August 10, 2023 (Revised)

KDDL Limited: Ratings upgraded

Summary of rating action

Instrument*	Previous Rated Amount (Rs. crore)	Current Rated Amount (Rs. crore)	Rating Action
Fund-based/ Cash Credit	33.0	33.0	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Fund-based/ Term Loan	24.90	24.90	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Non-fund Based	31.50	31.50	[ICRA]A1; upgraded from [ICRA]A2+
Fixed Deposits	15.00	15.00	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Unallocated	2.28	2.28	[ICRA]A (Stable); upgraded from [ICRA]A- (Stable)
Total	**106.68**	**106.68**	

**Instrument details are provided in Annexure-I*

Rationale

The rating upgrade reflects ICRA's opinion that KDDL Limited's (KDDL/ the company) operating and financial performance will be healthy, going forward, led by an expanding retail business and steadily growing manufacturing business. The company has been witnessing steady demand across its segments and has been expanding its product portfolio with focus on high-value accretive products. The ratings favourably factor in KDDL's prominent market position in manufacturing watch components as a leading supplier of watch hands and dials, and established relationships with leading global luxury watch manufacturers. The company's planned foray into bracelets and capex towards watch dials will support its manufacturing revenue growth. In addition, KDDL continues to benefit from its subsidiary Ethos Limited's (Ethos) position as the largest organised luxury watch retailer in the country. Ethos has continued to witness significant sales traction across its store network with growing average realisations, resulting in sustained margins. Consequently, on a consolidated basis, the company's credit metrics are expected to be comfortable with growing cash accruals and limited external debt dependence with a large part of its expansion, primarily in the retail business, being funded by equity and internal sources.

The ratings, however, are constrained by the susceptibility of the watch manufacturing segment to global demand volatility in the luxury and high luxury segments. Additionally, the company is exposed to forex fluctuation risk for both its manufacturing as well as retail businesses. Moreover, the business remains working capital intensive, led by high inventory requirements in retail along with moderate inventory and debtors at the manufacturing level. Nevertheless, ICRA notes that the retail business will be funding its expansion plans, including new store launches and additional inventory requirements, largely through equity funds in the medium term. Further, the company is exposed to competition from domestic players and international markets in the retail business and from other global manufacturers in the component segment. Also, its ability to expand its store network, which depends on the timely availability of store space from developers, remains a key rating sensitivity.

The Stable outlook on the long-term rating reflects ICRA's view that KDDL will continue to benefit from the experience of its promoters and leverage its established relationships with major watch manufacturers. The company will also benefit from the strong revenue visibility owing to its healthy order book in both export as well as domestic markets.

Key rating drivers and their description

Credit strengths

Buoyant demand across manufacturing as well as retail segments – After subdued performance in FY2021 in both manufacturing as well as retail divisions, the company witnessed revival in FY2022, which continued into FY2023 as well. In the manufacturing division, the company witnessed stable demand in the domestic as well as export segments, which reflected in ~40% growth in the top line through a mix of high and low-value units. Further, favourable forex movement helped the company in scaling up significantly as well. KDDL has a healthy order visibility, particularly in the watch component export and precision engineering segments, which will help it register steady growth in the current fiscal as well. In the luxury watches retail segment, the local demand grew with the company achieving revenue growth of ~35% from Rs. 585 crore in FY2022 to Rs. 790 crore in FY2023. In addition, the company witnessed significant traction in the high luxury segment, which has been growing for the past couple of years. Further, its increasing portfolio of exclusive brand sales augurs well for further growth and profitability. The company also witnessed significant Same Store Sales Growth (SSSG) of ~30% in FY2023, which resulted in operating leverage reflecting in the strong profitability of Ethos Limited at a standalone level. On a consolidated basis, the company's revenue increased by 36% from Rs. 824.3 crore in FY2022 to Rs. 1119.5 crore in FY2023. Focus on expanding its product portfolio, apart from growing brand tie-ups will support the company's growth prospects.

Improvement in financial risk profile, coverage metrics to remain healthy – With continued increase in the top line and sustained healthy profitability, the company's overall financial risk profile has been improving steadily. At a consolidated level, supported by high value-added sales and economies of scale in the retail segment, KDDL posted operating margin of 15% and net profit margin of 6.9% in FY2023, which improved from 14.6% and 4.5%, respectively, in FY2022. Moreover, the gearing improved to 0.35 time as on March 31, 2023 from 0.86 time as on March 31, 2022, largely on account of limited debt dependence and better internal accrual generation. Interest coverage and TD/OPBIDTA improved from 4.0 times and 2.2 times, respectively, in FY2022 to 5.49 times and 1.47 times, respectively, in FY2023. In the absence of any major debt raising plans apart from moderate level of working capital limits in Ethos and some capex related term loans for the manufacturing segment, the company's coverage metrics are expected to improve, supported by steady growth and profitability.

