

Rating Rationale
Balaji Cement Industries Private Limited

Rating

Facilities	Amount (Rs. In Million)	Rating ¹	Rating Action
Long Term Bank Facilities	1,142.25	CARE-NP BB- [Double B Minus]	Revised from CARE-NP BB [Double B]
Short Term Bank Facilities	1,857.75	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	3,000.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating to ‘CARE-NP BB-’ for the long-term bank facilities and reaffirmed ‘CARE-NP A4’ assigned to the short-term bank facilities of Balaji Cement Industries Private Limited (BCPL).

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the bank facilities of Balaji Cement Industries Private Limited (BCPL) takes into account negative implications of COVID-19 on the business of the company, subdued operational and financial performance of the company in FY19 (audited, refers to 12 months period ended mid-July 2019) with only one month of operation and weak financial performance during H1FY20 (unaudited, refers to 6 months period ended mid-January 2020) and expected losses for FY20. The rating is also constrained by leveraged capital structure and weak debt service coverage indicators, working capital intensive nature of operations, lack of backward integration and raw material price volatility risk. The rating also factors in company’s exposure to volatile interest rates and presence in highly fragmented and competitive nature of cement industry. The rating, however, derive strength from experienced promoters in the manufacturing industries, demand of cement products in the country, product diversification with own brands and locational advantage of the plant site. The ability of the company to manage growth in operations & maintaining the profit margins by passing through changes in raw material prices to the customers 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 Weakness

Impact of COVID-19 on the business of the company

With outbreak of Coronavirus disease 2019 (COVID-19) recognized as Pandemic by World Health Organization on March 11, 2020, which has affected Nepal as well, Government of Nepal (GoN) has imposed travel restrictions and countrywide lockdown since March 24, 2020 halting operations of most of the organizations and slowing down of the economic activities. Further, the lockdown has been extended multiple times with current extension till June 14, 2020. Due to the lockdown, manufacturing activities of

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

BCPL had been suspended which has directly impacted the revenue of the company. However, with the GoN giving some relaxation to manufacturing industries to commence production with necessary safety arrangements, the company started partial operation. During this period, the company has been able to make only limited sales. However, these sales have been made in cash through which company has been meeting its fixed expenditure. Further, with manufacturing units throughout the nation running partially, availability of raw materials such as clinker, gypsum and their shipment is also likely to affect operation of the company in the near future. The company has been making advance payment for procurement of raw materials and as a result working capital loans are being fully utilized against the drawing power. While BCPL's performance in 9MFY20 was moderate, the revenue growth momentum, profitability and debt coverage indicators are expected to be under pressure. The company's ability to achieve sales and profitability as envisaged and maintain its debt coverage indicators would remain critical.

Subdued operational and financial performance of the company in FY19 with only one month of operation and weak financial performance during H1FY20

BCPL commenced its manufacturing operations from June 15, 2019 with a total installed capacity of 1,400 MTPD for manufacturing of OPC, PPC and PSC cements. The company obtained Nepal Standard Council (NSC) final approval to commence sales on October 24, 2019. With one month of operation during FY19, BCPL generated total revenue of Rs. 6 Mn. The company registered net loss of Rs. 2 Mn majorly due to negative PBILDT and incurred cash loss in FY19. During H1FY20, BCPL has booked revenue of Rs. 509 Mn. Further, with reduction of COGS as a % of net sales to ~90% during the period, BCPL has booked PBILDT of Rs. 31 Mn with PBILDT margin of 6.15%. BCPL has however incurred net loss of Rs. 136 Mn during H1FY20 due to high depreciation and interest expenses.

Leveraged capital structure and weak debt service coverage indicators

Debt-equity ratio of the company was moderate at 1.76x at the end of FY19. Long term debt increased from Rs. 1,173 Mn in FY18 to Rs. 1,273 Mn in FY19. This was partially offset by addition of fresh capital by the promoters of Rs. 175 Mn. During FY19, BCPL was in operation for one month, hence not availed any short-term loans. Due to this, total gearing ratio of the company was moderate at 1.76x at the end of FY19. Total debt/ GCA for FY19 was negative on account of negative gross cash accruals generated during the year. Debt-equity ratio as well as total gearing ratio of the company was high at 2.36x and 2.91x respectively at the end of H1FY20. BCPL had low interest coverage of 0.38x during H1FY20 with negative total debt/ GCA on account of negative gross cash accruals generated during the period.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature. BCPL is involved in manufacturing cement by procuring raw materials both locally and by importing. Raw materials such as slag, gypsum and flyash are imported from India for which payment is made upon receipt of goods. Also, other raw material being clinker are procured locally for which company receives credit period for around

30 days. BCPL has to keep the inventory for smooth operations and extend credit to their dealers, which lead to reliance on working capital limits. BCPL generally allows four-five months credit period to its dealers. The company keeps inventory for around two months. Total operating cycle of the company was 102 days (annualized) during H1FY20. This leads high working capital requirement to fund the operations. The company started availing working capital loans from mid-September, 2019. The average monthly outstanding of fund-based working capital limit against drawing power was around 97.27% during last 5 months period ended mid-February, 2020.

