## Rating Rationale

## Ambe Cement Private Limited

**Rating**

| Facility | Amount (Rs. In Million) | Rating[1] | Rating Action |
|---|---|---|---|
| Long Term Bank Facilities | 39.00 | CARE-NP BBB- [Triple B Minus] | Reaffirmed |
| Short Term Bank Facilities | 950.00 | CARE-NP A3 [A Three] | Reaffirmed |
| **Total Facilities** | **989.00 (Decreased from Rs. 995.00 Mn)** | | |

*Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of 'CARE-NP BBB-' assigned to the long-term bank facilities and 'CARE-NP A3' assigned to the short-term bank facilities of Ambe Cement Private Limited (ACPL).

**Detailed Rationale & Key Rating Drivers**

The ratings assigned to the bank facilities of ACPL continue to derive strength from moderate financial and operational performance of the company coupled with moderate level of capital structure and debt service coverage indicators during FY20 (audited, refers to 12 months period ended mid-July 2020) as well as in H1FY21 (provisional, refers to 6 months period ended mid-January 2021). The rating also factors in established track record of operations along with strong promoters being part of Ambe Group of Companies and experienced management team in the related field, continuous enhancement of the capacity & addition of new machinery, product diversification and own brand, demand of cement products in the country. The ratings are, however, constrained by lack of backward integration and raw material price volatility risk, working capital intensive nature of operations, exposure to volatile interest rates and presence in highly fragmented and competitive nature of cement industry. 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.

***Negative implications of COVID-19 on the operations and financials of the company and on cement demand***

With the outbreak of Coronavirus disease 2019 (COVID-19) recognised as Pandemic by World Health Organization on March 11, 2020, which has affected Nepal as well, the Government of Nepal (GoN) had imposed travel restrictions and countrywide lockdown since March 24, 2020 till June 14, 2020. During the lockdown period, sales of the company has been directly impacted in FY20. However, with government easing restriction for various activities recently, operations, revenue and profitability of the company is also expected to improve in FY21. With various construction activities taking pace, demand of cement products is also likely to improve during current year

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

**Detailed Description of the Key Rating Drivers**

***Key Rating Strengths***

***Moderate financial and operational performance of the company during FY20 and H1FY21***

The company had moderate capacity utilization of ~49% during FY20 which reduced from ~53% during FY19. Manufacturing operations of ACPL was impacted by lockdown imposed by the GoN which has also resulted decline in total revenue by ~17% in FY20 to Rs. 1,784 Mn. With decline in total revenue, PBILDT of the company also reduced by ~5.73% in FY20, however with increase in PBILDT margin due to decline in raw material cost. As a result of decline in PBILDT, PAT of the company also declined by ~10% in FY20. Further during FY20, ACPL has installed ground granulated blast furnace slag system majorly for efficient production of PSC cement with which, depreciation of the company increased. During H1FY21, capacity utilization of the company has improved to ~50% with company booking total revenue of Rs. 879 Mn with PBILDT margin being maintained at same level of 10.58%.

***Moderate capital structure and debt service coverage indicators, with further improvement in H1FY21***

Debt equity ratio of the company was low at 0.30x at the end of FY20 which improved from 0.48x at the end of FY19 mainly due to repayment of the unsecured loans from the Directors followed by increase in net worth of the company upon accretion of profit. Total gearing ratio of the company was moderate at 1.98x at the end of FY20 which improved from 2.00x at the end of FY19. With decline in working capital loans in H1FY21, overall gearing ratio has further improved to 1.68x at the end of H1FY21. Interest coverage ratio of the company was moderate at 2.24x and total debt to Gross Cash Accruals was high at 10.56x during FY20. Interest coverage ratio and total debt to Gross Cash Accruals have further improved to 2.98x and 8.57x in H1FY21.

***Established track record of operations, strong Promoters, being part of Ambe Group of Companies and experienced management team in the related field***

ACPL has an operational track record of more than fifteen years in the cement manufacturing by grinding of clinker. ACPL is promoted by industrialists and traders who are related with Ambe Group of Companies, which have business interests in manufacturing and trading sectors. Mr. Shobhakar Neupane is the Chairman and Mr. Sajjan Kumar Agrawal is the Managing Director of the Company. Mr. Neupane is the Chairman/ Managing Director of Ambe Group. Mr. Agrawal looks after the day-to-day operations of the company and has 25 years of experience in trading and manufacturing. He is also director of Ambe Steels Pvt. Ltd. BoDs are supported by a team of experienced professionals. Promoters of the company have also infused additional funds in H1FY21 in the form of unsecured loan to support company operations.

