Rating Rationale

Ambe Cement Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating[1]	Rating Action
Long Term Bank Facilities	45.00	CARE-NP BBB- [Triple B Minus]	Assigned
Short Term Bank Facilities	955.00	CARE-NP A3 [A Three]	Assigned
Total Facilities	**1,000.00**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (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 Ambe Cement Private Limited (ACPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of ACPL derives strength from established track record of operations, comfortable financial risk profile and moderate debt service indicators, healthy demand for cement products in the country, product diversification and own brand. The ratings also factors in, strong promoters being part of Ambe Group of Companies and experienced management team. The ratings, however, are constrained by moderate scale of operations, exposure to volatile interest rates, stoppage on imports of clinker via railways resulting in increased production cost, lack of backward integration and raw material price volatility risk, working capital intensive nature of operations leading to high working capital utilization, presence in highly fragmented and competitive nature of cement industry.

Ability of the company to manage the growth in the operations & maintaining the profit margins and rationalization of its debt through efficient working capital management would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strength

Established track record of operations, strong promoters, being part of Ambe Group of companies and experienced management team

ACPL has an operational track record of more than thirteen years in the cement manufacturing by grinding of clinker. ACPL is promoted by industrialists and traders who are related with Ambe Group of Companies, which have business interests in manufacturing and trading sector. Mr. Shobhakar Neupane is the Chairman (major shareholder of the company) and Mr. Sajjan

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

Kumar Agrawal is the Managing Director of the Company. Mr. Neupane is the Chairman/ Managing Director of Ambe Group. Mr. Agrawal looks after the day to day operations of the company and is also director of Ambe Steels Pvt. Ltd. and have 25 years of experience in trading and manufacturing. He is supported by a team of experienced professionals. Promoters had infused unsecured loan of Rs.41.50 Mn during FY17 to support the operations of the company.

Comfortable financial risk profile and moderate debt service Indicators

ACPL's total revenue has been increased by ~64% during FY17 to Rs.2561 Mn over FY16, which experienced decline of ~5% during FY18 due to low production levels impacted by supply interruptions via railways at Raxaul border of India during FY18, though per bag realization was increased to Rs.620 per bag during FY18 over Rs.566 per bag during FY17. Further, PBILDT has been increased by ~11% during FY18 to Rs.253 Mn over FY17 with PBILDT margin improved to 10.40% due to higher realization and decline in selling & distribution cost leading to healthy cash accruals. The debt equity ratio of the company was low at 0.10x and overall gearing was at moderate level of 1.86x as on July 16, 2018. ACPL has moderate interest coverage ratio and total debt to GCA of 2.79x and 5.81x as on July 16, 2018 respectively.

Healthy demand for cement products in the country

The demand of the cement is increasing in Nepal and is expected to exceed 10 Million tons per year by 2023. The cement consumption in Nepal was estimated to be around 8 Million tons during FY18. The Nepalese economy has gone through several highs and lows, having been impacted by natural disasters, political instability and protests. 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 cement manufacturers like ACPL.

Product diversification and own Brand

ACPL is manufacturing PPC Cement under two brands, OPC cement under two brands and also manufactures PSC Cement under six brands, which has great usage on all types of residential, commercial & industrial projects, dams & other mass concrete works etc. Currently ACPL focus its sales in the territory of nine zones (out of 14 zones on Nepal) covering 38 districts (out of 77) of Nepal.

Key Rating Weakness

Stoppage on imports of clinker via railways resulting in increased production cost

ACPL used to import clinker from India via railways upto Raxaul of India, 11 Km from the plant site of ACPL, which had the competitive advantage of the grinding plants in Birgunj area over the other cement manufacturing plants in terms of transportation cost of the raw material. Due to pollution by unloading clinker at Raxaul, the local people of Raxaul protested and clinker unloading at Raxaul was stopped from December 2017. ACPL currently either imports clinker from India by Trucks or purchases clinker from local traders which has resulted in increased cost of production, which will be cost disadvantage for the company in the competitive market. However, the company is procuring clinker from domestic clinker manufacturing units also to fulfill its raw material requirement. ACPL had imported 66% of its total raw materials requirements from India during FY18.

Moderate scale of operations

At current production capacity of 1,000 metric tons per day, ACPL was operated at moderate capacity utilization of 59%, witnessing decline in the capacity utilization from 68% during FY17. Further, during first six months of FY19 ended on January 14, 2019, ACPL achieved sales revenue of Rs.956 Mn with 74,229 metric tons of cement sold. Considering ACPL's current production capacity in comparison to the production of cement in Nepal, ACPL's scale of operation seems relatively moderate.

Exposure to volatile interest rates

Nepalese banking sector fix interest rates on lending, based on quarterly published base rates by the banks. Due to tight liquidity in the market, the interest rate has been high and volatile during the last 12 months. Therefore, funding from Bank and Financial Institutions are exposed to volatile interest rate.

Lack of backward integration and raw material price volatility risk

ACPL is engaged in producing cement and does not possess its own clinker manufacturing unit. ACPL mainly use clinker, slag, flyash, gypsum etc. as the major raw materials and has to procure clinker from other cement manufacturers and majorly imports from India. Raw material cost continues to be the major cost component constituting around 87% of the total cost of sales in FY18. Hence, any adverse movement in raw material price without any corresponding movement in finished goods price can impact the profitability of the company. The ability of the company to pass through of changes in raw material prices to the customers will be the key rating sensitivities.

Working capital intensive nature of operations leading to high working capital utilization

The operations of the company are working capital intensive in nature. ACPL is involved in the manufacturing of cement by importing and locally purchased raw materials. The company has to make advance payments for the raw materials, have to keep the inventory for smooth operations and extend credit to their dealers. ACPL generally allows three months credit period to its customers and the company keeps inventory for around two months period. This leads to high reliance of the company on the bank finance for working capital needs. The working capital utilization of the company remained high at above 95% for the past 12 months.

Presence in highly fragmented and competitive nature of cement industry

ACPL is operating in a highly competitive market, dominated by the large cement manufactures with wide brand acceptability. There are more than 50 cement factories operating in the country that produce 160 Million bags of cement annually. Further many cement factories that are under construction will come into operation soon and other domestic cement factories are also expanding their production capacity. 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 cement industry is considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry.

About the Company

Ambe Cement Private Limited (ACPL) is a private limited company, established in 2004, promoted by the individuals involved in manufacturing industry and trading business, for setting up clinker grinding plant at Parsa District of Nepal. The company is engaged in manufacturing and selling of cement with grinding capacity of 1000 metric tons per day (MTPD). ACPL manufactures Portland Pozzolana Cement (PPC), Ordinary Portland Cement (OPC) and Portland Slag Cement (PSC) cement under ten different brands. The paid up capital of the company is Rs.285 Mn as on July 16, 2018.

Brief Financial Performance during last 3 years:

(Rs. In Million)

For the year ended Mid July,	FY16 (A)	FY17 (A)	FY18 (A)
Income from Operations	1,565	2,561	2,435
PBILDT	169	229	253
PAT	57	86	83
Overall Gearing (times)	1.69	2.23	1.86
Interest coverage (times)	4.10	4.19	2.79

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

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities (Proposed)	Term Loan	45.00	CARE-NP BBB-
Short Term Bank Facilities	Overdraft	70.00	CARE-NP A3
Short Term Bank Facilities	Working Capital Loan	740.00	CARE-NP A3
Short Term Bank Facilities (Proposed)	Working Capital Loan	105.00	CARE-NP A3
Short Term Bank Facilities	Letter of Credit	40.00	CARE-NP A3
Total		**1,000.00**	