Maruti Cements Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	**3,658.42**	**CARE-NP A- [Single A Minus]**	**Revised from CARE-NP BBB and removed from Issuer not Cooperating category**
Short Term Bank Facilities	**1,898.13**	**CARE-NP A2+ [A Two Plus]**	**Revised from CARE-NP A3 and removed from Issuer not Cooperating category**
Total Facilities	**5,556.55 (Five Billion Five Hundred Fifty-Six Million and Five Hundred Fifty Thousand Only)**		

Details of instruments/facilities in Annexure 1

In the absence of minimum information required for the purpose of credit rating, CARE Ratings Nepal Limited (CRNL) was earlier unable to express an opinion on the rating of Maruti Cements Limited (MCL) and in line with the extant SEBON guidelines, CRNL had revised the rating of bank facilities of the company to 'CARE-NP BBB/A3 and moved the ratings to 'ISSUER NOT COOPERATING'. However, the company has since submitted the requisite information to CRNL. CRNL has subsequently carried out a full review of the ratings and the ratings stand at 'CARE-NP A-' for long term bank facilities and 'CARE-NP A2+' for short term bank facilities of MCL.

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of MCL continue to factor in the strengths from its established track record of operations with strong brand presence, particularly in the eastern part of the country along with comfortably leveraged capital structure despite increase in debt levels attributed to the increase in capacity levels. The net worth base of the company continues to remain relatively strong, providing ample cushion for solvency indicators. The ratings also continue to consider the competitive advantage MCL has, particularly over the standalone grinding units, by having its own captive clinker unit with adequate access to quality limestones for over three decades, locational advantage of the manufacturing facilities, and stable outlook for cement products in the country over the long-term despite near-term challenges amid slow pace of economic growth leading to lower demand prospects. The ratings also take cognizance of completion of the company's brownfield expansion project, with trial run having commenced in July 2023 and commercial operations expected from mid-January 2024. Additionally, the company's venture into new product segment from FY24 (FY refers to the twelve-month period ending mid-July) is also likely to benefit capacity utilizations of the new unit going forward.

The ratings, however, remain constrained by operations stabilization and salability risk associated with the new unit. The ratings take cognizance of the decline in operating profitability of the company over FY22-FY23, primarily driven by the soaring input costs and the industry's inability to implement sustained and substantial price hikes amid sluggish demand and increasing competition. Although profitability is expected to rebound, to some extent, over the near-to-medium term aided by softening of input prices coupled with better operating efficiency expected from the new unit, the company's ability to achieve margins in range prior to FY21 is likely to remain a challenge in the current market dynamics. The debt protection metrics of the company have continued to moderate in FY23 amid increasing debt levels and suppressed profitability. Furthermore, the ratings continue to take into consideration MCL's elongated operating cycle, exposure to volatile raw material prices, foreign exchange rate fluctuations and raw material price volatility risk, and presence in a highly competitive market and cyclical nature of the cement industry.

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

Going forward, the company's ability to maintain a healthy profitability profile by absorbing vulnerability in prices in an increasingly competitive industry along with rationalization of its debt levels would be the key rating sensitivities. Furthermore, stabilization of the expansion project with sufficient capacity utilization levels to generate cash flows as envisaged will also be the key rating sensitivity. Any substantial outflow of dividend leading to material deviation in capital structure than expected shall also remain a monitorable aspect.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Established track record of operations along with experienced promoters

MCL has an operational track record of more than 15 years in cement manufacturing under its current management. MCL is managed by industrialists and traders of Nepal, belonging to the Rathi group and Goyal group of companies, who are involved in diversified business activities. 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. Nand Kishore Rathi is the Chairman and Mr. Sunil Khemka is the Managing Director of the Company.

Comfortable capital structure with low gearing profile

Although MCL's debt levels increased to around Rs. 5,005 Mn at the end of FY23 from Rs. 4,043 Mn at the end of FY22, the company continues to have ample gearing headroom amid substantial net worth base. MCL had Debt to Equity ratio and overall gearing ratio of 0.57x and 0.75x, respectively, at the end of FY23. MCL's interest coverage ratio remained satisfactory at 3.41x in FY23 although declining from 4.44x in FY22. However, total debt to GCA of the company for FY23 shot up to 16.80x from 9.74x in FY22 as total debt increased while GCA decreased owing to decline in margins. The capital structure is expected to remain steady with low gearing profile going forward as well with no major debt funded capex planned over the near-term, indicative of a fairly strong financial flexibility of the company.

