December 26, 2022

Calsea Footwear Private Limited: Ratings reaffirmed

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Domestic / Export Credit Facility	8.00	6.00	[ICRA]BBB- (Stable); reaffirmed
Domestic / Export Credit Facility	12.00	21.00	[ICRA]BBB- (Stable); reaffirmed
Interchangeable Limits ^^	(3.00)	(5.00)	[ICRA]A3; reaffirmed
Non Fund-based Facility	5.00	2.00	[ICRA]A3; reaffirmed
Non Fund-based Facility	4.00	-	-
Total	**29.00**	**29.00**	

**Instrument details are provided in Annexure-I, ^^ sublimit of Domestic / Export Credit Facility*

Rationale

The ratings reaffirmation factors in the operational synergies as well as the financial flexibility and need-based support derived by Calsea Footwear Private Limited (CFPL) for being a subsidiary of Tata International Limited (TIL). The ratings reaffirmation also factors in the experience of the management in the footwear business. The company has been able to tap TIL's management expertise in driving various growth opportunities, which include initiatives to explore new opportunities in the sports shoes segment to tide over the prevailing slowdown in the leather footwear segment. The ratings derive comfort from the gradual moderation in customer and geographical concentration with addition of new clients across various regions to its portfolio.

The ratings, however, continue to be constrained by the company's weaker-than-expected recovery in performance in the ladies' footwear segment in FY2022 and H1 FY2023 due to lower realisation from its customers, especially from the European and other western markets amid sluggish demand recovery. Consequently, the company continued to report operating losses, which further widened in FY2022 due to a large one-off provision made during the year against sticky receivables. While the operating losses have reduced to some extent in H1 FY2023, ICRA expects the overall performance to remain weak in the remainder of FY2023. However, the company's operating leverage is expected to improve in the medium term with considerable rise in turnover from the expected commissioning of new facilities in the high-margin sports shoe segment that are lined up over the next 3-15 months. The capitalisation and debt metrics have also been impacted by negative net worth and debt-funded capital expenditure. However, support extended by the parent through a combination of unsecured loans, letter of comfort for its external borrowings, and creditor funding are likely to continue, which support CFPL's ratings. ICRA notes that the proposed capital expenditure in setting up the sports shoes facility in the near term will predominantly be funded via unsecured loans from TIL, which would further exert pressure on the debt metrics unless the profitability improves. The ratings also reflect CFPL's moderate scale of operations and intense competition in the footwear manufacturing business, which limit its pricing flexibility and benefits arising from the economies of scale. The ratings also consider the elongated working capital cycle owing to significant investments in inventory and receivables, which is partly financed by favourable payment terms with creditors.

The Stable outlook reflects ICRA's expectations that CFPL will continue to benefit from the strong managerial, operational and financial support derived for being a subsidiary of TIL, which can help it establish its position in the growing sports shoe segment, which can help it become profitable again in the near-to-medium term.

Key rating drivers and their description

Credit strengths

Established track record and experienced management – Following 100% acquisition of CFPL by TIL from Moveon Componentes e calcado (Moveon) in November 2018, the company has become a direct subsidiary of TIL, which is one of the leading exporters of leather and leather products in India. The company is actively managed by the head of leather and leather products division of TIL, which enables it to manage risks effectively. Further, CFPL manufactures women's footwear under TIL at present. This complements TIL's product portfolio consisting of men's and children's footwear.

Operational synergies and financial flexibility derived for being a part of TIL – CFPL gets strong operational and financial support from TIL, as evident from the timely support through infusion of unsecured loans in the past. In addition, TIL has provided a letter of comfort for various external borrowings availed by CFPL. ICRA notes that the proposed capital expenditure in the near term will be predominantly funded via unsecured loans from TIL. Further, it has access to supply of components from TIL at favourable terms, which helps the company's working capital management to some extent. The parent entity supports in new customer acquisition and provides potential cross-selling opportunities with TIL's global customers. However, CFPL's moderate scale of operations and intense competition in the footwear manufacturing business limit its pricing flexibility and benefits arising from economies of scale.

