

Rating Rationale
Godawari Steel Private Limited

Rating

Facilities	Amount (Rs. In Million)	Rating ¹	Remarks
Long Term Bank Facilities	600.00	CARE-NP B+ [Single B Plus]	Revised from CARE NP BB [Double B]
Short Term Bank Facilities	2,900.00	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	3,500.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating to ‘CARE-NP B+’ assigned to the long-term bank facilities and reaffirmed the rating ‘CARE-NP A4’ assigned to the short-term bank facilities of Godawari Steel Private Limited (GSPL).

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to bank facilities of Godawari Steel Private Limited (GSPL) takes into account negative impact of COVID-19 on the business of the company, financial risk profile marked by subdued financial performance of the company during the first year of operation in FY19 (refers to 12 month period ended mid-July 2019) with net loss, leveraged capital structure of the company, working capital intensive nature of operations and. The rating is also constrained by foreign exchange fluctuating risk with raw material price volatility, exposure to volatile interest rates and competition from other steel players from industry. The rating, however, derives strength from established business group and experienced promoter, demand of steels products and locational advantage being located near from Nepal-India boarder. The ability of the company to maintain the revenue growth, improvement in the profitability margins and its overall solvency position will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Impact of Covid-19 on the business of the company

The outbreak of Coronavirus disease 2019 (COVID-19) which was recognized as Pandemic by World Health Organization on March 11, 2020, has affected Nepal as well. Government of Nepal (GoN) imposed travel restrictions and countrywide lockdown since March 24, 2020 closing most of the organizations which resulted in slowing down of the economic activities. Due to the lockdown, sales of GSPL has slowed down which has directly impacted the revenue of the company. Nepal Rastra Bank (NRB) has provided an extension of 3 months for the repayment of loans falling due in mid-April 2020 to provide some temporary relief. GSPL is eligible for 2% rebate on interest charged for the quarter ended on mid-July 2020 as per the provision of NRB. Lower sales than the projected levels and pressure on the profitability of the company due to high competition along with high interest cost and debt repayment obligations, the liquidity position of the company is expected to be remain stretched.

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com

Key Rating Weaknesses***Subdued financial performance of the company during the first year of operation in FY19 with net loss***

During FY19, GSPL commenced its operations for manufacturing of TMT bars which is its primary product. The company achieved Commercial Operation Date (COD) from April 2019 against the projected COD of October 2018 and FY19 was company's first year of operation. During FY19, on back of delay in COD, the company reported low revenue of Rs. 394 Mn and reported negative PBILDT of Rs. 1.33 Mn. Further, the company reported net loss of Rs. 70.39 Mn during FY19 on account of high interest cost of Rs. 21.61 Mn and depreciation of Rs. 47.90 Mn. Gross cash accruals of the company was negative Rs. 22.48 Mn in FY19.

Highly leveraged capital structure and weak debt service coverage indicators

Debt-equity ratio of the company was high at 4.28x at the end of FY19 with overall gearing ratio of 6.90x. Total debt of the company is high amounting to Rs. 1,583 Mn majorly on account of high working capital loans in the books amounting to Rs. 601 Mn at the end of FY19. Interest coverage ratio and Total Debt to GCA was negative on account of negative PBILDT. Also, the company has received loan from directors amounting to Rs. 379 Mn at the end of FY19 which increased from Rs. 75 Mn at the end of FY18 to fund the operations and financial obligations of the company.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature as GSPL is involved in the manufacturing of TMT & plain Steel Bars by procuring raw materials through imports. The company has to procure raw materials through Letter of credit at sight and also has to fund inventory and debtors which lead to high reliance on working capital limits. In FY19, the debtor's turnover days was 82 days. The company keeps inventory for around four months and the inventory turnover was 102 days for the FY19. Total operating cycle of the company was 154 days in FY19. This leads to high reliance of the company on the bank finance for working capital needs. The average monthly outstanding of fund-based working capital limit against drawing power was more than 90% during last 12 months period ended mid-June 2020.

Exposure to volatile interest rates

Nepalese banking sectors are fixing interest rate on lending by adding certain percentage of premium on quarterly base rate and interest rate is changed accordingly on quarterly basis. Base rate of the Bank and Financial Institutions is changed by change in liquidity position which leads to change in interest rate. Interest rate has been changing frequently in Nepal market since last 1-2 year. Therefore, funding from Bank and Financial Institutions are exposed to volatile interest rate.

