

September 22, 2022

Modenik Lifestyle Private Limited: Ratings reaffirmed; rated amount enhanced

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Long/Short term - Fund based limits	155.00	250.00	[ICRA]A+ (Stable)/ [ICRA]A1+ reaffirmed
Long/Short term – Unallocated facility	45.00	-	-
Total	200.00	250.00	

*Instrument details are provided in Annexure-I

Rationale

The ratings reaffirmation reflects the expected healthy operational and financial performances of Modenik Lifestyle Private Limited (MLPL) over the medium term on the back of its established market position in the branded innerwear industry and its comfortable financial profile, characterised by a conservative capital structure, comfortable credit metrics and adequate liquidity position. The company reported a healthy performance in FY2022, with a growth of ~16% in its turnover and more than 300-bps improvement in its operating profitability (as per provisional estimates) on the back of cost-control measures adopted and increase in share of premium products in revenues. With the expected steady growth in volumes across key brands, MLPL is likely to witness a comfortable double-digit revenue growth and healthy return metrics (with ROCE likely to be more than 20%) over the medium term, aided by improving operating efficiencies and asset-light operations. Reliance on outsourcing for part operations, resultant limited capex requirements and surplus cash flow generation capacity of the business have kept the company's dependence on term debt low over the years. ICRA has, however, noted the increase in the company's working capital intensity (as reflected by Net Working Capital/ Operating Income or NWC/ OI) to ~27% in FY2022 (estimated, E) from 17% in FY2021. Along with the interest payout of ~Rs. 30.0 crore per annum towards the CCDs issued, increasing working capital intensity has resulted in increased utilisation of its working capital facilities in the current fiscal (~70% in H1 FY2023, compared to ~15% in FY2022). Nevertheless, comfort is drawn from the cushion available in the company's working capital limits and its limited capex and debt repayment obligations. Also, ICRA understands that the cash outflow towards the CCD interest payout will be made only at the end of the fiscal after meeting all the operational requirements and financial debt obligations, which lend comfort.

The Stable outlook reflects ICRA's expectation that MLPL's healthy operational profile will help it in clocking a comfortable revenue growth and stable operating margin, despite intensifying competition. The resultant surplus cash flow generation and minimal reliance on term debt, are expected to keep the company's capitalisation and coverage indicators healthy, despite increased working capital requirements.

Key rating drivers and their description

Credit strengths

Healthy operational profile, characterised by an established and diversified brand portfolio; long presence spanning more than 30 years – MLPL has a strong operational profile, characterised by its diversified presence across the economy, mid premium and premium segments in men's, women's and kids innerwear, through brands like Dixcy, Scott, Enamor, Dixcy Slimz, Levis etc. Each of the brands operated by the company caters to different customer segments based on the price points. With its long presence spanning more than 30 years, the company has created a niche for itself in the premium and mid-premium inner wear segments. Besides an established brand portfolio, Modenik has also aggressively expanded its distribution network for products under the Dixcy umbrella. From less than 600 distributors before 2009, MLPL's network comprises more than

1,300 distributors as on date. This apart, MLPL also plans to open ~50-60 new exclusive stores under its Enamor brand in the current fiscal.

Asset light model of operations results in scalable business model and supports return metrics – The company operates an asset-light business model, with about 90% of its activities being outsourced to regional players on a job-work basis. While cutting is done in-house, which is the most important value addition in the industry, considerable portion of knitting and sewing operations are outsourced, resulting in a scalable business model, which supports healthy return on capital employed (~24% ROCE reported in FY2022, as per provisional estimates).

Comfortable financial risk profile with adequate coverage metrics and liquidity position – MLPL's capital structure and liquidity position remain comfortable, supported by the steady cash flow generation and adequate unutilised lines of credit. Its gearing and total outside liabilities to the tangible net worth have improved over the years, given its asset-light business model and limited dependence on external debt for funding its working capital requirements. While the coverage indicators have moderated in the recent fiscals after factoring in the interest costs for the CCDs issued, expected improvement in earnings and no long-term debt repayment obligations provide comfort.

Credit challenges

Moderate operating profitability amid intense competition limits pricing flexibility – Higher revenue concentration in the mid-premium segment and high marketing expenses over the years amid competitive pressure have resulted in moderate operating profit margin for the company. Intense competition across the segments from other large, branded players and the wide unorganised segment limit pricing flexibility. While ICRA has noted the improvement in the company's operating margins in FY2022, as per the provisional estimates arising from synergy benefits from the recent merger, the company's ability to sustain the same amid rising raw material prices and intense competition, remains to be seen. The extent of margin improvement over the medium term will depend on the successful ramping up of the women's innerwear segment.

Susceptibility of earnings to fluctuations in yarn prices – The company's profit margins are exposed to fluctuation in raw material (cotton yarn) prices as the same account for ~50% of its operating income. In the last couple of quarters, cotton yarn prices have remained volatile due to fluctuations in demand and uncertainty over cotton harvest. MLPL remains susceptible to any sharp correction in cotton yarn prices as the same would exert pressure on the company's contribution margins.

