Agni Cement Industries Limited

Ratings

Facilities	Amount (Rs. in Million)	Ratings[1]	Rating Action
Long Term Bank Facilities	**115.66**	**CARE-NP BB- [Double B Minus]**	**Revised from CARE-NP BB**
Short Term Bank Facilities	**690.00**	**CARE-NP A4 [A Four]**	**Reaffirmed**
Total Facilities	**805.66 (Eight Hundred Five Million and Six Hundred Sixty Thousand Only)**		

Details of instruments/facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the long term bank facilities of Agni Cement Industries Limited (ACIL) to 'CARE-NP BB-' from 'CARE-NP BB' and has reaffirmed the rating of 'CARE-NP A4' assigned to the short term bank facilities of ACIL.

Detailed Rationale & Key Rating Drivers

The revision in ratings assigned to the bank facilities of ACIL takes into account the deterioration in the financial performance of the company during FY22 (Audited, FY refers to the twelve-months period ending mid-July) amid challenging operating environment for cement manufacturers in Nepal amid low demand prospects and increased competition. Furthermore, the company's financial profile is likely to remain adversely impacted further in FY23 marked by lower income, squeezed profitability margins and elongated operating cycle. The ratings continue to be constrained by the leveraged capital structure of the company along with modest debt service coverage indicators, lack of backward integration and raw material price volatility risk. The ratings also factor in working capital intensive nature of operations and presence in highly competitive industry with cyclical nature.

The ratings, however, continue to derive strength from experienced promoters in the related field, established brand, and stable demand outlook for cement over the long term, however muted over the near term.

Going forward, the ability of the company to profitably scale up of its operations while efficiently managing the working capital cycle will be the key rating sensitivities. Any substantial debt funded capital expenditure leading material to deterioration in its capital structure and debt coverage indicators from current levels will also be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Deteriorated financial performance of the company over FY22-9MFY23 characterized by decline in sales amid industry-wide slowdown

ACIL's capacity utilization declined to 47% during FY22 from 49% during FY21 on account of decrease in market demand for cement in the country owing to slowdown in construction activities amid lower-than-expected government capital expenditure. This coupled with lower price realizations led to decline in the company's total income in FY22 by ~10% year-on-year (y-o-y) to Rs. 1,216 Mn. However, despite lower income, PBILDT margin improved to 8.57% in FY22 from 6.82% in FY21 on account of steps taken by the management to reduce the cost of sales by taking cost saving steps to reduce the sales and administrative expenses. The declining trend in operations continued in 9MFY23 (Unaudited, refers to the nine-months period ended mid-April 2023), with average capacity utilization falling sharply to 27%. Consequently, total income during 9MFY23 declined to Rs. 512 Mn. Cement industry in Nepal continues to be impacted by slow market demand owing to lower capital expenditure by the government. Retail demand also remains muted owing to the tight liquidity and reduced credit appetite of BFIs leading to lesser construction activities. Furthermore, the increased industry

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

capacity over the last couple of years means that the industry capacity utilizations are likely to remain below par over the near-to-medium term. Rebound in scale of operations amid the ongoing industry headwinds remains a key monitorable aspect.

Leveraged capital structure with modest debt service coverage indicators

The company's capital structure remains leveraged with gearing ratio of 2.69x at the end of FY22, increasing from 2.31x at the end of FY21 mainly on account of higher utilisation of working capital borrowings and infusion of unsecured loans from Directors in FY22. Interest coverage ratio of the company remained modest at 1.36x during FY22 which deteriorated from 1.50x during FY21 due to increase in interest cost of the company. Similarly, the total debt to Gross Cash Accrual Ratio remains substantially high at 41.27x during FY22 (FY21: 34.17x) as the company's cash accruals remain relatively low compared to its debt levels. Rationalization of debt levels will remain critical from credit perspective.

