Samrat Cement Company Private Limited

Ratings

Facility	Amount (Rs. in Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	10,154.77 (Increased from 8,722.09)	CARE-NP BB+ [Double B Plus]	Reaffirmed
Short Term Bank Facilities	2,490.98 (Decreased from Rs. 2,718.99)	CARE-NP A4+ [A Four Plus]	Reaffirmed
Total Facilities	12,645.75 (Twelve Billion Six Hundred Forty-Five Million and Seven Hundred Fifty Thousand Only)		

Details of Facilities in Annexure 1

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

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SCPL continue to remain constrained by its highly leveraged capital structure with modest debt service coverage indicators, raw material price volatility risk, working capital intensive nature of operations and presence in highly competitive nature of cement industry. Although the ratings also take cognizance of the commencement of operations of additional grinding unit in July 2022, the company's ability to achieve capacity utilizations at envisaged levels for a sustained period remains to be seen, particularly amid the sluggish demand scenario over the near-term and other industry headwinds currently faced by the cement industry.

The ratings, however, continue to derive strengths from experienced promoters, increase in scale of operations with moderate profitability in FY22 (Audited, FY refers to the twelve-month period ending mid-July), and competitive advantage over the standalone grinding units. The ratings further derive strength from locational advantage of the project site, accessibility to limestone mines, established brand presence and stable demand outlook for cement products in the country over the medium-term.

Going forward, the ability of the company to profitably scale up its operations along with rationalization of its debt levels would be the key rating sensitivities. Furthermore, stabilization of the expansion project with capacity utilization levels thereafter to generate sufficient cash flows as envisaged will be the key rating sensitivity.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Leveraged capital structure at the end of FY22 on account of large size debt funded capex

The capital structure of the company remained leveraged with overall gearing ratio of 3.93x at the end of FY22 (FY21: 3.98x) owing to high debt levels pertaining to the series of majorly debt-funded capacity expansions undertaken by the company over FY21-FY22. The total debt of the company stood at Rs. 11,616 Mn at the end of FY22, increasing from Rs. 10,920 Mn at the end of FY21. Debt to Equity ratio deteriorated to 3.43x at the end of FY22 from 3.11x at the end of FY21 amid higher long-term loans. High overall debt led to modest debt service coverage indicators of the company with interest coverage ratio and total debt to Gross Cash Accruals of 1.48x and 36.93x respectively during FY21 (FY20: 2.09x and 21.27x).

Although the company's major capex has been completed during FY22, its capital structure is likely to remain leveraged over the near-term with sequential improvement likely with repayments of the term loans coupled with accretion of profits to reserve. However, this hinges on the company's ability to achieve capacity utilization at envisaged levels, which will remain challenging in the current industry dynamics. Higher input prices emanating from increased power cost as well as continued pricing pressure from large new entrants and other established market players is likely to suppress profitability margins. The company's ability to achieve sales and profitability as envisaged will remain critical for its business prospects and will remain a key monitorable from credit perspective.

Project stabilization risk associated with its very large-size capex

SCPL has undertaken a brownfield expansion project to increase the installed capacity of grinding unit to 3,600 MTPD from 1,800 MTPD. The enhanced grinding unit came into operations on July 17, 2022. The company has also backward integrated its manufacturing facility by setting up a 4,000 MTPD clinker unit, which came into operations on January 14, 2021. The earlier estimated project cost for the clinker unit and the additional grinding unit was Rs. 10,132 Mn. However, the total cost of the capex increased to Rs. 13,128 Mn amid increased machinery prices, time-overrun and also on account of certain change in scope of the capex. The company has invested around Rs. 1,000 Mn in a waste heat recovery plant, which was out of scope during initial budget. With modest capacity utilizations in initial months of operations, the company remains susceptible to risk related to stabilization and streamlining of production process from the enhanced capacity.

