trade is increasing, the industry remains dominated by unorganised players that account for around 65% of the market (which has reduced from ~85%, a decade back). The industry's strong long-term fundamentals, driven by cultural underpinnings and large marketplace with a sizeable rural demand, allow room for multiple players to co-exist, leading to a fragmented base. The industry is characterised by high working capital intensity and moderate profit margins with limited product value addition, besides pricing pressures, given the intense competition. Moreover, the industry is highly exposed to commodity (gold) price and regulatory risks.

The broad list of rating factors is given below. While these do not necessarily represent an exhaustive set of factors, it provides an overall perspective to the lenders, investors and other market participants on the rating considerations that are usually the most important. For analytical convenience, the key factors are grouped under the following broad heads – Industry Risk Assessment, Business Risk Assessment, Financial Risk Assessment and other factors including an assessment of Environment, Social and Governance (ESG) risks.

ICRA's Risk Analysis Framework for Gems & Jewellery Retail Industry

The list of rating drivers covered here is not exhaustive but provides an overall perspective on the most important considerations. ICRA's risk analysis framework for jewellery retailers can be broadly divided into the following factors:

Industry Risk Assessment

- Demand-supply dynamics
- Regulatory risk
- Commodity price risks

Business Risk Assessment

- Scale of operations
- Market position and brand equity
- Operating efficiency
- Geographical diversity
- Product diversity

Financial Risk Assessment

- Profitability metrics
- Leverage, coverage and liquidity indicators
- Adequacy of future cash flows

Other Elements of Credit Risk Assessment

- Financial Flexibility
- Tenure mismatches and risks relating to interest rates and refinancing
- Foreign currency risks
- Debt servicing track record
- Accounting quality/ Contingent liabilities/ Off-balance sheet exposures
- Event Risk

Management Quality

- Quality of management
- Financial policy
- Governance structure and practices
- Parentage

Assessment of Environmental, Social and Corporate Governance Risks

Industry Risk Drivers

Demand-supply dynamics

Demand: Strong cultural affinity, favourable demographics, investment appetite for savings and rising disposable income support jewellery demand in India. Gold jewellery is an integral part of weddings, festivals and societal occasions in India, contributing to sizeable jewellery demand. Around 65% of India's population lives in rural areas and a major portion of the jewellery demand originates from the rural sector, where gold is considered an effective means of investment. A good monsoon, resulting in higher farm output, typically translates into favourable jewellery demand. Demand for value-added fashionable jewellery (like designer, light-weight, custom-made, low carat and high fabrication) has gained prominence in the recent years, largely driven by the urban, affluent population. ICRA assesses the impact of these drivers on the demand prospects for the sector.

Supply: Gold supply in India is regulated and jewellery retailers primarily rely on banking channels as well as nominated agencies for procurement of raw material, i.e. gold bullion. Despite the lack of domestic production from mines in India, the availability of gold bullion has not been a concern as these are largely supported by imports. The pricing is benchmarked according to the global prices. Nevertheless, as gold is one of the key items imported in the country, any policy decisions relating to managing the current account deficit (CAD) impacts gold supply. For example, restriction on bullion imports in 2014 (which required gold importers to re-export 20% of such imports as gold jewellery under the 20/80 scheme) had a large implication on supply-side dynamics, forcing jewellers to rely on other alternatives such as recycled gold, import of jewellery, etc. As policy measures can result in short-term supply-side concerns, diversified sourcing supports business continuity.

Regulatory risk

The jewellery retail sector is characterised by many unorganised players and involves a sizeable share of cash transactions. To curb unaccounted money amid the need for regulatory oversight, given the large share of overall imports in the country, periodic policy interventions by the Government and regulators have been seen over the years.

