

**Rating Rationale**  
**Reliance Spinning Mills Limited**

**Rating**

Facility/ Instrument	Amount (Rs. In Million)	Rating <sup>1</sup>	Rating Action
Long Term Bank Facilities	2,015.39	<b>CARE-NP BBB+ [Triple B Plus]</b>	Revised from CARE-NP BBB- and removal of ratings from credit watch with negative implications
Short Term Bank Facilities	5,080.00	<b>CARE-NP A2 [A Two]</b>	Revised from CARE-NP A3 and removal of ratings from credit watch with negative implications
<b>Total facilities</b>	<b>7,095.39 (Increased from Rs. 6,079.39 Mn)</b>		

*Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has revised the rating to ‘CARE-NP BBB+’ assigned to the long term bank facilities and to ‘CARE-NP A2’ assigned to the short term bank facilities of Reliance Spinning Mills Limited (RSML). The ratings have been removed from “credit watch with negative implications” considering comfortable financial profile of the company and its ability to withstand the implications of ongoing Covid-19 without impacting the debt servicing capability of the company.

**Detailed Rationale & Key Rating Drivers**

The revision in ratings assigned to the bank facilities of RSML takes into account healthy operational and financial performance of the company characterized by growth in sales and substantial improvement in the profitability parameters and debt service coverage indicators in FY20 (audited, refers to 12 months period ended mid-July 2020) and H1FY21 (Unaudited, refers to 6 months period ended mid-January 2021). The ratings also factor in established track record of operations of the company along with resourceful and experienced promoters in manufacturing industries, established presence in both domestic and export market, diversified product profile and support from the government policies stimulating export sales. The ratings are however, constrained by project risk associated with entirely debt-funded capex leading to moderate gearing levels, company’s exposure to contingent liability from Nepal Electricity Authority (NEA), working capital intensive nature of operations, raw material price volatility risk with susceptibility to adverse foreign exchange price movements and exposure to volatile interest rates. Timely completion of the large sized capex within envisaged cost estimations and derive the expected benefit therefrom and the impact of disputed contingent liability related to NEA remain the key rating sensitivities. Also, ability of the company to pass through changes in raw material prices to the customers and managing the foreign exchange fluctuation risk related to raw materials are the key rating sensitivities.

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com)

***Impact of COVID-19 on the operations and financials of the company***

With the outbreak of Coronavirus disease 2019 (COVID-19) recognized 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, the manufacturing operations of the company was only partially impacted, however the decline in revenue in FY20 was majorly due to problems in dispatch of export sales on account of border closure. Further, the Central Bank of Nepal had provided an extension of 3 months for the repayment of loans falling due in mid-April 2020 to provide some temporary relief. However, the company did not avail the relaxations and has made its debt repayments for the quarter ending mid-April 2020 timely and availed 10% rebate on interest charged for the quarter and also interest rebate of 200 bps.

**Detailed Description of the Key Rating Drivers*****Key Rating Strengths******Established track record of operations of the company with resourceful and experienced promoters in manufacturing industries***

RSML has an operational track record of around 25 years in yarn manufacturing industry. RSML is a joint venture of two leading groups of Nepal i.e. Golyan Group and MS Group and is promoted by Mr. Pawan Kumar Golyan, Chairman of the Golyan Group and Mr. Shashi Kant Agarwal, Managing Director of MS Group. The company is managed under the overall guidance of its three member Board of Directors (BoD) who possess wide experience in the related field. Mr. Pawan Kumar Golyan, Chairman & Managing Director of RSML is also Chairman of NMB Bank Limited. He is also currently the President of Nepal Yarn Manufacturing Association and member of Industry and Investment Promotion Board under Department of Industry. Mr. Shashi Kant Agarwal, Director in RSML has 30 years of experience in Trade and Industry. Mr. Agarwal is President of Nepal Sugar Mills Association and Executive Member of Nepal India Chamber of Commerce of Industry. Mr. Akshay Golyan, Director, has around 6 years of experience in manufacturing and real estate sector.