Established market position – KDDL has a prominent market position in manufacturing watch components, as a leading supplier of watch hands and dials, enjoying established relationships with leading luxury watch manufacturers in the world like Swatch, Tag Heuer, Gucci, Breitling, etc. Further, its subsidiary, Ethos, is the largest organised luxury watch retailing company in the country and operates from 56 stores spread across 22 cities in India (as of May 2023).

Credit challenges

High working capital requirements – The company's working capital intensity increased from ~31% in FY2022 to ~45% in FY2023 and is expected to remain high, largely driven by the high inventory levels required at the Ethos' stores, which are expanding at a healthy pace. The manufacturing segment also has raw material and work-in-progress (WIP) stocking requirements along with and a moderate receivable period given the export nature of its sales. While the inventory requirements are expected to increase, the funding for the same will be mostly through the IPO route, internal accruals and Ethos' plans to raise working capital debt. With Ethos expected to increase its footprints across the country with 40 new stores, along with increasing high-value and excusive brand sales, the overall inventory requirement will remain high. For manufacturing, KDDL has sufficient cushion in the form of drawing power and utilization, while maintaining healthy free cash balances for its funding requirements. Further, its ability to expand its store network, which depends on the timely availability of store space from developers, will remain critical for the company's planned growth, going forward.

Risk of fluctuating demand amid ongoing global scenario – The company's performance is directly dependent on demand across both its business segments, which mainly rely on discretionary consumer spending. While the company has depicted healthy growth in the past two years, the evolving nature of the economy and the demand outlook, particularly in European markets, might adversely impact overall market sentiments. The demand in the retail business also remains prone to regulatory headwinds such as changes in Government policies regarding taxation. Further, the company is exposed to competition from domestic players and international markets in the retail business and from other global manufacturers in the component business. ICRA notes that the company has also forayed into retailing jewelry and luggage from luxury brands, whose ramp up remains to be seen.

Exposed to forex risks – In the manufacturing segment, the company is exposed to forex fluctuations as it is a net exporter and is highly dependent on the Swiss market. However, the retailing business is a net importer with approximately 40% of its watches being imported. The company, thus, remains exposed to foreign currency fluctuation risk. ICRA notes that the company receives periodic price revisions from brands; and that it practices natural hedging to a certain extent; but there are receivables, which remain unhedged as well, which are prone to variations in foreign currency.

Environmental and Social Risks

Environmental: The company manufactures watch hands and dials and retails watches; and generally, its products do not harm the environment and nor are of any concern to the climate. Further, the company spends a part of its earning on corporate social responsibility (CSR) initiatives throughout the year. KDDL has also taken some energy efficient initiatives such as:

- Installation of LED lights and power saving equipment across stores to reduce energy consumption; and
- Optimal use of air conditioners at all offices to reduce energy consumption.

Social: KDDL has high dependence on human capital as the requirement of skilled craftsmen and manpower is critical for its operations. Retaining human capital, maintaining healthy employee relationships and a safe work environment remain essential for disruption-free operations. The company conducts training sessions for all employees to upgrade their knowledge and skills from time to time. The company also prohibits the employment or engagement of children in its workforce and expects its vendors to follow the same.

Liquidity position: Strong

KDDL's liquidity position is **strong** on account of the cushion available in its working capital limit and sufficient cash generation from its business to manage its working capital requirements and debt repayments. The company had free cash levels of ~Rs. 254.70 crore as on March 31, 2023, on a consolidated level, including Rs. 196.33 crore from IPO proceeds, earmarked for capex and working capital in Ethos. The repayments are modest as compared to the internal accruals and free cash available. While it has sizeable capex plans, led by its subsidiary, Ethos, the same is expected to be largely funded through available IPO funds and internal accruals. Further, Ethos is also raising working capital limits to additionally support its growth plans.

Rating sensitivities

Positive factors – The ratings could be upgraded if the company demonstrates significant improvement in its scale, profitability and working capital cycle on a sustained basis.

Negative factors – Negative pressure on the ratings could emerge if there is a dip in demand, leading to pressure on revenues and profitability. Stretch in working capital cycle and pressure on liquidity may also warrant a rating review. Debt/OPBIDTA higher than 1.8 times, on a sustained basis, might also lead to a rating downgrade.

Analytical approach

Analytical Approach	Comments
Applicable rating methodologies	Corporate Credit Rating Methodology
Parent/Group support	Not applicable
Consolidation/Standalone	For arriving at the ratings, ICRA has considered the consolidated financials of KDDL. The list of companies consolidated are given in Annexure-II.

About the company

Incorporated in 1981, KDDL manufactures watch components like dials and hands as well as precision engineering goods under the brand name, Eigen. The company is a leading supplier of high-quality dials and hands to watch manufacturers in India and Switzerland. KDDL enjoys a presence in Switzerland through its subsidiaries, Pylania SA and Estima AG, who are engaged in trading and manufacturing dials and hands for Swiss watch companies, respectively.

