March 2021

Rating Rationale

Godawari Steel Private Limited

Rating

Facilities	Amount (Rs. In Million)	Rating[1]	Remarks
Long Term Bank Facilities	570.45	**CARE-NP B+ [Single B Plus]**	Reaffirmed
Short Term Bank Facilities	2,929.45	**CARE-NP A4 [A Four]**	Reaffirmed
Total Facilities	**3,500.00**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating 'CARE-NP B+' assigned to the long-term bank facilities and 'CARE-NP A4' assigned to the short-term bank facilities of Godawari Steel Private Limited (GSPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to bank facilities of Godawari Steel Private Limited (GSPL) are continues to be constrained by weak financial risk profile marked by subdued financial performance and net loss in FY20 (refers to 12 month period ended mid-July 2020, Audited), highly leveraged capital structure of the company at the end of FY20 and working capital intensive nature of operations. The rating is also constrained by foreign exchange fluctuating risk with raw material price volatility, exposure to volatile interest rates and competition from other steel players from industry. The rating, however, derives strength from established business group and experienced promoter, demand of steels products and locational advantage being located near from Nepal-India boarder. The ability of the company to achieve growth in operations and revenue with improvement in profitability margins and its overall solvency position will be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Growth in revenue in FY20 being the first full year of operation, however marked by losses

During FY20, the company reported growth in revenue by ~272% to Rs. 1,467 Mn as against revenue of Rs. 394 Mn. in FY19 with PBILDT margin of 7.66% being a first full year of operation. Despite, growth in revenue, company incurred loss during FY20, majorly due to increase in interest expenses resulting from increased working capital loan utilization. During H1FY21 (refers to 6 month period ended mid-January, 2021, Unaudited), the company achieved revenue of Rs. 1,050 Mn.

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

Highly leveraged capital structure and weak debt service coverage indicators at end of FY20

Debt-equity ratio of the company was high at 8.13x at the end of FY20 with overall gearing ratio of 18.26x which has been deteriorated from 4.28x and 6.90x respectively at the end of FY19. This deterioration is majorly due to increase in loan from directors and decline in net worth due to high losses incurred during the year. Interest coverage ratio was low at 0.63x in FY20, though improved from negative interest coverage ratio in FY19. Due to negative Gross Cash Accrual (GCA) reported by the company, total debt to GCA was negative in FY20. Also, the company has received loan from directors amounting to Rs. 552 Mn at the end of FY20 which increased from Rs. 379 Mn at the end of FY19 to fund the operations and financial obligations of the company.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature as GSPL is involved in the manufacturing of TMT & plain Steel Bars by procuring raw materials through imports. The company has to procure raw materials through Letter of credit at sight and also has to fund inventory and debtors which lead to high reliance on working capital limits. In FY20, the average debtor's turnover days increased to 125 days in FY20 from 82 days during FY19. Company keeps inventory for around 187 days during FY20, which has increased from 102 days in FY19 accordingly, total operating cycle of the company was high at 280 days in FY20. This leads to high reliance of the company on the bank finance for working capital needs. The average monthly outstanding of fund-based working capital limit against drawing power was around 90% during last 12 months period ended mid-January, 2021.

Raw material price volatility risk and foreign exchange fluctuation risk

The major raw materials for GSPL are imported from India and the prices 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 contributed around 89% of the total operating income of the company during FY20, thus, any volatility in prices of the same impacts the profitability of the company. With prices of raw material imported linked to USD, the company is exposed to the foreign exchange fluctuation risk. 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.

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. 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 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 completion has intensifies which has resulted into substantial decline in profitability margins of the industry players in FY20.

Key Rating Strengths

Established business group and experienced promoter in trading business, however, limited experience in the manufacturing industry

GSPL is promoted by Mr. Munna Prasad Senuriya Baniya, who is associated with Godawari Business Organization (GBO) as an Executive Director. GBO is an ancestral business of the promoter and was established in 1950. The group has been involved in manufacturing of HDPE pipes, garden pipes & water tanks, trading and supply of construction materials, repairing of transformers and fabrication, trading of hardware in drinking water projects. Since the group is operating in the similar line of business in the Nepalese market for decades, it gives them an advantage of existing distribution channel for marketing of manufactured goods from GSPL. The day to day activities of the company are handled by Mr. Senuriya who possesses more than two decades of extensive experience in the related field.

Demand of steels products in the country

Nepalese economy is developing and growing and is in phase of investment in infrastructure, power sector and tourism sector. In the budget presented by finance minister of Nepal for FY21, government has allocated Rs. 55 Bn for reconstruction with major focus towards development of health sectors, tourism sectors and other infrastructure development. However, with economic activities affected by COVID-19 pandemic, demand for steel may be subdued in short term, but with government focus on infrastructure, demand is likely to grow in long run. Government's high emphasis on infrastructure development and power sector in the budget for FY20-21 is likely to benefit the steel manufacturers like GSPL.

Locational advantage

The plant site is located around 20 Kms from Nepal-India Border (Gaur Customs), which makes the location of the plant nearness to the big Indian State Bihar and give GSPL an advantage of supply of raw material at lower transportation cost. GSPL can also use Birgunj Border, either via railways till Raxaul (~75 kms from plant location) or via road.

About the Company

Godawari Steel Private Limited (GSPL) is a private limited company promoted by businessman, mainly engaged in manufacturing and trading businesses. The factory is located at Chandranigahapur, Rautahat, Nepal and operating since April 2019. The company is manufacturing TMT & plain Steel Bars with operational capacity of 350MT per day. The entire capital of the company will be held by the sole promoter Mr. Munna Prasad Senuriya Baniya.

Brief Financial Performance of GSPL during last 2 years is given below:

(Rs in Million)

For the year ended Mid July	FY19(A)	FY20(A)
Income From Operations	394	1,467
PBILDT Margin (%)	(0.34)	7.66
Overall Gearing (times)	6.90	18.26
Interest Coverage (times)	(0.06)	0.63
Total debt/GCA	Negative	Negative
Current Ratio (times)	1.31	1.18

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Annexure 1: Details of the Facilities rated

Nature of Facility	Type of Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	570.45	**CARE-NP B+**
Short Term Bank Facilities	Working Capital	1550.00	**CARE-NP A4**
Short Term Bank Facilities	Non-Fund Based Limit	550.00	**CARE-NP A4**
Short Term Bank Facilities (Proposed)	Working Capital	829.55	**CARE-NP A4**
Total		**3,500.00**	