Shiva Shikhar Agro Private Limited

Ratings

Facilities/Instrument	Amount (Rs. in Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	155.40	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	1,294.60	CARE-NP A4 [A Four]	Assigned
Total Facilities	1,450.00 (One Thousand Four Hundred and Fifty Million Only)		

** Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BB' to the long term bank facilities and 'CARE-NP A4' to the short term bank facilities of Shiva Shikhar Agro Private Limited (SSAPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SSAPL are constrained by its working capital intensive nature of business leading to reliance on bank borrowings to meet working capital requirements, low profitability margins and moderately leveraged capital structure. The ratings also factor in susceptibility to price fluctuation of seasonal agro products, fragmented and competitive nature of industry, high reliance on import and foreign exchange fluctuation risk on such import, and exposure to volatile interest rates.

The ratings, however, derive strengths from SSAPL's experienced promoters and management team in manufacturing and trading business, growing scale of operations. The ratings also factor in stable demand outlook of agro industry over the medium term and established marketing and distribution setup with own brand and locational advantage.

Going forward, the ability of the company sustain growth in operations while improving profitability margins and rationalize working capital requirements leading to improved coverage and solvency indicators would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Working capital intensive nature of business leading to reliance on bank borrowings

The operations of SSAPL are working capital intensive in nature due to high volume procurement of agro products through imports. Due to seasonal nature of raw materials, SSAPL has to keep enough inventory for smooth operations. In addition, the company needs to extend credit to their customers, leading to reliance on working capital borrowings. During FY22 (Unaudited; FY refers to the twelve-months period ending mid-July), the average collection period was 69 days, average inventory period was 67 days and average creditor period was 69 days, which led to an operating cycle of 67 days. This has led to reliance of the company on bank borrowings to fund its working capital requirements, resulting in average utilization of sanctioned working capital limits at over 90%. The ability of SSAPL to efficiently manage working capital requirements leading to lesser dependence on borrowings would be critical from credit perspective.

Moderate capital structure and debt coverage indicators

The capital structure of the company stood moderately leveraged at 1.71x at the end of FY22 (FY21: 1.87X). SSAPL improved its net worth to Rs. 326 Mn at the end of FY22 from Rs. 314 Mn at the end of FY21 (Audited) supported by accretion of

[1]Complete definitions of the ratings assigned are available at www.careratingsnepal.com and in other CRNL publications.

profits to the net worth. However, interest coverage ratio of the company was moderate at 1.92x during FY22 (FY21: 1.70x). Furthermore, amid relatively modest profitability, the total debt/GCA of the company stood high at 20.83x at the end of FY22 which however improved from 23.63x during FY21 on account of repayment of loan.

Susceptibility to price fluctuation of seasonal products

SSAPL is engaged in trading of different agro products as rice, lentils, beans and flour. As majority of sales (~75% of total sales) involves agro products, production is generally dependent on timing and intensity of the monsoon. Prices are highly volatile in nature, as their production and prices depend upon various factors like area under production, yield for the year, demand-supply scenario and inventory carry forward of last year. Furthermore, the supply is also dependent upon availability of seed, impacts of pests, as well as overall climatic condition during the year, exposing the fate of the company's operations to vagaries of nature.

Fragmented and competitive nature of industry

Import and processing of agro products is highly fragmented due to presence of several organized/ unorganized players owing to low entry barrier and low technology and capital requirement. Considering the fragmented and competitive nature of industry, small and medium sized traders have low pricing power over its products in the market. The pricing is mainly market driven and any such market price lower than the cost of procurement of product to SSAPL will hit the profitability of the company.

High reliance on import and foreign exchange fluctuation risk on such imports

SSAPL's business operations are dependent on imports as domestic production is not sufficient to fulfill the demand. As significant purchases (~50%) are made in the form of imports, the company is exposed to unfavorable changes in the government policy towards imports and also from the exporting countries. The company imports majorly from India, Canada, Turkey and Argentina through LC. With initial cash outlay for procurement in foreign currency and significant chunk of sales realization in domestic currency, the company's profitability margins are also exposed to volatility in foreign exchange.

