

Balaji Cement Industries Private Limited

Ratings

Facility	Amount (Rs. in Million)	Rating ¹	Rating Action
Long Term Bank Facilities	1,476.14 (Increased from 1,157.54)	CARE-NP B+ [Double B Minus]	Revised from CARE-NP BB-
Short Term Bank Facilities	940.30	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	2,416.44		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the long term bank facilities of Balaji Cement Industries Private Limited (BCPL) to 'CARE-NP B+' from 'CARE-NP BB-' and has reaffirmed the rating of 'CARE-NP A4' assigned to the short term bank facilities of BCPL.

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the bank facilities of BCPL takes into account the weakening of financial risk profile of the company on year on year basis marked by inability to scale up the operations as envisaged leading to net losses in FY21 (Audited; refers to the twelve-month period ended mid-July 2021). The ratings are constrained by BCPL's relatively short track record of operations, leveraged capital structure, weak debt service coverage indicators, lack of backward integration and raw material price volatility risk, and exposure to volatile interest rates. The ratings also factor in the company's elongated operating cycle leading to working capital intensive nature of operations, and presence in highly competitive industry.

The ratings, however, derive strength from the company's experienced promoters in manufacturing industries, product diversification with own brands, locational advantage of the manufacturing facility, and favorable demand outlook for cement products in the country over the medium term.

The ability of the company to improve its overall financial risk profile along with rationalization of its debt levels and improving its operating cycle would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Weakening of financial performance in FY21 and short track record of operations

During FY21, the second full year of operation, BCPL generated a total operating income (TOI) of Rs. 753 Mn, registering a decline by 28.96% over FY20. The decline in TOI was marked by decline in quantity sold coupled with decline in average price realizations, amid competitive pressures. The capacity utilization stood low at 16.24%, declined from 20.62% in FY20. With the decline in TOI, PBILDT of the company also stood negative in FY21, compared to a PBILDT margin of 11.79% in FY20. The company had significant interest expense in FY21, resulting in net loss of Rs. 191 Mn compared to net profit of Rs. 2 Mn in FY20. BCPL has a relatively short track record of operations as compared with other established players in the industry. The company's growth prospects hinge on its ability to profitably scale up its capacity utilization levels, which remains a challenge in an increasingly competitive landscape.

Leveraged capital structure with weak debt service coverage indicators

BCPL has a leveraged capital structure on account of high dependence on external debt taken to support its working capital requirements, in addition to the term loan taken to set up its manufacturing facilities. Debt-equity ratio of the company deteriorated to 2.62x at the end of FY21 from 1.67x at the end of FY20 due to decrease in tangible net worth on account of

net losses during FY21. This also resulted in the deterioration of overall gearing to 4.21x at the end of FY21, from 2.78x at the end of FY20. Furthermore, high finance expenses have restricted the company's profitability and has led to negative GCA levels. The interest coverage ratio of the company also stood negative in FY21 due to the company's inability to generate gross profits.

Elongated operating cycle and working capital intensive nature of operations

The operations of the company are highly working capital intensive as the company requires to maintain the requisite inventory to ensure smooth running of operations. The high credit period extended to its customers also keeps the working capital utilization on a higher side. In addition to this, raw materials for BCPL such as slag, gypsum and fly ash imported from India are purchased mainly against advances or cash payments. Average inventory period and average collection period were 56 days and 202 days respectively during FY21 (FY20: 25 days and 93 days respectively) whereas average payable period stood at 25 days, thus leading to an elongated operating cycle of 233 days, stretched from 93 days in FY20. The high working capital requirements were met largely through bank borrowings.

Lack of backward integration and raw material price volatility risk

BCPL's operations involves producing only cement through its grinding unit, as company does not possess its own clinker unit. Hence, the company needs to procure clinker from other clinker manufacturers within in Nepal, who are also its competitors. Raw material cost continues to be the major cost component of BCPL against the net sales. Hence, any adverse movement in raw material price without any corresponding movement in finished goods price is expected to affect the profitability of the company. The ability of the company to pass through adverse changes in raw material prices to its customers will be critical for ensuring its profitability.

