Samrat Cement Company Pvt Ltd

Ratings

Facilities	Amount (Rs. Million)	Rating[1]	Rating Action
Long Term Bank Facilities	8,722.09 (Increased from Rs. 8,527.57 Mn)	CARE-NP BB+ [Double B Plus]	Rating Revised from CARE-NP BB to CARE-NP BB+
Short Term Bank Facilities	2,718.99 (Increased from Rs.1,145.17 Mn)	CARE-NP A4+ [A Four Plus]	Rating Revised from CARE-NP A4 to CARE-NP A4+
Total Facilities	11,441.08 (Eleven Thousand Four Hundred Forty-One Million and Eight Thousand Only)		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has revised the rating to 'CARE-NP BB+' to the long-term bank facilities and 'CARE-NP A4+' to the short-term bank facilities of Samrat Cement Company Private Limited (SCPL).

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the SCPL factors in change in management with induction of established promoters having experience in manufacturing industries including cement manufacturing, increasing scale of operations market by growth in revenue and increased profitability in FY21. The ratings further derive strength from locational advantage of the project site, established brand presence and demand of cement products expected to grow in the long term.

However, the rating continues to be constrained by leveraged capital structure, project stabilization risk, raw material price volatility risk, working capital intensive nature of operations and presence in highly competitive nature of cement industry.

The ability of the company to profitable scale up its operations along with rationalization of its debt levels would be the key rating sensitivities. Furthermore, completion of the ongoing expansion project with-in the envisaged time and cost will be key rating sensitivity.

Detailed description of the key rating drivers

Key Rating Weaknesses

Leveraged capital structure at the end of FY21 on account of large size debt funded capex

The total debt of the company increased to Rs. 10,920 Mn at the end of FY21 from Rs. 8,145 Mn over previous balance sheet date. This substantial increase in debt levels is due to company availing most of the term debt required for financing the expansion project. Accordingly, overall gearing ratio of the company deteriorated to 3.98x during FY21(FY20: 3.61x). However, debt equity ratio remained high at above 3x on the balance sheet date of last 2 FYs. The interest coverage ratio and total debt to Gross Cash Accrual Ratio stood at 2.06x and 20.76x respectively during FY21 (FY20: 2.12x and 66.54x respectively).

Project stabilization risk associated with its very large-size planned capex

SCPL has undertaken a brownfield expansion project to increase the installed capacity of grinding unit to 3,600 MTPD from 1,800 MTPD. Also, for the backward integration of the plant, the company has set up the 4,000 MTPD clinker plant. The total estimated cost project cost for clinker unit and expansion project was 10,132.62 Mn out of which Rs. 8,194 Mn (earlier Rs. 8,106 Mn) was proposed to be funded through Term Loan and balance through equity. The equipment erection works of grinding unit has almost been completed and the same is expected to come into an operation in February 2022. The clinker plant has started commercial operation in January 2021. Being significant capacity expansion, the stabilization and streamlining of production remains to be seen.

[1]Complete definition of the ratings assigned are available at www.careratingsnepal.com and other CARE publications

Furthermore, post project implementation risk, risks in the form of achieving the envisaged scale of business and also scalability risk associated with the products in the light of competitive nature of industry remains crucial for credit prospective.

Raw material price volatility risk

SCPL currently uses coal, flyash, gypsum, clay, bauxite and iron ore as major raw materials. Coal constituted around 60-65% of major raw materials consumption in clinker and cement production. The company is exposed to the raw material price volatility risk due to the volatility experienced in the prices of coal respectively. The general volatility in the raw material prices also has an impact on the price of its final product. Any sudden spurt in these raw material prices might not be passed on to the end customers, instantly, on account of highly competitive nature of the industry, which could lead to decline in profitability margins. Raw material cost continues to be the major cost component of SCPL as cost of goods sold constituting around 69 % of the total sales in FY21 (FY20: 81%). Company imported the majority of coal from South Africa, Australia during FY21. And the procurement to raw material (fly ash, gypsum and coal) was mainly in the form of imports during FY21. The material is completely sold in the domestic market. Though the company tries to pass on the price and currency volatility to the end users, any adverse fluctuations in the currency markets may put pressure on the profitability of the company.

Working Capital Intensive Nature of Operations

The operations of the company are working capital intensive in nature. SCPL is involved in manufacturing cement and clinker by procuring raw materials both locally and by importing. The company has to maintain inventory for smooth operations and extend credit to their dealers, which lead to reliance on working capital limits. The company generally allows two to three months credit period for its cement sale to its customers and maintain inventory of raw materials for around one and half months. The operating cycle of the company elongated from 53 days in FY20 to 97 days in FY21. Inventory holding period increased from 89 days in FY20 to 190 days in FY21. The inventory days was significantly increased on account of high stock in the year end. This leads high working capital requirement to fund the operations. The month end working capital utilization of the company against drawing power was around 80% during last 5 months period ended mid-November 2021.

