Press Release

Sheetal Manufacturing Company Private Limited

January 06, 2022

Rating Reaffirmed

Product	Quantum (Rs. Cr)	Long Term Rating	Short Term Rating
Bank Loan Ratings	79.00		ACUITE A1 | Reaffirmed
Bank Loan Ratings	635.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable	
Total	714.00	-	-

Rating Rationale

Acuité has reaffirmed the long-term rating of **'ACUITE A+' (read as ACUITE Single A plus)** and the short term rating of **'ACUITE A1' (read as ACUITE A1)** on the Rs.714.00 Cr bank facilities of Sheetal Manufacturing Company Private Limited (SMCPL). The outlook has been revised from 'Negative' to 'Stable'.

Rationale for Rating Reaffirmation and Revision in Outlook

The reaffirmation of the rating and the reinstatement of the outlook takes into account the significant turnaround in the operations in FY21 & FY22. While the gems and jewellery (G&J) industry had witnessed a downturn in the initial phase of the COVID-19 pandemic and led to a moderation in the revenues of SMCPL in FY21, there has been a significant recovery in demand and exports in FY22. The rating reaffirmation also takes into account the diversification in the operations by way of incorporation of a step-down subsidiary and an improvement in the debtors position, albeit there has been a marginal elongation in the working capital cycle in FY21.

About the Company

Manufacturing Company Private Limited (SMCPL) is a part of the Mumbai-based larger Sheetal Group (SG, including SMCPL and its subsidiaries) which was established in 1985 by the first-generation entrepreneurs, Mr. Govind Kakadia and his two brothers - Mr. Vallabh Kakadia and Mr. Ravji Kakadia. The company is engaged in the manufacturing and export of cut & polished diamonds (CPD), and has become one of the world's leading diamond manufacturing companies with an annual sale of more than 3 million carats. It is a designated four-star export house status by the Government of India.

Analytical Approach

Acuité has considered the consolidated business and financial risk profile of SMCPL and its subsidiaries and step-down subsidiaries, on account of significant business and financial alignment between the entities. Apart from SMCPL, the companies taken into consolidation are: Sheetal Golden Works (India) LLP (SGW) (99.97% by SMCPL), Sheetal Group USA Inc. (100% by SGW), Sheetal (Far East) Limited (SFE) (100% by SGW), Hillier Diamond (Shanghai) Co. Limited (100% by SFE), Sheetal Middle East DMCC (48.67% by SFE and 51.33% by SMCPL), and Sheetal Europe BV (89.61% by SGW and 10.04% by SMCPL). Extent of consolidation: Full.

Key Rating Drivers

Strengths

Extensive experience of promoters and long track record of operations
SG, engaged mainly into manufacturing & exports of cut & polished diamonds, has a global presence and is among one of the leading diamond players in India. They have a diversified customer base based in USA, Europe, Hong Kong, Middle East, etc. among other countries. It is also designated as four-star export house by the Government of India. This has been facilitated by the extensive experience of promoter of the group, Mr. Govind Kakadia, who has an experience of more than 5 decades into this business segment. The promoter is well-supported by the second generation in the family – Mr. Ajay Kakadia, Mr. Bharat Kakadia and Mr. Chirag Kakadia.
Acuité believes that the extensive experience of the management and established global presence will strengthen the business risk profile over the medium term.

Long-standing relationship with reputed diamond mining companies in the world
SG has a long-term association with major diamond companies viz. De Beers, Rio Tinto and Alrosa for sourcing of rough diamonds. Such contracts with key suppliers like them allow a steady supply at competitive rates. Diamond Trading Company (DTC), the marketing arm of De Beers, sells rough diamonds only to an exclusive group of manufacturers throughout the world called sight-holders. The status of being a sight-holder with these mining companies lend significant comfort to the sourcing arrangements of SG whereby they procure rough diamonds as per fixed-term contracts with DTC that also assures uninterrupted supply at competitive pricing rather than sourcing from secondary markets.
Acuité believes that SG will benefit from its position as a sight-holder giving the company a higher competitive advantage in terms of quality over the other players present in the diamond industry.

