March 23, 2021

Pai International Electronics Limited: [ICRA]BBB (Stable)/[ICRA]A3+ assigned

Summary of rating action

Instrument*	Current Rated Amount (Rs. crore)	Rating Action
Long Term / Short Term - Fund Based	31.00	[ICRA]BBB (Stable)/[ICRA]A3+; Assigned
Total	**31.00**	

**Instrument details are provided in Annexure-1*

Rationale

The assigned ratings factor in the established market presence of Pai International Electronics Limited (PAI) in South India aided by established track record on the back of the vast experience of the promoters in the consumer durables retailing industry and strong brand pull. The company's operating income (OI) recorded a compound annual growth rate (CAGR) of 12.6% during the last five years, supported by healthy demand, sales mix, growth from the existing stores in addition to the sales in new stores (28 new stores in FY2020 and 4 new stores in 9M FY2021) and increase in the average selling price (ASP) of the products sold. PAI's dominant market position, favourable economies of scale, healthy bargaining power with counterparties and strong marketing & service network lend support to its business prospects. The company's financial profile is characterised by moderate leverage and coverage indicators (gearing of 1.3 times, total debt to OPBITDA of 2.8 times and interest coverage ratio of 2.5 times as of March 31, 2020 and 1.2 times, 3.0 times and 1.4 times, respectively, as on September 30, 2020).

The ratings, however, are constrained by the lower operating margins inherent to the retail nature of the operations, the high working capital requirements of the business, and the vulnerability of earnings to the fragmented and competitive nature of the domestic consumer durables retail market. The ratings also consider region-specific risks with ~70% of the company's revenues derived from a single market (Karnataka). However, PAI has expanded its presence in the markets of Telangana and Andhra Pradesh over the past 2-3 years with the revenue contribution from Karnataka declining to 68.4% in H1 FY2021 from 82.3% in FY2016. The company plans to add 70-90 showrooms to achieve business diversity in terms of segments and geographies (Karnataka, Telangana and Andhra Pradesh). The store expansions are likely to have an impact on the profitability and debt indicators in the near term, given the gestation period for new stores, though the same is likely to improve in a year.

The Stable outlook reflects ICRA's expectation that PAI will benefit from the extensive experience of its promoters and established brand presence in the market in South India.

Key rating drivers and their description

Credit strengths

Significant experience of promoters with presence in retail industry for over 20 years – The promoters have more than 20 years of experience in the consumer durables retailing (electronics and electricals) industry. Incorporated in 2000, PAI has a strong presence in Karnataka, Andhra Pradesh and Telangana, leading to an established market position in the region. It is one of the largest retailers in South India with 225 stores spread across three states. The company enjoys working relationships with all marquee names in the mobile consumer durables retail industry, aiding its sales growth.

Established tie-ups with major consumer durables OEMs – PAI has established relationships with major consumer durables original equipment manufacturers (OEMs) such as Samsung, LG Electronics, VIVO, Sony, Voltas, Whirlpool, etc., which have been contributing to the majority of its sales over the past few years. This, coupled with the long-term positive demand for the consumer durables industry, is likely to support the company's revenue growth prospects going forward.

Strong brand name in Karnataka, Andhra Pradesh and Telangana – PAI commenced operations in 2000 as a home appliance retailer and has been adding stores every year, primarily in the South Indian retail market. With the company covering all major products in the consumer durables and electronics space, supported by strong tie-ups with major players in the industry, the brand (PAI) has a well-established presence in the region with 225 stores as on September 30, 2020. PAI has aggressive expansion plans for FY2022 and FY2023 to diversify its segmental and geographical presence.

Credit challenges

High geographical concentration with entire revenues generated from three states – PAI derived ~70% of its revenues from Karnataka in FY2020, followed by Telangana and Andhra Pradesh, exposing its business profile to region-specific risks and uncertainties. However, the company has expanded its presence in Telangana and Andhra Pradesh over the past 2-3 years with the revenue contribution from Karnataka declining to 68.4% in H1 FY2021 from 82.3% in FY2016. With planned store expansions, the geographical concentration is likely to reduce further going forward.

Inherently low margins and intense competition – Inherent to the industry, PAI's margins are low due to limited value addition and competition from e-commerce players and brick & mortar players like Adishwar India Limited, Girias India, Reliance Digital, Croma, Sangeetha Mobiles Private Limited, Poorvika Mobiles Private Limited, etc. With the changing economic and demographic landscape of the country, intense competition is being witnessed in the consumer durables industry with demand emanating especially from tier II and III cities. The company's rising fixed costs on the back of the additional stores (28) opened in FY2020 further impacted margins. Going forward, while PAI has plans to continue its store expansions, its ability to manage the fixed costs and achieve higher operating margins remains to be seen.