Exposure to volatile interest rate

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 few quarters. A contractionary monetary policy for FY23 coupled with increasing inflation has only added to the upward pressure on interest rates, resulting in increased base rates of BFIs in the first half of FY23. 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.

Key Rating Strengths

Experienced promoters and management team in related business

SSAPL derives strength from its promoter group belonging to Shikhar Organization which has established presence in manufacturing and trading of Fast-Moving Consumer Goods (FMCG) products in Nepal. The group has presence in diversified businesses and is involved in trading/manufacturing products such as food, agro machinery, water pumps, sweets & and other FMCG products. The overall operations of the company is managed by Mr. Kedarnath Sharma, Chairman, who has experience of over 27 years in manufacturing and trading business. He is also chairman at Natraj Agro Private Limited (CARE-NP BB) and Garden Mart Private Limited (CARE-NP BB-). He is further supported by experienced management team.

Growing scale of operations albeit low profitability margins

SSAPL generates its revenue from sale of rice, lentils, beans, flour, tea, confectionery and agro machineries. The company's Total Operating Income (TOI) has been growing on y-o-y basis. During FY22, TOI increased by 8.05% to Rs. 2,462 Mn from Rs. 2,278 Mn during FY21 supported by increased demand for its products, majorly rice, supported by improving distribution network and increasing brand acceptance. However, operating profitability of the company has been modest over the years with PBILDT margin of 2.93% in FY22 (FY21: 2.74%) owing to thin scope for margin accretion in the products dealt by the company. Consequently, the company has been reporting modest net profits vis-a vis scale of operations (FY22: Rs. 11 Mn; FY21: Rs. 7 Mn). The scale of operations is likely to grow steadily over the medium term amid stable demand outlook. However, the company's credit profile would more hinge on its ability to improve profitability margins, which remains a challenge particularly given the increasingly competitive industry and will remain a key monitorable aspect.

Established marketing setup with own brand and locational advantage

SSAPL sells its products all over Nepal and has a customer base spread across all major cities in the country. The company sells its products under the brand name 'Upakar' which is an established brand name in Nepalese market, also well-known name in other products of their subsidiary companies for over a decade. Sales are made through direct marketing to exiting as well as new customer, operating from 16 branches located in different location across Nepal. SSAPL also makes direct selling to department stores. The company's main office and storage facility are located at Kohalpur, close proximity to the Indian border which eases procurement and storage of raw materials. Therefore, SSAPL has been getting locational benefit for import of raw materials at lower transportation cost and fast procurement.

Stable demand outlook of agro industry over medium term

Rice and lentils are a preferred staple food for majority of Nepalese. Rice ranks first among all the cereal crops in terms of acreage area, production and consumption. Furthermore, with demand higher than domestic production and slowdown in domestic agriculture production, large volume of rice and lentils is being imported in Nepal. With growing population, its consumption is also expected to increase, thereby leading to a stable demand outlook over the medium-long term.

About the Company

SSAPL is a private limited company incorporated on July 29, 2013 for trading of rice and other agro products like lentils, sugar, flour, tea, spices and trading of agro machinery like tillers, water pumps, spray pumps, and many other modern types of machinery depending on market demand. The agro foods product are sold in the market under the brand name Upakar. Brief financial performance of SSAPL during last 3 years is given below:

(Rs. In Million)

Particulars	FY20 (A)	FY21 (A)	FY22 (UA)
Income from Operations	2,095	2,278	2,462
PBILDT Margin (%)	3.92	2.74	2.93
Overall Gearing (times)	4.64	1.87	1.71
Interest coverage (times)	2.90	1.70	1.92
Current Ratio (times)	1.06	1.35	1.18
Total Debt/Gross Cash Accruals (times)	13.96	23.63	20.83

A: Audited, UA: Unaudited

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	155.40	CARE-NP BB [Double B]
Short Term Bank Facilities	Fund Based Limit	794.60	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non-Fund Based Limit	500.00	CARE-NP A4 [A Four]
Total		**1,450.00**	

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