

Arihant Import & Export Private Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	35.00	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	795.00	CARE-NP A4 [A Four]	Assigned
Total Facilities	830.00 (Eight Hundred and Thirty Million Only)		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (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 Arihant Import & Export Private Limited (AIEPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of AIEPL are constrained by its highly leveraged capital structure with weak debt service coverage indicators and working capital intensive nature of operations. The ratings also factor in limited track record of operations, exposure to volatile interest rate and foreign exchange fluctuation risk. The ratings, however, derive strength from AIEPL's experienced promoter in trading and manufacturing business and its growing scale of operations. The ratings also factor in established distribution network coupled with support from group associates with broadened yet interrelated scope of operations.

Going forward, the ability of the company to profitably scale up its operations on a sustainable basis and effective management of working capital leading to improved solvency indicators will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Working capital intensive nature of operations

AIEPL's operations are working capital intensive in nature. The company is required to maintain adequate level of inventory to avoid stock out as the supply is totally dependent upon imports. AIEPL imports its products from foreign countries and stocks them in its warehouse and the marketing and distribution happens through its three branches. AIEPL's average inventory holding period stood at 126 days in FY22. Furthermore, average collection period was also high at 156 days in FY22, which had increased from 90 days in FY21 due to ongoing liquidity crisis resulting in challenges in collection from its customers. Consequently, total operating cycle of the company was substantially high at 232 days in FY22. This resulted in increased reliance on bank borrowings to meet working capital needs leading to a relatively high debt levels. The average working capital utilization of the company against the drawing power remained high at more than 90% during the last 12 months ended mid-December 2022.

Highly leveraged capital structure with weak debt service coverage indicators of the company

The capital structure of AIEPL stood highly leveraged marked by overall gearing ratio of 4.38x as on mid-July 2022, albeit improving from 5.50x as on mid-July 2021 aided by increased net worth base supported by equity infusion coupled with accrual of profits. The increasing trend in networth, however, is likely to remain offset by increasing debt requirement of the company going forward to cater the ongoing capex as well as to support the growing scale of the company, which could lead to increased utilizations of the working capital facilities. This is likely to result in a sustained high gearing level of the company over the near-term with limited gearing headroom. Similarly, debt coverage indicators stood weak with interest coverage ratio

¹Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

of 1.29x in FY22 (Unaudited; FY refers to the twelve-month period ended mid-July). Total Debt/Gross Cash Accruals also stood high at above 50x during FY22. Although coverage indicators improved sequentially over FY21 (Audited), these remain below average as the total debt on AIEPL's books remains relatively higher commensurate to its operations.

Limited track record of operations, although part of an established group

AIEPL was incorporated in November 14, 2006, however it started its commercial operations in FY19 and therefore, has a limited track record of less than four years of commercial operations. However, AIEPL is a part of Arihant group which deals with a large number of wholesalers and traders, with whom it has been associated for over two decades. The group is involved in diversified business like automobiles, trading, and remittance service among others, which bodes well for the business prospect of the company going forward.

Exposure to volatile interest rate

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, with substantial upward pressure on interest rates in the last few quarters. A contractionary monetary policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in the rate hikes taken by BFIs so far in FY23. Any further 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.

Foreign exchange fluctuation risk and input price volatility risk

AIEPL imports diversified products such as coal, copper, sanitary wares, plastic, polymers, etc. from various countries and distributes them in Nepal. AIEPL has to make payment to its foreign suppliers in USD and hedging for the same is not exercised which exposes AIEPL to the risk associated with the fluctuation in foreign currency exchange rate. The raw material cost stood at around 90% of the total operating income of the company during FY22. The ability of the company to pass through changes in raw material prices to the customers and managing the foreign exchange fluctuation risks related to raw materials will be the key rating sensitivities.

Key Rating Strengths

Experienced promoter in trading and manufacturing business

AIEPL is owned by institutional promoters like Arihant Infrastructure Limited, Arihant Steel & Alloy Casting Private Limited and Arihant Real Estate Developers jointly owning 41.80% of the total capital of AIEPL. Furthermore, the company is managed under the overall guidance of the Company's Board of Directors (BoD) who possesses wide experience in the related field. Mr. Girish Kumar Lunia, Managing Director, has been involved in different businesses from the last two decades and is supported by team of qualified and experienced professionals to run the day-to-day operations of AIEPL.

Growing scale of operations, although net profitability remains minimal amid increasing finance cost

AIEPL's financial performance was marked by an increasing scale of operations over the past three years (FY20-FY22). AIEPL reported Total Operating Income of Rs. 1,049 Mn in FY22, growing at a CAGR of 119.32% over FY20-FY22. Boosted by higher revenues, PBIDLT margin of the company improved to 7.19% in FY22 from 2.68% in FY19. However, PAT of the company remains minimal at Rs. 13 Mn in FY22, albeit increasing from Rs. 6 Mn in FY2. The relatively lower net margin was on account of increasing finance cost of the company. Although scale of operations of the company has been growing, material improvement in

its credit risk profile going forward would hinge on its ability to expand net profitability and this will be crucial from credit perspective.

Established distribution network coupled with support from group associates with broadened yet interrelated scope of operations

AIEPL has its corporate office in Biratnagar and is operating via three branches located in Itahari, Bhairawa and Birgunj. Furthermore, having association with group companies that are diversified yet interrelated has supported AIEPL to generate organic and trajectory growth in the overall trading sectors, deriving the benefits of cross selling of products. Being a part of Arihant Group has aided the company in reducing the company's risk by product diversification followed by lowering the cost of marketing and sales. AIEPL also derives the benefit of retained customers due to selling to its associated entities. With the involvement of promoters in similar line of business, AIEPL stands to leverage on the group's experience, networking and existing distribution channel.

About the Company

Arihant Import & Export Private Limited (AIEPL) was incorporated on November 14, 2006 and started commercial operations during FY19. The company is involved in import and trading of coals, copper, aluminium, Gypsum, resins, as well as supporting manufacturing arms of Arihant group by importing necessary products related to sanitary wares, electrical or building materials. The company has its corporate office in Biratnagar and is operating via three branches located in Itahari, Bhairawa and Birgunj.

Brief financial performance of AIEPL during last 3 years is given below:

(Rs. in Million)

Particulars	FY20 (A)	FY21 (A)	FY22 (UA)
Income from operations	218	861	1,049
PBILDT Margin (%)	5.22	4.21	7.19
Overall Gearing (times)	3.21	5.50	4.38
Interest coverage (times)	1.25	1.23	1.29
Current Ratio (times)	1.12	1.13	1.19
Total Debt to Gross Cash Accruals (times)	104.09	96.86	52.03

A: Audited; UA: Unaudited

Annexure-1: Details of Facilities Rated

Name of the Instrument	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	35.00	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based Limit	580.00	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non-Fund Based Limit	215.00	CARE-NP A4 [A Four]
Total Facilities		830.00	

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