

Rating Rationale

Mainawati Steel Industries Private Limited

Rating

Facilities	Amount (Rs. In Million)	Rating ¹	Remarks
Long Term Bank Facilities	196	CARE-NP BBB [Triple B]	Assigned
Short Term Bank Facilities	4,769	CARE-NP A3 [A Three]	Assigned
Total Facilities	4,965		

Details of Facilities in Annexure 1

CRNL has assigned Rating of ‘CARE-NP BBB’ to the long term bank facilities and ‘CARE-NP A3’ to the short term bank facilities of Mainawati Steel Industries Private Limited (MSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of Mainawati Steel Industries Private Limited (MSPL) derives strength from established and long track record of operations, strong promoters, being part of Vishal group of companies and experienced management team in the related field, comfortable financial risk profile and debt service indicators, diverse product range catering to wide spectrum of industries and established marketing setup, healthy capacity utilization and demand of steels products in the country

The ratings, however, are constrained by exposure to volatile interest rates, raw material price volatility risk and foreign exchange fluctuation risk, high overall gearing level at the end of FY18 (refers to 12 months period ended mid-July 2018), working capital intensive nature of operations and presence in highly fragmented and competitive nature of steel industry.

The ability of MSPL to manage the growth in the operations & maintaining the profit margins and rationalization of its debt through efficient working capital management are the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strength

Established and long track record of operations, strong Promoters, being part of Vishal Group of Companies and experienced management team in the related field

MSPL has an operational track record of more than two decades in manufacturing of MS black pipes, galvanized pipes, tubes and pipes. The promoters of MSPL have an experience of over two decades in the tubes & pipes industry. MSPL derives strength from its strong promoters and

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

being a part of the Vishal Group of Companies, which have a strong presence in Nepal through their group entities in trade, manufacturing, hospitality, insurance and banking. MSPL is managed under the overall guidance of its two member Board of Directors (BoD) which includes eminent Businessmen/Industrialists with wide experience in the manufacturing sectors. Mr. Tulsi Ram Agrawal is the Chairman of MSPL, and has more than 45 years of experience in manufacturing industry, banking sector, insurance sector and trading business. He is the Chairman of NIC Asia Bank Limited (rated CARE NP A). Mr. Trilok Chand Agrawal is another director of MSPL and has more than 47 years of experience in manufacturing industry, banking sector, insurance sector and trading business. He is Director of NIC Asia Bank Limited. The promoters are supported by a team of technically qualified and experienced professionals to run the day-to-day operations of MSPL.

Comfortable financial risk profile and debt service indicators

MSPL sales revenue has been increased by ~77% during FY18 to Rs. 4,749 Million from Rs. 2,686 Million during FY17 majorly due to increase in demand, higher per unit sales realization on back of increase in the raw material prices and higher tender based sales to Nepal Electricity Authority during FY18. Owing to increase in the sales revenue, PBILDT has been increased by ~79% during FY18 to Rs. 496 Mn over FY17 with PBILDT margin of 10.41%. PAT of the company increased by ~89% to Rs. 322 Million during FY18 as compared to Rs. 170 Million of FY17 as a result of higher PBILDT. MSPL has healthy interest coverage ratio and total debt to GCA of 7.28x during FY18 and 5.23x as on July 16, 2018 respectively.

Diverse product range catering to wide spectrum of industries and established marketing setup

MSPL has been manufacturing iron & steel products in wide range having different usages. They are manufacturing mild steel (MS) black pipes & galvanized (GI) pipes and their variants. Tubular pole, telescopic pole, structure, shutter profile etc. are the major products that MSPL are selling in the market along with selling galvanized plain sheets (GP Sheet), hot rolled coil (HRC) sheet and cold rolled coil (CRC) sheet by cutting it in different sizes. MSPL sell its product all over Nepal and the sales are majorly through direct marketing to existing as well as new customers. Most of the sales revenue comes through direct domestic sales, followed by tender based sales and a minimal sales is through export to India and Bhutan. During FY18, MSPL

reported 72.67% of revenue through direct domestic sales, 26.82% through tender based sales and 0.51% through export.

Healthy capacity utilization

MSPL has installed capacity of 90,450 MTPA during FY18. Although the capacity utilization was declined to ~66% during FY18 against capacity utilization of ~72% during FY17, the actual production increased to 59,853 MT during FY18 from 45,614 MT during FY17.

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. Further, the demand for the iron & steel products is expected to grow at about 10% for the coming few years. 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 MSPL.

Key Rating Weakness

Exposure to volatile interest rates

Nepalese banking sectors are fixing lending interest rate based on quarterly base rate and interest rate will 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 Bank and Financial Institutions to the company is exposed to volatile interest rate.

Raw material price volatility risk and foreign exchange fluctuation risk

H.R. Coils, C.R. Coils, GP Coils, Zinc Ingots etc. are the major raw materials for MSPL and are majorly imported from India. The prices of the MSPL's raw materials 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. Cost of sales (including raw material consumption) contributed around 86% of the total operating income of the company during FY18, thus, any volatility in prices of raw materials impacts the profitability of the company.

Further, the majority of the raw material requirements are met through imports and the price of the same are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. MSPL has incurred foreign exchange fluctuation loss of Rs.47 Mn during FY18.

High overall gearing level at the end of FY18

The debt equity ratio of the company was low at 0.31x as on July 16, 2018. However, overall gearing ratio has increased and was high at 2.78x at the end of FY18 in comparison of 1.93x at the end of FY17 due to increase in the working capital loans to fund increased debtors and inventory on back of increased sales volume during FY18.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature. MSPL make advance payment for the raw materials and the company has to fund inventory and debtors which lead to high reliance on working capital limits. MSPL's average debtors turnover days was 59 days and the average inventory turnover was 62 days during FY18. This leads to high reliance of the company on the bank finance for working capital needs. The month end working capital utilization against the drawing power of the company for last 12 months ending October 17, 2018 was more than 90%.

Presence in highly fragmented and competitive nature of 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 iron & steel products 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 M.S. black, galvanized pipes & related products 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.

About the Company

Mainawati Steel Industries Private Limited (MSPL) is a private limited company incorporated on May 17, 1995 for setting up of M.S. Black & Galvanized pipe plant in Sunsari district of Nepal.

The company is operating from more than 2 decades and manufacturing wide range of steel products with total installed plant capacity of 90,450 metric tons per annum. MSPL primarily manufactures MS black pipes, galvanized pipes, tubes and its variants. Most of the sales revenue comes through direct domestic sales, followed by tender based sales and minimal sales is through export to India and Bhutan. All the shares have been held by individual promoter group shareholders.

Brief Financial Performance during the last three years:

(Rs. In Million)

Particulars	FY16 (A)	FY17 (A)	FY18 (A)
Income from Operations	2,000	2,700	4,766
PBILDT	242	277	496
PAT	153	170	322
Gross Cash Accruals (GCA)	178	197	361
Overall Gearing (times)	2.87	1.93	2.78
Interest coverage (times)	10.54	6.07	7.28

Analyst Contact

Mr. Giri Raj Kandel

giriraj.kandel@careratingsnepal.com

Tel No.: +977-01-4232610

Relationship Contact

Mr. Sajan Goyal

sajan.goyal@careratingsnepal.com

Tel No.: 9818832909/+977-01-4233436

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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	196	CARE-NP BBB
Short Term Bank Facilities	Working Capital Loan	4,436	CARE-NP A3
Short Term Bank Facilities	Letter of Credit	115	CARE-NP A3
Short Term Bank Facilities	Bank Guarantee	218	CARE-NP A3
Total Bank Facilities	Total Bank Facilities	4,965	