Rating Rationale

Shree Krishna Steel Industries Private Limited

Rating

Facility/ Instrument	Amount (Rs. In Million)	Rating	Rating Action
Long Term Bank Facilities	66.75	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	1,640.00	CARE-NP A4 [A Four]	Reaffirmed
Total facilities	**1,706.75 (Reduced from Rs. 2,464.25)**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Ltd. (CRNL) has reaffirmed rating of 'CARE-NP BB' assigned to the long-term bank facilities and 'CARE-NP A4' assigned to the short-term bank facilities of Shree Krishna Steel Industries Private Limited (SSPL).

Detailed Rationale & Key Rating Drivers

The reaffirmation of the ratings assigned to the bank facilities of SSPL factors in deteriorated financial performance of the company during FY20 (audited, refers to 12 months period ended mid-July 2020) mainly due to impact of Covid-19, characterized by decline in sales and PBILDT along with net loss coupled with leveraged capital structure and weak debt service coverage indicators at the end of FY20, however with significant improvement in H1FY21 (provisional, refers to 6 months period ended mid-January 2020).The ratings continue to factor in SSPL's working capital intensive nature of operations, raw material price volatility and foreign exchange fluctuation risk, exposure to volatile interest rates coupled with presence in highly fragmented and competitive nature of steel industry. The ratings, however, derive strength from strong presence of the promoter group in steel sector supported by experienced management team, diverse product range catering to wide spectrum of industries, established brand and marketing network of the group with country wide presence, demand of steel products in the country and locational advantage with scope of export. Ability of the company to pass through changes in raw material prices to the customers to improve the operating profit margins and rationalization of its debt through efficient working capital management will be the key rating sensitivities.

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

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.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

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

Deteriorated financial performance of the company during FY20 characterized by decline in sales and PBILDT along with net loss, however improvement in profitability during H1FY21

Manufacturing operations as well as revenue of SSPL has been impacted by lockdown imposed by the GoN resulting decline in total revenue of the company by ~47% in FY20 to Rs. 1,683 Mn. With decline in total revenue, PBILDT and PBILDT margin also declined substantially in FY20. With decline in PBILDT resulting company not being able to cover its interest cost, SSPL incurred net loss in FY20. Despite decline in working capital loans at the end of FY20, interest expense was at same level compared to FY19, due to higher utilization of working capital loans before the lockdown period. During H1FY21, SSPL has booked total revenue of Rs. 933 Mn and PBILDT margin has improved to 11.66% mainly due to improvement in the average price realization for its products.

Leveraged capital structure and weak debt service coverage indicators at the end of FY20, however improvement in H1FY21

Debt-Equity ratio of the company was moderate at 1.05x at the end of FY20 which deteriorated from 0.53x at the end of FY19 mainly due to decline in the networth due to net losses incurred. Total Gearing Ratio of the company was high at 14.59x at the end of FY20 which deteriorated from 7.17x at the end of FY19 due to decline in the net-worth, however partially offset by decline in the total loan of the company. With improvement in the networth as well as lower utilization of working capital loans during H1FY21, overall gearing ratio, although being high, has improved to 5.20x. SSPL had a low interest coverage ratio of 0.25x in FY20 which has improved to 4.34x in H1FY21.

Working capital intensive nature of operations

The operations of the company are working capital intensive in nature as SSPL manufactures wide range of steel products by majorly importing raw materials through Letter of Credit. SSPL also has to fund the inventory and debtors which lead to high reliance on working capital limits. Total operating cycle of the company was 211 days in FY20 which increased from 115 days in FY19 mainly due to increase in inventory days leading to high reliance of the company on the bank finance for working capital needs. The average utilisation 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 SSPL are majorly imported from India, the prices of which are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices having a bearing on its profitability margins. The raw material consumption cost along with trading purchases contributed around 96% of the total operating income of the company during FY20, thus, any volatility in prices of the same impacts the profitability of the company. Also, the company is exposed to foreign exchange fluctuation risk as the prices of imported raw materials are linked to USD. SSPL incurred foreign exchange loss of Rs. 8 Mn during FY20 due to foreign exchange fluctuations increased from Rs. 1 Mn during FY19. The ability of the company to pass through changes in raw material prices to the finished products 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 like pipes, sheets & 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 competition has intensified which has resulted into substantial decline in profitability margins of the other industry players in FY20.

