

T.G. Auto Group Private Limited

Ratings

Facilities/Instrument	Amount (Rs. Million)	Rating ¹	Rating Action
Long Term Bank Facilities	164.48	CARE-NP BB [Double B]	Assigned
Short Term Bank Facilities	535.52	CARE-NP A4 [A Four]	Assigned
Total Facilities	700.00 (Seven Hundred Million Only)		

* Details of Facilities in Annexure 1

CARE Ratings Nepal Limited (CRNL) has assigned the rating of 'CARE-NP BB' to the long-term bank facilities and 'CARE-NP A4' to the short-term bank facilities of T.G. Auto Group Private Limited (TGPL).

Detailed Rationale & Key Rating Drivers

The ratings assigned to the bank facilities of TGPL are primarily constrained by operations stabilization risk associated with its recently set-up two-wheeler assembly unit. The ratings factor in TGPL's short operational track record, working capital intensive nature of operations and cyclical nature of auto industry along with competition from other automobile players, which could be further heightened by prospective commencement of assembly units of other major market players. The ratings also factor in the exposure of automobile industry to regulatory risk along with reliance of TGPL's business model on favourable duty regime of Government of Nepal (GoN) currently for assembly units vis-à-vis direct importers of finished goods.

The ratings derive strengths from experienced promoters and directors of TGPL and it being a part of Triveni Group, which has an established and diversified business presence in Nepal. In addition, TGPL, being an assembly unit, also derives strength from competitive advantage owing to favourable duty regime for import of Completely Knocked Down (CKD) over Completely Built Up (CBU) vehicles. The resulting lower selling price augur well from volume offtake for CKD motorbikes assembled in Nepal compared to those imported as CBUs. The ratings also take cognizance of the established brand presence of Royal Enfield in the premium two-wheeler (2W) segment further enhanced by TGPL being the sole manufacturer & supplier of Royal Enfield motorbikes in Nepal, technical support and guidance from Eicher Motors Limited (EML, parent company of Royal Enfield) and stable demand outlook for 2W industry over the medium term despite near-term headwinds.

Going forward, the ability of TGPL to profitably scale up the operations while maintaining favourable capital structure and coverage indicators as envisaged would be the key rating sensitivity. Furthermore, the ability of the company to efficiently manage working capital requirements and any unfavorable regulatory changes would also be the key rating sensitivities.

Detailed Description of the Key Rating Drivers

Key Rating Weaknesses

Operations stabilisation risk

TGPL started commercial operations from mid-May, 2023 and therefore has a very short operational track record. The assembly unit was constructed at total cost of around Rs. 275 Mn. During the operational period of ~2MFY23 (Unaudited), the company's total operating income amounted to Rs. 189 Mn. However, amid high operational and fixed costs, the company reported losses in FY23. The profitability margins of TGPL are expected to improve as the business stabilizes over FY24 and

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

beyond. However, the company's ability to achieve the sales volume as envisaged could be a challenge particularly given the ongoing slow pace of economic growth in the country and relatively low consumer sentiments. Hence, stabilization of operations with ramping up of scale as expected will remain a key monitorable aspect.

Working capital intensive nature of operations

Automobiles manufacturing / supplying business in Nepal is inherently working capital intensive by nature mainly due to high inventory holding requirements and procuring of inventory by making advance payments to the suppliers. The company is required to maintain minimum level of inventory to guard against supply shortages as the supply is totally dependent upon imports and to meet immediate demand of its customers. The company procures its products from EML India, assembles it and supplies it to distributor, the sole authorized distributor of Royal Enfield motorcycles in Nepal. TGPL imports CKD parts against letter of credit on sight. As a result, TGPL has to rely on short term bank borrowings to meet the requirements. Although this is mitigated by low collection period as majority of sales to AAPL is on cash basis.

Cyclical nature of the auto industry and high competition from other automobile players

The demand for automobiles is inherently vulnerable to the economic cycles and is highly sensitive to interest rates. Demand for motorcycles generally increases during period of high economy growth rate and low interest rate regime and vice-versa. There are large numbers of players operating in market for two wheelers. Further, competition is also intensified due to introduction of electric vehicles in the market. There are other two-wheeler assembling units already operating in Nepal and a few major players are expected to establish their assembling units in the near future. Consequently, TGPL could face stiff competition to grab and maintain market position. However, major 2W players currently present in the country are more present in the below 250cc segment, while Royal Enfield excels in the 250cc+ segment, where there are few other established players in the market. Cost benefits from CKD assembly units leading to availability of 2Ws at a much lower price points, however, could lead to more competition from premium offerings by established 2W OEMs.

