

Rating Rationale
Panchakanya Steel Private Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	219.93	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	5,030.07	CARE-NP A4 [A Four]	Assigned
Total facilities	5,250.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Ltd. (CRNL) has assigned rating of ‘CARE-NP BB’ to the long-term bank facilities and ‘CARE-NP A4’ to the short-term bank facilities of Panchakanya Steel Private Limited (PSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of PSPL factors in declining scale of operations on y-o-y basis, leveraged capital structure and weak debt service coverage indicators. The ratings also factor in PSPL’s working capital intensive nature of operations, raw material price volatility and foreign exchange fluctuation risk, exposure to volatile interest rates coupled with presence in highly fragmented and competitive nature of steel industry.

The ratings, however, derive strength from established and long track record of operations along with experienced management team in the related field, established brand with country wide market presence and demand of steel products in the country. The ratings also factor in improvement in margins and profitability in H1FY21 (unaudited, refers to 6 months period ended mid-January, 2021).

Ability of the company to increase its scale of operations while improving its profitability margins and rationalization of its debt through efficient working capital management will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Below Average financial risk profile

For the period FY18-FY20 (FY refers to 12 months period ended mid-July), PSPL’s total operating income has been declining on y-o-y basis from Rs. 5,221 Mn. in FY18 to Rs. 3,265 Mn. in FY20. The decline in scale of operations was on account of decline in quantity sold. The decline in TOI in FY20 was mainly on account of impact on the business operations of the company as GON imposed the lockdown in Q4FY20. The same led to temporary shut-down of operations of the company.

PBIDLT margin of the company remained range bound at around 7% except for FY19. PBIDLT and PAT margin declined in FY19 due to decline in capacity utilization which resulted in increase in cost due to high

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

proportion of fixed cost which deprived it of its scale benefits and increase in interest expenses respectively. The company also reported net losses during FY19.

The company had leveraged capital structure due to high dependence on external borrowings to meet its working capital requirements. As on mid-July, 2020, the overall gearing ratio of the company stood high at 5.11x. Apart from overall gearing, other coverage indicators including total debt to GCA and Interest coverage ratios for the company stood weak at above 74x and 1.15x for FY20 respectively on account of declining PBIDLT and increasing debt levels on y-o-y basis.

Current year performance in H1FY21: In H1FY21 (refers to 12 months period ended mid-January, 2021), the company has reported total revenue of Rs. 2,586 Mn and achieved PBIDLT margin of 9.31%. The improvement in margin was support by increase in average selling price per ton and also the cost cutting measure adopted by the management.

Working capital intensive nature of operations

The company has working capital intensive nature of operations as reflected by high working capital utilization of about 90% for the last 12 months ended Mid-January, 2021. Moreover, the company had a low current ratio of 1.14x as at the end of FY20. The company has exceptional high average operating at the end of FY20. Being a highly competitive business, the company has to extend credit period to its dealers which is upto 90 days whereas company has to make immediate payment to its suppliers. The company is required to maintain adequate inventory of raw material for smooth running of its production processes. Furthermore, being a manufacturer, it is critical for the company to maintain minimum inventory levels to meet immediate demand of its customers; all this led to elongated operating cycle which resultant into high working capital requirements.

Raw material price volatility risk and foreign exchange fluctuation risk

The major raw materials for PSPL are majorly imported from India, the prices of which are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices which has a bearing on its profitability margins. The raw material cost contributed around 88% of the total operating income of the company during FY20, thus, any volatility in prices of the same impacts the profitability of the company. Also, the company is exposed to foreign exchange fluctuation risk as the prices of imported raw materials are linked to USD. 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. 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 like TMT bars, sheets & related products is low, resulting into low product differentiation in the market.

Key Rating Strengths

Established brand and long track record of operations along with experienced management team in the related field

PSPL has an operational track record of more than two decades in manufacturing of TMT Bars. PSPL derives strength from its strong promoter group belonging to Panchakanya Group. Panchakanya Group is one of the established business group having presence from 1970s in the market of Nepal and involved in diversified business of trading, automobiles, manufacturing etc. The company is managed under the overall guidance of its seven-member board of directors who possess wide experience in various industries and trading business. Mr. Prem Bahadur Shrestha, is Director and Chairman of PSPL and is engaged in industry, import, export, and service and commerce/business sector for more than 5 decades. Mr. Pradip Kumar Shrestha is the Managing Director of PSPL and he supervises the operations of the various companies in the Group and has an experience of more than 4 decade through various entities in the same group.

Established brand with country wide market presence

The company sells TMT bars under the brand name of “Panchakanya” which is an established brand in the Nepal market on account of its long-standing presence in the construction industry. This provides leverage to the company in front of new players entering the industry. Further, PSPL has a customer base of around 90 dealers across all major cities and 7 depots in Balkhu, Lalitpur, Bhairahawa, Pokhara, Dhangadi, Nepalgunj and Bitrtamode; which provides a ready market for its products.

Demand of steels products in the country

Nepalese economy is developing and growing and is in phase of investment in infrastructure, power sector and tourism sector. In the budget presented by finance minister of Nepal for FY21, government has allocated Rs. 55 Bn for reconstruction with major focus towards development of health sectors, tourism sectors and other infrastructure development. However, with economic activities affected by COVID-19 pandemic, demand for steel may be subdued in short term, but with government focus on infrastructure, demand is likely to grow in long run. Government’s high emphasis on infrastructure development and power sector in the budget for FY20-21 is likely to benefit the steel manufacturers like PSPL.

About the Company

Panchakanya Steel Private Limited (PSPL) is a private limited company incorporated on May 31, 1995 for manufacturing TMT Steel bars, Wires, Nails etc, having plant in Birgunj, Nepal. As on Mid-January, 2021, the company has installed capacity of 150,000 Metric Tons Per Annum (MTPA).

Brief financials of PSPL during last 3 years and H1FY21 is given below:

(Rs. Million)

For the year ended Mid-July	FY18	FY19	FY20	H1FY21
	(Audited)			(Unaudited)
Income from Operations	5,221	4,574	3,265	2,586
PBILD Margin (%)	7.11	5.44	7.78	9.31
Overall Gearing (times)	3.51	4.66	5.11	5.65
Interest Coverage (times)	2.03	0.88	1.15	2.53
Current Ratio (times)	1.14	1.01	1.14	1.20
Total Debt/Gross Cash Accruals (times)	12.04	NM	74.75	28.17

Analyst Contact Mr. Rishi Ram Poudel rishi.poudel@careratingsnepal.com Tel No.: +977-01-4012629	Group Head Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4012629	Relationship Contact Mr. Achin Nirwani achin.nirwani@careratingsnepal.com Tel No.: 9818236069/+977-01-4012628/29/30
--	--	---

Disclaimer

CRNL's ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	219.93	CARE-NP BB
Short Term Bank Facilities	Fund Based Limit	4,580.00	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limit	450.07	CARE-NP A4
Total		5,250.00	