Life Care Distributors Private Limited

Rating

Facility	Amount (Rs. In Million)	Ratings[1]	Rating Action
Short Term Bank Facilities	950.00 (Decreased from 1,650.00)	CARE-NP A4+ [A Four Plus]	Revised from CARE-NP A3
Total Facilities	950.00 (Nine Hundred Fifty Million Only)		

Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has revised the rating assigned to the short term bank facilities of Life Care Distributors Private Limited (LCD) to 'CARE-NP A4+' from 'CARE-NP A3'.

Detailed Rationale & Key Rating Drivers

The revision in the rating assigned to the bank facilities of LCD factors in deterioration in financial and operational performance of the company during FY22 (Audited, FY refers to the twelve-month period ending mid-July) leading to deteriorating capital structure and debt service coverage indicators. Amid sluggish demand leading to muted operational performance during FY23 as well, the company's coverage indicators are likely to remain suppressed over the near-term. The rating remains constrained by LCD's working capital intensive nature of operations, exposure to volatile interest rates, foreign exchange fluctuation risk and competitive nature of Fast Moving Consumer Goods (FMCG) trading industry. The rating also factors in LCD's exposure to regulatory risk and takes cognizance of the near-term challenges faced by the FMCG traders in Nepal, particularly due to the liquidity stress built up in the banking sector coupled with inflationary impact on prices potentially impacting demand prospects.

The rating, however, continues to derive strength from its experienced and resourceful promoters, established distribution network coupled with association with reputed brands along with comfortable liquidity profile of the company supported by liquid investments in listed shares.

Going forward, the ability of the company to profitably scale up its operations on a sustainable basis leading to improved debt service coverage indicators shall be the key rating sensitivities. Furthermore, effective management of working capital with improvement in solvency position and maintaining its relationship with its key suppliers will also remain key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Moderation in financial risk profile during FY22, further deterioration likely in FY23

During FY22, total operating income (TOI) of the company declined by ~47% over FY21 to Rs. 2,127 Mn. The decline was mainly on account of discontinuation of distribution of products from Mondelez India Foods Private Limited since December 2021. Additionally, demand in FY21 was high on account of increased demand of products like sanitizers, handwash, soaps, etc. and other FMCG products in the consumer level amid pandemic. With decline in TOI, PBILDT of the company deteriorated in FY22 by ~65% to Rs. 92 Mn with decline in PBILDT margin to 4.31% in FY22 compared to 6.48% in FY21. Consequently, PAT margin declined by 275 bps to 1.55% in FY22.

The declining financial performance led to deterioration in debt service coverage indicators of the company in FY22. Interest coverage ratio deteriorated to 2.07x in FY22 compared to 6.02x in FY21. Moreover, Total debt/ GCA for FY22 stood high at 19.17x, deteriorated from 3.55x in FY21 on account of decline in gross cash accruals (GCA). Furthermore, overall gearing ratio of the company stood leveraged at 2.34x at the end of FY22 which deteriorated from 1.23x at the end of FY21 majorly due to deterioration in tangible net worth of the company amid dividend distribution of Rs. 187 Mn during FY22.

During FY22, sales have been impacted by muted demand for various consumer products impacted by the slowdown in the economy of the country. Amid increased inflation and higher custom duty for imports, the prices of the FMCG products had been increasing, which has also impacted consumption to some extent. Furthermore, sales are expected to remain sluggish in the near term amid increased price of goods at consumer level. During 9MFY23 (Unaudited; refers to nine months period ended mid-April 2023), the company has booked total income of Rs. 822 Mn. Lower income levels coupled with relatively high debt levels, albeit on a declining trend in commensurate with the declining operations, is likely to result in suppressed coverage indicators of the company over the near-term. The company's ability to grow its operations while rationalizing its debt levels will remain a key monitorable aspect.

Working capital intensive nature of business leading to elongated operating cycle

The operations of the company are working capital intensive in nature as the company imports its products mainly from foreign countries and sells it in the domestic market. The company needs to maintain adequate stock in order to ensure regular supply to its customers. Average inventory days of the company was around 84 days during FY22 increased from 44 days during FY21. The average collection period increased to 70 days during FY22 from 47 days during FY21 on account of easing of credit policy by the company to its customers. Consequently, Operating cycle of the company increased substantially to 151 days in FY22 from 89 days in FY21. 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-June 2023.

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

LCD is involved in import/ trading of FMCG products from various countries and selling them in the domestic market. LCD operates in the highly competitive industry, as the company has to compete with several local players as well as other international players who are into the business of importing similar products from foreign countries and selling them domestically.