ICRA monitors the various regulatory/Government measures to assess the impact on demand/supply. Some of the key measures in the recent years include imposition of import duty, excise duty [now subsumed under the Goods and Service Tax (GST)], regulation on jewellery savings schemes, restriction on supply of gold metal loan (GML), disclosure of permanent account number (PAN) card details for transactions over Rs. 2.0 lakh and mandatory hallmarking among others. In this backdrop, ICRA assesses the regulatory framework and makes appropriate adjustments to the demand/supply outlook from time to time.

Commodity price risks

Jewellery retail operations involve relatively low value addition and hence, the profitability is exposed to the fluctuation in international gold prices, which is influenced by the global demand-supply dynamics, macro-economic trends and volatility in forex rates. The commodity price risk may be hedged by availing metal gold loans, or by hedging through derivatives in commodity exchanges.

Business Risk Assessment

Scale of operations

The scale of operations of a retailer is an important determinant of its operating leverage against its peers. The scale is characterised by the retailer's presence across geographies and market position in key locations. The revenues and the number of stores are key indicators of the scale of operations of a jewellery retailer. Generally, a large revenue base leads to economies of scale in terms of cost efficiencies in procurement and administrative functions, thereby supporting the operating profit margins (OPMs) of the retailer. Furthermore, other factors remaining similar, a large-scale retailer is more likely to exhibit higher operational stability and financial flexibility.

Market position and brand equity

While assessing the competitive position of a retailer, ICRA considers its market position and brand equity as critical parameters. Strong brand recall and sustained growth in footfalls support the market position of retailers. With over 65% of the market being unorganised and fragmented, it is critical for retailers to create unique positioning in the market through brand promotions and/or advertisements. That said, the industry is partly represented by traditional business families that possess significant industry experience yet lack adequate resources or financial flexibility to scale up their market presence amid intense competition.

ICRA assesses the market position of jewellery retailers through various parameters, including share of business in the regions they operate, trends in same-store sales growth and stock rotation, and compares the same with its peers. Entities demonstrating consistent growth and garnering higher market share are assessed favourably on this parameter. Strong market positioning enables retailers to better manage stress in the operating environment.

Operating efficiency

An entity's operational efficiency is reflected in its ability to sustain or improve operating profit margins and return indicators and exhibit a healthy inventory turnover. Operating margins, apart from reflecting the company's pricing flexibility and product mix, indicate the value addition in business and ability to control costs. Jewellers with integrated presence across manufacturing enjoy better value addition and can adapt to changing consumer demand trends. Other parameters include a mix of owned to franchise stores and sales and gross profits per square feet of operations.

The operating efficiency is measured through stock rotations and inventory management practices. In this context, ICRA assesses the entity's ability to maintain high inventory churn by effecting granular control over stock movement within and across stores with the aid of management information systems (MIS). Further, given the considerable fluctuations in raw material prices, entities with sound risk management systems including prudent/formal hedging practises, which lends stability to earnings, are viewed more favourably.

Geographical diversity

An adequate degree of geographical diversification reduces a retailer's vulnerability to (i) variability in demand in a single region, and (ii) demand disruptions caused by force majeure events in a single geography. Earnings of single-store retailers are more vulnerable to competitive risks, apart from being exposed to risks arising from region-specific demand trends. ICRA has seen instances of retailers concentrated towards specific high growth markets exhibiting better revenue growth and returns than an entity that is geographically well-diversified but faces demand weakness in select geographies. However, ICRA does not view the latter unfavourably as an entity which is diversified across geographies with healthy long-term demand potential, is more likely to demonstrate a balanced performance over a longer time horizon, even if there are intervening periods of lower average growth.

Product diversity

Given the competitiveness in the industry, one of the key factors that drives the jewellers' ability to attract footfalls and convert these into sales depends on the assortment of the jewellery offered. The inherent variation in consumer preferences owing to various demographic factors requires higher product variety to sustain the footfalls. Product diversity also aids margin expansion, where presence in value-added jewellery shields the earnings of jewellers, buffering the impact of commodity risk. ICRA assesses revenue contribution from studded/value-added jewellery for a retailer, as it enables them to create a unique market position and supports better margins.

