Rating Rationale

Annapurna Vegetable Products Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating[1]	Rating Action
Long Term Bank Facilities	92.39	CARE-NP BB+ [Double B Plus]	Assigned
Short Term Bank Facilities	2,929.77	CARE-NP A4+ [A Four Plus]	Assigned
Total Facilities	**3,022.16**		

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 Annapurna Vegetable Products Private Limited (AVPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of AVPL are constrained by fluctuating financial profile of the company during the last three years ending mid-July 2019 with leveraged capital structure and moderate debt coverage indicators, working capital intensive nature of business and high raw material price volatility risk and foreign exchange fluctuation risk. The ratings also factor in susceptibility to price fluctuation of seasonal agro products, fragmented and competitive nature of industry and exposure to volatile interest rates and regulatory risk. The ratings however, derives strength from established and adequate track record of operations along with experienced management team in the related field with presence and experience in various manufacturing, trading and services in Nepal and comfortable financial profile characterized by healthy growth in sales and profitability during FY19 (audited, refers to 12 months period ended mid-July 2019), after weak financial performance during FY18. The ratings also factor in stable demand and steady growth in the revenue with edible oil being essential part of cooking, locational advantage for both imports and exports and sizeable exports to India during last 2 years; albeit it is now curbed to a great extent. Ability of AVPL to manage growth in the operations & maintaining the profit margins and rationalization of its debt through efficient working capital management would be the key rating sensitivities.

Impact of Covid-19 on the business of the company

With global outbreak of Coronavirus disease 2019 (COVID-19) recognized as Pandemic by World Health Organization, 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. However, GoN had provided relaxation in operation of companies dealing in essential items during the lockdown period. Considering the same, AVPL has been running its normal operations and revenue of the company has not been impacted due to

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

effects of lockdown. Further, the central bank of Nepal has provided an extension of 3 months for the repayment of loans falling due in mid-April 2020 to provide temporary relief. However, AVPL has made its debt repayments for quarter ending mid-April 2020.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Leveraged capital structure and moderate debt coverage indicators

The financial risk profile of the company was below average marked by eroded Networth in the books of the company at the end of FY18. However, with company earning net profit of Rs. 239 Mn in FY19 followed by infusion of additional capital of Rs. 20 Mn by the promoters, the networth of the company improved during FY19. Overall gearing was high at 9.62x on account of increase in working capital loans of the company and low networth. The interest coverage ratio of AVPL was moderate at 3.49x in FY19 which increased from 0.60x in FY18.

Working capital intensive nature of business

The operations of AVPL are working capital intensive as company imports its raw materials from various countries through Letter of Credit. AVPL has to keep the inventory for smooth operations and extend credit to their customers, which lead to reliance on working capital limits. AVPL generally allows two months credit period to its customers and keeps inventory for around 1-1.5 months. Total operating cycle of the company improved to 77 days in FY19 from 99 days in FY18. This has led to high reliance of the company on the bank finance for working capital needs. The average utilization of fund-based working capital limit against drawing power was around 82% during last 12 months period ended mid-May, 2020.

Raw material price volatility risk and foreign exchange fluctuation risk

Crude soyabean, palmolien, sunflower oil and rape seed are the major raw materials for AVPL which are imported from various countries. The prices of the AVPL’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 cost was around 79% of the total sales of the company during FY19. Further, the total raw material requirement is met through imports and the prices of the same are linked to USD, for which the company is exposed to the foreign exchange fluctuation risk. AVPL incurred high foreign exchange loss of Rs. 57 Mn during FY19 due to foreign exchange fluctuations. The ability of the company to pass through changes in raw material prices to the finished products and managing the foreign exchange fluctuation risks will be the key rating sensitivities.

Susceptibility to price fluctuation of seasonal agro products

Prices of crude oils are highly volatile in nature and being agro products are seasonal in nature with production and prices dependent on various factors like area under production, yield for the year, demand supply scenario and inventory carry forward of last year. Further, the supply is dependent upon monsoon and climatic condition, exposing the fate of the company’s operation to vagaries of nature.

Fragmented and competitive nature of industry

Import and processing/refining of edible oils is highly fragmented due to presence of several organised/ unorganised players owing to low entry barrier and low technology and capital requirement. Low product differentiation of AVPL's product results in high competition from other players including traders. Considering the fragmented and competitive nature of industry, the millers have low pricing power.

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.