Lack of backward integration and raw material price volatility risk

ACIL is engaged in producing cement through its grinding unit and does not possess its own clinker unit. Hence, it procures clinker majorly from other cement manufacturers in Nepal. Having to procure a bulk of its raw materials from competitors remains a disadvantage, as scope for margins generally remain slim compared to competitors that have their own clinker units. ACIL mainly uses clinker, slag, flyash, gypsum, etc. as its major raw materials. Raw material cost continues to be the major cost component of ACIL constituting around 87% of the net sales in FY22. Hence, the company's ability to generate profits hinge in its ability to pass on any adverse movement in raw material price to the customers in a timely manner, which tends to be more difficult for a manufacturer with only grinding unit.

Working capital intensive nature of operations

Operations of the company are highly working capital intensive marked by average operating cycle of around 257 days in FY22 which increased from 198 days in FY21. Amid increased competition, the average collection period is quite high in the cement industry. APL's average collection period remained particularly high at around 302 days during FY22 which increased from 253 days in FY21. Furthermore, the company is required to maintain adequate inventory of raw materials to avoid any stock out issues. Although payable period also remained on the higher side, 92 days in FY22, the company's net operating cycle remains highly elongated, resulting in increased reliance on bank borrowings. Average utilization of fund based working capital limits were high at ~80% of ACIL's sanctioned limits for twelve-month period ended mid-April, 2023.

Presence in a competitive industry with cyclical nature

ACIL is operating in a highly competitive market, dominated by the large cement manufacturers with wide brand acceptability. Given the increased competition, the players in the industry do not have pricing power and are exposed to competition induced pressures on profitability. The demand of cement industry is considered cyclical as it depends upon the capital expenditure plan of major players in the end-user industry. Furthermore, with increase in the capacities of the existing plants and new capacities coming into operation, competition has intensified which has resulted into substantial decline in profitability margins of the industry players in the recent years.

Key Rating Strengths

Experienced promoters in the related field

ACIL is promoted by individuals who have experience in cement industry, medical and education sectors. The company is managed under the overall guidance of its Board of Directors (BoD), with members having wide experience in the related field. Mr. Krishna Prasad Pokharel, Chairperson, has been involved in different businesses for 25 years and is also a director of Shubhashree Agni Cement Udhyog Limited (SSL) (CARE-NP BB+/A4+). Dr. Tara Prasad Pokharel, Managing Director, is also the Managing Director of SSL. The BoD is supported by management team of qualified professionals with wide experience in cement industry.

Moderate brand presence marketing network

ACIL has an operational track record of over twelve years in the manufacturing of cement by grinding clinker. During this course, it has established four brands namely; Agni, Orient and Tridev for PPC brand and Alfa for OPC brand. ACIL has focused its sales in the territory of nine zones (out of 14 zones of Nepal) covering 31 districts (out of 77) of Nepal.

Stable demand outlook of cement products in the country in the long term, however muted in the near term

Demand of cement 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 cement 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 cement manufacturers like ACIL. 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 cement industry in Nepal is challenging in the near term

About the Company

Agni Cement Industries Limited (ACIL) is a public limited company, established in 2007 and converted from Private to Public Limited on July 14, 2022. ACIL is engaged in producing cements like Portland Pozzolana Cement (PPC) and Ordinary Portland Cement (OPC) having installed capacity of 900 metric tons per day (MTPD). ACIL had started its cement grinding plant in December 2009 with 600 MTPD which was later enhanced to 900 MTPD in May 2018.

Financial Performance

(Rs. Million)

For the Period	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	1,305	1,352	1,216
PBILDT Margin (%)	9.81	6.82	8.57
Overall Gearing (times)	2.28	2.31	2.69
Total Outstanding Liabilities/Tangible Net worth (times)	2.99	3.22	3.25
Interest Coverage (times)	1.44	1.50	1.36
Current Ratio (times)	1.16	1.17	1.32
Total Debt/Gross Cash Accruals (times)	24.17	34.27	41.42

A: Audited

Annexure 1: Details of the Facilities Rated

Name of the Bank Facilities	Type of the Facility	Amount (Rs. In Million)	Ratings
Long Term Bank Facilities	Term Loan	115.66	CARE-NP BB- [Double B Minus]
Short Term Bank Facilities	Fund/Non-Fund Based Limits	690.00	CARE-NP A4 [A Four]
Total		**805.66**	

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About CARE Ratings Nepal Limited:

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