Summary of the Salient Business Risk Factors

	Strongest	Weakest
Scale	Revenue > Rs. 5000 crores	Revenue < Rs. 250 crores
	Store count > 100	Store count < 5
Market Position	Ranks among top 2 in key markets (based on revenue)	Ranks outside top 10 in key markets (based on revenue)
Operating Efficiency	Stock holding period < 3 months	Stock holding period > 9 months
	Inventory hedged > 80%	No inventory hedging
Geographic Diversification	No single state accounts for more than 25% of revenues	A single state accounts for >80% of revenues
Product Diversification	Share of studded jewellery sales >= 25%	Share of studded jewellery sales < 5%

Financial Risk Drivers

ICRA analyses the past financial performance trends and estimates the future financial performance to assess the financial risk exposure of an entity. The financial metrics provide a useful reference not only to evaluate the performance trends of an entity over a given time horizon, but also enable a comparison with its peers. The financial risk assessment is not done in isolation but in conjunction with the business and the industry risks that the entity is exposed to. An entity with low exposure to business risks would generally have stable cash flows and thus would have a higher tolerance to operate with a relatively modest financial risk profile. In contrast, entities that are exposed to high business risks need to maintain a stronger financial risk profile to have adequate cushion to manage cash flow volatility. The various financial metrices assessed by ICRA could be divided into five categories viz., profitability, leverage, coverage, liquidity and cash flows. This document provides a summary of why ICRA considers these ratios to be important. For a more detailed description, the readers may refer to the note titled, '*Approach for Financial Ratio Analysis*' published on ICRA's website. Depending on the uncertainty around how the various credit drivers could evolve in the future, ICRA carries out the sensitivity analysis to assess the impact of the key variables including commodity prices, inventory stocking and turnover, store expansion and funding mix, etc, on the various financial metrics. Jewellery retailers traditionally carry out operations through several legal entities to align operations in line with regional preferences, apart from other business considerations. ICRA evaluates the consolidated operational and financial risk profile of such entities, in case the management is common and there are strong operational/ financial linkages between the entities.

Profitability metrics

The profitability is a measure of the earnings generated by an entity in a given time period in relation to the resources deployed or alternatively a measure of how efficiently an entity utilises its assets. ICRA assesses the entity's ability to manage the business risk and limit volatility in margins and achieve stability in earnings and return ratios. A consistent track record of higher profitability shown by an entity against its peers reflects a superior competitive position arising from one or more factors, including greater brand strength, better distribution reach, attractive product profile, or higher cost efficiency. Entities with higher profitability than peers are likely to show stronger resilience against economic downturns and generate relatively higher internal resources for re-investment as well as debt servicing, and also attract fresh capital.

For the jewellery sector, the customers' preference for the product and consequently the profitability of market players vary across geographies – where retailers in South India sell higher share of plain gold jewellery than the studded variety and vice versa in other parts of India. Given the intensifying competition, the pricing flexibility of jewellers is limited, exposing earnings to price risks. Margins, apart from being vulnerable to the volatility in gold prices, depend on efficiency in inventory turnover, managing fixed cost including employee expenses and lease rental payouts, etc. Factors like supply management and hedging practises determine the operating margin performance of retailers. The ability of retailers to have presence across a wide product range and adopt a cautious mix of various procurement methods and forward contracts or other means to mitigate the price risk are critical in generating stable profit margins.

ICRA also considers the nature of stores managed by retailers – through owned, leased and franchise route. While most of the retailers commenced their initial stores on owned mode, expansions in the recent years were primarily done on asset-light models (lease mode or franchise mode). Especially by operating through the franchise mode, retailers managed to reduce their operating costs and, in a few cases, mitigated the inventory carrying risks. With the jewellery industry being highly working capital intensive, return on capital employed (while including the metal loans and customer advances from saving schemes as a part of the capital employed) gives an insight into the capacity to efficiently deploy capital to generate economic profits over and above their cost of capital. The trend in the volatility in profitability metrics is also a rating factor.