Key Rating Strengths

Strong presence of the promoter group in steel sector supported by experienced management team

SSPL has an operational track record of more than two decades in manufacturing of Pipes and Sheets. The promoters of the company have wide experience in manufacturing steel and other construction materials for more than three decades. SSPL is part of the Keyal group of companies of Nepal which is a diversified business group with strong presence in a broad range of business, manufacturing and industrial interests with main focus on manufacturing construction materials. The group also has 15 hardware outlets across the country which are strongly contributing to the group's steel business. The company is managed under the overall guidance of its ten members Board of Directors (BoD) which includes experienced businessmen/industrialist from the Keyal group with wide experience in the manufacturing sector. Mr. Satya Narayan Keyal, Chairman of NSPL and also the chairman of the Keyal group of companies has more than 30 years of experience in trading and manufacturing industry. Mr. Bikash Kumar Keyal, Director, has been involved in the groups business for the past 16 years and looks after the whole group's accounting and finance.

Diverse product range catering to wide spectrum of industries

SSPL is into manufacturing Hot Rolled (HR) and Cold Rolled (CR) pipes, and their variants along with shutter patti, Chequer plate etc. Company is also involved in selling hot rolled coil (HRC) sheet and cold rolled coil (CRC) sheet by cutting it in different sizes. These products have various household, official and engineering applications. SSPL sells its product all over Nepal and the sales are through direct marketing to existing as well as new customers. Most of the sales revenue comes through direct domestic sales through its trading houses.

Established brand and marketing network of the group with country wide presence

The company sells pipes, sheets and other allied products under the brand name of "Narayani Steels" which is already an established brand in the Nepal market on account of its long-standing presence in the construction materials manufacturing and trading industry. This provides leverage to the company in front of new players entering the industry. The group also has 15 in-house hardware trading outlets in and around the Kathmandu Valley along with a well-established dealer/distributor network in around 129 areas across the country which provides a ready market for its products.

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 SSPL.

Locational advantage and scope of export

The plant site is located in Chhatapipra, Simara, around 15 Kms from Indo-Nepal borders in Birgunj dry-port. Since majority of raw materials used by SSPL are imported from India, the factory's proximity to the border remains a positive point leading to savings in huge freight cost. Upon favorable market conditions in the future, SSPL can also exploit the opportunity of exporting its products such as pipes and other products to India and Bhutan.

About the Company

Shree Krishna Steel Industries Private Limited (SSPL) is a private limited company incorporated on February 28, 1995 for manufacturing Pipes, Sheets, Shutter Patti, having plant in Chhatapipra, Bara, Nepal and is in operation for more than two decades. SSPL is part of the Keyal group of companies of Nepal and all the shares of the company are held by individual promoters from Keyal group.

Brief financials of SSPL during last 3 years and H1FY21 is given below:

(Rs. Million)

For the year ended Mid-July	FY18	FY19	FY20	H1FY21
	(Audited)			(Unaudited)
Income from Operations	3,194	3,161	1,683	933
PBILDT Margin (%)	5.78	3.94	1.57	11.66
Overall Gearing (times)	5.01	7.17	14.59	5.20
Interest Coverage (times)	3.05	1.20	0.25	4.34
Current Ratio (times)	1.04	1.00	0.88	0.90
Total Debt/Gross Cash Accruals (times)	10.22	70.79	(11.69)	9.75

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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	66.75	CARE-NP BB
Short Term Bank Facilities	Fund Based Limit	300.00	CARE-NP A4
Short Term Bank Facilities	Non-Fund Based Limit	1,340.00	CARE-NP A4
Total		**1,706.75**	