Maruti Cements Limited

Ratings

Facilities	Amount (Rs. Million)	Rating[1]	Rating Action
Long Term Bank Facilities	4,486.07 (Decreased from 4,630.82)	**CARE-NP A- [Single A Minus]**	**Reaffirmed**
Short Term Bank Facilities- Fund based and non-fund based limits	1,070.48	**CARE-NP A2+ [A Two Plus]**	**Reaffirmed**
Total	**5,556.55**		

Annexure-1 Details of Facilities/Instruments to be rated

CARE Ratings Nepal Limited (CRNL) has reaffirmed rating of 'CARE-NP A-' assigned to the long term bank facilities and 'CARE-NP A2+' assigned to the short term bank facilities of Maruti Cements Limited (MCL).

Detailed Rationale & Key Rating Drivers

The reaffirmation of ratings assigned to the bank facilities of MCL continue to factor in strength from the established track record of operations and brand presence of the company along with comfortably leveraged capital structure and debt service coverage indicators. The ratings also consider the competitive advantage MCL has over standalone grinding units by having its own captive clinker unit, locational advantage of the manufacturing facilities, accessibility to limestone mines and stable demand outlook for cement products in the country over the medium-term. Additionally, the ratings also take cognizance of rebound in financial performance of the company in FY21 (audited, refers to the twelve-month period ended mid-July, 2021) marked by growth in revenue and improving profitability, albeit some moderation in FY22.

The ratings are however, constrained by implementation and stabilization risk associated with large-size ongoing capex, foreign exchange fluctuation risk and raw material price volatility risk. The ratings also factor in working capital intensive nature of business, although low reliance on bank finance, exposure to volatile interest rates and presence in highly competitive market and cyclical nature of the cement industry.

Going forward, timely completion of the ongoing project within the cost estimates, satisfactory operations thereafter leading to capacity utilizations to generate sufficient cash-flows as envisaged will be the key rating sensitivity. Furthermore, the company's ability to maintain a healthy profitability profile by absorbing vulnerability in prices in an increasingly competitive industry and its ability to sustain gearing levels and debt coverage indicators at current levels will also remain the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Established track record of operations and experienced promoters in manufacturing industries including cement

MCL has an operational track record of more than 12 years in cement manufacturing under the new management. MCL is managed by industrialists and traders of Nepal, belonging to the Rathi group and Goyal group of companies, who are involved in diversified business activities. 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. Nand Kishore Rathi is the Chairman and Mr. Sunil Khemka is the Managing Director of the Company.

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

Competitive advantage over the standalone grinding units

MCL currently has mining license of one mine, located in Jhanki Khola (Katari) with estimated limestone deposit of ~ 140 Million ton which is sufficient to run 3,300 MTPD clinker unit (enhanced capacity) for more than 3 decades. Now, Nepal is manufacturing its own clinker and dependence upon the import of the clinker has reduced substantially over the period. Clinker manufacturing units generally have added cost competitive advantage over standalone grinding units. Having both clinker and grinding units, licensed limestone mines and enhanced capacity augurs well for the business prospects of the company over the medium term.

Locational advantage of the project site and accessibility to Limestone mines

The plant site is well connected to East-West Highway and with major cities and town nearby. Furthermore, the mines are located close to the clinker and grinding unit (~ 50 Km) which reduces logistics cost. Also, the plant is located in the eastern part of the country where presence of other clinker based cement manufacturing companies is limited.

Established brand presence and strong market position with product diversification plans

MCL sells its product all over Nepal with primary focus towards eastern part of Nepal, with main market being Narayanghat to Kakarbhitta and to north of Narayanghat with a network of around 200 dealers. The company's established brand presence and strong market position has supported the company to sustain competition induced volatility in prices over the years. Further, MCL is currently producing only OPC cement under the brand name "Maruti". The company plans to produce PPC after the expansion of the facilities to diversify its product range.

Satisfactory financial risk profile marked by comfortably leveraged capital structure with adequate debt service coverage indicators, albeit some moderation likely in FY22 amid sluggish sales

MCL's Total Operating Income (TOI) increased by 21.90% year on year to Rs. 6,864 Mn during FY21 mainly on account of rebound in demand despite decrease in average price realization amid increasing competition. PBILDT margin of the company improved to 22.29% in FY21 from 21.98% in FY20, with benefit on account of economies of scale offset to some extent by lower price realization. Similarly, absolute PBILDT increased by 23.65% to Rs. 1,530 Mn and net profits increased by 36.34% to Rs. 977 Mn in FY21 with margin of 14.23%. Operational performance is likely to moderate in FY22 on account of disrupted production amid quality checks from government of Nepal leading to lower sales. This has since been resolved and operational performance is likely to improve going forward amid uninterrupted production. During 9MFY22 (Unaudited, refers to the nine-month period ended mid-April 2022), the company achieved sales of Rs. 2,265 Mn.