Leverage

Financial leverage is a measure of an entity's dependence on borrowed funds. Lower the dependence on borrowings, the lower (better) the leverage. When an entity borrows, it is obliged to pay both interest as well as principal to the lenders as per a defined schedule. This increases the fixed cost burden on the borrowing entity and in the limiting case, increases the default risk. While high leverage may mean high risk from a credit perspective, it is an often-adopted course by shareholder-oriented managements, given that high leverage, in good times, leads to high returns on equity capital. An entity's financial leverage could thus be a function of its management's financial policy and risk tolerance, besides being a point-in-time reflection of its business and financial choices. An entity with lower leverage is better equipped to withstand volatility in cash flow generation in situations of economic downturn, competitive challenges, unexpected costs, changing consumer preferences, or regulatory changes.

In the jewellery retail industry, entities are vulnerable to competitive pricing pressures and shifts in buying patterns of end markets, mandating steady investments in continuous development of new product designs, marketing and management of inventory and supply chain. Further, with same-store sales growth limited by competitive factors, retailers have been investing in new stores to sustain growth in sales volume, leading to rising capital intensity in the business. Apart from the traditional avenues of funding including, working capital debt (including metal loans) and supplier credit, a sizeable portion of retailer's funding requirement is met through jewellery savings schemes. ICRA considers the interest-bearing gold metal loans and customer advances, leases (related to showrooms, etc) and loans from promoters/group entities as debt. Lower the total debt/OPBITDA multiple, better the company's ability to service its debt obligations. Despite the limitations of OPBITDA as a principal determinant of cash flow, it lends industry-wide comparison of the entity's ability to repay debt with profits from operations as well as capital structure decisions that can affect interest outflows.

Coverage

Coverage is a measure of an entity's debt-servicing ability and is calculated as the ratio of profits to the debt servicing obligations in a given time period. Higher the ratio, higher the cushion available with an entity to withstand variability in profits for making good its financial obligations. The coverage is a function of an entity's profits, leverage and debt characteristics (in terms of cost of debt and repayment schedule). Entities with higher profitability and lower leverage will generally have better coverage ratios and thereby healthier financial risk profiles. With working capital debt constituting a major portion of a retailers' overall debt, the interest coverage provides an indication of the financial health of the retailer and its ability to service its obligations with profits from operations. The ratio also indicates the entity's flexibility to absorb any decline in operating profits in relation to interest pay-outs.

Some of the key leverage and coverage indicators assessed include:

Key Indicators	Ratios
Leverage ratios	Debt/OPBITDA, total outside liability/tangible net worth, total outside liability/OPBDITA, net cash accruals/total debt
Coverage ratios	Interest coverage, Debt Service Coverage Ratio (DSCR)

Assessment of profitability, leverage and coverage metrics

[Indicative Metrics]

Salient Parameters	Key Ratios	Strongest	Weakest
Leverage	Total Debt/ OPBITDA	<0.50	>=5.00
	Total Outside Liabilities/ TNW	<0.90	>=3.00
Coverage	Interest Cover	>=18.00	<2.00
	DSCR	>=4.00	<1.10
Profitability	RoCE	>=25%	<10%

Liquidity profile

Liquidity is the measure of an entity's ability to meet its short-term cash obligations from various internal or external resources. ICRA evaluates the liquidity profile to assess the entity's ability to generate cash from internal resources and its access to committed sources of external financing, in relation to obligations like debt repayments and near-term investments /working capital requirements. The key parameters assessed include the levels of working capital utilisation on a monthly basis against an entity's sanctioned lines and drawing power. The higher the cushion available between the resources available (especially earnings from operations) and the funding requirements, better the liquidity profile of an entity. ICRA notes that the liquidity available with an entity may be for a temporary period and hence an entity's overall policy towards maintaining adequate liquidity in the form of adequate undrawn working capital lines and free cash balances is accorded due importance in the analytical approach (especially given the high working capital requirements in the business).