***Continuous enhancement of the capacity & addition of new machinery***

Company has been continuously incurring capex in increasing the installed capacity and is currently operating three clinker grinding plants with total clinker grinding capacity of 1000 metric tons per day in the same premises. ACPL commenced commercial operation from June, 2005 by setting up clinker grinding unit of 300 MTPD capacity. Immediately during 2006, the company installed new plant of 300 MTPD and then in FY11 added another grinding unit of 400 MTPD which increased the total installed capacity to 1000 MTPD. ACPL has also installed ground granulated blast furnace slag (GGBS) system in FY20 for production of PSC cement.

***Product diversification and own brand***

ACPL is manufacturing PPC Cement under two brands, OPC cement under two brands and also manufactures PSC Cement under six brands, which has great usage on all types of residential, commercial & industrial projects, dams & other mass concrete works etc. Currently ACPL focus its sales in the territory of nine zones (out of 14 zones on Nepal) covering 38 districts (out of 77) of Nepal.

***Demand of cement products in the country***

Demand of cement products in the country is expected to grow in the long-term. 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, 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 ACPL.

**Key Rating Weaknesses**

***Lack of backward integration and raw material price volatility risk***

ACPL is engaged in producing cement and does not possess its own clinker unit. Hence, it has to procure clinker from other cement manufacturers. The company also imports slag from India. ACPL mainly use clinker, slag, fly ash, gypsum etc. as the major raw materials. Raw material cost continues to be the major cost component of ACPL constituting around 74% of the net sales in FY20. 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 of changes in raw material prices to the finished products will be the key rating sensitivities.

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

The operations of the company are working capital intensive in nature as ACPL manufactures cement by procuring raw materials both locally and by importing. Raw materials such as slag is imported from India for which advance payments has to be made whereas clinker, gypsum is procured locally for which company receives credit period for around 20 days. ACPL has to keep the inventory for smooth operations and extend credit to their dealers, which lead to reliance on working capital limits. Total operating cycle of the company was 239 days in FY20 which increased from 175 days in FY19 mainly due to increase in average collection period and inventory holding period. This leads to high working capital requirement to fund the operations. The average utilisation of fund-based working capital limit against drawing power was around 77.65% during last 12 months period ended mid-January, 2021.

***Presence in highly fragmented and competitive nature of cement industry***

ACPL is operating in a highly competitive market, dominated by the large cement manufactures with wide brand acceptability. The demand of cement 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 in Nepal, competition has intensified that has resulted into substantial decline in profitability margins of the industry players during the last 2 year.

**About the Company**

Ambe Cement Private Limited (ACPL) is a private limited company, established in 2004, promoted by the individuals involved in manufacturing industry and trading business, for setting up clinker grinding plant at Parsa District of Nepal. The company is engaged in manufacturing and selling of cement with grinding capacity of 1000 metric tons per day (MTPD). ACPL manufactures Portland Pozzolana Cement (PPC), Ordinary Portland Cement (OPC) and Portland Slag Cement (PSC) cement under ten different brands.

Brief financial performance of ACPL during last 3 years ending FY20 and H1FY21 is given below:

(Rs. Million)

| Particulars | FY18 | FY19 | FY20 | H1FY21 |
|---|---|---|---|---|
| | (Audited) | | | (Unaudited) |
| Income from Operations | 2,435 | 2,158 | 1,784 | 879 |
| PBILDT Margin (%) | 10.44 | 9.51 | 10.85 | 10.58 |
| Overall Gearing (times) | 1.96 | 2.00 | 1.98 | 1.68 |
| Interest coverage (times) | 2.80 | 2.22 | 2.24 | 2.98 |
| Current Ratio (times) | 1.12 | 1.30 | 1.26 | 1.40 |
| Total Debt/ Gross Cash Accruals (times) | 6.12 | 9.79 | 10.56 | 8.57 |


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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 | 39.00 | CARE-NP BBB- |
| Short Term Bank Facilities | Fund Based Limit | 910.00 | CARE-NP A3 |
| Short Term Bank Facilities | Non-Fund Based Limit | 40.00 | CARE-NP A3 |
| **Total** | | **989.00** | |