KDDL's subsidiary, Ethos, was incorporated in 2003. The company is engaged in retailing luxury watches in India. It retails various premium, and luxury watch brands such as Omega, Jaeger LeCoultre, Panerai, Bvlgari, H. Moser & Cie, Rado, Longines, and Tissot, among others. The company runs 56 retail stores across 22 cities in India (as on May 12, 2023), including New Delhi, Mumbai, Bengaluru, Hyderabad, Chennai and Kolkata. Ethos was listed in Q1 FY2023; however, KDDL continues to hold ~61% as a parent.

Key financial indicators (audited)

KDDL consolidated	FY2021	FY2022	FY2023*
Operating income	562.8	824.3	1119.5
PAT	7.0	37.2	77.0
OPBDIT/OI	14.6%	14.6%	15.0%
PAT/OI	1.2%	4.5%	6.9%
Total outside liabilities/Tangible net worth (times)	1.68	1.36	0.63
Total debt/OPBDIT (times)	3.03	2.20	1.47
Interest coverage (times)	2.73	4.00	5.49

Source: Company, PAT: Profit after tax; OPBDIT: Operating profit before depreciation, interest, taxes and amortisation; Amounts in Rs. crore

Status of non-cooperation with previous CRA: CRISIL migrated the company's ratings to 'CRISIL FB+ (Stable) ISSUER NOT COOPERATING' on December 31, 2020; on best available information with the credit rating agency.

https://www.crisil.com/mnt/winshare/Ratings/RatingList/RatingDocs/KDDL_Limited_December_31_2020_RR.html

Any other information: A member of the Board of Directors of ICRA Limited is also an Independent Director on the Board of Directors of KDDL Limited. This Director was not involved in any of the discussions and processes related to the Rating of the instrument(s) mentioned herein.

Rating history for past three years

	Instrument	Current rating (FY2024)				Chronology of rating history for the past 3 years				
		Type	Amount Rated (Rs. crore)	Amount Outstanding (Rs. crore) ^	Date & rating in FY2024	FY2023			FY2022	FY2021
					Aug 10, 2023	Nov 22, 2022	Oct 25, 2022	June 09, 2022	Dec 08, 2021	Dec-08-2020
1	**Fund-based/Cash Credit**	Long-term	33.00	33.00	[ICRA]A(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable);	[ICRA]BBB+(Positive);	[ICRA]BBB+(Positive);	[ICRA]BBB+(Stable)
2	**Fund-based/Term loan**	Long-term	24.90	23.32	[ICRA]A(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable);	[ICRA]BBB+(Positive);	[ICRA]BBB+(Positive);	[ICRA]BBB+(Stable)
3	**Non-fund Based**	Short-term	31.50	31.50	[ICRA]A1	[ICRA]A2+	[ICRA]A2+	[ICRA]A2	[ICRA]A2	[ICRA]A2
4	**Fixed Deposits**	Long-term	15.00	15.00	[ICRA]A(Stable)	[ICRA]A-(Stable)	[ICRA]A-(Stable);	[ICRA]BBB+(Positive);	MA-(Positive)	MA- (Stable)
5	**Unallocated**	Long-term	2.28	2.28	[ICRA]A(Stable)	[ICRA]A-(Stable)	-	-	-	-
6	**Fund-based**	Short-term	-	-	-	-	[ICRA]A2+	[ICRA]A2	[ICRA]A2	[ICRA]A2

Source: Company, ^outstanding as of March 2023

Complexity level of the rated instruments

Instrument	Complexity Indicator
Fund-based/Cash Credit	Simple
Fund-based/Term loan	Simple
Non-fund Based	Very Simple
Fixed Deposits	Very Simple
Unallocated	Not Applicable

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	Fund-based/Cash Credit	NA	NA	NA	33.00	[ICRA]A(Stable)
NA	Fund-based/Term loan	FY2018	NA	FY2025	24.90	[ICRA]A(Stable)
NA	Non-fund Based	NA	NA	NA	30.00	[ICRA]A1
NA	Non-fund Based-LER	NA	NA	NA	1.50	[ICRA]A1
NA	Fixed Deposits	NA	NA	NA	15.00	[ICRA]A(Stable)
NA	Unallocated	NA	NA	NA	2.28	[ICRA]A(Stable)

Source: Company

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

Annexure II: List of entities considered for consolidated analysis

Company Name	Ownership	Consolidation Approach
KDDL Limited	-	Full consolidation
Ethos Limited*	61.07%	Full consolidation
Pylania SA	100.00%	Full consolidation
Kamla International Holdings AG	100.00%	Full consolidation
Mahen Distribution Limited	100.00%	Full consolidation
Kamla Tesio Dials Limited	99.99%	Full consolidation
Cognition Digital LLP	99.99%	Full consolidation
Pasadena Retail Private Limited	50.00%	Full consolidation
Estima AG	100.00%	Full consolidation
Silvercity Brands AG	100.00%	Full consolidation

*Source: Company, *parent company*

Corrigendum

Rationale dated August 10, 2023 has been revised with following changes as below:

On page 5, complexity indicators for Fixed deposits and unallocated limits have been revised to Very Simple and Not Applicable respectively.

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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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