Cash flows

An entity requires cash to service the obligations and the cash flow statement represents the sources from which cash is generated and its deployment. ICRA analyses the trends in an entity's funds flow from operations, cash consumed to fund the working capital, the retained cash flows after paying out dividends or carrying out share buy-backs, and the free cash flows after meeting debt repayment obligations and capital expenditure needs. The cash flow analysis helps in understanding the external funding requirements that an entity has, to meet its maturing obligations and for incremental working capital funding. This assumes more significance, considering the impact of regulatory and commodity price risks on the earnings and liquidity position of jewellers.

Other Elements of Credit Risk Assessment

Tenure mismatches and risks relating to interest rates and refinancing

Large dependence on short-term borrowings to fund long-term investments or other long-term funding requirements can expose an entity to significant re-financing risks, especially during periods of tight systemic liquidity. ICRA evaluates the extent of such mismatches and the mitigating factors therein, and the extent to which an entity might be impacted by movement in interest rates. Given the aggressive store expansions being undertaken by retailers, the dependence on short-term borrowings to meet increasing investments in store infrastructure would expose retailers to funding mismatches and refinancing risks. Thus, ICRA assesses the management's approach and track record of maintaining sufficient buffers of liquid assets/bank lines and flexibility to access longer tenure funding to absorb any reasonable stress on cash flows.

Financial flexibility

An entity's financial flexibility (or the lack thereof) is reflected in its ability to access capital or money markets at a short notice and enjoy the confidence of banks, financial institutions, and intermediaries. A strong financial flexibility allows an entity to raise fresh borrowings or refinance existing ones in quick time, whenever required. Financial flexibility could arise from factors such as an entity's large scale of operations with strong financials, large unencumbered cash flows, unencumbered assets and the flexibility to borrow against such assets, or strong parentage or linkages with a strong Group. In contrast, among the various measures of an entity's depleting financial flexibility, one relates to a high share of pledged promoter shareholding. A sign such as this may imply that the entity might be persuaded to distribute high dividends or support the promoter group through other means to the detriment of its own credit profile.

ICRA derives comfort from the highly liquid nature of the gold inventory held by the retailers, with jewellery/gold being a readily marketable commodity. It also considers the debt/inventory and total outside liability/inventory as measures to assess the extent of inventory being funded externally, where a low ratio lends considerable financial flexibility to access additional funding to meet requirements.

Foreign currency-related risks

Foreign currency exposure for jewellery retailers primarily arises from – [i] direct import of gold (allowed under special approval), [ii] export of jewellery, and [iii] liability on metal gold loans (gold prices being fixed in US dollars). While forex fluctuations affect the earnings for exporters and direct importers of bullion to the extent of their unhedged exposures, liabilities arising on Gold Metal Loans (GML) are typically hedged through a back-to-back arrangement with the originating bank (i.e., bullion supplier). ICRA considers the entity's hedging policy towards mitigating such foreign currency risks and the impact of adverse movement in foreign exchange rates on earnings, apart from factoring in the volatility in gold prices.

Accounting quality

ICRA reviews the accounting policies, notes to accounts, auditors' comments and other disclosures that are parts of the Annual Report of a rated entity. Deviations, if any, from the accounting standards/ practices are assessed and the financial statements of the entity are adjusted to reflect the impact of such deviations.

Contingent liabilities / off-balance sheet exposures

The likelihood of devolvement of contingent liabilities/ off-balance sheet exposures and the financial implications of the same are evaluated for this.