Presence in highly competitive industry

BCPL is operating in a highly competitive market, dominated by the large cement manufacturers with wide brand acceptability. Given the presence of large number of established players in the industry, new players do not have pricing power and are exposed to competitive pressures thus impacting profitability. The demand for cement is also considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry. Furthermore, with the increase in capacities of the existing plants, and new plants coming into operation, competition has intensified and has resulted into substantial decline in profitability margins of the industry players in the recent years.

Exposure to volatile interest rates

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy. Furthermore, increased bank rates announced in the Monetary Policy for FY23 is likely to add to the upward pressure on interest rates going forward. Any significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company from BFIs is subject to volatile interest rate.

Key Rating Strengths Experienced promoters in manufacturing industries

BCPL is promoted by industrialists and traders who have diversified businesses interests such as manufacturing of cement, agro processing, textiles, steel trading and building construction materials. Mr. Rahul Kumar Agrawal, Chairman, has also been the Managing Director of Shiv Shakti Group for 23 years, engaged in manufacturing of plastic fabric, packaging, laundry soap and agriculture-based products. Mr. Gaurav Agrawal Gadia, Managing Director, has more than 14 years of experience in textiles industry, including import of industrial raw materials and readymade garments. The promoters have been infusing funds to cover shortfall in operational cash flow of the company.

Product diversification with own brands and locational advantage of the manufacturing facility

BCPL manufactures Ordinary Portland Cement (OPC), Portland Pozzolana Cement (PPC) and Portland Slag Cement (PSC) under four brands (Chandrauta, Natraj, Shristi and Bahubali), which has usages on all types of residential, commercial & industrial projects, dams & other mass concrete works, water retaining structures, concrete roads & flyovers etc. Currently, BCPL is focusing its marketing and distribution setup in the western region of Nepal.

The manufacturing facility of BCPL is located in the western region of Nepal at a distance of 65 km from Butwal city and at a distance of 80 km from Bhairahawa (one of the biggest industrial belts in Nepal). It gives the company an opportunity to market its products in the western and mid-western region of Nepal at low cost, as the major cement manufacturers with established brands are located in central and eastern cities. In addition, it is also nearby the Indian border (17 Km), thus having an advantage in terms of transportation cost while importing raw materials.

Stable demand outlook for cement products in the country over medium-term

Nepalese economy is developing and is in the phase of investment and growth in infrastructure, power and tourism sector, notwithstanding the impact of the covid-19 pandemic. In the recent budget presented by finance minister of Nepal for FY23, Rs. 161.56 Bn has been allocated for infrastructure development along with an estimated GDP growth of 5.20%. Government's continued high emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures augurs well for the business prospects of cement manufacturers like BCPL over the medium term. Furthermore, as per Department of Customs, Nepal imported cement worth ~Rs. 47 Mn and clinker worth ~Rs. 321 Mn during 11MFY22 (refers to the eleven month period ended mid-June 2022) which indicates that domestic demand for cement and its raw materials is yet to be fully met through internal production.

About the Company

Balaji Cement Industries Private Limited (BCPL) is a private limited company, established in May 13, 2016 and commenced operations from June 15, 2019. BCPL has a clinker grinding unit with installed capacity of 1,800 metric tons per day. The company is engaged in manufacturing of Ordinary Portland Cement (OPC), Portland Pozzolana Cement (PPC), Portland Slag Cement (PSC) and selling them under four registered brands.

Brief financials of BCPL for the past three years ended FY21 are given below:

	(Rs. Million)		
For the year ended Mid-July	FY19 (Audited)	FY20 (Audited)	FY21 (Audited)
Income from Operations	6	1,060	753
PBILDT Margin (%)	-ve	11.79	-ve
Overall Gearing (times)	1.76	2.78	4.21
Interest Coverage (times)	NM	1.63	-ve
Current Ratio (times)	2.87	0.94	0.68
Total Debt/Gross Cash Accruals (times)	-ve	39.40	-ve

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	1,476.14	CARE-NP B+
Short Term Bank Facilities	Fund Based Limit	740.00	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limit	200.30	CARE-NP A4
Total		2,416.44	

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