***Healthy operational and financial profile characterized by growth in sales and substantial improvement in profitability parameters at the end of FY20 and H1FY21***

Manufacturing operations of RSML in FY20 was impacted by lockdown imposed by the GoN due to Covid-19 pandemic, wherein the company was operating partially. With closure of border impacting dispatch of export sales, the revenue of the company declined by 17% in FY20 to Rs. 6,278 Mn over FY19. Despite decline in sales, margin of the company improved substantially to 12.89% in FY20 majorly on account of decline in cost of raw material consumed and higher realization from the products sold. With improvement in PBILDT and decline in interest cost, profitability of the company increased in FY20. During H1FY21,

the company has achieved total income of Rs. 3,720 Mn with further improvement in PBILDT margin to 14.16% leading to improved PAT and gross cash accruals.

***Moderate debt service coverage indicators of the company at the end of FY20 and H1FY21***

Debt-equity ratio of the company was low at 0.61x at the end of FY20 which improved from 0.88x at the end of FY19, on back of repayment of term loans and accretion of the profit to net-worth. Total gearing ratio of the company was moderate at 1.76x at the end of FY20 with comfortable interest coverage ratio of 5.92x in FY20. Total debt/ GCA for FY20 was moderate at 6.95x which improved from 8.79x in FY19. At the end of H1FY21, Debt- equity ratio has deteriorated to 0.89x on account of part disbursement of term loan for the expansion project. However, overall gearing ratio has improved to 1.22x on account of lower utilization of working capital loans at the end of H1FY21. Further, the upcoming project of the company with entirely debt-funded capex of Rs. 3,000 Mn to be funded in two tranches of Rs. 1,500 Mn each in FY21 and FY22 is expected to moderately deteriorate the debt service coverage indicators which is expected to be partially offset by improved profitability of the company.

***Established presence both in domestic and export market***

RSML has international market in India, Turkey, UK, Bangladesh and Yemen and around 74% of total sales generated by the company is through export sales mainly to India and Turkey. RSML is a major exporter of Nepal contributing nearly 4.65% of total exports of the country in FY20. The company has a strong dealer network in Nepal, India and Turkey as well.

***Diversified product profile***

RSML is one of the largest producers and exporters of polyester, viscose and acrylic yarns and its blend. Company has strength and expertise to deliver Nepal's largest quantities of grey, dyed and mélange yarns and also a variety of synthetic yarns in a variety of blends and counts for all kinds of weaving and knitting requirements. Further, with capacity expansion the company will be in position to develop new products and cater to wide range of customer.

***Support from the government policies stimulating export sales***

RSML's revenue from export sales is supported by both domestic and foreign government policies. As per the new provision in FY19, Nepal government has announced cash incentives of three percent on yarn made out of polyester, viscose, acrylic and cotton in a bid to boost export earnings and manage increasing pressure on balance of payment. Also the new provision now provides incentives to goods exported even to India, whereas in the previous provision, the incentives were given only to goods exported to the third country. This increase in export incentive by the government is expected to further boost export sales of synthetic yarn from Nepal. Government's continued thrust on increasing export from Nepal is likely to benefit the yarn spinning manufacturers like RSML. However, any change in the incentive policy of the Government will have an impact on the profitability of the company.

**Key Rating Weaknesses*****Project risk associated with entirely debt-funded capex leading to moderate gearing levels***

The estimated total cost of capacity expansion by 9,360 MT in cotton and synthetic spun yarn is envisaged at Rs. 3,000 Mn which is proposed to be funded entirely through term loan from Banks. The financial closure for the projects has been achieved. Company plans to take disbursement of loan in two tranches of Rs. 1,500 Mn each in FY21 and FY22 as the capacity addition will be done in two phases with synthetic spun yarn unit coming into operation during March 2021 and cotton spun yarn unit during July 2022. Size of the project compared to company's existing net worth is moderate at ~1.7 times at the end of FY20 and ~1.4 times at end of H1FY21. However, with the existing term loans of the company being repaid fully till mid- FY22, the existing cash-flows are expected to support the debt servicing of the additional term loans for the expansion.

***Exposed to contingent liability from Nepal Electricity Authority (NEA)***

During FY19, RSML had received demand notice from Nepal Electricity Authority (NEA) towards additional electricity charges as dedicated feeder charges for the period Aug 2016 to April 2018. The matter was referred to the court, however recently the high court has referred back the matter to the Review Committee under Nepal Electricity Distribution Regulation. Impact of this contingent liability on the books of the company if the same crystallizes will be a key rating sensitivity.