Exposure to regulatory risk

The operations of the AVPL are partially constrained by regulatory risk arising from various laws and policies of both Nepal and India. Earlier, before F/Y 2018-19, mustard oil, vanaspati ghee or other processed oil producing industries used to get 40 percent VAT refund at the end of the fiscal year. But the budget announcement for 2018-19 scrapped the provision. Further, ~27% of total revenue of the company during FY19, was from export of palmolien oil and soyabean oil to India. With this company is further exposed to import regulations of India. Recently, India had cancelled permission to import over three lakh tonnes of refined palm oil from Nepal and Bangladesh.

Key Rating Strengths

Established and adequate track record of operations along with experienced management team in the related field with presence and experience in various manufacturing, trading and services in Nepal

AVPL derives strength from its strong promoter group belonging to the Shanghai Family Brothers. They are one of the largest business group of Nepal involved in diversified business of banking, insurance, manufacturing, trading and other businesses. The promoters of company have an experience of over three decades in trading of imported and processed edible oils. AVPL is managed under the overall guidance of its two members Board of Directors (BoD) which includes experienced businessmen/industrialist with wide experience in the food processing and trading sector.

Fluctuating financial profile, however, healthy growth in sales and profitability during FY19

The company had moderate capacity utilization of ~57% in FY19 which improved from ~36% in FY18. However, the financial profile of the company was fluctuating in the past three years and company incurring high losses during FY18. Total revenue of the company increased by ~74% during FY19 majorly on account of increase in total quantity sold followed by improvement in overall average price realization of its products. Revenue during FY19 has been boosted majorly due to company exporting palmolien oil and soyabean oil to India. On back of high quantity sold and export to India with better profitability margins the PBILDT of the company improved substantially in FY19. The company achieved sales of Rs. 6,257 Mn upto mid-June 2020. The ability of the company to manage growth in the operations & maintaining the profit margins and rationalization of its debt through efficient working capital management would be the key rating sensitivities.

Essential part of cooking leading to stable demand and steady growth in the revenue

The demand prospect of edible oil industry is stable as oil is one of essential commodity for cooking. The company has been able to achieve CAGR growth of around 39% in the last four years ending FY19. Further, with demand higher than domestic production and slowdown in domestic agriculture production, large volume of edible as well as crude oil is being imported in Nepal giving importers like AVPL a favourable environment. Nepal has seen a steady growth in import of edible oil over the years.

Locational advantage for both imports and exports

The plant site is located in Lipanimal, Birgunj around 11 Kms from Indo-Nepal borders in Birgunj dry-port. Since all of the raw materials requirements of AVPL are imported from various countries followed by export prospects for the company, the factory's proximity to the border remains a positive point leading to savings in freight cost.

Sizeable exports to India during last 2 years; albeit it is now curbed to a great extent

With an objective to curb imports and boost local refining, India had imposed tax on import of refined palm oil with duty of 50% increased from 45% earlier. However, as per agreement on SAFTA (South Asian Free Trade Area), lower tariff of 6% is imposed on import of refined palm oil from Nepal. With this companies in Nepal had been exporting palm oil to India taking advantage from duty arbitrage. In the same line, AVPL had also been exporting palmolien oil to India. During FY19, export sales of the company contributed 27% of total revenue.

About the Company

Annapurna Vegetable Products Private Limited (AVPL) is a private limited company established in 1988 for processing/refining of edible oils, having plant in Adarshnagar, Birgunj, Nepal. Currently, the total installed capacity for refined soyabean/palmolien/sunflower oil is 60,000 MTPA, for vegetable ghee is 7,000 MTPA and for mustard oil is 10,000 MTPA. AVPL sells these edible oils under 3 different brands viz. Amrit, Sunstar and Rani in the domestic market.

Brief financial performance of AVPL during last 3 years is given below:

(Rs. Million)

Particulars	FY17	FY18	FY19
	(Audited)		
Income from Operations	2,560	3,116	5,435
PBILDT	51	56	488
PAT	7	(88)	239
Overall Gearing (times)	15.72	(147.65)	9.62

Interest coverage (times)	1.24	0.60	3.49

Analyst Contact	**Group Head**	**Relationship Contact**
Mr. Utsav Baral utsav.baral@careratingsnepal.com Tel No.: +977-01-4445473	Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4445474	Mr. Sajan Goyal sajan.goyal@careratingsnepal.com Tel No.: 9818832909/+977-01-4445472/3/4

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	92.39	CARE-NP BB+
Short Term Bank Facilities	Working Capital Limit	839.77	CARE-NP A4+
Short Term Bank Facilities	Non-Funded Limit	2,090.00	CARE-NP A4+
Total		**3,022.16**	