

Sona Packaging Industries Private Limited

Ratings

Facilities/Instrument	Amount (Rs. in Million)	Ratings ¹	Rating Action
Long Term Bank Facilities	104.06	CARE-NP BBB- [Triple B Minus]	Assigned
Short Term Bank Facilities	645.94	CARE-NP A3 [A Three]	Assigned
Total Facilities	750.00 (Seven Hundred Fifty Million Only)		

* Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned rating of 'CARE-NP BBB-' to the long term bank facilities and 'CARE-NP A3' to the short term bank facilities of Sona Packaging Industries Private Limited (SPIPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of SPIPL derive strengths from its moderate financial risk profile marked by growing scale of operations and moderate capital structure leading to adequate debt service coverage indicators of the company. The ratings also factor in experienced and resourceful promoters of the company in the related field, locational advantage and diversified customer profile, moderate operating cycle and steady demand outlook of packaging business over the medium term.

The ratings, however, are constrained by volatile profitability owing to limited ability to pass through changes in raw material price, competitive nature of industry with low product differentiation. The ratings also factor in high reliance on import and foreign exchange fluctuation risk on such imports and exposure to volatile interest rates.

Going forward, the ability of the company to manage growth in operations while maintaining the profit margins and rationalization of its debt through efficient working capital management would be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Strengths

Experienced and resourceful promoters of the company

SPIPL is managed under the overall guidance of the company's board of directors (BOD) who possess wide industry experience. Mr. Chunna Prasad Sharma, Chairman, has around four decade of cross-sector experience and holds position as Chairman and Director in various other businesses. He is also chairman in Yashoda Foods Private Limited [CARE-NP BBB/A3+]. Mr. Umashankhar Malpani, Managing Director is involved in the packaging business since its inception. Similarly, other directors of the company also have work experience in various businesses such as manufacturing, hospitality, spices, real estate etc. The BOD's are further supported by a team of experienced management team members.

Moderate financial risk profile marked by growing scale of operations, low gearing and adequate coverage indicators

SPIPL generates its revenue from sales of packaging products (laminated roll and BOPP roll) which are used in different industries. The company's total operating income (TOI) grew at a compounded annual growth rate over the last 4 years (FY19-FY22; FY refers to the twelve-month period ending mid-July) at around 12%, aided by sustained demand amid

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

increasing consumption of fast moving consumer goods. During 9MFY23 (Provisional, refers to the nine-month period ended mid-April 2023), the company achieved TOI of Rs. 1,341 Mn.

Capital structure of the company stood comfortable with overall gearing ratio of 0.93x as on mid-April 2023 improving from 1.10x as on mid-July 2022 majorly on account of accretion of profits to the reserve backed by improved operational performance of the company during the year. Total debt to equity stood comfortable at 0.07x as on mid-April 2023 (FY22: 0.13x, FY21: 0.20x). With healthy improvement in PBILDT, interest coverage ratio stood comfortable at 5.33x during 9MFY23. Furthermore, total debt/ GCA of the company improved to 3.85x in 9MFY23 from 4.84x in FY22.

Locational advantage and diversified customer profile

SPIPL's manufacturing facility is located in Omsatiya, Rupandehi, Nepal around 10 Kms from Indo-Nepal borders in Sunauli. Since the procurement of raw materials is mainly in the form of imports and routes through Indian ports, the factory's proximity to Indian border remains added advantage in terms of freight cost saving. Also, the plant site is located proximity to various customers in different industries such as food industries, soap industries and many others.

The customer profile consists of players in the FMCG industry, Food and Agro processing industry, soap and detergent industry and others including a few reputed ones. the company caters to customers across Nepal. The diversified customer base / industry not only diffuses the risk of dependency on single industry; however, also allows the company to cater to a larger market.