Significant turnaround in the operations in FY21 & 8MFY22 despite a moderation in revenues marked by recovery in demand and consumer sentiments in FY22
As per GJEPC (Gem & Jewellery Export Promotion Council), after having faced a downturn in FY20 due to various domestic & global factors and in FY21 due to the COVID-19 pandemic, the diamonds industry has shown a robust resurgence in FY22, especially in the exports market, after starting to make a slow comeback from the end of FY21. Due to the uncertainty surrounding the COVID-19 pandemic, it was expected that the recovery in the G&J industry might not reach the pre-COVID levels. However, the G&J exports increased by 6.04% from the pre-COVID levels of USD 11.84 billion in April 2019 to July 2019, to USD 12.55 billion in April 2021 to July 2021, which translates to a robust growth of 223.87% over the COVID levels of USD 3.88 billion in April 2020 to July 2020. Similarly, the cut & polished diamonds exports increased by 27% from the pre-COVID levels of USD 6.7 billion in April 2019 to July 2019, to USD 8.52 billion in April 2021 to July 2021, which translates to a robust growth of more than 200% over the COVID levels of USD 2.72 billion in April 2019 to July 2019. The aforementioned robust growth is owing to various factors viz. pent-up in demand and aggressive buying in key exports markets viz. USA, China and Hong Kong, restocking & management of rough diamonds inventory, mass inoculation drives, rise in purchasing power due to support by the US government for its common masses in various subsidized forms.
In line with the industry, SG's operating income declined marginally by 6.05% to Rs.2088.60 Cr in FY21 owing to disruptions caused by the COVID-19 pandemic leading to a decline in the polished diamonds carat sales in that year. However, on a standalone basis, the net sales increased significantly from Rs.1470.18 Cr in FY21 to Rs.1850.13 Cr in 8MFY22, surpassing the whole-year revenue of FY21 in 8 months. This was owing to increase in the revenues from polished diamonds on the back of a resurgence and a robust growth in the demand thereof after the gradual reduction in the impact of the COVID-19 pandemic, coupled with increased focus on certified diamonds than uncertified diamonds.
The operating margin improved from 3.86% in FY20 to 4.89% in FY21 primarily owing to decrease in proportionate material consumption costs and contract expenses on the back of increasing focus from uncertified diamonds to certified diamonds. Moreover, the employee costs also decreased owing to salary cuts and decrease in directors' remuneration undertaken in that year on the back of the COVID-19 pandemic. Given the improvement in the operating margin, the net margin also improved from 1.79% in FY20 to 3.01% in FY21. Given all of the above, the profitability increased significantly with the increase in PAT from Rs.39.76 Cr in FY20 to Rs.62.88 Cr in FY21.

Healthy financial risk profile

SG's financial risk profile is strong, marked by healthy tangible net-worth, low gearing and healthy debt coverage indicators. The tangible net-worth stood healthy at Rs.971.51 Cr as on March 31, 2021 as against Rs.931.36 Cr as on March 31, 2020. The Group's leverage policy is supported by the healthy tangible net-worth levels, reflected through its peak gearing and Total Outside Liabilities to Tangible Net-worth (TOL/TNW) levels of 1.06 times and 1.25 times respectively as on March 31, 2018. The leverage level continues to remain supported by healthy tangible net-worth with a gearing of 0.73 times and TOL/TNW of 0.99 times as on March 31, 2021. The total debt of the Group stood at Rs.707.94 Cr as on March 31, 2021, comprising working capital bank borrowings and unsecured loans from promoters & related parties. There was no significant debt-funded capital expenditure during FY21 except for routine capex entailing an expense of Rs.3.50-4 Cr funded completely out of internal accruals. The gearing is expected to be healthy in the range of 0.70-0.80 times over the medium term. On the other hand, given the healthy profitability, the debt coverage indicators also stood healthy with the interest coverage and DSCR of 4.44 times and 3.78 times respectively in FY21 as against 2.77 times and 2.08 times respectively in FY20.

Acuité expects the financial risk profile to remain healthy over the medium term on account of large scale of operations, sound debt protection measures and moderate reliance on the external borrowings resulting in stable debt protection measures.

Weaknesses

Marginal elongation in the WC cycle in FY21

The operations of SG are working capital intensive in nature with a majority of funds blocked in inventory followed by debtors. The inventory holding elongated from 115 days in FY20 to 185 days in FY21 owing to proportionately lower sales in Q1FY21 than usual, on the back of the COVID-19 pandemic. Moreover, the company underwent aggressive purchases in the month of March 2021, thereby leading to higher year-end stock. However, the collection period improved from 102 days in FY20 to 89 days in FY21 owing to increasing focus from uncertified diamonds to certified diamonds, thereby requiring comparatively lower credit period to be extended. On the other hand, the creditors' period also elongated from 7 days in FY20 to 47 days in FY21, in line with the elongation in the inventory holding. Given all of the above, the WC cycle also elongated marginally from 210 days in FY20 to 227 days in FY21, whereas the GCA days also elongated from 227 days in FY20 to 296 days in FY21. Given this, the working capital utilization stood moderately high at 69.74% in the last 6 months ended November 2021.

