

United Distributors (Nepal) Private Limited (Revised)

Ratings

Facility	Amount (Rs. In Million)	Rating ¹	Rating Action
Short Term Bank Facilities	7,120.00	CARE-NP A2 [A Two]	Reaffirmed
Total Facilities	7,120.00		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has reaffirmed the rating of 'CARE-NP A2' assigned to the short term bank facilities of United Distributors (Nepal) Private Limited (UDN).

Detailed Rationale & Key Rating Drivers

The reaffirmation of the rating assigned to the bank facilities of UDN continues to derive strength from established track record of operations along with strong promoters and experienced management team, diversified distribution network and association with established brands, and adequate liquidity profile supported by liquid investments in listed shares. The rating also factors in sustained growth in scale of operations with satisfactory profitability margins, comfortable capital structure with improving debt service coverage indicators. The rating, however, remains constrained by UDN's elongated operating cycle, exposure to foreign exchange fluctuation risk and volatile interest rate risk, competitive nature of industry with presence of both domestic and international players, and exposure to regulatory risks.

Going forward, ability of the company to continue scaling up its operations while maintaining its financial risk profile will remain the key rating sensitivities. Any substantial increase in debt levels and investments will be a key monitorable aspect.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Established track record of operations along with strong promoters and experienced management team

UDN has an operational track record of almost two decades in import and trading of fast moving consumer goods (FMCG) in Nepal. UDN derives strength from its strong promoters, being part of the Vishal Group of Companies which has a strong presence in Nepal through various group entities engaged in trade, manufacturing, hospitality, insurance and banking. Mr. Anuj Agrawal, Chairman, has more than two decades of experience in FMCG business. He is also the chairman of Nepal Infrastructure Bank Limited and honorary vice president of Confederation of Nepalese Industries (CNI). Mr. Vivek Agrawal, Managing Director, has more than 10 years of experience in FMCG business. The board is aptly supported by a team of qualified and experienced members.

Diversified distribution network and association with established brands

Currently UDN operates its business within the territory of Nepal through three locations in Bara, Parsa, and Kathmandu. With more than 650 dealers, UDN has countrywide presence covering all the districts of Nepal. UDN has diverse customer base with top ten customers contributing around 14% of the total sales during FY21 (Audited, refers to the twelve-month period ended mid-July 2021). The company is sole importer and distributor of some of the leading global FMCG companies with well-established brand presence such as Procter & Gamble, GlaxoSmithKline, Britannia Industries, Gujarat Co-operative Milk Marketing, etc. Association with strong brands ensures customer loyalty and aids in the differentiation of products with the competitors.

Satisfactory financial risk profile

The financial risk profile of the UDN is satisfactory marked by sustained growth in scale of operations with comfortable profitability margins and capital structure with improving debt service coverage indicators in FY21.

Total operating income of the company increased by 26% year on year (yoy) to Rs. 12,231 Mn during FY21 boosted by increased sales volume aided by continuously increasing customer base coupled with sustained demand for UDN's traded products. During FY21, PBILDT and PAT increased which were supported by growth in total operating income. PBLIDT margin was around 11% in the last two fiscal years (FY20 & FY21). During H1FY22 (Unaudited, refers to the six-months period ended mid-January 2022), the company reported total sales of Rs. 7,266 Mn.

The capital structure of the company stood comfortable marked by overall gearing ratio of 0.64x at the end of FY21, improved from 1.45x at the end of FY20 on account of accretion of the profits to the net worth and lower working capital loan utilization amidst shortened operating cycle during FY21. At the end of H1FY22, however, overall gearing ratio moderated to 0.97x on account of higher working capital borrowings amid growing operations.

Apart from overall gearing, other debt coverage indicators including total debt to GCA and interest coverage ratios for the company also showed improvement in FY21. The interest coverage ratio of the company stood comfortable at above 3x during FY20 and FY21. Similarly, total debt/ GCA improved to 2.50x during FY21 from 5.99x in FY20 on account of reduced total debt coupled with increased gross cash accruals. The average working capital utilization against the drawing power of the company during the last twelve-month period ended mid-February 2022 was moderate at approximately 70%.

