

## Vijayshri Steel Private Limited

### Rating

Facility/Instrument	Amount (Rs. in Million)	Ratings <sup>1</sup>	Rating Action
Long Term Bank Facilities	1,160.50 (Increased from 869.83)	CARE-NP BB- [Double B Minus]	Revised from CARE-NP BB
Short Term Bank Facilities	2,900.00 (Decreased from 3,200.00)	CARE-NP A4 [A Four]	Revised from CARE-NP A4+
<b>Total Facilities</b>	<b>4,060.50</b> <b>(Four Billion Sixty Million and Five Hundred Thousand only)</b>		

*Details of Facilities in Annexure 1*

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the long-term bank facilities of Vijayshri Steel Private Limited (VSPL) to 'CARE-NP BB-' from 'CARE-NP BB'. CRNL has also revised the rating assigned to the short-term bank facilities of VSPL to 'CARE-NP A4' from 'CARE-NP A4+'.

### Detailed Rationale & Key Rating Drivers

The revision in the ratings assigned to the bank facilities of VSPL factors in the decline in operational performance of the company in FY22 (Audited, FY refers to the twelve-month period ending mid-July) and H1FY23 (Unaudited, H1 refers to the six-month period ending mid-January) amid sluggish demand leading to suppressed profitability and modest debt service coverage indicators. The ratings continue to be constrained by VSPL's working capital intensive nature of operations, raw material price volatility and foreign exchange fluctuation risk, and presence in highly fragmented and competitive nature of steel industry. The ratings, however, derive strength from the company being a part of an established business group with promoters' experience in cement manufacturing and trading businesses, locational advantage and demand of steel products in the country in the long run, although muted in the near term. The ratings also take cognizance of the company's recently concluded backward integration project of installing a Continuous Casting Machine (CCM) for in-house manufacturing of billets, which became operational in February 20, 2023. However, amid near-term industry headwinds given the slowdown in construction activities in the country, achieving operational benefits from the backward integration as envisaged could be a challenge and remains to be seen.

*Going forward, the ability of the company to profitably scale up its operations with sustained improvement in capacity utilization will be the key rating sensitivities. Also, stabilization of company's newly operational CCM plant and its ability to derive envisaged benefits from the backward integration will also be the key rating sensitivities.*

### Detailed Description of the Key Rating Drivers

#### Key Rating Weaknesses

#### Declined operational and financial performance in FY22 and H1FY23

The total operating income (TOI) of the company declined by 11.79% year-on-year (y-o-y) to Rs. 4,718 Mn in FY22 on account of decrease in sales volume. In FY22, the company sold 47,521 MT of TMT bars, which declined by 32% y-o-y amid low demand. Sales were also impacted, in part, by disruption in production due to installation of the CCM plant during the year. The relatively lower decline in income was on account of increased price realization. The higher price realization was also not enough to offset the increase in input cost. Consequently, PBILDT margin declined to below 2% in FY22. Furthermore, amid substantial rise in interest expenses in FY22, VSPL booked net loss of Rs. 63 Mn with negative gross cash accruals, compared to net profit of Rs 0.31 Mn in FY21.

The operating environment remained impacted during H1FY23 as the company booked total income of around Rs. 894 Mn

<sup>1</sup>Complete definitions of the ratings assigned are available at [www.careratingsnepal.com](http://www.careratingsnepal.com) and in other CRNL publications.

(H1FY22: Rs. 2,505 Mn). The slowdown in economic activities has resulted in lower government revenue collection and therefore lower capital expenditure, which has impacted construction related demand in Nepal. This led to low demand for construction materials, thereby impacting sales performance of steel bar manufacturers like VSPL.

### **Leveraged capital structure and weak debt service coverage indicators**

The capital structure of VSPL remained leveraged, albeit improved to 1.94x at the end of FY22 from 2.81x at the end of FY21, majorly on account of lower utilization of working capital facilities as on mid-July 2022 amid declining sales. The company's short-term debt outstanding decreased to Rs. 1,222 Mn at the end of FY22 from Rs. 1,500 Mn at the end of FY21. VSPL's long term debt increased to Rs. 402 Mn at the end of FY22 from Rs. 309 Mn at the end of FY21 due to the ongoing capex. However, amid higher interest rates, interest expense increased substantially to Rs. 83 Mn in FY22 from Rs. 27 Mn during FY21, which, along with lower PBILDT, led to sharp decline in interest coverage ratio to 1.12x during FY22 from 4.44x during FY21. Total debt to gross cash accruals of the company was negative in FY22, owing to negative cash accruals.

### **Working capital intensive nature of operations**

The operations of the company are working capital intensive marked by low creditor period and high collection period. VSPL is involved in the manufacturing of TMT bars by importing raw materials (sponge iron, pig iron and wire rod) from India through letter of credit, mostly at sight. Average creditor period in FY22 was five days (FY21: Four days), whereas average collection period was 58 days (FY21: 70 days). With average inventory holding period of around twenty days, total operating cycle of the company remained high at 74 days during FY22, although decreased from 96 days in FY21. Elongated operating cycle leads to increased reliance of the company on the bank finance for working capital requirements.