Moderation in customer and geographical concentration – The company's customer and geographical concentration moderated following addition of new customers and merger with Euro Shoes. In FY2022, the top three customers contributed ~44% to its total revenues (compared to ~78.9% in FY2021). The contribution from top three customers further reduced to ~18% in H1 FY2023. Sales to the exports market reduced as it has been catering to the domestic market through the Euro Shoes division. The trade war between the US and China augured well for CFPL as witnessed from an increase in revenues from the US market. Healthy demand for footwear, especially the casual and athleisure segment, in the global markets and the company's foray in the sports shoes segment are likely to further diversify the company's geographical presence in the medium term.

Credit challenges

Weaker-than-expected recovery in performance of ladies footwear section – The company reported weaker-than-expected recovery in performance in the ladies footwear segment in FY2022 and H1 FY2023 due to lower realisation from its customers, especially from the European and other western markets amid sluggish demand recovery. Consequently, the company continued to report operating losses, which further widened in FY2022 due to a large one-off provision made during the year against sticky receivables. While the operating losses have reduced to some extent in H1 FY2023, ICRA expects the overall performance to remain weak in the remainder of FY2023. However, the company's operating leverage is expected to improve in the medium term with a considerable rise in turnover from the expected commissioning of the new facilities in the high-margin sports shoe segment that are lined up over the next 3-15 months.

Stretched capitalisation and debt protection metrics in the near term – The company's coverage indicators remained adverse in FY2022 as its operating profits turned negative, and subsequently its debt levels rose to support its funding requirements. Post the merger, CFPL's debt metrics and capital structure improved in FY2019 on account of the stronger financial profile of Euro Shoe. However, both Calsea and Euro Shoe divisions experienced adverse business environment due to the pandemic, which impacted its capital structure, with the net worth slipping into negative in FY2022.

Elongated working capital cycle – The new customers have been offered 90 days of credit, which increased the company's debtor days in the recent past. Additionally, retail sales were affected in FY2022 due to mobility restrictions, so many European customers delayed payments, which is reflected in the higher collection period of 122 days. In FY2022, the company also created a large one-off provision of Rs. 14 crore against its sticky receivables owing to doubt about collection recovery. This increase in working capital requirement was largely funded by a stretch in the creditors, which partly supported its liquidity position.

Liquidity position: Stretched

The liquidity position of the company remains stretched with limited headroom in the working capital limits, loss-making operations, and modest free cash balance of Rs. 2.7 crore as on September 30, 2022. The funding gap has been met through a stretch in the creditor funding and non-operating income. Moreover, the company plans to further increase its borrowings from its parent company to fund the proposed capex in the near term towards setting up of a sports shoe facility. This would continue to exert pressure on the liquidity unless the profitability improves. ICRA, however, notes that a healthy uptick in demand from its customers, particularly from the soles and sports shoes segment in the near term, is expected to lead to a sequential improvement in profitability from FY2024. This, along with a reduction in dependence on the working capital facilities would remain crucial to improve the company's liquidity position.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings if there is a considerable improvement in the credit profile of the parent. The ratings could also be upgraded if there is an improvement in the company's scale of operations and profitability metrics.

Negative factors – ICRA could downgrade the ratings if there is any adverse change in the ownership of the company or a reduction in the extent of support provided by TIL or if the credit profile of the parent weakens considerably. The ratings could also be downgraded if there is any significant deterioration in the profitability or liquidity position of the company for a prolonged period.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Footwear Industry
Parent/Group support	Parent Company: Tata International Limited (TIL) Given the 100% ownership and demonstrated track record of operational and financial support from TIL, ICRA expects such need-based support from the parent to continue to protect its reputation from the consequences of a Group entity's distress
Consolidation/Standalone	Standalone financial statement of the issuer

About the company

CFPL is a manufacturer and exporter of women's footwear and is based out of Walajapet, Vellore (Tamil Nadu). The company commenced operations in 2006, with a full shoe manufacturing facility in Vellore. At present, it has a capacity to manufacture ~3,000 full shoe pairs per day. It primarily supplies to its Portuguese parent, Moveon. CFPL has employed around 420 people for its various shoe-assembly processes in Vellore and outsources the rest of its component requirements to tanneries and cutting units in and around Vellore and Ranipet (Tamil Nadu). CFPL has been operating as TIL's subsidiary since May 2011 after TIL acquired a predominant stake in Moveon. In November 2018, TIL purchased 100% share of CFPL from Moveon and CFPL became a direct subsidiary of TIL. Euro Shoe Components Limited, a subsidiary of TIL, was merged with CFPL in October 2019. Post the merger, the company is now vertically integrated to manufacture soles. The soles manufactured are used mainly used for in-house needs as well as sold to Group companies. At present, it has a capacity of producing 13,500 soles per day.