Raw material price volatility risk and foreign exchange fluctuation risk

GSPL does not have any backward integration for basic raw material (MS Billets) required for producing TMT & plain steel bars and would imports from India. The prices of the billets are market linked and

determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. The raw material cost generally stands at around ~89% of the total operating income in the steel industries, thus, any volatility in prices of the same impacts the profitability of the company. Further, majority of raw material requirement is met through imports and the prices of the same are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. The ability of the company to pass through changes in raw material prices to the finished products and managing the foreign exchange fluctuation risks related to raw materials will be the key rating sensitivities.

Presence in highly fragmented and competitive nature of steel industry

The iron and steel industry is intensely competitive and fragmented marked by the presence of both larger players and numerous smaller players in the unorganized segment. Given the fact that the entry barriers to the industry are low, the players in the industry do not have pricing power and are exposed to competition-induced pressures on profitability. The demand of iron & steel products is considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry. Furthermore, the value addition in the steel products TMT bars and related products is low, resulting into low product differentiation in the market. Further, with increase in the capacities of the existing plants and new capacities coming into operation competition has intensified which has resulted into substantial decline in profitability margins of the industry players in the current year. As per latest NRB report published on mid-January, 2020, the total capacity utilization of TMT Bars and other allied products in Nepal was at 63.60% during FY18 which reduced to 61.50% during FY19, however with increase in total production by ~8% during FY19.. Also, in order to push sales to sustain the competition credit sales in the market has substantially increased leading to increased debtor days and high working capital requirement for companies. The producers of steel construction materials are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility in the steel prices.

Key Rating Strengths

Established business group and experienced promoter in trading business, however, limited experience in the manufacturing industry

GSPL is promoted by Mr. Munna Prasad Senuriya Baniya, who is associated with Godawari Business Organization (GBO) as an Executive Director. GBO is an ancestral business of the promoter and was established in 1950. The group has been involved in manufacturing of HDPE pipes, garden pipes & water tanks, trading and supply of construction materials, repairing of transformers and fabrication, trading of hardware in drinking water projects. Since the group is operating in the similar line of business in the Nepalese market for decades, it gives them an advantage of existing distribution channel for marketing of manufactured goods from GSPL. The day to day activities of the company are handled by Mr. Senuriya who possesses more than two decades of extensive experience in the related field.

Demand of steels products in the country

Nepalese economy is developing and growing, as is in phase of investment in infrastructure sectors, power sector and tourism sector. It is highly probable that the national economy will be in need of construction materials in developing public as well as private infrastructures, road, bridges and other public facilities. Also, in the recent budget presented by finance minister of Nepal for FY21, the Government has allocated budget of Rs. 55 Billion for reconstruction and also government has majorly focused towards development of health sectors, tourism sectors and other infrastructure development. Further, the government's high emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures and estimated GDP growth of 7.00% as included in the budget for FY20-21 is likely to benefit the cement manufacturers like GSPL.

Locational advantage

The plant is located nearby the proposed Nijgadh International Airport of Nepal; it is expected to create demand for its products in the nearby market as the nearby areas are expected to be developed. In addition, the construction of proposed fast track from Nijgadh to Kathmandu will also positively create demand at local level for the products of the company. Furthermore, the plant site is located around 20 Kms from Nepal-India Border (Gaur Customs), which makes the location of the plant nearness to the big Indian State Bihar and give GSPL an advantage of supply of raw material at lower transportation cost. GSPL can also use Birgunj Border, either via railways till Raxaul (~75 kms from plant location) or via road. The Gaur border is less busy than Birgunj and hence imports of raw material will be more convenient for GSPL. GSPL can exploit opportunity by focusing nearby markets for finished goods at lower transportation cost than its competitors.

About the Company

Godawari Steel Private Limited (GSPL) is a private limited company promoted by businessman, mainly engaged in manufacturing and trading businesses. The factory is located at Chandranigahapur, Rautahat, Nepal and operating since April 2019. The company is manufacturing TMT & plain Steel Bars with operational capacity of 350MT per day by importing raw materials (mainly Ms Billet) from India and selling them into Nepal's market. The entire capital of the company will be held by the sole promoter Mr. Munna Prasad Senuriya Baniya.

Brief Financial Performance of GSPL during last year is given below:

(Rs in Million)

Particulars	FY19 (A)
Income from operations	394
PBILDT	(1)
PAT	(70)
Interest Coverage ratio (times)	Negative
Overall gearing (times)	6.90

**Audited*

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Annexure 1: Details of the Facilities rated

Nature of Facility	Type of Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	600.00	CARE-NP B+
Short Term Bank Facilities	Working Capital	1550.00	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limit	550.00	CARE-NP A4
Short Term Bank Facilities (Proposed)	Working Capital	800.00	CARE-NP A4
Total		3,500.00	