***Working capital intensive nature of operations, with high reliance on bank finance for funding, however improvement in H1FY21***

The operations of the company are working capital intensive in nature as it is involved in manufacturing yarns by primarily importing raw materials through Letter of Credit from countries like China, India, HongKong, Indonesia, Malaysia and Thailand coupled with labour intensive operations. The company has to maintain inventory for smooth operations and also extend credit to dealers, which lead to reliance on working capital limits. The operating cycle of the company was high at 200 days in FY20 on account of substantial inventory days. The month end working capital utilization against the drawing power of the company for last 12 months ending mid- December, 2020 was at 72%. However, at the end of H1FY21, RSML had sizeable unutilized short term bank loan providing liquidity cushion to the company coupled with low interest expenses.

***Exposed to global competition as major sales are exports oriented***

India and Turkey are the major export market for synthetic yarn manufactured by RSML contributing nearly 70%-74% to total sales. Both India and Turkey are major export markets for most of the other countries which are more competitive in pricing thereby exposing RSML to domestic competition as well as competition from other countries. Also, the export sales of the company are concentrated as top 10 customer

base contribute nearly 50% to the total sales. This exposes the company to losing a substantial customer base and revenue if RSML is not able to compete with other countries/local manufacturers.

**About the Company**

Reliance Spinning Mills Limited (RSML) is a public limited company established in the year 1994 and is the largest spinning mill in Nepal. RSML is engaged in manufacturing of Polyester, Viscose, Acrylic/Blended & Polyester Textured Yarns. The company has two factories: Unit A located at Khanar, Sunsari and Unit B located at Duhabi, Sunsari, Nepal. Currently, the total installed manufacturing capacity of the company is 36,000 MT per year. The company is now planning to expand its capacity in two phases by setting up a synthetic spun yarn unit of 4,680 MT and cotton spun yarn unit of 4,680 MT capacity as part of its expansion program and is expected to come in operation during March 2021 and July 2022 respectively.

**Brief Financial Performance during the last 3 years and H1FY21 is as follows:**

(Rs. In Million)

For the year ended Mid July	FY18	FY19	FY20	H1FY21
	<i>Audited</i>	<i>Audited</i>	<i>Audited</i>	<i>(Un-audited)</i>
Income from Operations	6,201	7,536	6,278	3,720
PBILDT Margin (%)	10.89	10.07	12.89	14.16
Overall Gearing (times)	2.57	2.26	1.76	1.22
Interest coverage (times)	3.90	4.73	5.92	10.58
Current Ratio (times)	1.02	1.09	0.92	1.35
Total Debt/Gross Cash Accruals (times)	8.78	8.79	6.95	5.41

<b>Analyst Contact</b> Ms. Shalini Sanghai <a href="mailto:shalini.sanghai@careratingsnepal.com">shalini.sanghai@careratingsnepal.com</a> Tel No.: +977-01-4012629	<b>Relationship Contact</b> Mr. Sajan Goyal <a href="mailto:sajan.goyal@careratingsnepal.com">sajan.goyal@careratingsnepal.com</a> Tel No.: 9818832909/+977-01-4012628/29/30
---	---

<b>Disclaimer</b>
CRNL’s ratings are opinions on credit quality and are not recommendations to sanction, renew, disburse or recall the concerned bank facilities or to buy, sell or hold any security. CRNL has based its ratings on information obtained from sources believed by it to be accurate and reliable. CRNL does not, however, guarantee the accuracy, adequacy or completeness of any information and is not responsible for any errors or omissions or for the results obtained from the use of such information. Most entities whose bank facilities/instruments are rated by CRNL have paid a credit rating fee, based on the amount and type of bank facilities/instruments.

**Annexure 1: Details of the Facilities Rated**

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	Term Loan	2,015.39	CARE- NP BBB+
Short Term Bank Facilities	Working Capital Limits	2,175.00	CARE-NP A2
Short Term Bank Facilities	Non-Fund Based Limits	2,905.00	CARE-NP A2
<b>Total</b>		<b>7,095.39</b>	