ESG Factors Relevant for Rating

The gems and jewellery industry and particularly the cut and polished diamond segment plays an important role in generating employment particularly in India. While employment is material from the social perspective, the sector needs to ensure a healthy and safe working environment for its employees. On the governance aspect, ethical business practices and adherence to appropriate accounting norms including arms-length accounting with overseas group entities are important for the sustainability of the business and enjoying the confidence of the stakeholders including the lenders. Although the environmental factors are not highly material, the industry has to be vigilant that the mining of the raw materials do not damage the environment in a significant manner.

SMCPL has taken some initiatives to make its business sustainable and compatible with the generally accepted ESG norms. The company's business operations abide by a code of practices outlined by the Responsible Jewellery Council (RJC). These practices address issues such as human rights, labour rights, environmental impact, mining operations and product disclosure. On the social front, SMCPL had undertaken a special vaccination drive at its manufacturing facility in Surat last year to safeguard its employees from the pandemic. This apart, the company is involved in several CSR activities which includes investment in education and healthcare. The company also provides support to people in rural areas to make their livelihoods and activities environmentally sustainable.

Rating Sensitivities

- Deterioration in the operating performance
- Any stretch in working capital operations leading to liquidity constraints

Material covenants

None

Liquidity Position: Adequate

The liquidity profile of the Group is adequate marked by healthy net cash accruals, comfortable current ratio and healthy free cash & bank balance. The operations of the company are working capital intensive in nature with GCA days and working capital cycle of 296 days and 227 days respectively in FY21 as against 227 days and 210 days respectively in FY20. Given this, the average working capital utilization in the last 6 months ended November 2021 stood moderate at 69.74%. However, the company generated healthy net cash accruals worth Rs.51.15 Cr and Rs.72.03 Cr in FY20 and FY21 respectively as against minimal debt repayment obligations worth Rs.7.35 Cr and Rs.0.21 Cr in those respective years. The company is expected to generate net cash accruals in the range of Rs.90-100 Cr over FY22-FY23, as against no debt repayment obligations over the same period. Moreover, the current ratio stood comfortable at 2.12 times as on March 31, 2021 as against 2.69 times as on March 31, 2020. Furthermore, the free cash & bank balance also stood healthy at Rs.29.39 Cr as on March 31, 2021 as against Rs.39.61 Cr as on March 31, 2020.

Outlook: Stable

Acuité believes that SMCPL will maintain a 'Stable' outlook led by strong demand sentiments leading to a favourable revenue visibility in the near term, thereby translating to healthy profitability. The outlook may be revised to 'Positive' in case the Group reports significant growth in revenue and significant improvement in the profitability. Conversely, the outlook may be revised to 'Negative' in case of a deterioration in the revenue growth and operating performance, thereby impacting its overall financial risk profile and the overall liquidity position.

Key Financials

Particulars	Unit	FY 21 (Actual)	FY 20 (Actual)
Operating Income	Rs. Cr.	2088.60	2223.22
PAT	Rs. Cr.	62.88	39.76
PAT Margin	(%)	3.01	1.79
Total Debt/Tangible Net Worth	Times	0.73	0.66
PBDIT/Interest	Times	4.44	2.77

Status of non-cooperation with previous CRA (if applicable)

Not Applicable

Any other information

Not Applicable

Applicable Criteria

• Entities In Manufacturing Sector -https://www.acuite.in/view-rating-criteria-59.htm
• Default Recognition: https://www.acuite.in/view-rating-criteria-52.htm
• Application Of Financial Ratios And Adjustments: https://www.acuite.in/view-rating-criteria-53.htm
• Consolidation Of Companies: https://www.acuite.in/view-rating-criteria-60.htm

