

**Rating Rationale  
Narayani Ispat Private Limited**

**Rating**

Facility/ Instrument	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	1,189.59	CARE-NP BB- [Double B Minus]	Assigned
Short Term Bank Facilities	2,806.00	CARE-NP A4 [A Four ]	Assigned
<b>Total facilities</b>	<b>3,995.59</b>		

*Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (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 Narayani Ispat Private Limited (NIPL).

**Detailed Rationale & Key Rating Drivers**

The ratings assigned to the bank facilities of NIPL are constrained by subdued operational and financial performance of the company during the first year of operation in FY19 (audited, refers to 12 months period ended mid-July 2019), leveraged capital structure coupled with weak debt service coverage indicators at the end of FY19 and raw material price volatility risk along with foreign exchange fluctuation risk. The ratings also factor in working capital intensive nature of operations, exposure to volatile interest rates and presence in highly fragmented and competitive nature of steel industry. The ratings however, derives strength from strong presence of the promoter group in steel sector supported by experienced management team, backward integration of the plant likely to provide cost benefits in future, established brand and marketing network of the group with country wide presence. The ratings also factor in locational advantage with scope of export and demand of steels products in the country. The ability of the company to manage growth in the operations & improve profit margins along with rationalization of its debt through efficient working capital management would be the key rating sensitivities.

**Detailed Description of the Key Rating Drivers**

**Key Rating Weaknesses**

***Subdued operational and financial performance of the company during the first year of operation in FY19***

During FY19, the company generated total revenue of Rs. 4,229 Mn out of which Rs. 3,880 Mn was from manufacturing activity and Rs. 349 Mn from trading activity. PBILDT of the company in FY19 was of Rs. 183 Mn with low PBILDT margin of 4.33%. PBILDT of the company was impacted on account of higher proportionate increase in cost of raw material prices than increase in sales realizations. Also, with addition of the new capacities in the market and increase in the intensity of the competition, the company was not able to pass on the increased cost to its customers fully. During FY19, the company incurred loss of Rs. 139 Mn majorly due to lower PBILDT generated coupled with high depreciation of Rs. 139 Mn and interest expense of Rs. 206 Mn. During 6 months period ended mid-January 2020, the company has achieved sales of Rs. 2,174 Mn.

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

***Highly leveraged capital structure and weak debt service coverage indicators***

Debt-equity ratio of the company was high at 3.03x at the end of FY19 which improved from 3.61x at the end of FY18, due to increase in equity share capital from Rs. 170 Mn in FY18 to Rs. 500 Mn in FY19 to fund the project as well as operations of the company. Total debt of the company is high majorly on account of high working capital loans in the books at the end of FY19. Total gearing ratio of the company was high at 8.98x at the end of FY19 with below unity interest coverage ratio of 0.89x in FY19. Total debt/ GCA for FY19 was negative on account of gross cash accruals generated during the year being negative. Debt-equity ratio of the company is high as the company commenced operations from July 2018 with on-going capex to set up the Billet manufacturing plant which commenced operations from May 2019.

***Raw material price volatility risk and foreign exchange fluctuation risk***

During FY19, the company majorly relied on imported billets to manufacture TMT bar. Post commencement of the in-house billet manufacturing plant of the company in May 2019, the major raw materials of NIPL was sponge iron, ferro alloys and scrap. Sponge iron will be imported from India and scrap will be procured from the domestic market. The prices of the NIPL'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. The raw material consumption cost contributed around 93% of the total operating income of the company during FY19, thus, any volatility in prices of the same impacts the profitability of the company. Further, In FY19, ~ 82% of the total raw material requirement was imported and the prices of the same are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. NIPL incurred foreign exchange fluctuation loss of Rs. 11.74 Mn during FY19. The ability of the company to pass through 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.

***Working capital intensive nature of operations***

The operations of the company are working capital intensive in nature as NIPL is involved in manufacturing of TMT Bars by procuring raw materials domestically as well as through imports. The company has to procure raw materials through Letter of Credit and also has to fund inventory and debtors which lead to high reliance on working capital limits. In FY19, NIPL generally allowed more than 3 months credit period to its customers, debtors turnover days was 94 days during FY19. The company keeps inventory for more than three months and the inventory turnover was 98 days for the FY19. Total operating cycle of the company was 141 days in FY19. This leads to high reliance of the company on the bank finance for working capital needs. The average monthly outstanding of working capital limits against the drawing power was around 94% during last 12 months period ended mid-January 2020 marked by overutilization of limits against the drawing power in few instances.

