

United Traders Syndicate Private Limited

Rating

Facility/Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Short Term Bank Facilities- Fund Based Facilities	4,000.00 (Increased from 3,100.00)	CARE-NP A3 [A Three]	Revised from CARE-NP A4+
Total Facilities	4,000.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the short term bank facilities of United Traders Syndicate Private Limited (UTSPL) to CARE-NP A3 from CARE-NP A4+.

Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities of UTSPL takes into account the company's improved financial risk profile marked by rebound in sales and profitability along with moderate capital structure during FY21 (Audited, refers to the twelve-month period ended mid-July 2021) and H1FY22 (Unaudited, refers to the six-month period ended mid-January 2022). The rating continues to derive strength from UTSPL's experienced and resourceful promoters, its long track record of operations, association with strong brand as sole distributor in Nepal, and presence of an established dealer network.

The rating, however, continues to remain constrained by working capital intensive nature of operations, exposure to volatile interest rate, foreign exchange rate fluctuation risk, cyclical nature of auto industry and high competition from other automobile players. The rating also factors in exposure to regulatory risk related to the automobile industry, particularly the near-term impact of the import restriction for passenger vehicles announced by the Government of Nepal (GoN) till mid-July 2022.

Going forward, the ability of the company to profitable scale up its operations and improvement in its overall solvency position will be the key rating sensitivities. Going forward, any further regulatory development related to tightening the imports, which would impact the business profile of the company will also be key rating sensitivity.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Improved financial risk profile marked by rebound in sales and profitability along with moderate capital structure

The total income of UTSPL grew 47% year on year to Rs. 4,864 Mn during FY21 from Rs. 3,304 Mn during FY20 backed by higher sales volume during the year (526 units sold in FY21 compared to 310 units in FY20) mainly due to increased demand of vehicles after gradual normalization of economic activities after relaxation of government announced lockdown. The demand for passenger vehicles continued into H1FY22 with the company reporting Rs. 4,445 Mn revenue on sale of 305 units. Higher demand for newly launched models (in Nepal) and new facelifted variants of established models, in particular, has added to UTSPL's sales growth over FY21-H1FY22. Consequently, PBILDT margin of the company improved from 5.13% in FY20 to 8.09% in FY21 boosted by increased price realization coupled with better absorption of fixed expenses amid increased revenue. The company reported net profit of Rs. 126 Mn during FY21 as compared to net loss of Rs. 47 Mn in FY20. The improvement in profitability continued into H1FY22 with the company reporting PBILDT margin of 9.87% and net profit of Rs. 217 Mn for H1FY22. The overall gearing ratio of the company improved to 2.30x at the end of FY21 compared to 2.86x at the end of FY20 aided by accretion of profit to the reserves. The overall gearing improved further to 2.19x at the

¹Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications.

end of H1FY22 amid improved profitability. Similarly, the interest coverage ratio of the company remained adequate at 4.98x during H1FY22 improving further from 2.26x in FY21.

Established brand presence of Toyota vehicles in Nepal, boosted further by new models/variant launches

UTSPL is the authorized distributor of Toyota Motor Corporation (TMC), which is among the market leaders in global passenger vehicle segment. Known for its durability, innovation and product quality, Toyota has built a strong brand equity over the years and has a strong brand presence in Nepal, particularly in the SUV segment. As a sole authorized distributor of Toyota vehicles and established dealer network, UTSPL has a large demand catering opportunity in Nepal, which links the fortune of the company to demand for Toyota vehicles in the country. UTSPL has introduced new models such as RAV4 Hybrid, Corolla crossover and new variants of segment leading Fortuner and Prado models during FY21. Improved sales of these new models/variants have particularly helped the company's financial performance over FY21 and H1FY22. Updated portfolio coupled with strong brand recall of Toyota augurs well for the business prospects of the company over the long run in the highly competitive automotive industry.

Experienced and resourceful promoters with long track record of operations

Incorporated in June 1971, UTSPL has a long track record of over 5 decades as the sole distributor of Toyota vehicles in Nepal. UTSPL derives strength from its strong shareholders being a part of the Vaidya's Organization of Industries and Trading Houses, which has a long established presence in Nepal through their group entities engaged in automobile trading and agro based industry. Mr. Suraj Vaidya, is the president of UTSPL since last 30 years. He is a past President of Federation of the Nepal Chamber of Commerce and Industries. Mrs. Ritu Singh Vaidya, managing director, looks after day-to-day operations of the company along with an experienced management team.