Presence in highly competitive nature of cement industry

SCPL 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. 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. As per latest Nepal Rastra Bank (NRB) report published on May 2021, 55 industries are in operation with combined installed capacity of 15 million MTPA. However, capacity utilization has reduced as a result of addition of new capacities during the year. In order to push sales to sustain the competition, credit sales in the market have substantially increased leading to increased debtor days and high working capital requirement for companies. 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.

Key Rating Strength

Change in management with induction of established and financially strong promoters having experience in manufacturing industries including cement

There was change in the shareholders of Samrat Cement Private Limited with Chaudhary Group Pvt Limited acquiring the major shareholding of 35.85% as on July 16, 2021. Chaudhary Group Pvt Ltd is one of the leading business groups of Nepal and is involved in diversified business like FMCG, manufacturing, real estate, cement and other businesses. Being a part of the prominent group SCPL has privilege in term of technical and financial assistance.

The company is managed under the overall guidance of the 5 Board of Directors (BoD) who possesses wide experience in the related field. The two directors, Mr. Nirvana Chaudhary and Mr. Barun Chaudhary are from Chaudhary Group Pvt Ltd. Mr. Anil

Kumar Rugata is the Chairman and Mr. Bashudev Pandeya is the Managing Director of the Company. Mr. Rungta, has more than 25 years of experience in different sector like cement, iron, wire etc. Mr Pandeya, Managing Director of SCPL has more than two decades of experience in the field of coal mining, bricks industry, rice mills and trading of grain items and having 4 years of experience as Executive Director of Sonapur Cement Pvt. Ltd.

Increasing scale of operations market by growth in revenue and increased profitability in FY21

SCPL reported increase in total operating income by 94% to Rs. 4,104 Mn during FY21 as compared to Rs.2,113 Mn in FY20. The increase in total revenue in FY21 was on account of increase in quantity sold of cement coupled with the clinker plant coming into operation on January 14, 2021. This increase in quantity sold was partially offset by decline in average price realization of the cement to Rs. 472 per bag in FY21 from Rs.520 per bag in FY20 due to increased competition and subdued demand on account of pandemic.

PBILDT margin increased significantly to 25% during FY21 from 11% in FY20 on account of rationalization of the clinker cost due to the backward integration and increase in total revenue. Further, SCPL reported sales revenue of Rs. 1,507 Mn during Q1FY22, out of which Rs. 552 Mn was through cement sales and Rs. 954 Mn was through clinker sales.

Locational advantage of the project site and license of Limestone mines

The plant is located in the mid-western part of Nepal nearby the big cities Ghorahi, Tulsipur, Kohalpur, Dhangadi, Nepalgunj, Butwal, Bhairahawa, etc. which are major local market for the SCPL's product. The limestone mine is located at a distance of 50 km from the plant site which eases the extraction of limestone from the mines. Further, there are only three clinker and grinding plant operating around SCPL's site. Furthermore, there are also numerous small grinding plants nearby SCPL's site to which SCPL is proposing to sell excess manufactured clinker.

Established Brand Presence

SCPL is manufacturing PPC Cement that has great usage for brick masonry, plastering, tiling and waterproofing works. OPC cement is manufactured which has great usage for Structural Concrete or Reinforced. SCPL is manufacturing PPC and OPC cement under seven brands namely Gajraj, Gajraj Premium, Baaj, Baaj Premium, Badshah, Samrat and Samrat Premium. Gajraj, Baaj, Badshah & Samrat are PPC cement brands and Gajraj Premium, Baaj Premium & Samrat Premium are OPC cement brands. SCPL is planning to increase its market presence and improve brand image by conducting dealers meet all over the Nepal, designing brochure & website, expenditure towards advertisement and business promotion followed by capacity enhancement.

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. In the recent budget of Nepal for FY22, government has majorly focused towards development of health sectors, tourism sectors and other infrastructure development. 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 SCPL.

About the Company

Samrat Cement Company Private Limited (SCPL) is a private limited company, established in 2013. The company is engaged in manufacturing of cement having an installed capacity of 1800 MTPD as on January 2022. The company is in process of expanding its grinding capacity to 3,600 MTPD. Further, the company has also backward integrated its plant by setting a clinker manufacturing unit of 4,000 MTPD capacity which came into operation on January 14, 2021. The manufacturing facilities are located in Dang District of Nepal.

Financial Performance

(Rs. in Mn)

Particulars	FY19	FY20	FY21
	Audited	Audited	Audited
Income from Operations	3,168	2,113	4,104
PBILDT Margin (%)	13.05	11.31	25.11
Overall Gearing (times)	1.32	3.61	3.98
Interest coverage (times)	2.52	2.12	2.06
Current Ratio (times)	1.42	1.17	1.09
Total Debt/Gross Cash Accruals (times)	10.71	66.54	20.76

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Type of the Facility	Amount (Rs. Million)	Rating
Long Term Bank Facilities	**Term Loan**	**8,722.09**	**CARE-NP BB+**
Short Term Bank Facilities	**Working Capital**	**2,718.99**	**CARE-NP A4+**
Total Facilities		**11,441.08**	

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