Raw material price volatility risk

SCPL currently uses coal, fly ash, gypsum, clay, bauxite and iron ore as major raw materials. Coal constituted around 65-70% 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 price of coal. 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 constituted around 78% of the total sales in FY22 (FY21: around 70%). Company imported the majority of coal from South Africa, Australia and India during FY22, while the final products are sold completely 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 needs to maintain inventory for smooth operations and extend credit to their dealers, which leads to reliance on bank borrowings on working capital requirements. The company generally allows two to three months of credit period for its cement sale to its customers and maintains inventory of raw materials for around one and a half months. All this leads to high working capital requirements and are met largely through bank borrowings which resulted in a high average utilization. The average month-end working capital utilization of the company against the sanction limit was around 92% during last 12 months period ended mid-October 2022.

Presence in highly competitive nature of cement industry

SCPL 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.

Key Rating Strengths

Experienced promoters in the related field

SCPL is managed under the overall guidance of its five-member Board of Directors (BoD) comprised of individuals who possess wide experience in the related field. The two directors, Mr. Nirvana Chaudhary and Mr. Barun Chaudhary are from Chaudhary Group (CG). CG 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 terms of technical and financial assistance. Mr. Anil Kumar Rungta, Chairman, has more than 25 years of experience in different sector like cement, iron, wire etc. Mr. Bashudev Pandeya, Managing Director, has more than two decades of experience in the field of coal mining, bricks industry, rice mills and trading of grain items and has 5 years of experience as Executive Director of Sonapur Cement Private Limited.

Increasing scale of operations with moderate profitability in FY22

SCPL reported increase in total operating income by 32% to Rs. 4,875 Mn during FY22 as compared to Rs. 3,704 Mn in FY21. The increase in total revenue in FY21 was on account of increase in quantity sold of clinker. This increase in quantity sold was partially offset by lower average price realization of the clinker to Rs. 7,188 per MT in FY22 from Rs. 7,766 per MT from FY21 due to increased competition in cement industry and company giving additional trade discounts in order to boost up the sales. Similarly, average price realization of cement declined to Rs. 442 in FY22 from Rs. 472 in FY21. PBILDT margin decreased to ~20% during FY22 from ~27% in FY21 owing to increased cost of raw materials. Further, SCPL reported sales revenue of ~Rs. 600 Mn during Q1FY23 (quarter ended mid-October 2022).

Established Brand Presence and locational advantages

SCPL manufactures PPC cement (used for brick masonry, plastering, tiling and waterproofing works) and OPC cement (used for reinforced concrete structures). SCPL sells its products 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.

The company's manufacturing facility is located in the mid-western part of Nepal nearby the big cities like Ghorahi, Tulsipur, Kohalpur, Dhangadi, Nepalgunj, Butwal and Bhairahawa, which are major local market for the SCPL's product. One of the limestone mines is located at a distance of 50 km from the plant site which eases the extraction / transportation of limestone from the mines. Clinker manufacturing units generally have added cost competitive advantage over standalone grinding units. Having both clinker and grinding units, three licensed limestone mines and enhanced capacity augurs well for the business prospects of the company over the medium term.

Stable demand outlook for cement products in the country over medium term

Nepalese economy is developing and growing, and is in phase of investment in infrastructure sectors, power sector and tourism sector. Despite the seemingly underwhelming pace of economic activity over the last 12-18 months, 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 over the medium-term. 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 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 with an installed capacity of 3,600 MTPD, expanded from 1,800 MTPD on July 17, 2022. 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.

(Rs. Million)

For the year ended Mid-July	FY20 (Audited)	FY21 (Audited)	FY22 (Unaudited)
Income from Operations	2,113	3,704	4,875
PBILDT Margin (%)	11.31	26.79	19.97
Overall Gearing (times)	3.61	3.98	3.93
Interest Coverage (times)	2.12	2.09	1.48
Current Ratio (times)	1.17	1.09	0.79
Total Debt/Gross Cash Accruals (times)	66.54	21.27	36.93

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Long Term Bank Facilities	Term Loan	10,154.77	CARE-NP BB+
Short Term Bank Facilities	Fund Based Limit	2,490.98	CARE-NP A4+
Total		**12,645.75**	

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