Note on complexity levels of the rated instrument

https://www.acuite.in/view-rating-criteria-55.htm

Rating History

Date	Name of Istruments/Facilities	Term	Amount (Rs. Cr)	Rating/Outlook
05 Oct 2020	Packing Credit	Long Term	22.88	ACUITE A+ | Negative (Reaffirmed)
	Packing Credit	Long Term	19.00	ACUITE A+ | Negative (Reaffirmed)
	Letter of Credit	Long Term	104.00	ACUITE A+ | Negative (Reaffirmed)
	Bills Discounting	Short Term	15.00	ACUITE A1 (Assigned)
	Bills Discounting	Long Term	69.00	ACUITE A+ | Negative (Reaffirmed)
	Cash Credit	Long Term	45.00	ACUITE A+ (Withdrawn)
	Packing Credit	Long Term	44.12	ACUITE A+ | Negative (Reaffirmed)
	Packing Credit	Long Term	132.00	ACUITE A+ | Negative (Reaffirmed)
	Packing Credit	Short Term	25.00	ACUITE A1 (Assigned)
	Letter of Credit	Long Term	70.00	ACUITE A+ | Negative (Reaffirmed)
	Packing Credit	Long Term	133.00	ACUITE A+ | Negative (Reaffirmed)
	Proposed Bank Facility	Short Term	11.00	ACUITE A1 (Assigned)
	Bills Discounting	Long Term	25.00	ACUITE A+ | Negative (Reaffirmed)
	Packing Credit	Long Term	4.00	ACUITE A+ (Withdrawn)
	Packing Credit	Long Term	20.00	ACUITE A+ | Negative (Reaffirmed)
	Proposed Bank Facility	Long Term	11.00	ACUITE A+ (Withdrawn)
	Packing Credit	Long Term	24.00	ACUITE A+ | Negative (Reaffirmed)
01 Aug 2019	Letter of Credit	Long Term	70.00	ACUITE A+ | Stable (Assigned)
	Bills Discounting	Long Term	69.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	54.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	4.00	ACUITE A+ | Stable (Assigned)
	Bills Discounting	Long Term	25.00	ACUITE A+ | Stable (Assigned)
	Letter of Credit	Long Term	104.00	ACUITE A+ | Stable (Assigned)
	Cash Credit	Long Term	45.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	28.00	ACUITE A+ | Stable (Assigned)
	Bills Discounting	Long Term	58.30	ACUITE A+ | Stable (Assigned)
		Long		

	Packing Credit	Term	35.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	166.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	25.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	169.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	25.00	ACUITE A+ | Stable (Assigned)
	Packing Credit	Long Term	26.00	ACUITE A+ | Stable (Assigned)
	Proposed Bank Facility	Long Term	11.00	ACUITE A+ | Stable (Assigned)

Annexure - Details of instruments rated

Lender's Name	ISIN	Facilities	Date Of Issuance	Coupon Rate	Maturity Date	Quantum (Rs. Cr.)	Rating
Union Bank of India	Not Applicable	FBN/FBP/FBD/PSFC/FBE	Not Applicable	Not Applicable	Not Applicable	60.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
Bank of India	Not Applicable	PC/PCFC	Not Applicable	Not Applicable	Not Applicable	44.12	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
State Bank of India	Not Applicable	PC/PCFC	Not Applicable	Not Applicable	Not Applicable	132.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
Union Bank of India	Not Applicable	PC/PCFC	Not Applicable	Not Applicable	Not Applicable	60.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
State Bank of India	Not Applicable	Post Shipment Credit	Not Applicable	Not Applicable	Not Applicable	133.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
Bank of India	Not Applicable	Post Shipment Credit	Not Applicable	Not Applicable	Not Applicable	22.88	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
IDBI Ltd	Not Applicable	Post Shipment Credit	Not Applicable	Not Applicable	Not Applicable	24.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
Yes Bank Ltd	Not Applicable	Post Shipment Credit	Not Applicable	Not Applicable	Not Applicable	65.00	ACUITE A1 | Reaffirmed
							ACUITE A1

Not Applicable	Not Applicable	Proposed Short Term Bank Facility	Not Applicable	Not Applicable	Not Applicable	14.00	| Reaffirmed
State Bank of India	Not Applicable	Stand By Line of Credit	Not Applicable	Not Applicable	Not Applicable	97.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable
Union Bank of India	Not Applicable	Stand By Line of Credit	Not Applicable	Not Applicable	Not Applicable	62.00	ACUITE A+ | Stable | Reaffirmed | Negative to Stable

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About Acuité Ratings & Research

Acuité Ratings & Research Limited is a full-service Credit Rating Agency registered with the Securities and Exchange Board of India (SEBI). The company received RBI Accreditation as an External Credit Assessment Institution (ECAI), for Bank Loan Ratings under BASEL-II norms in the year 2012. Since then, it has assigned more than 8,850 credit ratings to various securities, debt instruments and bank facilities of entities spread across the country and across a wide cross section of industries. It has its Registered and Head Office in Kanjurmarg, Mumbai.