Established dealer network

UTSPL has an established dealer network with total 10 dealers in major cities of Nepal (i.e. Kathmandu, Lalitpur, Pokhara, Chitwan, Butwal, Biratnagar, Janakpur, Dhangadi, Nepalgunj, Jhapa). Additionally, the company has three owned showrooms (one showroom for vehicles and two showrooms for spares parts) along with two owned service centers. The company has an integrated mode of operations, functioning in various verticals of automobile dealership business to provide one stop solution to its customers. It operates service stations, sells spare parts, and has tie-ups for vehicle finance and insurance. This allows it to provide a comprehensive range of services to the customer at a single point.

Key Rating Weaknesses

Working capital intensive nature of operation

Automobile dealership business in Nepal has inherent high working capital intensity due to high inventory holding requirements and credit to the dealers. The company needs to maintain fixed level of inventory for display and high level of inventory to guard against supply shortages as the supply is totally dependent upon imports. Apart from this, the vehicle manufacturer/ supplier delivers vehicle only against the letter of credit. Thus, the business operations depend heavily on working capital borrowings. Average utilization of working capital limit was around 82% of drawing power during twelve-month period ended January 2022. During FY21, UTSPL had average inventory holding period of 62 days (FY20: 87 days) and average collection period of 99 days (FY20: 143 days). As a result, the overall operating cycle during FY21 decreased to 156 days from 224 days in FY20. The overall operating cycle returned to normal levels after being stretched in FY20 due amid the first wave of the pandemic.

Exposure to volatile interest rate and foreign exchange rate fluctuation risk

Nepalese banking sectors are fixing floating interest rate on lending by adding certain percentage of premium on quarterly base rate and interest rates are updated accordingly on quarterly basis. Base rate of the Bank and Financial Institutions (BFIs) remains volatile to change in liquidity position which lead to change in interest rate. Therefore, funding from BFIs is subject to volatile interest rate. Furthermore, UT SPL imports vehicles from various countries like India, Japan, Thailand and Indonesia. The pricing of imported vehicles from Japan is in Yen, India in INR and everywhere else in USD, exposing the company to foreign currency exchange rate fluctuation risk. The company currently does not hedge its forex exposure.

Cyclical nature of the auto industry and high competition from other automobile players

The demand for passenger vehicles is inherently vulnerable to the economic cycles and is highly sensitive to interest rates. Demand for passenger vehicles increases during period of high economy growth rate period and low interest rate regime and vice-versa. Also, there is stiff competition from other automobile dealerships in Nepal with large number of players operating in market. Competition is also intensified due to introduction of electric vehicles, which have a lower duty/tax regime. Due to high competition, dealers are forced to provide discounts and schemes to attract customer, which put pressure on its profitability.

Exposure to regulatory risk related to automobile industry

The demand in automobile sector is impacted by heavy import duty (which include custom duty, excise duty and value added tax) imposed on the import of automobiles which are still considered as luxury items in Nepal. Amid a slew of restrictions to limit outflow of foreign reserve, the Government of Nepal (GoN) recently decided to ban import of non-essential items listed under 10 categories on April 26, 2022 which included jeeps, cars and vans. Although the imposition is announced till mid-July 2022, continuation of the same for a longer period will have an adverse impact on the automobile trading industry. Dealership business of UT SPL remains exposed to similar policies of the GoN/Central Bank. This will remain a key monitorable.

About the Company

United Traders Syndicate Private Limited (UT SPL) was incorporated in June 18, 1971 by Dr. Vijay G. Vaidya as a sole distributor of Toyota vehicles for Nepal. The group is involved in trading Toyota vehicles, spare parts and services since 1967. The company shares are owned by mainly three shareholders, Mr. Suraj Vaidya (60%), Mrs. Ritu Singh Vaidya (30%) and Mrs. Susan Vaidya Shrestha (10%).

Brief financials of UT SPL for FY20, FY21 and H1FY22 are given below:

(Rs. Million)

For the year ended Mid-July	FY20 (Audited)	FY21 (Audited)	H1FY22 (Unaudited)
Income from Operations	3,305	4,864	4,445
PBILDT Margin (%)	5.13	8.09	9.87
Overall Gearing (times)	2.86	2.30	2.19
Interest Coverage (times)	0.79	2.26	4.98
Current Ratio (times)	1.22	1.27	1.32
Total Debt/Gross Cash Accruals (times)	Negative	11.79	4.85

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Short Term Bank Facilities	Fund Based Limit	3,060.00	CARE-NP A3
Short Term Bank Facilities	Non-Fund Based Limit	830.00	CARE-NP A3
Short Term Bank Facilities	Proposed	110.00	CARE-NP A3
Total		4,000.00	

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