Event risk

ICRA recognises the possibility of events such as unrelated diversification, mergers and acquisitions, business restructuring, asset sales and spin-offs, litigations, equity infusion and refinancing, which could materially affect the entity's credit profile. Incorporating the impact of such discrete events in the credit rating, from the beginning, is often difficult. Depending on whether and when such events occur, the rating opinion could be substantially different. To take rating decisions in such cases, ICRA applies its analytical judgment based on the rated entity's track record, the credibility of the management and the experience of having seen similar situations play out in other entities. However, given the nature of such events, it is possible that the rating may undergo a material change later, upon the occurrence of the event.

Parentage

Apart from standalone credit considerations, the likelihood of extraordinary support coming in from the parent/ Group to an entity, or the support that an entity is likely to extend to the other Group entities, is factored in while assessing the entity's credit profile. This process involves an assessment of the ability and willingness of the parent/Group to extend support to the entity (and vice-versa), the strategic importance of the entity to the Group to which it belongs, along with the financial strength of Group entities, among others[1].

Debt servicing track record

The entity's debt servicing track record forms an important rating consideration. Any history of past delays or defaults in meeting the interest and principal repayment obligations reduces the comfort level with respect to the entity's future debt servicing capability and willingness. Nevertheless, the reason behind past defaults is also analysed, which could be due to adverse demand situations in the underlying industry. The company's ability to honour its debt obligations during the period of cyclical stress is also factored in.

Management Quality Assessment

In addition to the industry, business and financial risk analysis, all credit ratings incorporate an assessment of the quality of the rated entity's management and financial policies.

Quality of management and financial policies

As a part of its process, ICRA undertakes discussions with the rated entity's management to understand its views on the past performance as well as its future plans and strategies, besides the outlook on the industry. Some of the points assessed are:

- Experience of the promoter/management in the line of business concerned
- Commitment of the promoter/management to the rated entity
- Risk appetite of the promoter/management and risk mitigation plans
- Policies on leveraging, managing interest rates and currency risks
- Management's past success in introducing new projects and managing changes in the external environment
- Management's plans on new projects, acquisitions, expansion, etc
- Track record of balancing the interests of shareholders, creditors and other stakeholders

Periodic interactions with the management help in ascertaining the shifts, if any, in the issuer's financial policies.

Assessment of Environmental, Social and Governance (ESG) Risks

The assessment of ESG risks by ICRA involves a broad range of considerations that pertain to the sustainability of an entity with focus on aspects that can materially impact its credit quality. While E&S risks tend to be both sector-related as well as entity-specific and could be driven by external factors such as regulations or demographic changes, the governance (G) risks are largely entity-driven. The impact of the E&S risks on an entity's credit profile tends to be asymmetric. If the ESG risks are material but unmitigated, these generally translate into pulling down the rating, but generally the ratings are not pushed up even when the ESG context is favourable.

1 For more details on this, readers may refer to the document titled, "Impact of Parent or Group Support on an entity's Credit rating", available on ICRA's website

Environment (E) and Social (S) Risks

While undertaking credit assessment of entities, ICRA seeks to incorporate all relevant credit considerations into its rating decisions, while taking a forward-looking view on the risks and the mitigating elements. The relevant credit considerations include (sometimes overtly, sometimes covertly) the E&S factors that could affect the rated entity/ transaction. While ICRA's analytical approach does not explicitly disaggregate these risks to assess their impact on the rating, these risks are often assessed broadly. Further, it is not always feasible to fully or precisely disaggregate the sub-components of E&S risks in credit analysis since these considerations often tend to overlap.

That said, the materiality of the E&S risks and the time horizon over which they are expected to crystallise differs widely across sectors and entities. In some cases, while the E&S risks could be material, their effect on the credit profile may be muted because of other fundamental strengths of the entity. In other cases, the adverse impact of the E&S risks is expected to play out in the distant future, and hence these considerations do not necessarily weigh on the rating today—with the expectation that when these risks manifest in the distant future, the rated entity by then would possibly adapt itself by realigning its business model.