Exposure to regulatory risk related to automobile industry

The demand in automobile sector is impacted by heavy import duty (which includes custom duty, excise duty and value added tax) imposed on automobiles, which are still considered as luxury items in Nepal. Although CKD units currently benefit from favourable duty regime, the business remains exposed to regulatory risks. GoN has in recent times introduced several measures to discourage purchase of premium luxury items. Nepal Rastra Bank has time and again introduced several counter measures such as decreasing cap on bank financing, imposing higher margin for opening letter of credit for import of automobiles and spare parts, and increasing risk weights on personal hire purchase loans to discourage import of automobiles. Hence, automobile manufacturing and supplier business remains exposed to risk related to similar policies of the GoN/Central Bank.

Key Rating Strengths

Experienced promoters and directors along with the company being part of Triveni Group of Nepal

TGPL derives strength from its strong promoter group belonging to Triveni Group. The Group has diversified presence in Nepal across banking, insurance, manufacturing, trading and other industries. TGPL is managed under the overall guidance of the Company's Board of Directors (BoD) who possess wide experience across sectors. Mr. Subash Chandra Sanghai, Chairman, has more than 4 decades of experience in vegetable oil refinery, vanaspati, textile and tea. Mr. Harshwardhan Sanghai, Director, currently manages both the distribution arm of Triveni group and the group's activities in the energy sector. The BoD is well supported by experienced management team in the related field.

Competitive advantage owing to favourable duty regime for Completely Knocked-Down (CKD) over Completely Build-up Units (CBU)

TGPL is in the business of producing fully assembled motorcycles from CKD (completely Knocked Down) components. The CKD units are supplied from Eicher Motors India to TGPL and are assembled in TGPL's assembly plant near Birgunj, which is in close proximity to the Indian Boarder. Assembly of CKD components presents a clear advantage over trading of CBU (Completely built unit) as the Government of Nepal (GoN) has provided rebate on excise duty and customs duty of 50% and 25% respectively to CKD over CBU for establishing assembly unit in Nepal. This provides direct cost benefit to assembly units of two-wheelers, which can lead to higher volume growth as the cost benefits are passed on to the end consumers.

Established brand presence of Royal Enfield in the premium 2W segment

Royal Enfield has for many years been revolutionising the mid-size motorcycle segment. It has successfully established its unique brand proposition, and has scaled its presence across markets. Royal Enfield, with long established global brand, has been able to quickly develop its presence and following in the premium two-wheeler segment in Nepal as well. TGPL is likely to benefit from the steady demand for Royal Enfield 2Ws as a well-established brand in the niche 350cc+ segment.

Stable demand outlook for 2Ws over the medium term

The demand prospects of 2W market in Nepal is estimated to grow at a steady rate over the medium term on the back of rising disposable income, growing young population, improved infrastructures, growing tourism sector and changing lifestyles. Also, the government has been supporting the growth of the 2W market through various policies and initiatives such as lowering import duties on 2Ws CKD parts for assembling in Nepal. However, major hurdles over the near term for the industry remain availability of affordable financing options for buyers and lower consumer sentiments amid muted economic growth in the country. Although Royal Enfield 2Ws generally tend to have a niche customer segment, increasing presence of other 2W assembly units coupled with relatively higher price segment of Royal Enfield 2Ws could limit the market share potential of the company over the medium -term.

About the Company

TGPL is a private limited company incorporated on May 24, 2022 and is a part of Triveni Group of Nepal. The company is the sole manufacturer/supplier of Royal Enfield motorcycles in Nepal. The company has a state-of-the-art assembly unit spread over 100,000 square feet in Bare district of Nepal. The installed capacity of the assembly plant is 20,000 units per year and started commercial operations from mid-May 2023. The registered office of the company is located at Kathmandu, Nepal.

Annexure 1: Details of the Facilities Rated

Nature of the Facility	Type of the Facility	Amount (Rs. Million)	Rating
Long-Term Bank Facilities	Term Loan	250.00	CARE-NP BB
Short-Term Bank Facilities	Fund Based Limits	200.00	CARE-NP A4
Short-Term Bank Facilities	Non-Fund Based Limits	250.00	CARE-NP A4
Total		700.00	

Contact us**Analyst Contact**

Ms. Poonam Agarwal

+977-01-4012630

poonamagarwal@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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