Moderate operating cycle

SPIPL is involved in manufacturing and printing of various packaging materials by procuring the raw materials both locally and importing from India. The company is required to keep adequate inventory for smooth operations and extend reasonable credit to their customers, leading to reliance on bank borrowings to meet working capital requirements. SPIPL generally allows 60-90 days credit period to its customers. During FY22, average collection period was 84 days (FY21: 88 days). The company keeps inventory for around 1.5 months; inventory holding days was 53 days for FY22. Consequently, total operating cycle of the company was around 94 days in FY22 (FY21: 76 days). The average utilization of working capital limits against sanctioned limit remains moderate around 60% of its working capital limits for the twelve-month period ended mid-April 2023.

Stable demand outlook of packaging business over the medium term

The Nepalese packaging industry has potential for growth since wide range of packaging materials required for various industries are imported from India and other countries. It is highly probable with the growing economy; the need of packaging materials will also increase as demand for packaging increases with the increase in the industrial output. Additionally, Nepal Standards (Certification Mark) Regulation issued by Nepal Bureau of Standards and Metrology has mentioned various products and range of weight for which details of products such as price, weight shall be mentioned and for which packaging is mandatory. The outlook for the packaging industry in the long term remains stable cause of key demand drivers such as increased economic activity leading to industrial growth and industrial outputs.

Key Rating Weaknesses

Volatile profitability owing to limited availability to pass through changes in raw material price

Major raw materials of SPIPL are polyester/BOPP/ CPP film, chemicals, ink, reducer, coated paper, poly film which are majorly imported from India. The prices of these raw materials are market linked and determined on a periodic basis, thus exposing the company to the volatility in the prices of raw materials which has a bearing on its profitability margins. The prices of these raw materials are directly linked to the prices of petroleum products in international market. Price of crude oil remains

volatile over the year leading to volatile profitability, evident also in the highly volatile profitability margins of the company over FY20-FY22. SPIPL's PBILDT margin had declined to 7.25% in FY22 from 15.22% amid increased input prices, which the company was not able to fully pass through to its customers.

Any sudden spurt in these raw material prices, as seen in second half of FY22, might not be fully passed on to the end customers on account of highly competitive nature of the industry, which impacts the company's profitability margins. The ability of the company to pass through changes in raw material prices to the finished products related to raw materials leading to a more stable profitability will be critical from credit perspective.

Competitive nature of industry

Manufacturing and printing of packaging materials is highly competitive due to presence of several organized / unorganised players being both local and international players owing to low entry barrier and low technology and capital requirement. Low product differentiation of SPIPL's product results in high competition from other players including traders.

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

SPIPL's business operations are dependent on imports as domestic production is not sufficient to fulfill the demand. As significant purchases (~70%) are made in the form of imports, the company is exposed to unfavourable changes in the government policy towards imports and also from the exporting countries. 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. Furthermore, the company has not hedged its foreign currency exposure, thus unveiling itself to foreign currency fluctuation risk. During 9MFY23, the company incurred foreign exchange loss of Rs. 6 Mn (FY22: Rs. 6 Mn).

Exposure to volatile interest rates

Sustained requirement for short-term working capital borrowings results in a high interest expense for SPIPL. The company's interest rates are based on 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. Hence, funding taken by the company remains exposed to volatile interest rate. Sustained high interest rates, as seen over the last year or so, have added to the interest burden of the company, squeezing its profitability and impacting its liquidity position.

About the Company

Sona Packaging Industries Private Limited (SPIPL) is a private limited company incorporated on March 15, 2007 for manufacturing of various flexible wrappers and packaging materials, having plant at Omsatiya, Rupandehi Nepal. The company has total installed capacity of 600 MT per month for production of various packaging materials.

Financial Performance

(Rs. In Million)

Particulars	FY20 (A)	FY21 (A)	FY22 (A)
Income from Operations	1,373	1,735	1,695
PBILDT Margin (%)	14.75	15.22	7.25
Overall Gearing (times)	0.85	1.13	1.10
Interest coverage (times)	7.43	19.37	7.47
Current Ratio(times)	1.28	1.18	1.20
Total Debt/Gross Cash Accruals (times)	1.97	1.97	4.84

A: Audited

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	104.06	CARE-NP BBB-
Short Term Bank Facilities	Fund Based	184.94	CARE-NP A3
Short Term Bank Facilities	Non-Fund Based	461.00	CARE-NP A3
Total		750.00	

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