Narayani Oil Refinery Udhyog Private Limited

Ratings

Facilities	Amount (Rs. Million)	Rating[1]	Rating Action
Short Term Bank Facilities	5,210.00 **(Increased from Rs. 4,650 Mn)**	CARE-NP A3 [A Three]	Reaffirmed
Total Facilities	**5,210.00 [Five Thousand Two Hundred and Ten Million Only]**		

Details of instruments/facilities in Annexure-1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP A3 [Single A Three]' to the short-term bank facilities of Narayani Oil Refinery Udhyog Private Limited (NOPL).

Detailed Rationale & Key Rating Drivers

The rating assigned to bank facilities of NOPL continues to derives strength from established track record of operations, experienced management team, moderate financial performance as reflected from growing scale of operations on y-o-y basis, satisfactory profitability margins, moderate capital structure and comfortable debt service coverage indicators at the end of FY21 (Audited; refers to 12 months period ended mid-July 2021). The rating also factors in established distribution network, stable demand of edible oil, and locational advantage of manufacturing facilities.

The rating, however, are constrained by working capital intensive nature of business, susceptibility to price fluctuation of seasonal agro products, and competitive nature of industry. The rating is also constrained by raw material price volatility risk, foreign exchange fluctuation risk, exposure to regulatory risk and exposure to volatile interest rates.

Ability of NOPL to manage growth in operations & maintaining the profit margins, rationalization of its debt through efficient working capital management would be the key rating sensitivities. Furthermore, the ability of the company to pass through changes in raw material prices to the customers and managing the foreign exchange fluctuation risks related to raw materials will also be the key rating sensitivities.

Detailed description of the key rating drivers

Key Rating Strengths

Established and long track record of operations along with experienced management team

The company has been into processing and marketing of edible oil for more than 30 years and has developed a market for itself in domestic as well as export markets through its long-standing presence in this sector. NOPL is part of Chachan family group which is one of the established business groups in Nepal. The group is involved in various businesses like cement manufacturing, edible oil refinery and import and trading of fertilizers. The company is managed under the overall guidance of its six members Board of Directors (BoD) which includes experienced businessmen/industrialist with wide experience in the food processing and trading sector. Day to day operations of the company is handled by Mr. Nikhil Chachan, who have been director of this company since last six years. The directors of the company are supported by a team of experience professionals in running the day-to-day operations.

Locational advantage for both imports and exports

The plant site is located in Bara District, Nepal around 4 kms from Birgunj dry port. Since most of the raw materials requirements of NOPL are imported from various countries are unloaded on Indian ports, the factory's proximity to the border remains a competitive advantage leading to savings in freight cost. Furthermore, NOPL also exports its products to India which accounted for 44% of total revenue in FY21. The factory's proximity to Indian border remains a positive point with regards to freight cost saving in export of goods.

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

Established distribution network

NOPL sells its products through whole sellers throughout Nepal. The company has sales depot in Itahari and Pokhara whereas main selling activities are done through the Birgunj office. Export to India is majorly in the north-Eastern part of the country in West Bengal, Bihar, Uttar Pradesh, Rajastan and Delhi etc.

Growing scale of operations with improving profitability

NOPL generates its revenue from sale of refined edible oil (sunflower, soyabean, mustard etc). The company had moderate capacity utilization of ~51% in FY21 (FY20:52%). Total revenue of the company increased by ~31% during FY21 to Rs. 10,741 Mn which also had seen growth by 51% during FY20. Revenue during FY21 was increased majorly due to export of soyabean oil to India. Soyabean accounted for 52% of total sales during FY21 out of which export sales comprised 70% of total sales. The company has been able to achieve CAGR growth of around 16% in quantity sold in the last three years ending FY21.

PBILDT margin of the company has been improving on y-o-y basis from 7.62% in FY19 to 15.42% in FY21. The improvement in margins was on account of economies of scale and change in product mix. PAT margin of the company stood at 8.29% in FY20 which increased to 13.09% on back of increase in PBILDT margin which is further support by foreign exchange gain and decline in interest cost. During FY20, the foreign exchange fluctuation loss of the company was Rs. 83 Mn and the company reported the foreign exchange gain of Rs. 30 Mn in FY21. The interest expenses of the company declined to Rs 63 Mn during FY21 from Rs. 80 Mn in FY20 due to company as the company availed foreign currency denomination borrowings which has comparatively low interest rates.

NOPL has achieved sales of Rs. 7,473 Mn in H1FY22 (refer to 6 months period up to Mid-January 2022) and the company has done export of Rs. 4,096 Mn during the said period.

Moderate capital structure and comfortable debt coverage indicators

The company has mainly borrowings in the form of working capital loans. The capital structure of the company was moderate as reflected by overall gearing ratio of 2.38x at the end of FY21 which improved from 3.04x over previous balance sheet date. Despite increase in working capital loans from Rs. 2,289 Mn at the end of FY20 to Rs. 4,323 Mn at the end of FY21, there was improvement in overall gearing which was mainly attributed to accretion of profit leading to increase in net-worth base

Interest coverage ratio of the company was comfortable at 26.47x in FY21 which is also showing positive trend over previous year. This improvement in interest coverage ratio was due to growth in PBILDT of the company coupled with decline in interest cost. Also, as a result of increased GCA of Rs. 1,461 Mn during FY21, total debt/GCA improved to 2.96x during FY21 from 3.17x in FY20.