Key financial indicators

CFPL	FY2021 (Audited)	FY2022 (Audited)	H1 FY2023 (Provisional)
Operating income	87.7	120.1	75.6
PAT	-16.0	-25.3	-3.5
OPBDIT/OI	-7.7%	-16.1%	-1.3%
PAT/OI	-18.2%	-21.0%	-4.6%
Total outside liabilities/Tangible net worth (times)	22.6	-6.3	-5.2
Total debt/OPBDIT (times)	-8.5	-2.9	-26.3
Interest coverage (times)	-1.7	-3.4	-0.4

PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amount in Rs crore

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current rating (FY2023)				Chronology of rating history for the past 3 years		
		Type	Amount rated (Rs. crore)	Amount outstanding as of Nov 31, 2022 (Rs. crore)	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
					Dec 26, 2022	Sep 23, 2021	Jun 30, 2020	-
1	**Domestic / Export Credit Facility**	Long Term	6.00	-	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
2	**Domestic / Export Credit Facility**	Long Term	21.00	-	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	[ICRA]BBB- (Stable)	-
3	**Interchangeable Limits ^^**	Short Term	(5.00)	-	[ICRA]A3	[ICRA]A3	[ICRA]A3	-
4	**Non Fund-based Facility**	Short Term	2.00	-	[ICRA]A3	[ICRA]A3	[ICRA]A3	-
5	**Non Fund-based Facility**	Short Term	-	-	-	[ICRA]A3	[ICRA]A3	-

^^ sublimit of Domestic / Export Credit Facility

Complexity level of the rated instruments

Instrument	Complexity Indicator
Domestic / Export Credit Facility	Simple
Domestic / Export Credit Facility	Simple
Interchangeable Limits ^^	Simple
Non Fund-based Facility	Very Simple

^^ sublimit of Domestic / Export Credit Facility

The Complexity Indicator refers to the ease with which the returns associated with the rated instrument could be estimated. It does not indicate the risk related to the timely payments on the instrument, which is rather indicated by the instrument's credit rating. It also does not indicate the complexity associated with analysing an entity's financial, business, industry risks or complexity related to the structural, transactional or legal aspects. Details on the complexity levels of the instruments are available on ICRA's website: Click Here

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	**Domestic / Export Credit Facility**	NA	NA	NA	6.00	[ICRA]BBB- (Stable)
NA	**Domestic / Export Credit Facility**	NA	NA	NA	21.00	[ICRA]BBB- (Stable)
NA	**Interchangeable Limits ^^**	NA	NA	NA	(5.00)	[ICRA]A3
NA	**Non Fund-based Facility**	NA	NA	NA	2.00	[ICRA]A3

Source: Company; ^^ sublimit of Domestic / Export Credit Facility

Please click here to view details of lender-wise facilities rated by ICRA

Annexure II: List of entities considered for consolidated analysis: Not Applicable

ANALYST CONTACTS

Jayanta Roy
+91 33-71501100
jayanta@icraindia.com

Priyesh Ruparelia
+91 22-61693328
priyesh.ruparelia@icraindia.com

Ritabrata Ghosh
+91 33-71501107
ritabrata.ghosh@icraindia.com

Brinda Goradia
+91 22-6169 3341
brinda.goradia@icraindia.com

RELATIONSHIP CONTACT

Jayanta Chatterjee
+91 80 4332 6401
jayantac@icraindia.com

MEDIA AND PUBLIC RELATIONS CONTACT

Ms. Naznin Prodhani
Tel: +91 124 4545 860
communications@icraindia.com

Helpline for business queries

+91-9354738909 (open Monday to Friday, from 9:30 am to 6 pm)

info@icraindia.com

About ICRA Limited:

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For more information, visit www.icra.in

ICRA Limited

Registered Office

B-710, Statesman House, 148, Barakhamba Road, New Delhi-110001
Tel: +91 11 23357940-45

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