Liquidity profile supported by liquid investments in listed shares

UDN had an investment portfolio of Rs. 1,401 Mn at the end of FY21 based on fair market value. Most of the investments (over 90%) are in shares of different listed banks and financial institutions, insurance companies etc. which are readily marketable in nature, providing additional cushion to the company at the time of any liquidity stress that may arise in the future.

Key Rating Weaknesses**Elongated operating cycle**

The company has an elongated operating cycle marked by an average operating cycle of around 101 days during FY21, primarily on account of the high collection period, moderate inventory period and lower creditor days. Being a highly competitive business, the average collection period remained high at around 69 days during FY21. The company imports most of the traded products and is required to maintain adequate inventory in order to avoid any stock-outs. Inventory holding period was around 43 days in FY21. Furthermore, the company received a payable period of upto 45 days from its suppliers and average payable period stood at 20 days for FY21. Combining all these factors entails to an elongated operating cycle for the company, which leads to increased dependence on bank borrowings to meet working capital requirements. However, despite increasing scale of operations, the company has been able to rationalize its working capital needs through more efficient management and hence operating cycle had reduced in FY21 from around 130 days in FY20 resulting in decreased utilization of the working capital limits during FY21. The company's ability to efficiently manage working capital cycle leading to lower dependence on borrowings will add favorably to its profitability profile.

Exposure to volatile interest rate risk and foreign exchange fluctuation 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, with

substantial upward pressure on interest rates in the last 2-3 quarters. Any further 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. Furthermore, a substantial portion of purchases (around 30% in FY21) are invoiced in foreign currency other than Nepalese and Indian Rupees for which the company is exposed to the fluctuation in foreign exchange rates.

Competitive nature of industry with presence of both domestic and international players

UDN is involved in import/ trading of FMCGs from various countries and selling in domestic market. UDN operates in a fragmented industry where it competes with various local players as well as several international players who are into the business of importing similar products and selling domestically.

Exposure to regulatory risks

Trading of imported FMCG products in Nepal is exposed to regulatory risks due to change in government policy towards import of certain items and also its custom duty. Recently, the Government of Nepal (GoN) imposed restriction in import of certain non-essential items in April 2022 aimed at limiting outflow of foreign reserves. Furthermore, GoN also has issued similar orders in the past to restrict imports of certain products such as synthetic energy drinks, as well as to increase / reduce duties on imports. Therefore, the company remains exposed to unfavorable changes in the government policy towards imports, however, it may be partially insulated as the products the company deals with are high value branded and quality products of which replacement may not be easily available.

About the Company

United Distributors (Nepal) Private Limited (UDN) was registered as a private limited company in April 2003. Having its registered office at Kathmandu-22, Khichapokhari, UDN is involved in import/trading of FMCGs. Currently, UDN is the distributor of more than 1,350 varieties of products manufactured by 12 FMCG companies around the globe under more than 70 brands, for the most of which UDN is the sole distributor in Nepal.

Brief financials of UDN are given below:

(Rs. Million)

For the year ended Mid-July	FY19 (Audited)	FY20 (Audited)	FY21 (Audited)
Income from Operations	9,334	9,736	12,231
PBILDT Margin (%)	8.77	10.61	11.68
Overall Gearing (times)	2.00	1.58	0.64
Interest Coverage (times)	2.49	3.23	7.83
Current Ratio (times)	1.10	1.13	1.40
Total Debt/Gross Cash Accruals (times)	8.85	5.99	2.50

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Short Term Bank Facilities	Working Capital Loans	3,230.00	CARE-NP A2
Short Term Bank Facilities	Non-Fund Based Loans	3,890.00	CARE-NP A2
Total		7,120.00	

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