While evaluating the E&S risks, ICRA's objective is only to assess the direct and indirect risks that an entity faces and how it already is or is intending to mitigate the impact of such risks on its credit profile. As an example, ICRA only assesses whether an entity is exposed to physical climate risks or carbon transition risks, such as those arising from changes in regulations or other environmental and social risks. It seeks to understand the various mitigation and adaptation approaches that the entity is implementing to mollify these risks.

The exposure to environmental risks is low for the jewellery retail sector. Few issues of concern include jewellery stores being exposed to episodes of temporary disruptions caused by excess rainfall/ flooding in the operating regions. Also, there exists an indirect risk of rural demand for jewellery moderating during periods of crop loss, caused by physical climate change, or otherwise.

Exposure to social risks is moderate for the jewellery retail sector. The sector has seen increased focus on product quality and transparency in product pricing, to build customer confidence and mitigate potential reputation risks. Yet, to some extent, the industry participants remain exposed to changes in consumer behaviour including, among other things, a shift towards less gold-intensive daily/ fashion jewellery. Further, with a relatively high requirement of workforce for store operations and jewellery manufacturing, the level of wages and associated fixed costs could weigh on the margins, especially given the skilled nature of the job involved in jewellery manufacturing.

Governance Practices

Corporate governance remains a complex and an evolving subject. From a risk perspective, the same tends to hold as high an importance as an entity's business strategy. A sound corporate governance structure attempts to make clear the distinction of power and responsibilities between the Board of Directors and the management. The constitution of an entity's Board and the Board of Directors' participation in strategy formulation, besides the entity's adherence to legal and statutory compliance requirements are factored in during credit assessments. ICRA seeks to gain a qualitative understanding of an entity's commitment to following transparent and credible practices by the way its financial statements are reported, their level of disclosures, consistency in communication and the openness about sharing information during the credit rating exercise. Besides the corporate group structure (whether simple or complex), the rated entity's related party transactions and instances of supporting group entities at the expense of debt holders are assessed.

Summing Up

ICRA's credit ratings are a symbolic representation of its opinion on the relative credit risk associated with the instrument being rated. This opinion is arrived at following a detailed evaluation of the issuer's business and financial risks, its competitive strengths, its likely cash flows over the life of the instrument being rated and the adequacy of such cash flows vis-à-vis its debt servicing obligations and other funding requirements. ICRA's approach to rating gold jewellery retailers incorporates a number of qualitative factors, which includes an assessment of the demand-supply trends, regulatory risks, the company's geographical spread, market position and brand recall, product diversity, the management's philosophy towards gold procurement, inventory holding and hedging against price risks, and its overall approach towards expansion and growth.

ANNEXURE

Summary of rating factors and an example to illustrate the key building blocks of a credit rating

		Strong	Comfortable	Adequate	Moderate	Weak
Industry Risk	Industry Position					
Business Risk	Scale of Operations					
	Market Position					
	Geographic Diversification					
	Product Diversification					
	Operating Efficiency					
Financial Risk	Leverage					
	Coverage					

		Enhance	Support/ Neutral	Hinder
Do these factors enhance or hinder the credit profile?	Diversification			
	Liquidity and Financial Flexibility			
	Currency Risk			
	Financial Policy			
	Management, Governance & Reporting			

Final Rating	AAA	AA+	AA	AA-	A+	A	A-	BBB+	BBB	BBB-	BB+	BB	BB-	B/ C category

The above graphic is only for illustration purpose and does not represent a rating output from a formulaic model. The ratings assigned by ICRA are determined by Rating Committees based on both quantitative and qualitative considerations.

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About ICRA Limited:

ICRA Limited was set up in 1991 by leading financial/investment institutions, commercial banks and financial services companies as an independent and professional investment Information and Credit Rating Agency.

Today, ICRA and its subsidiaries together form the ICRA Group of Companies (Group ICRA). ICRA is a Public Limited Company, with its shares listed on the Bombay Stock Exchange and the National Stock Exchange. The international Credit Rating Agency Moody's Investors Service is ICRA's largest shareholder.

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