Exposure to volatile interest rate and foreign exchange fluctuation risk

Sustained requirement for short-term working capital borrowings has led to a relatively high interest outgo for LCD (Rs. 44 Mn during FY22), impacting its net profitability. The company's interest rates are based on 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. Any further significant rate hikes could put increased interest burden on the company, squeezing its profitability and impacting its liquidity position. Furthermore, substantial portion of purchases (around 30-40% in FY22) are invoiced in foreign currency other than Nepalese and Indian Rupees for which the company is exposed to the fluctuation in foreign exchange rates. LCD doesn't undertake any hedging mechanism while importing trading items at foreign convertible currency other than Nepalese and Indian Rupees, which exposes LCD to foreign exchange fluctuation risks. The company has the policy to pass on the fluctuation in cost to the consumers to maintain the bottom line.

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 on custom duty. In December 2021, Nepal Rastra Bank set a 100% cash margin to open letter of credit for the imports of various items including chocolates and certain cosmetic products which was discontinued by government from December 2022. Furthermore, in order to provide impetus to the local FMCG manufacturing industry, Nepal Government has increased import duty on most of the imported products to 15% from 5% from FY23. This follows various counter measures the GoN has been taking to curb outflow of foreign reserve of the country. As a result of increased custom duty and requirement of cent percent cash margin, imported products are available to the consumers at a higher price and could impact their demand, which could lead to increased pressure on the turnover and profitability of the company. However, the effect may be partially insulated as the products the company deals with are high value branded products of which replacement may not be easily available. Hence, overall demand is likely to sustain over the medium period.

Key Rating Strengths

Experienced and resourceful promoters and long track record of operations

LCD has an operational track record of more than a decade in import/ trading of FMCGs in Nepal. LCD is managed under the overall guidance of Mrs. Jamuna Agrawal and Mr. Saurav Garg. Mrs. Jamuna Agrawal is associated with the company since inception and looks after the overall affairs of the company. She has relevant experience of over two decades. Mr. Saurav Garg is the Managing Director and has more than a decade of experience in FMCG business. The board is aptly supported by an experienced management team across various functions.

Diversified distribution network and established brands

LCD has national presence reaching all parts of Nepal and covering all major towns and cities. Currently, the company has more than 100 stockiest / sub-distributors in Nepal. LCD is presently involved in supplying varieties of products manufactured by six FMCG companies which have strong brand recognition in Nepal. For most of these products, the company is the sole distributor in Nepal.

Liquidity profile supported by liquid investments in listed shares

Liquid investment of the company was Rs. 60 Mn at the end of FY22 compared to Rs. 120 Mn at the end of FY21. These are mainly in the form of shares of the publicly listed companies and financial institutions. The investments are readily marketable in nature and lends liquidity cushion to the company. Furthermore, moderate cash flow generation has helped the company continue to not avail any long-term debt. LCD's only debt remains working capital related short-term borrowings. Furthermore, the company has decent GCA of Rs. 43 Mn during FY22, which can be considered adequate, particularly in absence of principal repayments of any long-term debt.

About the Company

Life Care Distributors Private Limited (LCD) was registered as a private limited company in June 2011. LCD principally involves in import/ trading of FMCGs. Currently LCD is involved in supplying more than 100 varieties of products manufactured by 6 FMCG companies around the globe. For most of the products, the company is sole distributor in Nepal.

Financial performance

(Rs. In Million)

For the year ended Mid-July	FY20(A)	FY21(A)	FY22(A)
Income from Operations	2,264	4,003	2,127
PBILDT Margin (%)	4.88	6.52	4.31
Overall Gearing (times)	1.88	1.23	2.34
Interest Coverage (times)	1.64	6.02	2.07
Current Ratio (times)	1.12	1.13	0.95
Total Debt/Gross Cash Accruals (times)	30.93	3.55	19.17

A: Audited

Annexure 1: Details of the Facilities rated

Nature of the Facility	Type of the Facility	Amount (Rs. in Million)	Rating
Short Term Bank Facilities	Fund Based/ Non- Fund Based	950.00	CARE-NP A4+ [A Four Plus]
Total		**950.00**	

Contact us

Analyst Contact
Ms. Anusha Thapa
+977-01-4012630
anusha.thapa@careratingsnepal.com

Mr. Santosh Pudasaini
+977-01-4012628
pudasaini.santosh@careratingsnepal.com

Relationship Contact
Mr. Achin Nirwani
+977 9818832909
achin.nirwani@careratingsnepal.com

About CARE Ratings:

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