High working requirements in the business – The industry is characterised by high working capital requirements to support stock holding across a wide product range. Moreover, the company is required to extend moderate credit to its partners along the supply chain. Stock levels increase in the second half of the fiscal to meet the high demand for innerwear during the summer season and reduce gradually between February and July with liquidation of inventory (stock levels also rise to an extent in the second quarter for the ensuing winter season). Despite the same, lower-than-industry working capital intensity (supported by favourable credit terms enjoyed from the suppliers) and its comfortable liquidity position provide comfort.

Liquidity position: Adequate

MLPL's liquidity position is expected to remain adequate, with fund flow from operations expected to be adequate to fund the margin requirements for working capital and capital expenditure. The company also has a comfortable liquidity cushion in the form of free cash and bank balances (~Rs. 11 crore as on March 31, 2022) and unutilised lines of credit (with an average cushion of ~Rs.60 crore in the current fiscal). ICRA notes that the liquidity cushion remains comfortable despite an increase in the average working capital limit utilisation for the company from less than 20% in FY2022 to ~70% in the current fiscal due to increased working capital requirements. ICRA also notes that the company does not have any external term debt repayment obligations, and the capital expenditure plans are moderate in the near term.

Rating sensitivities

Positive factors – ICRA could upgrade the ratings if there is a significant growth in its scale of operations and earnings, supported by enhanced product/ brand portfolio and/or geographical presence and increasing market share while sustaining its comfortable capital structure and liquidity position. Key credit metrics, which could trigger a rating upgrade includes an interest coverage above 7.0 times on a sustained basis.

Negative factors – ICRA could downgrade the ratings if there is sustained pressure on the operating performance or a stretch in the working capital cycle, which adversely impacts the credit metrics and liquidity position of the company. Further, any large debt funded capital expenditure could also exert pressure on the ratings. Key credit metrics which could trigger a downgrade include TOL/ TNW increasing to above 1.3 times on a sustained basis.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology Rating Methodology for Entities in the Textiles Industry- Apparels
Parent/Group support	Not Applicable
Consolidation/Standalone	The ratings are based on the standalone financial profile of the company

About the company

Wholly owned by Advent International, Modenik Lifestyle Private Limited (MLPL, erstwhile Dixcy Textiles Private Limited) is primarily involved in making innerwear for men, women and kids. The company's products are sold in the domestic market under two major brands namely Dixcy and Enamor. This apart, the company has a licence agreement with Levis in the male innerwear segment, as per which it has design, production and marketing licence for the products sold under the Levis brand.

Pursuant to a National Company Law Tribunal (NCLT) order in May 2021, Advent International (the common parent entity) had amalgamated Gokaldas Intimatewear Private Limited (GIPL) and Hinduja Investments Private Limited (HIPL) with MLPL, with the merger effective from September 16, 2019.

Key financial indicators

MLPL Standalone	FY2021	FY2022*
Operating income	1,125	1,309
PAT	18	85
OPBDIT/OI	8.0%	11.1%
PAT/OI	1.6%	6.5%
Total outside liabilities/Tangible net worth (times)	1.2	1.1
Total debt/OPBDIT (times)	1.1	0.8
Interest coverage (times)	2.0	3.7

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

Note: Debt outstanding in the books of the company also includes lease liabilities, arising on account of Ind AS 116

Status of non-cooperation with previous CRA: Not applicable

Any other information: None

Rating history for past three years

Instrument	Type	Current rating (FY2023)		Chronology of rating history for the past 3 years			
		Amount rated (Rs. crore)	Amount outstanding (Rs. crore)*	Date & rating in FY2023	Date & rating in FY2022	Date & rating in FY2021	Date & rating in FY2020
				Sep 22, 2022	Aug 19, 2021	Nov 11, 2020	Mar 05, 2020
1	Fund-based bank facilities	250.0	~130	[ICRA]A+(Stable)/ [ICRA]A1+	[ICRA]A+(Stable)/ [ICRA]A1+	[ICRA]A+(Stable)/ [ICRA]A1+	[ICRA]A+(Stable)/ [ICRA]A1+
2	Unallocated	0.0	-	-	[ICRA]A+(Stable)/ [ICRA]A1+	-	-

*Amount outstanding as on August 31, 2022

Complexity level of the rated instruments

Instrument	Complexity Indicator
Long-term/ Short -term – Fund-based bank facilities	Simple

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: www.icra.in

Annexure I: Instrument details

ISIN	Instrument Name	Date of Issuance	Coupon Rate	Maturity	Amount Rated (Rs. crore)	Current Rating and Outlook
NA	Fund-based bank facilities	NA	NA	NA	250.0	[ICRA]A+(Stable)/[ICRA]A1+

Source: Company

[Please click here to view details of lender-wise facilities rated by ICRA](#)

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

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About ICRA Limited:

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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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