***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.

***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 TMT bar and related products is low, resulting into low product differentiation in the market. Further, with increase in the capacities of the existing plants and new capacities coming into operation competition has intensified which has resulted into substantial decline in profitability margins of the industry players in the current year. 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 Strengths*****Strong presence of the promoter group in steel sector supported by experienced management team***

Although NIPL commenced its operations only in July 2018, the promoters of the company have wide experience in manufacturing steel and other construction materials for more than three decades. NIPL is part of the Keyal group of companies of Nepal which is a diversified business group with strong presence in a broad range of business, manufacturing and industrial interests with main focus on manufacturing construction materials. The group also has 15 hardware outlets across the country which are strongly contributing to the group's steel business. The company is managed under the overall guidance of its nine members Board of Directors (BoD) which includes experienced businessmen/industrialist from the Keyal group with wide experience in the manufacturing sector. Mr. Bikash Kumar Keyal, Chairman of NIPL, has been involved in the groups business for the past 15 years and looks after the whole group's accounting and finance. Mr. Satya Narayan Keyal, Director of NIPL and also Chairman of the Keyal group of companies has more than 30 years of experience in trading and manufacturing industry.

***Backward integration of the plant likely to provide cost benefits in future***

The company has setup its own unit for manufacturing M.S. Billets with capacity of 87,000 MTPA which will be used for in- house consumption for manufacturing TMT Bars. The in house consumption of M.S. Billets into TMT Bars is expected to reduce the production cost of the company. The key raw material required in manufacturing of MS Billets is sponge iron and scrap, where sponge iron will be imported from India and scrap

will be locally procured from the vendors directly. Also fully automated manufacturing facilities is expected to reduce labour requirement and thereby being more economical to the company.

***Established brand and marketing network of the group with country wide presence***

The company sells TMT bars under the brand name of “Narayani Steels” which is already an established brand in the Nepal market on account of its long-standing presence in the construction materials manufacturing and trading industry. This provides leverage to the company in front of new players entering the industry. The group also has 15 in-house hardware trading outlets in and around the Kathmandu Valley which makes it easier to penetrate into the market and cater to large section of customers. Also, the group already has a well-established dealer/distributor network in around 129 areas across the country which provides a ready market for its products.

***Locational advantage and scope of export***

The plant site is located in Chhatapipra, Simara, around 15 Kms from Indo-Nepal border in Birgunj dry-port. Since majority of raw materials used by NSPL are imported from India, the factory’s proximity to the border remains a positive point leading to savings in huge freight cost. Upon favorable market conditions in the future, it can also exploit the opportunity of exporting its products such as TMT bars to nearby places of India.

***Demand of steels products in the country***

Nepalese economy is developing and growing, and is in phase of investment in infrastructure sectors, power sector and tourism sector. It is highly probable 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 rebuilding the housing sector has increased demand of iron and steel products in Nepal. As a result of increased development works, demand for iron and steel is expected to grow by 10% annually.

***About the Company***

Narayani Ispat Private Limited (NIPL) is a private limited company incorporated on September 17, 2009 for manufacturing of TMT bars and other allied steel products at factory located in Simara, Nepal. NIPL is part of the Keyal group of companies of Nepal and all the shares of the company are held by individual promoter from Keyal group. The company commissioned operations in July 2018 with capacity of 216,000 MTPA for manufacturing rolled products such as TMT bars, M.S Round etc. The company has also set up a M.S. Billet manufacturing plant of 87,000 MTPA capacity which commissioned operations in May 2019.

***Brief Financial Performance during the last 2 years is as follows:***

(Rs. In Million)

For the year ended Mid July	FY18 (A)	FY19 (A)*
Income from Operations	315	4,229
PBILDT	9	183
PAT	-	(139)
Overall Gearing (times)	8.22	8.98
Interest coverage (times)	1.23	0.89

\*Audited

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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	1,189.59	<b>CARE-NP BB-</b>
Short Term Bank Facilities	Working Capital Loan	870.00	<b>CARE-NP A4</b>
Short Term Bank Facilities	Letter of Credit	1,936.00	<b>CARE-NP A4</b>
<b>Total</b>		<b>3,995.59</b>	