Essential part of cooking leading to stable demand

The demand prospect of oil industry is growing as oil is one of essential commodity for cooking. Further, with demand being higher than domestic production and slowdown in domestic agriculture production, large volume of edible as well as crude oil is being imported in Nepal giving importers like NOPL a favorable business environment. Nepal has seen a steady growth in import of crude and refined edible oil over the years as per data published in annual foreign trade statistics by Customs Nepal.

Key Rating Weaknesses

Working capital intensive nature of business

The operations of the company are working capital intensive in nature as the company imports its raw material from various countries through Letter of Credit. NOPL has to keep the inventory for smooth operations and extend credit to their customers, which lead to reliance on working capital limits. Company generally allows 1.5 to 2 months credit period to its customers; debtors turnover days was 50 days during FY21 (FY20:52 days). The company keeps inventory for around 1 months and the inventory turnover was 29 days for FY21 (FY20:23 days). Further, the average credit period allowed to the company during FY21 was at 7 days (FY20:9 days). Total operating cycle of the company was 72 days in FY21 which slightly elongated from 66 days in FY20 as a result of higher inventory holding period. The working capital intensity of the business had led to high reliance of the company on the bank finance for working capital requirements.

Raw material price volatility risk and foreign exchange fluctuation risk

Crude soyabean, palmolein, sunflower oil and crude palm oil are the major raw materials for NOPL which are imported from various countries. The prices of the NOPL's raw materials are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. The raw material cost contributed around 83% of the total operating income of the company during FY21. Thus, any volatility in prices of the same impacts the profitability of the company.

The business operations of NOPL involve both imports and exports resulting in sales realization and cash outflow in foreign currency, thereby exposing to volatility in foreign exchange rates. The company doesn't have any policy to hedge its foreign currency risk. However, being importer and exporter, the foreign currency risk is partially mitigated through a natural hedge.

Susceptibility to price fluctuation of seasonal agro products

NOPL is engaged in import and processing of crude oils into refined soyabean oil, sunflower oil and palmolein oil. Prices of crude oils are highly volatile in nature and being agro products are seasonal in nature with production and prices dependent on various factors like area under production, yield for the year, demand supply scenario and inventory carry forward of last year. Furthermore, the supply is dependent upon monsoon during the particular year as well as overall climatic condition, exposing the fate of the company's operation to vagaries of nature.

Fragmented and competitive nature of industry

Import and processing/refining of edible oils is highly fragmented due to presence of several organized/ unorganized players owing to low entry barrier and low technology and capital requirement. Low product differentiation of NOPL's product results in high competition from other players including traders. Considering the fragmented and competitive nature of industry, the millers have low pricing power.

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.

Exposure to regulatory risk

NOPL is partially constrained by regulatory risk arising from various laws and policies from both Nepal and India. The business of BVOPL is primarily dependent on imported crude edible oil and exporting the same to India. Over past few years, there has been in regular/frequent changes in government policies, either domestic or international. Company's revenue is highly susceptible to regulatory policies relating to tariff barriers (differential trade tariffs among South Asian Free Trade Area), non-tariffs barriers (restriction on the quality of imports), international freight rates etc. Any unfavorable change in policy could impact the financial profiles of entities operating in the importing of crude edible oil and exporting to India. Government on India has reduced custom duty multiple times on edible oil in last 6 months ending March 2022 which might have negative impact on the edible oil refiners in Nepal and exporting to India.

About the Company

Narayani Oil Refinery Udhyog Private Limited (NOPL) is a private limited company incorporated on September 20, 1989 for processing/refining of edible oils, having plant in Lipanimal, Bara District, Nepal. The company has been in operation for more than 30 years. Currently, the total installed capacity for refined soyabean, palmolein, vegetable oil, mustard oil, sunflower oil and palm oil is 117,000 MTPA. NOPL sells these edible oils under the brand names of "Trishakti", "Smile", "Aarogya", "Shree" "Neelmani", "Kundan" and "Nilkamal" in the domestic market.

Financial Performance

(Rs. in Mn)

Particulars	FY19	FY20	FY21
	Audited	Audited	Audited
Income from Operations	5,403	8,169	10,741
PBILDT Margin (%)	7.62	13.30	15.42
Overall Gearing (times)	7.54	3.04	2.38
Interest coverage (times)	2.97	13.60	26.47
Current Ratio (times)	1.03	1.17	1.30
Total Debt/Gross Cash Accruals (times)	11.14	3.17	2.96

Annexure-1: Details of Instruments/Facilities

Name of the Instrument	Type of the Facility	Amount (Rs. Million)	Rating
Short Term Bank Facilities	**Working Capital Loan**	**5,210.00**	**CARE-NP A3**
Total Facilities		**5,210.00**	

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