Rating Rationale

Agni Cement Industries Private Limited

Rating

Facility	Amount (Rs. In Million)	Rating[1]	Rating Action
Long Term Bank Facilities	141.62 (decreased from 165.48)	CARE-NP BB [Double B]	Reaffirmed
Short Term Bank Facilities	709.62	CARE-NP A4 [A Four Plus]	Reaffirmed
Total Facilities	**851.24**		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (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 Agni Cement Industries Private Limited (APL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of APL continue to be constrained by leveraged capital structure and deteriorating debt service coverage indicators, working capital intensive nature of operations. The ratings also factor in raw material price volatility risk, presence in cyclical and highly competitive nature of cement industry along with exposure to volatile interest rates. The ratings also took cognizance of decline in revenue and profitability in FY20 (Audited, FY refer to 12 months' period ended mid-July 2020.)

The ratings, however, derive strength from experienced promoters, established brand with growing marketing network and favorable demand outlook of the industry.

Going forward, the ability of the company to profitable scale up of its operations while efficiently managing the working capital cycle will be the key rating sensitivities. Any un-envisaged debt funded capital expenditure leading to deterioration in its capital structure and debt coverage indicators from current levels will also be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Decline in revenue and profitability in FY20

APL reported decline in total sales by ~34% during FY20 over FY19 to Rs. 1,305 Mn due to decrease in average price realization of cement coupled with decline in quantity sold. Despite the decline in total operating income, PBILDT margin slightly improved during the same period from 9.48% in FY19 to 9.81% in FY20 on account of decline in cost of production on account of steps taken by the company to rationale

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

its operating cost. Though the PBIDLT margin improved, PAT margin is showing negative trend on account of higher proportion of finance cost and depreciation as percentage of total operating income. During Q3FY21, APL has achieved total revenue of Rs. 1,073 Mn while maintaining the PBILDT margin at 6.70%.

Leveraged capital structure and deteriorating debt service coverage indicators

APL's capital structure stood leveraged on account of high dependence on external borrowings to meet its working capital requirements. At the end of last 2 FYs (FY19 & FY20: refers to 12 months' period ended mid-July 2020), overall gearing of the company stood almost stable at around 2.25x. Though the company has paid dividend in FY20 which led to decline in net worth base; however, reduction in debt levels led to almost stable overall gearing. The company has high working capital loans utilization of ~88% for the last 8 months' period ended mid-July 2020.

Also, due to declining scale of operations has led to low GCA levels. Therefore, the interest coverage ratio of the company remained weak and stood at 1.44x in FY20. Furthermore, the total debt/ GCA remained high at 24.10x in FY20.

Working capital intensive nature of operation

Operations of the company are highly working capital intensive marked by an average operating cycle of around 211 days in FY20. Being a competitive business, the average collection period remained high at around 258 days during FY20. Also, being a manufacturer, the company is required to maintain adequate inventory of finished goods and clinker to meet the immediate demand of its customers. The high working capital requirements were met largely through highly payable period of 90 days in FY20 and bank borrowings which resulted in a high average utilization of around ~88% of its sanctioned working capital limits for 8 months' period ended mid-March, 2021.

Raw material price volatility risk

APL uses clinker, gypsum and fly ash as the major raw materials. All the clinker requirements are locally purchased within Nepal whereas gypsum and fly ash are imported from India. Raw material cost continues to be the major cost component of APL as cost of goods sold constituting around 82% of the total sales in FY20. As clinker constitutes major component in the manufacturing of cement, APL being standalone grinding unit, will have cost competitive disadvantage over the cement companies having both clinker production unit and grinding unit. 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.

Presence in cyclical and competitive nature of cement industry

APL is operating in a highly competitive market, dominated by the large cement manufacturers with wide brand acceptability. Given the fact that the entry barriers to the industry are low, the players in the industry do not have pricing power and are exposed to competition-induced pressures on profitability. The demand of cement industry is considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry. The producers of cement are essentially price-takers in the market, which directly expose their cash flows and profitability to volatility in the prices of cement.

Cement industry is highly cyclical in nature and depends largely on the economic growth of the country. There is a high degree of correlation between the GDP growth and the growth in cement consumption. Cement being a cyclical industry goes through phases of ups and downs, and accordingly impacts the unit realizations.

Key Rating Strengths

Experienced promoters in the related field

APL is promoted by Nepalese individuals involved in cement industry, hospital and education sectors. The company is managed under the overall guidance of the Company's Board of Directors (BoD) who possesses wide experience in the related field. Mr. Krishna Prasad Pokharel is the Chairman and Dr. Tara Prasad Pokharel is the Managing Director of the Company. Mr. Krishna has been involved in different businesses from the last 25 years and is director in Shubhashree Agni Cement Udhyog Pvt. Ltd. (SPL) [CARE-NP BB+/A4+]. Dr. Tara Prasad, is also the Managing Director of SPL. As on July 16 2020, APL holds around 10.84% stake in SPL. SPL has been operating both clinker production and grinding plant since past seven years.

Established brand and growing marketing network

APL has been on market for more than 10 years. During this course, APL has established four brands like Agni, Orient and Tridev as PPC brand and Alfa as OPC brand. APL has focused its sales in the territory of nine zones (out of 14 zones of Nepal) covering 31 districts (out of 77) of Nepal. Additionally, to ramp up production and increase TOI, APL has taken various measures over the period which has then led to growing market network.

Demand of cement products in the country 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. The Government has allocated Rs. 55 Bn towards post-earthquake reconstruction of private housing, archaeological heritage, school building, and government building. Furthermore, government has majorly focused towards development of health sectors, tourism sectors, agriculture and other infrastructure development. Cement being fundamental requirement for any construction activity is therefore going to be in regular demand. 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 APL.

About the Company

Agni Cement Industries Private Limited (APL) is a private company and was established in 2007. APL is engaged in producing cements like Portland Pozzolana cement (PPC) and Ordinary Portland cement (OPC) having installed capacity of 900 metric tons per day (MTPD). ACPL had started its cement grinding plant in December 2009 with 600 MTPD which was later enhanced to 900 MTPD in May 2018.

Brief Financial Performance of APL during last 3 years ending FY20 and Q3FY21 is given below:

(Rs. In Million)

For the year ended Mid July	FY18	FY19	FY20	Q3FY21
	(Audited)			(Provisional)
Period of operation	**12 months**	**12 months**	**12 months**	**9 months**
Income from Operations	1,974	1,972	1,305	1,073
PBILDT Margin (%)	8.59	9.48	9.81	6.70
Overall Gearing (times)	1.91	2.23	2.27	2.10
Interest coverage (times)	3.14	2.15	1.44	1.47
Current Ratio (times)	1.14	1.11	1.16	1.18
Total Debt/ Gross Cash Accruals (times)	8.30	12.52	24.10	-

Analyst Contact	Group Head	Relationship Contact
Mr. Rujan Bajracharya rujan.b@careratingsnepal.com Tel No.: +977-01-4445473	Ms. Shalini Sanghai shalini.sanghai@careratingsnepal.com Tel No.: +977-01-4445474	Mr. Achin Nirwani achin.nirwani@careratingsnepal.com Tel No.: 9818832909/+977-01-445472/3/4

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, Auto loan and Equipment Loan	141.62	CARE-NP BB
Short Term Bank Facilities	Working Capital Loan	659.62	CARE-NP A4
Short Term Bank Facilities	Letter of Credit	50.00	CARE-NP A4
Total		**851.24**	