

Rating Rationale
Godawari Steel Private Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	600	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	2900	CARE-NP A4 [A Four]	Assigned
Total Facilities	3,500 (Rs. Three Thousand Five Hundred Million Only)		

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 Godawari Steel Private Limited (GSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of GSPL are constrained by project implementation risk and stabilization risk thereafter coupled with promoters limited experience in the manufacturing industry. The rating also factors in GSPL’s exposure to volatile interest rates, raw material price volatility, foreign exchange fluctuation risk and its presence in highly fragmented & competitive steel industry. The ratings, however, derive strength from established business group and promoter’s experience in the related field of trading business, healthy demand of steels products in the country and locational advantage of its facilities. The rating also favorably factors in financial closure achieved for the initial project cost and threats of imports minimized by Import Parity Price.

Going forward, timely completion of the project within the time and cost estimates, ability of the company to achieve envisage revenue and profitability and pass through the changes in raw material prices to the customers and managing the foreign exchange fluctuation risks are the key rating sensitivities. Also ability of the company to tie up the debt for the increased project cost shall also be the key sensitivity.

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

Detailed Description of the Key Rating Drivers

Key Rating Weakness

Project implementation risk and stabilisation risk

The project is almost in completion stage as 87% of the project has been completed in financial terms. The mechanical and civil work of the project are in the final stage. However, delays in project execution cannot be totally ruled out, given that the project is not fully complete and financial closure for the increased debt portion is yet to be achieved. The company has projected to achieve commercial operation for the project during October 2018. Timely completion of the project within the cost estimates and satisfactory operations thereafter are the key rating sensitivities.

Exposure to volatile interest rates

Nepalese banking sectors are fixing lending interest rate based on quarterly base rate and interest rate can be changed accordingly on quarterly basis. Due to tight liquidity in the market, the interest rate has been high and volatile during the last 12 months. Therefore, the funding from banks and financial institutions is subject to volatile interest rate.

Raw material price volatility risk and foreign exchange fluctuation risk

GSPL does not have any backward integration for its major raw material (MS billets) for producing TMT & plain steel bars. The billets are proposed to be majorly imported from India. The prices of the billets are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. The raw material cost is expected to contribute around 80% of the total operating income of the company, thus, any volatility in prices of the same impacts the profitability of the company. Further, the majority of its raw material is proposed to be met through imports and the price of the same will be linked to USD, for which exposes the company to foreign exchange fluctuation risk. The ability of the company to pass through the 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 fragmented and competitive 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. 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 demand of TMT & plain bars 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 & plain bars, MS pipes and construction material etc. is low, resulting into low product differentiation in the market. The producers of steel construction materials are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility in the steel prices.

Key Rating Strength

Established business group and experienced promoter in the related field in trading business, however, limited experience in the manufacturing industry

GSPL is promoted by Mr. Munna Prasad Senuriya Baniya, who is associated with Godawari Business Organization (GBO) as an Executive Director. GBO is an ancestral business of the promoter and was established in 1950. The group has been involved in manufacturing of HDPE pipes & water tanks, trading and supply of construction materials, repairing of transformers, trading of hardware. Since the group is operating in the similar line of business in the Nepalese market for decades, it gives them an advantage of existing distribution channel for marketing of manufactured goods from GSPL. The day to day activities of the company are handled by Mr. Senuriya who possesses more than two decades of extensive experience in the related field.

Healthy demand of steels products in the country

Nepalese economy is developing and growing leading to increasing investment in infrastructure sectors, power sector and tourism sector. It is expected that the national economy will be in need of construction materials in developing public as well as private infrastructures, road, bridges and other public facilities. Further followed by devastating earthquake of April 2015, Government commitment towards infrastructure and the rebuilding the housing sector has increased demand of iron and steel products in the country. Due to the demand supply gap of the steel products manufactured in the domestic markets, the scope for sale of the products manufactured by GSPL is positive. However, the government's continued thrust on the construction, infrastructure development and power sector and targeted GDP growth of 8% is likely to benefit the long products manufacturers like GSPL.

Locational advantage

Since the plant site is located nearby the proposed Nijgarh International Airport, it is expected to create demand for its products in the nearby market as the nearby areas are expected to be developed. In addition, the construction of proposed fast track from Nijgarh to Kathmandu will also positively create demand at local level for the products of the company. Furthermore, the plant site is located around 20 Kms from Nepal-India Border (Gaur Customs), near the big Indian State Bihar which gives GSPL an advantage of supply of raw material at lower transportation cost. GSPL can also use Birgunj Border, either via railways till Raxaul (~75 kms from plant location) or via road. The Gaur border is less busy than Birgunj and hence imports of raw material will be more convenient for GSPL. GSPL can exploit opportunity by focusing nearby markets for finished goods at lower transportation cost than its competitors.

Financial closure achieved for the initial project cost; however, financial closure for the increased project cost yet to be achieved

The financial closure for the initial project cost for manufacturing of 350 TPD steel products with debt of Rs. 540 Million was achieved on May 19, 2017. The initial project cost estimates of Rs. 938 Million was proposed to be financed in a debt-equity mix of 58:42. Due to the enhancement in the capacity of the plant from 350 MT per day to 600 MT per day, the project cost was increased to Rs. 1,210.54 Million as per the latest estimates by the company. At present, the financial closure for the escalated amount is not yet achieved to increase term loan of Rs. 540 Million to Rs. 600 Million. Going forward, the term debt to equity is expected to be at comfortable level, however, the overall gearing ratio of the company is expected to be on higher side after the working capital limits are availed. GSPL has incurred Rs. 851 Million on the project till May 20, 2018 as certified by M/s G.P. Rajbahak & Co., Chartered Accountants. Further, the cost incurred towards the project till August 10, 2018 was Rs. 1,055 Million and the same is funded through debt of Rs. 524 Million, equity of Rs. 300 Million and rest in form of unsecured loans from promoter and creditors.

Threats of imports minimized by Import Parity Price

The import parity price of TMT bars after adding 30% import duty and other incidental expenses, the price of imported products will be higher than that of domestic manufacturers are offering to the customers. The threats of price of imported TMT bars in Nepalese market is somehow nullified by import parity price.

About the Company

GSPL is a private limited company promoted by individual, who is engaged in manufacturing and trading businesses, to set up rolling mill to manufacture TMT & Plain Steel Bars in Rautahat district of Nepal. The project is located at Chandranigahapur, Rautahat of Nepal with expected operation date of October 2018. The company will manufacture TMT & plain Steel Bars by importing raw materials from India and China and selling them into Nepal’s market with production capacity of 600 MT of TMT & Plain Steel Bars per day. The entire capital of the company will be held by the sole promoter Mr. Munna Prasad Senuriya Baniya.

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Annexure 1: Details of the Facilities

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	540.00	CARE-NP BB
Short Term Bank Facilities	Working Capital	250.00	CARE-NP A4
Short Term Bank Facilities	Letter of Credit	250.00	CARE-NP A4
Long Term Bank Facilities (Proposed)	Term Loan	60.00	CARE-NP BB
Short Term Bank Facilities (Proposed)	Working Capital	1,350.00	CARE-NP A4
Short Term Bank Facilities (Proposed)	Letter of Credit	1,050.00	CARE-NP A4
Total		3,500.00	