The credit profile of the company remains robust indicated by low Debt to Equity and overall gearing ratio of 0.27x and 0.35x respectively at the end of FY21 and remained almost stable over previous balance sheet date. The working capital utilization of the company is at moderate level aided by sustained cash accruals from operations. Similarly, debt service coverage indicators also stood comfortable with interest coverage ratio of 13.45x and Total debt to GCA of 1.69x in FY21.

Stable demand outlook for cement products in the country

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. Furthermore, the government's high emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures as included in the budget for FY23 is likely to benefit the cement manufacturers like MCL.

Key Rating Weakness

Project implement and stabilization associated with debt-funded expansion

MCL is currently undertaking a capacity expansion project to increase clinker capacity from 1,500 MTPD to 3,300 MTPD and grinding capacity from 2,000 MTPD to 4,000 MTPD. The estimated cost of the project is Rs. 5,622 Mn, which is being funded by debt of Rs. 3,935 Million and remaining through internal accruals of the company. The debt equity ratio for the expansion project is 70:30. Expected COD has been revised to mid-October 2022 from March 2022 as the construction work was disrupted due to COVID. Though the capital expansion will increase the company's installed capacity, the company however remains susceptible to risk related with residual project implementation and swift stabilization thereafter. Any delays in the implementation may impact the company's financial risk profile adversely. Despite majorly debt-funded capex, the company's overall gearing level is likely to remain at satisfactory levels, supported by a strong net worth base. The successful execution of the expansion project within cost and time estimates and early stabilization thereafter will be crucial for the company for generation of incremental revenue and key monitorable from credit perspective.

Working capital intensive nature of business, although low reliance on bank finance

The operations of the company are working capital intensive in nature as it is involved in manufacturing of cement by procuring raw materials both domestically and imports. The company has to make advance payments for the raw materials, maintain inventory for smooth operations and extend credit to dealers, which leads to reliance on working capital limits. MCL generally allows two months credit period to its dealers and maintains inventory for around 4 months. The company also needs to maintain huge stock of limestone as access to mine is through seasonal road which is accessible for only six months. This led to high operating cycle of 211 days in FY21. However, MCL has sizeable unutilized working capital limits in the last 11 months ended in mid-June 2022, which provides financial flexibility given the increasing working capital intensity.

Foreign exchange fluctuation risk and raw material price volatility risk

MCL currently uses coal, limestone, bauxite, gypsum, clay and iron ore as major raw materials. Coal constitutes around 60% of raw materials consumption during clinker production and the coal requirements are met through import from South Africa and other countries. Invoicing of the imported coal is done in USD which exposes MCL to foreign exchange fluctuation risk. MCL has not taken any hedging mechanism to minimize the risk associated with fluctuation in foreign currency. Raw material cost continues to be the major cost component of MCL as direct material cost constitutes around 50% of total cost of goods sold in FY21. 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 adverse changes in raw material prices to the customers and managing the foreign exchange fluctuation risks related to raw materials will be the key rating sensitivities.

Presence in highly competitive and cyclical nature of cement industry

MCL is operating in a highly competitive market, dominated by the large cement manufactures 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 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 as seen in decline in price of cement and clinker during last three years.

Exposure to volatile interest rate risk

Nepalese banking sector has a floating interest rate regime, where a certain premium is added to the quarterly base rate and interest rate is changed accordingly on quarterly basis. The base rates of the banks and financial institutions (BFIs) in Nepal remain quite volatile as they are impacted by available liquidity in the system which leads to change in interest rates. The volatility in interest rate is more evident currently on account of the ongoing liquidity stress in the economy. Furthermore, increased bank rates announced in the Monetary Policy for FY23 is likely to add to the upward pressure on interest rates going forward. Any significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Therefore, funding taken by the company from BFIs is subject to volatile interest rate.

About the Company

Maruti Cement Limited (MCL) was incorporated on October 31, 1994 and the current management took over the company in 2005. MCL is managed by industrialists and traders of Nepal, belonging to the Rathi group and Goyal group of companies and all the shares of the company are held by the promoters. The company is presently engaged in manufacturing and selling cement with clinker capacity of 1500 MTPD and grinding capacity of 2000 MTPD respectively. The manufacturing facilities are located in Mirchaiya, Siraha District of Nepal. Brief financials of MCL for last three years ending FY21 are given below:

(Rs. in Million)

Particulars	FY19	FY20	FY21
	Audited	Audited	Audited
Income from Operations	7,504	5,631	6,864
PBILDT Margin	22.49	21.98	22.29
Overall Gearing (times)	0.38	0.36	0.35
Interest coverage (times)	9.99	8.83	13.45
Current ratio (times)	1.34	2.06	1.33
Total Debt/GCA	1.21	1.76	1.69

Annexure-1 Details of Facilities/Instruments to be rated

Name of Instrument	Type of Facility	Amount(Rs in Million)	Rating
Long Term Bank Facilities	Term Loan	4,486.07	CARE-NP A-
Short Term Bank Facilities	Working Capital Loans	678.48	CARE-NP A2+
Short Term Bank Facilities	Non–Fund Based Loans	392.00	CARE-NP A2+
Total		**5,556.55**	

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About CARE Ratings:

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