### **Raw material price volatility risk and foreign exchange fluctuation risk**

VSPL imports its major raw materials which are sponge iron and pig iron from India, prices of which are market linked and exposes the company to the volatility in the prices of raw materials, which has a bearing on its profitability margins. Raw material costs accounted for around 94% of the total operating income during FY22. Thus, any volatility in raw material prices impacts the profitability of the company. Also, the company is exposed to foreign exchange fluctuation risk as the raw material prices are linked to USD. VSPL incurred foreign exchange loss of Rs. 36 Mn during FY22 (FY21: Rs. 53 Mn). The ability of the company to pass through changes in raw material prices to the finished products and manage the foreign exchange fluctuation risks related to raw materials will be the key rating sensitivities.

### **Presence in highly fragmented and competitive nature of steel industry**

The iron and steel industry in Nepal is intensely competitive and fragmented marked by presence of both larger players and numerous smaller players in the unorganized segment. The demand for iron & steel products is considered cyclical as it depends upon the capital expenditure plans of major players in the end-user industry. Furthermore, the value addition in the TMT bars and other related products is relatively low, resulting in low product differentiation in the market. Further, with increase in the capacities of the existing plants and new capacities coming into operation, competition has intensified and resulted in lower price realizations and profitability margins.

### **Key Rating Strengths**

#### **Established business group and experienced promoter in cement manufacturing and trading business**

VSPL is promoted by individuals who are associated with Vijaya Group of Companies which has a presence of more than 30 years in Nepal's industrial sector. Currently, the group is involved in importing and manufacturing cement, manufacturing batteries, trading bitumen, and also in agriculture and education sector. Since the group is operating in cement business in the Nepalese market for more than a decade with over 400 dealers, it gives them an advantage of existing distribution channel

for marketing of goods manufactured by VSPL. The company is managed under overall guidance of its Board of Directors, led by Mr. Vikash Kedia, who has industrial experience of more than 19 years.

### Locational advantage

VSPL's manufacturing facility is located at Shivaraj, Kapilvastu which is at a distance of around 11 km from Barhani border, India and around 98 km from Sunauli border, India, which gives the company an advantage of lower transportation cost during raw material procurement. Presently, VSPL is importing raw materials from Barhani border. Furthermore, the plant is situated nearby the East-West Highway of Nepal which provides road access for supply of products to the major markets. With most of the steel factories concentrated in Eastern region of Nepal, VSPL has locational advantage to exploit market opportunities in Central and Western regions.

### Demand of steel products in the country in the long run, however muted in the short term

Demand of steel products in the country is expected to grow in the long term. Nepalese economy is developing and growing, and is in phase of investment in infrastructure sectors, power sector and tourism sector. Sustained demand for steel is likely given the need of construction materials in developing public as well as private infrastructures, road, bridges and other public facilities. Furthermore, the government's continued emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures etc. is likely to benefit the steel manufacturers like VSPL. However, with the construction sector in Nepal impacted by slower pace of economic growth coupled with relatively lower infrastructure spending by the government, the outlook of steel industry in Nepal is challenging in the near term. Also, in the recent budget presented by finance minister of Nepal for FY23, Government of Nepal allocated Rs. 161.56 Bn in the infrastructure sector, which was Rs. 2 Bn less compared to the previous fiscal year. While the government's long term emphasis on infrastructure development, namely development of roads, hydropower, airports and other infrastructures is likely to benefit the TMT bar manufacturers like VSPL in the long term, the demand for steel is expected to be muted in the short term.

### About the Company

VSPL is a private limited company, incorporated on February 23, 2017 to set up a TMT bar manufacturing plant in Kapilvastu district of Nepal. The company has rolling mill with production capacity of 700 Metric Ton Per Day (MTPD) to manufacture TMT bars and CCM plant with installed capacity of 400 MTPD to manufacture billets. The plant started commercial operation of its rolling mill on November 25, 2018 and its CCM plant was operational since February 20, 2023.

Brief financials of VSPL for the past three years are given below:

(Rs. Million)

For the year ended Mid-July	FY20 (Audited)	FY21 (Audited)	FY22 (Audited)
Income from Operations	3,954	5,349	4,718
PBILDT Margin (%)	4.59	2.28	1.97
Overall Gearing (times)	4.73	2.81	1.94
Interest Coverage (times)	1.89	4.44	1.12
Current Ratio (times)	0.98	0.93	0.80
Total Debt/Gross Cash Accruals (times)	68.52	44.62	Negative

### 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	1,160.50	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund Based Limit	1,900.00	CARE-NP A4 [A Four]
Short Term Bank Facilities	Non-Fund Based Limit	1,000.00	CARE-NP A4 [A Four]
<b>Total</b>		<b>4,060.50</b>	

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### About CARE Ratings:

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