

**Rating Rationale
Narayani Rolling Mills Private Limited**

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating	Rating Action
Short Term Bank Facilities	2,540.00	CARE-NP A4 [A Four]	Assigned
Total facilities	2,540.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Ltd. (CRNL) has assigned rating of ‘CARE-NP A4’ to the short-term bank facilities of Narayani Rolling Mills Private Limited (NRPL).

Detailed Rationale & Key Rating Drivers

The rating assigned to the bank facilities of NRPL are constrained by decline in financial and operational performance during FY19 (audited, refers to 12 months period ended mid-July 2019) with net loss coupled with leveraged capital structure and weak debt service coverage indicators. The ratings also factor in NRPL’s working capital intensive nature of operations, raw material price volatility and foreign exchange fluctuation risk, exposure to volatile interest rates coupled with presence in highly fragmented and competitive nature of steel industry. The ratings, however, derive strength from strong presence of the promoter group in steel sector supported by experienced management team, established brand and marketing network of the group with country wide presence, demand of steel products in the country and locational advantage of the company. Ability of the company to pass through changes in raw material prices to the customers to improve the operating profit margins and rationalization of its debt through efficient working capital management will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Decline in financial and operational performance during FY19 with net loss

NRPL had moderate capacity utilization of 60% in FY19 which reduced from 76% in FY18 with major decline in production of TMT Bars and allied products. NRPL’s total revenue declined by ~ 24% during FY19 to Rs. 3,584 majorly due to reduction in quantity sales of TMT bar. NRPL had a marginal increase in PBILDT to Rs. 203 Mn during FY19 with increase in PBILDT margin to 5.66% compared to PBILDT of Rs. 201 Mn in FY18 with PBILDT margin of 4.27%. The company reported net loss of Rs. 2 Mn during FY19 compared to PAT of Rs. 66 Mn during FY18. This decline was due to substantial increase in interest expense in FY19 coupled with increase in foreign exchange loss amounting to Rs. 22 Mn. NRPL generated Gross Cash Accruals (GCA) of Rs. 33 Mn during FY19.

Leveraged capital structure and weak debt service coverage indicators

The company doesn’t have any long-term loan at the end of FY19 and has only availed short term borrowings for financing the operations. Total Gearing Ratio of the company was high at 5.19x during

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

FY19 which increased from 3.20x during FY18. This was due to increased debt levels as a result of high utilization of working capital limits. NRPL had a moderate interest coverage ratio of 1.44x during FY19 declined from 2.54x in FY18. Total debt/ GCA for FY18 was high at 12.36x which further deteriorated to 50.31x during FY19.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature as NRPL is involved in the manufacturing wide range of steel products by procuring raw materials locally as well as through imports through Letter of Credit. NRPL also has to fund inventory and debtors which lead to high reliance on working capital limits. In FY19, debtor turnover days for NRPL was 78 days and the inventory turnover was 79 days. Total operating cycle of the company was 145 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 drawing power was around 90% during last 12 months period ended mid-January 2020 marked by overutilization of limits against the drawing power in few instances.

Raw material price volatility risk and foreign exchange fluctuation risk

Billet and Wire Rod are the major raw materials for NRPL which are majorly imported from India. The prices of the raw material 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 along with trading purchases contributed around ~90% of the total operating income of the company during FY19, thus, any volatility in prices of the same impacts the profitability of the company. Also, the company is exposed to foreign exchange fluctuation risk as the prices of imported raw materials are linked to USD. The ability of the company to pass through changes in raw material prices to the finished products and managing the foreign exchange fluctuation risks related to raw materials will be 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 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.

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 bars 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

NRPL has an operational track record of more than two decades in manufacturing of TMT Bars, angles, flats, sections and other allied steel products. The promoters of the company have wide experience in manufacturing steel and other construction materials for more than three decades. NRPL 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. Satya Narayan Keyal, Chairman of NRPL and also the Chairman of the Keyal group of companies has more than 30 years of experience in trading and manufacturing industry. Mr Anuj Keyal, Director, joined the business 5 years back and is involved in setting up all the new plants within the group.

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

The company sells TMT, angles, flats, wires and other allied products 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 along with a well-established dealer/distributor network in around 129 areas across the country which provides a ready market for its products.

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.

Locational advantage

The plant site is located in Chhatapipra, Simara, around 15 Kms from Indo-Nepal borders in Birgunj dry-port. Since majority of raw materials used by NRPL are imported from India, the factory's proximity to the border remains a positive point leading to savings in huge freight cost.

About the Company

Narayani Rolling Mills Private Limited (NRPL) is a private limited company incorporated on May 15, 1992 which came into operation from 1995 for manufacturing TMT Bars, angles, and other allied products having plant in Chhatapipra, Bara, Nepal. NRPL is part of the Keyal group of companies of Nepal and majority of the shares of the company are held by individual promoter from Keyal group. Currently, the total installed capacity of the entire plant is 48,300 Metric Tons Per Annum (MTPA).

Brief financials of NRPL during last 3 years is given below:

(Rs. Million)

For the year ended Mid-July	FY17 (A)	FY18 (A)	FY19 (A)
Income from Operations	3,221	4,698	3,584
PBILDIT	155	201	203
PAT	48	66	(2)
Overall Gearing (times)	2.00	3.20	5.19
Interest Coverage (times)	2.27	2.54	1.44

*Audited

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Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. In Million)	Rating
Short Term Bank Facilities	Working Capital Loan	90.00	CARE-NP A4
Short Term Bank Facilities	Trust Receipts	500.00	CARE-NP A4
Short Term Bank Facilities	Letter of Credit	1,950.00	CARE-NP A4
Total		2,540.00	