

Rating Rationale

Advanced Automobiles Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	21.21	CARE-NP BB [Double B]	Downgraded from CARE NP BBB- [Triple B Minus]
Short Term Bank Facilities	960.00	CARE-NP A4 [A Four]	Downgraded from CARE NP A3 [A Three]
Total Facilities	981.21		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating to ‘CARE-NP BB’ for long term bank facilities and to ‘CARE-NP A4’ for the short term bank facilities of Advanced Automobiles Private Limited (AAPL).

Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of AAPL takes into account deteriorated financial risk profile marked by decline in revenue, net loss, stressed debt service indicators and leveraged capital structure during FY19 (refers to 12 months’ period ended mid-July 2019). The ratings also factored in limited track record of operations and working capital intensive nature of operation. The rating is also constrained by cyclical nature of the auto industry and high competition from other automobile players, exposure to volatile interest rates, and exposure to regulatory risk related to automobile industry. The ratings, however, derive strength from experienced and resourceful promoters and company being part of Vishal Group of Companies; established brand and sole distributor of Renault SAS in Nepal; and established dealer network. Ability of the company to improve its revenue growth, profitability margins and overall solvency position will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Financial risk profile marked by decline in revenue, net loss, stressed debt service indicators and leveraged capital structure

Financial risk profile of the company is characterised by decline in scale of operations, net loss and stressed debt service coverage indicators during FY19. The total income of AAPL significantly declined by ~36% to Rs. 1,898 Mn during FY19 mainly on account slowdown of automobile industry coupled with regulatory push back and evolving electronic vehicles market. Further, PBILDT of the company declined by ~68% in FY19 coupled with decrease in PBILDT margin to ~3% mainly due to decline in revenue and huge discounts offered to customers and dealers to liquidate inventory. The company incurred loss during FY19 due to decline in the PBILDT and

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

increase in interest expenses. The debt service coverage indicators were stressed with total debt to gross cash accruals of -ve 13.96x and interest coverage ratio of below unity in FY19 on account of lower PBILDT during the year. The company had leveraged capital structure marked by high overall gearing ratio of 5.25x at the end of FY19.

Limited track record of operations

AAPL was incorporated in September 13, 2013 and started operation for the sale of Renault cars from October 2016. Thus, the company is having limited track record of only three years into operations. However, the promoters have over 8 years of experience in auto dealership business along with other group companies.

Working capital intensive nature of operation

Automobile dealership business has inherent high working capital intensity due to high inventory holding requirements and credit to the dealers. Further, the vehicle manufacturers/ suppliers deliver the vehicles against letter of credit. Thus, the business depends heavily on working capital borrowings. During FY19, AAPL had inventory holding period of 93 days and operating cycle of 135 days. Accordingly, the average utilization of working capital limit was on the higher side at around 87% during the last 12 months ended on mid-July 2019.

Cyclical nature of the auto industry and high competition from other automobile players

The demand for passenger vehicles is inherently vulnerable to the economic cycles and is highly sensitive to interest rates. Demand for passenger vehicles increases during high economy growth rate period and low interest rate regime and vice-versa. Also, there is stiff competition from other automobile dealerships in Nepal. There are large number of players operating in market like Hyundai, Honda, Toyota, Nissan, Volkswagen, Ford, TATA Motors, Jeep etc. Further, competition is also intensified due to introduction of electric vehicles in the market which seems to be a viable option for customer. Due to high competition, dealers are forced to pass on discounts and exchange schemes to attract customer.

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, funding from Bank and Financial Institutions is exposed to volatile interest rate.

Exposure to regulatory risk related to automobile industry

The automobile industry is still taken as luxury items in Nepal on back of hefty excise duty imposed on the import of automobiles and sharp increase in taxes for FY19. Further, there has been overall decline in the automobile industry in FY19. Additionally, as per circular dated on November 6, 2018, the Central Bank has reduced the cap on bank financing to 50% of value of vehicle used for personal purpose which could slow down

demand growth in the industry. Further, the government has been incentivizing growth of electric vehicles in the market which could affect sale of the company.

Key Rating Strengths

Experienced and resourceful promoters

AAPL derives strength from its strong promoters and 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. Along with AAPL, Vishal Group of companies are dealing with other automobile's sole distributorship / dealership from more than 8 years and have a wide dealer network of automobile distributorship. The other companies in the group are having authorized distributorship of Volkswagen cars, Kobelco construction equipment and Suzuki motorcycles in the country.

The day to day operations of the company are managed by Mr. Nikunj Agrawal, who is Managing Director of the company. Mr. Agrawal supervises the operations of the automobile distributorship/ dealership in the Group and has an experience of more than a decade through various entities in the same. He is also a director of NIC Asia Bank Limited. The promoters have infused equity amounting to Rs. 75 Mn during FY19 to support the operations and fund the losses of the company.

Established brand, sole distributor of Renault SAS and established dealer network

The company is presently the only authorized dealer in Nepal for Renault SAS. Renault is a French multinational automobile manufacturer which was founded 120 years ago and has worldwide presence in 134 countries and has sold 3.88 million vehicles in 2018. AAPL mostly imports Renault cars from Renault India Private Limited. Presently, AAPL has established dealer network of 12 dealers strategically located covering major parts of Nepal together with two showrooms and two service centres owned by the company.

About the Company

Advanced Automobiles Private Limited was incorporated in September 13, 2013 by Mr. Nikunj Agrawal and started its operation from October 2016 as a sole authorized distributor for Renault SAS, France in Nepal. The company is engaged in the sale of passenger vehicles of Renault, servicing of the vehicles and sale of spare parts. The company owns and operates two showrooms and two service centers that are situated in Kathmandu. During FY19, the company generated ~96% of the revenue from the sale of vehicles, while the balance was achieved from service charge income, sale of spare parts and accessories.

Brief financials of AAPL for last three years ending FY19 are given below:

(Rs. Million)

For the year ended Mid July	FY17	FY18	FY19
	(Audited)	(Audited)	(Audited)
Income from Operations	2,659	2,982	1,898
PBILDT	230	181	57
PAT	134	52	(68)
Overall Gearing (times)	5.00	6.74	5.25
Interest Coverage (times)	5.35	1.96	0.53

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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. In Million)	Rating
Long Term Bank Facilities	Term Loan	21.21	CARE-NP BB
Short Term Bank Facilities	Working Capital Limit	620.00	CARE-NP A4
Short Term Bank Facilities	Non-Funded Limit	340.00	CARE-NP A4
Total		981.21	