Lack of backward integration and Raw material price volatility risk

BCPL is engaged in producing cement and does not possess its own clinker unit. Hence, it has to procure clinker from other clinker manufacturing plants located in Nepal. Also, raw materials such as slag, gypsum and flyash are imported from India. BCPL mainly uses clinker, slag, fly-ash, gypsum etc. as the major raw materials. Raw material cost continues to be the major cost component of BCPL of the net sales. Hence, any adverse movement in raw material price without any corresponding movement in finished goods price is expected to affect the profitability of the company. The ability of the company to pass through adverse changes in raw material prices to the customers will be the key rating sensitivities.

Exposure to volatile interest rates

Nepalese banking sector fixes lending interest rate based on quarterly base rate and interest rate can 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 banks and financial institutions is subject to volatile interest rate.

Presence in highly fragmented and competitive nature of cement industry

BCPL is operating in a highly competitive market, dominated by the large cement manufacturers with wide brand acceptability. 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. 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 cement are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility in the prices of cement.

Key Rating Strengths

Experienced promoters in the manufacturing industries

BCPL is promoted by industrialists and traders of Nepal, who are involved in manufacturing of cement, agro processing, packaging, textiles, mattresses, etc. and trading of steel, building construction material, industrial raw materials, etc. The company is managed under the overall guidance of its the Board of

Directors (BoD) who possess wide experience in the related field. Mr. Rahul Kumar Agrawal is the Chairman and Mr. Gaurav Agrawal Gadia is the Managing Director of the Company. Mr. Rahul has been involved in family business for 22 years as Managing Director of Shiv Shakti Group, engaged in manufacturing of plastic fabric, packaging, laundry Soap and agriculture-based products (Rice, edible oils). Mr. Gaurav has more than 13 years of experience in textiles industry, import of industrial raw materials & readymade garments. Mr. Hemant Kumar Agrawal, director, has more than 34 years of experience in cement manufacturing and steels trading business and is also the managing director of Nepal Ambuja Cement Udhyog Pvt. Ltd.

Demand of cement 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. In the recent budget presented by finance minister of Nepal for FY21, government has allocated Rs. 55 Bn towards post-earthquake reconstruction of private housing, archeological heritage, school building, and government building. Further, government has majorly focused towards development of health sectors, tourism sectors, agriculture and other infrastructure development. Cement being fundamental requirement for any construction activity is therefore going to be in regular demand. Further, the government's high emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures and estimated GDP growth of 7.00% as included in the budget for FY20-21 is likely to benefit the cement manufacturers like BCPL.

Product diversification and own brand

BCPL is manufacturing PPC and OPC Cement under four brands and also manufactures PSC Cement under two brands, which has great usage on all types of residential, commercial & industrial projects, dams & other mass concrete works, water retaining structures, concrete roads & flyovers etc. Currently BCPL is majorly focusing its sales in Kathmandu valley and western part of Nepal.

Locational advantage of the plant site

The plant is located in the western region of Nepal. It is located at a distance of 65 kms from Butwal city and at a distance of 80 kms from one of the biggest industrial belts in Nepal (Bhairawa). On the other side it is at a close distance (17 kms) from the Indian Border of Uttar Pradesh. Being located nearby Indian border, BCPL can import its raw material requirements with low transportation costs. Also, it gives the plant an opportunity to market its products to the western, mid-western and central part of Nepal as the costs for transporting cement will be less compared to the industries which are in far eastern Nepal or far western Nepal.

About the Company

BCPL is a private limited company, established in May 2016, promoted by the individuals involved in cement industry and other manufacturing industries, for setting up clinker grinding plant at Kapilvastu District of Nepal. The promoters of the company have set up a clinker grinding unit to with cement manufacturing capacity of 1400 metric tons per day which came into operation from June 15, 2019. BCPL is engaged in manufacturing of Portland Pozzolana Cement (PPC), Portland Slag Cement (PSC) and Ordinary Portland Cement (OPC) under various brands.

Brief financial performance of BCPL during FY19 and 6 months period ended FY20 is given below:

(Rs. In Million)

Particulars	FY19 (A)	H1FY20 (UA)
Income from Operations	6	510
PBILDT	(1)	31
PAT	(2)	(136)
Overall Gearing (times)	1.76	2.91
Interest coverage (times)	-	0.38

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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	1,142.25	CARE-NP BB-
Short Term Bank Facilities	Working Capital Limit	740.00	CARE-NP A4
Short Term Bank Facilities (Proposed)	Working Capital Limit	917.45	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limit	200.30	CARE-NP A4
Total		3,000.00	