Strong brand presence in eastern region, proposed product diversification plans to boost business profile going forward

MCL sells its product all over Nepal with primary focus towards eastern part of Nepal, with main market being Narayanghat to Kakarbhitta and to north of Narayanghat with a network of around 200 dealers. The company's established brand presence and strong market position, mainly in the eastern region, has supported the company to sustain competition induced volatility in prices over the years. Further, MCL is currently producing only OPC cement under the brand name "Maruti". The company plans to produce PPC after the expansion of the facilities to diversify its product range, which augurs well for its business prospects going forward.

Relatively low reliance on borrowings despite substantial inventory holding

The operations of the company are working capital intensive in nature as it is involved in manufacturing of cement by procuring raw materials both domestically and imports. The company also keeps limestone reserve for around a year to ensure uninterrupted operations, which led to a high inventory holding period of ~300 days in FY23. MCL generally allows three months credit period to its dealers and collection period has been around steady at ~90 days historically (85 days in FY23). Despite the long inventory holding, MCL has had a relatively low reliance on bank borrowings, reflective in its sizeable average unutilized working capital limits (~40% average utilization over the last 12 months ended mid-October 2023). This is likely to support MCL's financial flexibility in case of further increase in working capital intensity going forward.

Competitive advantage over the standalone grinding units with accessibility to captive limestone mines

MCL currently has mining license of one mine, located in Jhanki Khola (Katari) with estimated limestone deposit of ~ 140 Million ton, which is expected to be sufficient to run 3,300 MTPD clinker unit (enhanced capacity) for more than 3 decades. The plant site is well connected to East-West Highway and with major cities and town nearby. The plant is located in the eastern part of the country where presence of other clinker-based cement manufacturing companies is limited. Clinker manufacturing units generally have added cost competitive advantage over standalone grinding units. Having both clinker and grinding units, licensed limestone mines and enhanced capacity augurs well for the business prospects of the company over the medium term.

Stable long-term demand outlook of cement industry in the country, however muted over the short-term

Nepalese economy is developing and growing, and is in phase of investment in infrastructure sectors, power sector and tourism sector. Sustained demand for cement is likely given the need of construction materials in developing public as well as private infrastructures, road, bridges and other public facilities. Hence, demand of cement in the country is expected to grow over the long term. However, with the construction sector in Nepal currently impacted by slower pace of economic growth coupled with relatively lower infrastructure spending by the government, the outlook of cement industry in Nepal remains challenging over the near term. Nevertheless, the government's long-term emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures is likely to benefit cement manufacturers like MCL in the long term.

Key Rating Weaknesses

Moderation in operating performance with sustained pressure on margins in FY23 amid industry headwinds

The overall sales volume of the company declined by ~11% year-on-year during FY23 amid muted demand. Consequently, MCL's total operating income (TOI) decreased by 14.08% to Rs. 4,339 Mn during FY23, partly also due to lower average sales realization amid increased competition. Lower capital expenditure for construction activities and slowdown in economy impacted cement manufacturers' income industrywide during FY22 and FY23. Amid increasing selling pressure, the cement industry was further aggravated due to rise in input prices. The cement sector for the large part of FY22 was grappling with soaring coal and diesel prices, with coal prices remaining on historically high levels for the major part of H1FY23 as well. This coupled with relative inability of the industry to pass through the increased cost to consumers led to suppressed margins for cement manufacturers like MCL in both FY22 and FY23. Accordingly, PBILDT margin of the company deteriorated to 9.36% in FY23 from 13.27% in FY22. Similarly, MCL achieved PAT of Rs. 143 Mn with PAT margin of 3.30% in FY23 as compared to Rs. 255 Mn with PAT margin of 5.05% in FY22. However, with softening of input costs from H2FY23 coupled with expected commencement of enhanced capacity during H2FY24, MCL's TOI as well as operating profit margin are expected to sequentially improve from latter half of FY24.

