Nepal Ultratech Cements Private Limited

Ratings

Instrument / Facilities*	Amount (Rs. in Mn)	Rating[1]	Rating Action
Long-term Bank Facilities	1,223.41 (Increased from 1,144.00)	CARE-NP BB [Double B]	Reaffirmed
Short-term Bank Facilities	725.59 (Increased from 725.00)	CARE-NP A4 [A Four]	Reaffirmed
Total Facilities	**1,949.00 (One Billion Nine Hundred Forty Nine Million)**		

**Details of instrument / facilities in Annexure-1*

CARE Ratings Nepal Limited (CRNL) has reaffirmed ratings of 'CARE-NP BB' assigned to the long term bank facilities and 'CARE-NP A4' assigned to short term bank facilities of Nepal Ultratech Cements Private Limited (NUCPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of NUCPL continue to be constrained by short track record of operations, leveraged capital structure, working capital intensive nature of operations. The ratings also factor in its presence in highly competitive industry and lack of backward integration leading to raw material price volatility risk.

The ratings, however, derives strength from the experienced promoters, locational advantage of manufacturing facilities and growing scale of operations.

Going forward, the ability of the company to profitably scale up its operations while managing the raw material prices fluctuations along with rationalization of its debt levels would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Constraints

Short track record of operation though growing

NUCPL started with its commercial production during December 2018 and has a relatively short track record of operations as compared with other established players. FY20 was the first full financial year of operation. However, the risk is partially mitigated by the fact that the scale of operations is growing continuously. For the period FY19 ((FY refer to 12 months ending in Mid-July) to FY21 (based on provisional results), the company's total operating income grew from Rs. 564 Mn to Rs. 1,620 Mn reflecting a compounded annual growth rate (CAGR) of ~50%. The growth in Total Operating Income (TOI) was mainly supported by increase in quantity sold. The company has sold 1,382,622 bags and 2,664,761 bags of cement in FY20 & FY21 respectively.

Highly leveraged capital structure and below average debt service indicators

The total debt of the company increased by Rs.125 Mn and stood at Rs. 1,801 Mn at the end of FY20. This increase in debt levels was on account increase in the term loan along with the higher utilization of working capital borrowings. As on mid-July 2020, the capital structure of the company stood leveraged marked by debt equity ratio and overall gearing of 1.70x and 2.53x respectively (PY: 1.88X & 2.80x respectively). The debt equity ratio and overall gearing improved over previous balance sheet date on account of infusion by promoters and retention of profits leading to increase in net worth base.

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

Apart from overall gearing, other coverage indicators including total debt to GCA and Interest coverage ratios also improved for the company to 74.77x and 1.21x for FY20 respectively (PY: 157.40x and 1.26x respectively). The same was supported by growing scale of operations which led to increase its GCA levels. Though improved, it continued to remain weak.

Lack of backward integration and raw material price volatility risk; presence only in clinker grinding

NUCPL is engaged in manufacturing cement and does not possess its own clinker unit. Company mainly imports Gypsum and fly-ash from India, for which the payments are made in Indian currency (INR), whereas the clinker and coal are majorly purchased from domestic markets where the prices tend to be volatile. Furthermore, the company's manufacturing processes are also dependent on the imports of raw materials from India. The cost of goods sold including raw material cost constituted more than 80% of TOI. 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.

Working capital intensive nature of operations

Operations of the company are highly working capital intensive marked by an average operating cycle of around 246 days. Being in a competitive business, the average collection period remained high at around 159 days during FY20. Also, being a manufacturer, the company is required to maintain adequate inventory of its raw materials like Gypsum, fly-ash and slag which is mainly imported from India along with stockpile of finished goods to meet the immediate demand of its customers. This has led to inventory holding period of 96 days during FY20. The high working capital requirements were met largely through bank borrowings which resulted in a high average utilization of around ~90% of its drawing power for the last 12 months ending in mid-July 2021.