Aggressive expansion plans – PAI plans to open 70-90 stores in the near-to-medium-term. Though the asset-light model supports scalability, the expansion plans will entail incremental investments towards stores as well as inventory. Besides, expansions expose the company to risks pertaining to the gestation period for new stores as well as risks related to venturing into newer tier II/III markets, considering the different target market. In this scenario, PAI's ability to reach its targeted sales growth, while sustaining its operating profitability and managing the working capital cycle, remains crucial for a stable credit profile.

Liquidity position: Adequate

PAI's liquidity position is adequate with its fund flow from operations increasing over the years, given the increase in the scale of operations. However, the free cash flow has been negative owing to the significant capex over the last few years mainly towards setting up new stores, with the same largely funded through bank borrowings and unsecured loans from directors. Going forward, the company's ongoing capex for store expansion is expected to exert pressure on free cash flow. As on September 30, 2020, PAI had a cash and bank balance of Rs. 22.3 crore and sanctioned working capital limits of Rs. 185.0 crore, of which 30-40% remained unutilised on an average in the last one year. Further, the company has debt repayments of Rs. 6-7 crore on its existing loans in FY2021, FY2022 and FY2023. ICRA expects PAI to meet its near-and-medium-term commitments through internal accruals and debt.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings on sustained growth in revenue and profitability and an improvement in the liquidity profile. Specific credit metrics that could lead to an upward revision in the ratings include an interest coverage ratio of more than 3.5 times and TOL/TNW (Total outside liabilities / Tangible Networth) of < 1.5 times on a sustained basis.

Negative factors – Pressure on the ratings could arise from a sharp deterioration in the profitability, credit metrics or liquidity profile. Specific credit metrics that could lead to a downward revision in the ratings include interest cover of < 2.5 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable Rating Methodologies	Corporate Credit Rating Methodology Rating Methodology for Retail Industry
Parent/Group Support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financials of the issuer

About the company

Mr. Rajkumar Pai started PAI in 2000 as a proprietary concern for dealing with home appliances with one store in Indira Nagar, Bengaluru (Karnataka). In 2005 the proprietary concern was converted into a limited company, PAI International Electronics Limited. The company sells consumer electronics, home appliances, mobiles, IT and furniture products.

PAI deals in all kinds of home and kitchen appliances like washing machines, refrigerators, air conditioners, air coolers, microwave ovens, chimneys, mobile phones, home theatres, vacuum cleaners, wet grinders and furniture. It has a presence in three states, namely Karnataka, Telangana, and Andhra Pradesh.

The company deals with major multinational and domestic companies and distributes various products of Godrej, LG Electronics India Private Limited, Sony India Private Limited, IFB Industries Limited, Samsung India Electronics Private Limited, Voltas Limited, Whirlpool of India Ltd and other reputed distributors. As on September 30, 2020, the company had 225 outlets across Karnataka, Telangana, and Andhra Pradesh.

Key financial indicators (audited)

Pai International Electronics Limited	FY2019	FY2020
Operating Income (Rs. crore)	1,190.3	1,390.0
PAT (Rs. crore)	23.3	23.6
OPBDIT/OI (%)	5.3%	4.5%
PAT/OI (%)	2.0%	1.7%
Total Outside Liabilities/Tangible Net Worth (times)	2.4	2.0
Total Debt/OPBDIT (times)	2.3	2.8
Interest Coverage (times)	2.9	2.5

Source: *Company and ICRA research; PAT: Profit after Tax; OPBDIT: Operating Profit before Depreciation, Interest, Taxes and Amortisation*

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

	Instrument	Current Rating (FY2021)					Chronology of Rating History for the past 3 years		
		Type	Amount Rated (Rs. crore)	Amount Outstanding as of Sep 30, 2020 (Rs. crore)	Date & Rating in FY2021		Date & Rating in FY2020	Date & Rating in FY2019	Date & Rating in FY2018
					Mar 23, 2021	Sep 11, 2020	Sep 12, 2019	Jun 28, 2018	NA
1	Fund based	Long term / Short term	31.00	0.00	[ICRA]BBB (Stable)/[ICRA]A3+	MA-(Stable); withdrawn	MA-(Stable)	MA-(Stable)	NA
2	Fixed Deposit	Medium Term	50.00	0.00	NA	MA-(Stable); withdrawn	MA-(Stable)	MA-(Stable)	NA

Source: *Company and ICRA research*

Complexity level of the rated instrument

ICRA has classified various instruments based on their complexity as "Simple", "Complex" and "Highly Complex". The classification of instruments according to their complexity levels is available on the website www.icra.in

Annexure-1: Instrument details

ISIN No	Instrument Name	Date of Issuance / Sanction	Coupon Rate	Maturity Date	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based facilities	NA	NA	NA	31.00	[ICRA]BBB (Stable)/[ICRA]A3+

Source: *Company*

Annexure-2: List of entities considered for consolidated analysis

Company Name	PAI Ownership	Consolidation Approach
NA	NA	NA

Source: *Company*

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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.

For more information, visit www.icra.in

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