Stabilization risk associated with its recently completed large-size capex

MCL has undertaken a brownfield expansion project to increase the installed capacity of clinker unit from 1,500 MTPD to 3,300 MTPD and grinding unit from 2,000 MTPD to 4,000 MTPD at a project cost of Rs. 6,210 Mn, which has been financed through debt to equity in the ratio of 63:36. The expanded unit is currently running under trial phase with commercial operations expected by mid-January 2024. Given the relatively sluggish demand outlook for cement products over the near-term, the company remains susceptible to risk related with swift stabilization and scalability risk for the enhanced capacity. However, with expected rebound in demand over the medium term, the expansion is likely to boost MCL's income profile and be margin accretive for the company.

Foreign exchange fluctuation risk and raw material price volatility risk

MCL currently uses coal, limestone, bauxite, gypsum, clay and iron ore as major raw materials. Coal constitutes around 60% of raw materials consumption during clinker production and the coal requirements are met through import from South Africa and other countries. Invoicing of the imported coal is done in USD which exposes MCL to foreign exchange fluctuation risk. MCL has not taken any hedging mechanism to minimize the risk associated with fluctuation in foreign currency. Raw material cost continues to be the major cost component of MCL as direct material cost constitutes around 70% of total cost of goods sold in FY23. 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 the customers and managing the foreign exchange fluctuation risks related to raw materials will be the key rating sensitivities.

Presence in highly competitive and cyclical nature of cement industry

MCL is operating in a highly competitive industry, dominated by the large cement manufactures with wide brand acceptability. 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 producers of cement are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility in the prices of cement as seen in decline in price of cement and clinker during last three years.

About the Company

Maruti Cement Limited (MCL) was incorporated on October 31, 1994 and the current management took over the company in 2005. MCL is managed by industrialists and traders of Nepal, belonging to the Rathi group and Goyal group of companies and all the shares of the company are held by the promoters. The company is presently engaged in manufacturing and selling cement with clinker capacity of 1,500 MTPD and grinding capacity of 2000 MTPD respectively. The company is undertaking a brownfield expansion program to enhance its existing clinker capacity by 1,800 MTPD and grinding unit by 2,000 MTPD (trial run started in July 2023 and commercial operations expected by mid-January 2024). The manufacturing facilities are located in Mirchaiya, Siraha District of Nepal. Brief financials of MCL for last three years ending FY23 are given below:

(Rs. Million)

For the year ended mid-July	FY21 (A)	FY22 (A)	FY23 (UA)
Income from Operations	6,908	5,050	4,339
PBILDT Margin (%)	22.79	13.27	9.36
Overall Gearing (times)	0.35	0.61	0.75
Total Outstanding Liabilities/Tangible Net worth (times)	0.55	0.75	0.86
Interest Coverage (times)	13.81	4.44	3.41
Current Ratio (times)	2.51	2.71	2.09
Total Debt/Gross Cash Accruals (times)	1.69	9.74	16.80

A: Audited, UA: Unaudited

Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the facility	Amount (Rs. In Million)	Ratings
Long Term Bank Facilities	Term Loan	3,658.42	CARE-NP A-
Short Term Bank Facilities	Working Capital Loans	1,298.13	CARE-NP A2+
Short Term Bank Facilities	Non–Fund Based Limits	600.00	CARE-NP A2+
Total		**5,556.55**	

Contact Us

Analyst Contact
Ms. Poonam Agarwal
+977-01-4012630
poonamagarwal@careratingsnepal.com

Mr. Santosh Pudasaini
+977-01-4012628
pudasaini.santosh@careratingsnepal.com

Relationship Contact
Mr. Achin Nirwani
+977-9818832909
achin.nirwani@careratingsnepal.com

About CARE Ratings Nepal Limited:

CARE Ratings Nepal Limited (CRNL) is licensed by the Securities Board of Nepal w.e.f. November 16, 2017. CRNL is supported by CARE Ratings Limited through a technical services agreement to provide technical support in the areas such as rating systems and procedures, methodologies, etc. from CARE Ratings on an ongoing basis. The technical support shall ensure that CRNL has adequate resources to provide high quality credit opinions in Nepal.

Our parent company, CARE Ratings Limited commenced operations in April 1993 and over two decades, it has established itself as one of the leading credit rating agencies in India. CARE is registered with the Securities and Exchange Board of India (SEBI) and also recognized as an External Credit Assessment Institution (ECAI) by the Reserve Bank of India (RBI).