Distribution channel of the company is currently in nascent stage and yet to be fully develop

NUCPL commenced its operation only in December 2018 and its brand "Bandhan" is new in the market. NUCPL is exposed to competition from existing brands in the market which have wide acceptability. Also, distribution channel of the company is currently in nascent stage and yet to fully develop and cover the target markets.

Exposure to volatile interest rates

Nepalese banking sectors are fixing floating interest rate on lending by adding certain percentage of premium on quarterly base rate and interest rate will be changed accordingly on quarterly basis. Base rate of the Bank and Financial Institutions (BFIs) remains volatile to change in liquidity position which lead to change in interest rate. Interest rate has been changing frequently in Nepal market since last 2-3 years. Therefore, funding from BFIs is subject to volatile interest rate.

Competitive and cyclical nature of cement industry

NUCPL is operating in a highly competitive market, dominated by the large cement manufacturers with wide brand acceptability. Given the fact that there are large number of players in the industry, the new 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. 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 industry players in the current year.

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

Key Rating Strengths

Experienced promoters in trading field related to construction items

NUCPL is promoted by industrialists and traders from different district of Nepal, who are involved in various trading and manufacturing business. It is managed under the overall guidance of the Company's Board of Directors (BoD) who possesses wide experience in related field. Mr. Manish Kumar Maru, Chairman & Managing Director of the company has more than 11 years of experienced and he is also involved in trading of hardware material including cement.

Product Diversification and locational advantage of manufacturing facility

NUCPL has been manufacturing OPC and PSC cement and the PPC plant of the company has come into operations during FY21. The cement manufactured are being sold under the "Bandhan Brand" and premium quality cement is sold under brand name "L&T premium gold'. Currently, NUCPL is focused in selling cement in the nearby areas and increase its market presence and improve brand image.

The plant is located at eastern part of Nepal where concentration of cement factories is relatively less than the western part of the country. Bhadrapur, Birtamod, Biratnagar, Itahari etc. are the big cities nearby which is the major local market for the NUCPL's product. As NUCPL imports around 80% of clinker from India its proximity to Indian border reduces the logistic cost. NUCPL imports raw material from its suppliers in India till Bathnaha railway station (Bihar) which is approximately 5 kms from Biratnagar. It is then transferred via road to the plant site in Morang District which is 15 Kms from Biratnagar custom point. This connectivity enables NUCPL to get raw materials at lower logistic cost.

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 infrastructure, road, bridges and other public facilities. Cement being fundamental requirement for any construction activity is therefore going to be in regular demand. Also, the government's high emphasis on infrastructure development namely development of roads, hydropower, airports and other infrastructures and estimated GDP growth of 6.50% as included in the budget for FY21-22 is likely to benefit the cement manufacturers like NUCPL.

About the Company

Nepal Ultratech Cement Private Limited (NUCPL) was incorporated in August 27, 2015. The company is in manufacturing of cement and the manufacturing plant is located in Hattimuda, Morang District of Nepal with total grinding capacity of 300,000 MTPA.

Financial Performance

(Rs. in Million)

For the Period Ended / as at Mid-July	2019 (7.3m, A)	2020 (12m, A)
Total Operating Income	564	832
PBILDT Margin (%)	9.17	16.71
Overall Gearing Ratio (times)	2.80	2.53
Interest Coverage (times)	1.26	1.21
Current Ratio (times)	1.00	1.18
Total Debt/ Gross Cash Accruals (times)	157.40	74.77

A: Audited

Annexure 1: Details of Instrument / Facilities

Name of the Instrument / Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings assigned
Long Term Bank Facilities	Term Loan	1,223.41	**CARE-NP BB**
Short Term Bank Facilities	Fund Based Limits	600.59	**CARE-NP A4**
Short Term Bank Facilities	Non-Fund Based Limits	125.00	**CARE-NP A4**
Total		**1,949.00**	

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